

**BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

NORTHWEST NATURAL GAS, d/b/a
NW NATURAL,

Respondent.

DOCKET UG-181053

ORDER 06

FINAL ORDER REJECTING
TARIFF SHEETS; APPROVING
AND ADOPTING JOINT
SETTLEMENT AGREEMENT;
REJECTING PARTIAL
MULTIPARTY SETTLEMENT
AGREEMENT ON DECOUPLING;
AND AUTHORIZING AND
REQUIRING COMPLIANCE
FILING

***Synopsis:** The Washington Utilities and Transportation Commission (Commission) approves and adopts a Joint Settlement Agreement (Settlement) that all parties to this proceeding support as a proposed resolution of all but one contested issue. The Settlement does the following: sets forth a revenue requirement for Northwest Natural Gas, d/b/a NW Natural (NW Natural or Company), specifying the capital structure and cost of capital, as well as certain adjustments used to derive the agreed-upon revenue requirement; revises the proposed effective date of the new rates; establishes an environmental cost recovery mechanism; implements income tax changes; revises energy conservation tariffs; and addresses rate design. The Settlement also revises the Company's low-income bill assistance program, implements a methodology for investor-supplied working capital (ISWC), and requires the Company to file an updated feasibility study and to track unauthorized gas usage by interruptible customers during curtailments. The parties have agreed to, and the Commission approves in this Order, an increase to annual revenues recovered through base rate changes of \$5,138,531 for the Company's Washington customers.*

The Commission also resolves the contested issue in the proceeding related to NW Natural's proposed decoupling mechanism. The Commission rejects the partial multiparty settlement in principle on the issue of decoupling (Decoupling Agreement). We find that the Company and other parties to the Decoupling Agreement have not shown that the proposed decoupling mechanism is tailored to address revenue volatility due to

variations in customer energy usage, but to address revenue sufficiency due to variations in fixed costs resulting from significant customer growth. Revenue insufficiency from actions unrelated to usage are more appropriately recovered through ratemaking mechanisms other than decoupling. Because we do not implement a decoupling mechanism for the Company, we decline to address, as moot, the rate-class decoupling methodology alternatively proposed by the Public Counsel Unit of the Attorney General's Office (Public Counsel).

SUMMARY

- 1 **PROCEDURAL HISTORY.** On December 31, 2018, NW Natural filed with the Commission revisions to its currently effective Tariff WN U-6 for natural gas service provided in Washington. NW Natural requested authority to increase annual revenues by \$8.3 million, a 12.6 percent increase to overall base rates. The Company's request was based on: a proposed Washington-allocated rate base of \$186,478,943, derived from a 12-month test period ending September 30, 2018; a rate of return (ROR) of 7.63 percent, with a return on equity (ROE) of 10.3 percent and a capital structure of 49.5 percent equity, 49.5 percent long-term debt, and 1 percent short-term debt.
- 2 On January 8, 2019, the Commission entered Order 01 in this docket, suspending the tariff revisions and allowing further investigation to determine if the proposed tariff filing is in the public interest.
- 3 On January 24, 2019, the Commission convened a prehearing conference. The Commission granted unopposed petitions to intervene filed by the Alliance of Western Energy Customers (AWEC) and The Energy Project (TEP), and established a procedural schedule.
- 4 The Company filed a motion to modify the procedural schedule (Motion) on May 15, 2019, explaining that the parties in the proceeding had reached an agreement in principle for a partial, all-party settlement resolving all issues concerning the Company's initial filing other than the Company's proposed decoupling mechanism. NW Natural, Staff, AWEC, and TEP (Settling Parties) were also signatories to the multiparty Decoupling Agreement, while Public Counsel contested the Decoupling Agreement. The Company thus moved to amend the procedural schedule, incorporating new and modified deadlines for filing, *inter alia*, testimony on the two settlement agreements. The Commission granted the Motion by order on May 16, 2019. The Company submitted the all-party

Settlement and the Decoupling Agreement on May 23, 2019. The parties then filed joint testimony in support of the Settlement on June 6, 2019, and the Settling Parties also filed joint testimony in support of the Decoupling Agreement. Public Counsel subsequently filed testimony in response to the Decoupling Agreement, and NW Natural and Staff filed rebuttal testimony on the same issue. The parties reserved for litigation the issue of whether and how to appropriately structure a decoupling mechanism for NW Natural.¹

5 The Commission conducted an evidentiary hearing on the Settlement and the contested issue on August 14, 2019. The Commission also held a public comment hearing on July 16, 2019, in Vancouver, Washington. By August 15, 2019, the Commission received four comments submitted by the public through the Commission's web portal, all opposing a rate increase.² On September 12, 2019, Staff, Public Counsel, and NW Natural filed post-hearing briefs.

6 **PARTY REPRESENTATIVES.** Lisa Rackner and Jocelyn Pease, McDowell Rackner & Gibson PC, Portland, Oregon, represent NW Natural. Chad M. Stokes and Tommy A. Brookes, Cable Huston LLP, Portland, Oregon, represent AWEC. Simon J. ffitch, Attorney at Law, Bainbridge Island, Washington, represents TEP. Lisa W. Gafken and Nina Suetake, Assistant Attorneys General, Seattle, Washington, represent Public Counsel. Jennifer Cameron-Rulkowski, Assistant Attorney General, Lacey, Washington, represents Staff.³

7 **COMMISSION DETERMINATIONS.** We find that the rates, terms, and conditions in the Settlement are fair, just, reasonable, and sufficient. We accordingly approve the proposed Settlement in full, without conditions.

8 We reject the Decoupling Agreement. We determine that the Settling Parties have failed to provide an appropriate record to support the Decoupling Agreement and thus have not demonstrated that the Decoupling Agreement is in the public interest. Because we do not

¹ Settlement at ¶ 1.

² Exh. BR-4.

³ In formal proceedings such as this, the Commission's regulatory staff participates like any other party, while the Commissioners make the decision. To assure fairness, the Commissioners, the presiding administrative law judge, and the Commissioners' policy and accounting advisors do not discuss the merits of this proceeding with the regulatory staff, or any other party, without giving notice and opportunity for all parties to participate. *See* RCW 34.05.455.

implement a decoupling mechanism for the Company, we decline to address, as moot, Public Counsel’s alternative rate-class decoupling proposal.⁴

MEMORANDUM

I. CONTESTED ISSUE—DECOUPLING

A. Decoupling Agreement

9 The single issue raised in the Company’s initial filing that is not addressed in the Settlement is decoupling; specifically, whether the Commission should implement a decoupling mechanism for NW Natural, and if so, whether the mechanism should use a per-customer or per-rate class revenue calculation methodology.

10 In its initial filing, NW Natural proposed a permanent decoupling mechanism that would apply to all residential and commercial firm and interruptible sales customers.⁵ NW Natural’s proposed mechanism would set the Company’s allowed revenue on a per-customer basis, which would allow it to recover a fixed amount of revenue for each customer.

11 Specifically, the proposed mechanism would decouple base revenue, derived from the volumetric base rate portion of each applicable rate schedule, from sales on a monthly basis.⁶ A revenue-per-customer true-up would be calculated during each month’s accounting close, and any revenue above or below the normalized revenue-per customer would be deferred on the Company’s balance sheet until it is reviewed for prudence and amortized over the following year’s annual purchased gas adjustment (PGA) period.⁷ Under NW Natural’s proposed mechanism, each residential and commercial customer class would be divided into two groups based on usage characteristics, resulting in four separate customer groups.

⁴ See Public Counsel Post-Hearing Brief at 12 (“If the Commission decides to implement a decoupling mechanism for NW Natural, the decoupling should occur on a rate class basis) (emphasis added).

⁵ Walker, Exh. KTW-1T at 3:15-18.

⁶ Walker, Exh. KTW-1T at 11:2-4. “The mechanism would not factor in the monthly Customer Charge, temporary rate adjustments, any amortizations built into the permanent (base) rate, or cost of gas revenue.” *Id.* at 11:4-6 (footnote omitted).

⁷ The deferral account would accrue interest. *Id.* at 13:1-3.

- 12 The Company's proposal includes an earnings test and a soft cap on deferrals. Upon application of the earnings test, the Company would share 50 percent of pre-tax operating revenues in excess of the Company's authorized rate of return; if the Company has a decoupling surcharge balance, the earnings sharing would effectively reduce the surcharge balance.⁸ Under the proposed 5 percent soft cap, any decoupling surcharges that would result in a rate increase of 5 percent or more would remain on the Company's balance sheet and not be included in rates that year, but would be included in rates the following year, subject to the cap.⁹
- 13 The Company states that conservation measures implemented by customers through participation in the Company's Schedule G Energy Efficiency Services Program had decreased energy usage for residential and commercial customers.¹⁰ NW Natural argues that it has experienced lost margin as a result of its conservation efforts, noting that the Company recovers about 66 percent of its fixed costs on a volumetric, *i.e.*, per-therm basis.¹¹ In pre-filed testimony, however, the Company's witness on decoupling did not identify the Company's lost margin.
- 14 In its initial filing and the Decoupling Agreement, the Company does not make any commitments to increase conservation efforts upon implementation of its proposed decoupling mechanism, but the Company separately states that it "would continue to pursue cost-effective energy efficiency through [its] existing programs."¹²
- 15 The mechanism proposed in the Decoupling Agreement is substantially similar to the Company's initial proposal. The parties to the Decoupling Agreement ask that the Commission approve the Company's proposed decoupling mechanism, with the following six clarifications and modifications:¹³

⁸ *Id.* at 14:1-16.

⁹ *Id.* at 17:14-20. Deferrals could continue indefinitely. *See Wash. Utils. & Transp. Comm'n v. Puget Sound Energy*, Dockets UE-170033 and UG-170034, Order 08 at ¶ 303 (Dec. 5, 2017) ("large deferrals have developed under the natural gas decoupling mechanism with unrecovered balances remaining on PSE's books for more than one year").

¹⁰ Walker, Exh. KTW-1T 7:7-9, 8.

¹¹ *Id.* at 6:1-3, n.5. This number does not include temporary rates, the weighted average cost of gas, demand, or the monthly charge portion of customer bills.

¹² Walker, Exh. KTW-1T at 16:10-12.

¹³ Decoupling Agreement at ¶ 4.

- a. The Company would calculate “Actual Revenue” with tariff rates and billing determinants, rather than the Company’s proposed weighted average group rate. The revenue per customer amount would not change annually.¹⁴
- b. The Company would request reauthorization within five years after the effective date of the decoupling mechanism tariff, which need not be made in a general rate case filing.
- c. The Company would include residential customers on Rate Schedule 3 and combine them with commercial customers on Rate Schedule 3.
- d. The Company would decouple commercial customers on Rate Schedule 1 and Rate Schedule 3 separately.
- e. Industrial customers would not be subject to the decoupling mechanism.
- f. The Decoupling Agreement would be implemented on November 1, 2019, the rate effective date under the Settlement Agreement, rather than December 1, 2019, as initially proposed.¹⁵

16 In joint testimony filed in support of the Decoupling Agreement, the Settling Parties list first among the benefits of decoupling that it would allow the Company “to recover the costs incurred to serve customers.”¹⁶ AWEC states that it is a signatory to the Decoupling Agreement because it does not apply to industrial customers,¹⁷ and TEP similarly makes little comment on the Decoupling Agreement, stating that it joined the Decoupling Agreement as part of the overall settlement.¹⁸

17 Staff witness Jing Liu, in separately filed testimony in support of the Decoupling Agreement, focuses on the Company’s recovery of incremental costs of serving new customers as the basis for implementing a per-customer decoupling mechanism: “Staff believes it is appropriate to recognize the incremental cost associated with serving [new]

¹⁴ Walker *et al.*, Exh. JT-3T at 8:7-11.

¹⁵ *Id.* at 7:1-9.

¹⁶ *Id.* at 12:10-12.

¹⁷ *Id.* at 13:11-16.

¹⁸ *See id.* at 14:14.

customers, and to provide a mechanism that helps recover those costs.”¹⁹ Liu argues that the decoupling proposal would provide “fair compensation for incremental costs associated with serving each additional customer.”²⁰ Liu notes that, despite steep annual growth in the Company’s customer base, “the increase in rate base, operation and maintenance (O&M) expense, both over 7 percent, far outpaced customer growth”; the Company’s per-customer O&M expense had a compound annual growth rate of 4.6 percent.²¹ Staff concludes by explaining that it agrees with dividing commercial customers into two separate decoupling groups because combining customers with different usage characteristics into one decoupling group creates the risk that one group may cross-subsidize the other.²²

18 Public Counsel echoes this argument in the context of consistent differences in usage for existing customers and new customers, the latter of whom tend to use less natural gas. In response to the Decoupling Agreement, Public Counsel requests that, if the Commission implements a decoupling mechanism for the Company, the decoupled revenue be set on a rate-class basis. Under Public Counsel’s proposal, the Company’s allowed revenue recovery would be fixed in this rate case for each rate class and the set amount would continue to be recovered from the relevant rate class on an annual basis, uninfluenced by changes in customer counts.

19 Public Counsel witness Scott Rubin argues that the per-customer decoupling proposed by the Settling Parties is not appropriate for a utility experiencing significant customer growth.²³ Rubin asserts that, under per-customer decoupling, high incremental revenue per customer will more than offset the costs to connect new customers.²⁴ Because NW Natural forecasts significant customer growth over the next few years, Rubin argues that per-customer decoupling would result in a significant windfall to the Company.²⁵

20 Rubin further asserts that, because new customers tend to use less natural gas than existing customers, per-customer decoupling requires existing customers to guarantee

¹⁹ Liu, Exh. JL-1T at 9:15-17.

²⁰ *Id.* at 7:5-11.

²¹ *Id.* at 8:9-18.

²² *Id.* at 17:2-6.

²³ Rubin, Exh. SJR-1T at 3:4-7.

²⁴ *See id.* at 18.

²⁵ *Id.*

higher consumption from each new customer than the customer is expected to use.²⁶ New homes tend to be more energy efficient than existing homes, and Rubin concludes that new construction uses about 14 percent less natural gas, on average, than older homes.²⁷ NW Natural does not dispute this approximation, and indeed the Company assumes that new customers “would come on using quite a bit less [natural gas] than existing customers.”²⁸ As a result, according to Rubin, a cost shift would occur, with existing customers making up for the new customers’ preexisting efficiency.²⁹ Thus, Public Counsel urges the Commission to reject the Decoupling Agreement, or, Rubin concludes, if “the Commission determines that some form of decoupling is appropriate, it should adopt rate class decoupling.”³⁰

21 In rebuttal testimony, NW Natural witness Kyle Walker submits that the revenue-per-customer approach is appropriate for the Company even in light of the Company’s expected customer growth because the cost to serve new customers would exceed revenues received from those customers.³¹ He rebuts Public Counsel’s argument that the proposed decoupling mechanism would result in a windfall for the Company, arguing that Public Counsel significantly underestimates the cost to serve new customers.³² Walker agrees with Rubin, however, that new customers’ lower usage would lead to “surcharge pressure” from the new customers that would be recovered across the customer base.³³ Finally, Walker claims that Public Counsel’s proposed rate-class

²⁶ *Id.* at 10:1-7.

²⁷ *Id.* at 9 (citing U.S. Energy Information Administration, *Residential Energy Consumption Survey, 2015 RECS Survey Data* (Dec. 2018) www.eia.gov/consumption/residential/data/2015/index.php?view=microdata); *id.* at 14 (citing U.S. Department of Energy, *Low-Income Energy Affordability Data (LEAD) Tool*, OPENEI.ORG, <https://openei.org/doe-opendata/dataset/celica-data>); *id.* at 14:15-19, 15:1-9 (citing NW Natural’s response to Public Counsel Data Request 137).

²⁸ Walker, TR 111:10-17. Staff also agrees that new customers generally use less gas than existing customers. Liu, Exh. JL-5Tr at 11:11-12.

²⁹ Rubin, Exh. SJR-1T at 10:5-7.

³⁰ *Id.* at 25.

³¹ Walker, KTW-4Tr at 3:12-16.

³² *Id.*

³³ *Id.* at 23:12-15.

decoupling approach would not provide the Company with the opportunity to earn a reasonable return,³⁴ a statement with which Staff concurs.³⁵

22 Like NW Natural, Staff's view is that Public Counsel's witness Rubin unrealistically underestimates the costs of serving new customers.³⁶ Staff thus contradicts the claim that NW Natural would receive a windfall under revenue per-customer decoupling and urges the Commission to reject Public Counsel's rate-class fixed revenue decoupling proposal. Indeed, Staff witness Liu projects that the Company would be much worse off financially under Public Counsel's proposal that without any decoupling mechanism: total revenue recovered from Schedule 2 residential customers in 2019-2024 with no decoupling would be \$202,894,039, compared to \$207,405,308 with revenue-per-customer decoupling, and \$188,762,005 under fixed, or rate-class decoupling.³⁷ For Staff, allowing the Company to earn additional revenue under the proposed decoupling mechanism "is a positive step forward in addressing regulatory lag and rate case fatigue."³⁸

23 Staff reiterated at hearing its view that decoupling should be used to address the Company's revenue sufficiency. Staff's witness Liu discussed using decoupling to provide for future revenue sufficiency where "the authorized revenue from the [general rate case] may not be sufficient over time" due to increased costs,³⁹ and agreed 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.⁴⁰ Public Counsel's witness disagreed that decoupling was designed to fully compensate a utility for investment occurring between rate cases, arguing instead that the purpose of decoupling is "to insulate the utility from some of the effects of changes in consumption, whether it's due to increased conservation or weather conditions."⁴¹

³⁴ *Id.* at 17.

³⁵ *See, e.g.,* Liu, JL-5Tr at 3:10-12.

³⁶ *Id.* at 7:10-13.

³⁷ *Id.* at 20:1, Table 1.

³⁸ *Id.* at 21:16-20. NW Natural's last general rate case before the Commission was in 2008-09. *Wash. Utils. & Transp. Comm'n v. Nw. Natural Gas Co.*, Docket UG-080546, Order 04 (Dec. 26, 2008).

³⁹ Liu, TR 106:4-5.

⁴⁰ Liu, TR 69:22-25 – 70:1.

⁴¹ Rubin, TR 107:7-15.

- 24 In its post-hearing brief, Public Counsel urges the Commission to reject the Decoupling Agreement. Public Counsel reiterates its position that revenue-per-customer decoupling is not appropriate for a utility experiencing significant customer growth because new customers would use less gas per customer than existing customers, resulting in cost-shifting from new to existing customers. Because existing customers set the baseline usage and new customers later added to the system will likely use less gas, a shortfall would result, requiring an increase in revenues collected from existing customers.⁴²
- 25 Public Counsel also counters Staff by arguing that decoupling is not intended to fully compensate a utility for the cost of serving new customers, to address regulatory lag, or to reduce the frequency of rate cases. According to Public Counsel, if the Commission allows any decoupling mechanism at all for the Company, it should occur on a rate-class basis, which would provide 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.”⁴³
- 26 Staff justifies the rate increase that would result under per-customer decoupling by noting that increases in the costs associated with serving new customers exacerbate regulatory lag, *i.e.*, impede timely cost recovery.⁴⁴ While “NW Natural could have proposed other regulatory mechanisms to address earnings erosion ... the mechanism that is before the Commission is decoupling,”⁴⁵ and the Commission, Staff notes, has discretion to adopt a variety of regulatory mechanisms to serve multiple purposes.⁴⁶ Staff does not claim that decoupling is the best mechanism for addressing recovery of fixed costs, or even that using decoupling as an attrition mechanism aligns with the Commission’s policy statement on decoupling, *Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, to Encourage Utilities to Meet or Exceed Their Conservation Targets*.⁴⁷ Ultimately, Staff recognizes its position that decoupling should be used to recover fixed costs of serving new customers “may depart from portions of the original

⁴² Public Counsel Post-Hearing Brief at ¶¶ 9-11.

⁴³ *Id.* at ¶ 29.

⁴⁴ *See* Staff Post-Hearing Brief at ¶ 8.

⁴⁵ *Id.* at ¶ 14.

⁴⁶ *Id.* at ¶ 19.

⁴⁷ *Wash. Utils. & Transp. Comm’n’s Investigation into Energy Conservation Incentives*, Docket U-100522 (Nov. 4, 2010) (Decoupling Policy Statement).

policy statement that indicate decoupling should address revenue deficiencies stemming only from a company's conservation efforts."⁴⁸

27 Unlike Staff, NW Natural claims in its post-hearing brief that the Decoupling Agreement is consistent with Commission precedent, including the Decoupling Policy Statement.⁴⁹ NW Natural also argues that its decoupling proposal aligns with other Commission-approved decoupling mechanisms,⁵⁰ even though the Company does not commit to achieving incremental conservation under the mechanism.⁵¹ Realizing that the focus of the Decoupling Policy Statement is a utility's conservation efforts, NW Natural describes its conservation programs and the commendable successes achieved therein.⁵² The Company also discusses how it meets the minimum elements required under the Decoupling Policy Statement, mainly: (1) true-up mechanism; (2) impact on rate of return; (3) earnings test; (4) accounting for off-system sales and avoided costs; (5) application to customer classes; (6) weather adjustment mechanism; (7) incremental conservation; (8) low-income; (9) duration of program and demonstrated need; (10) reporting; and (11) other factors impacting the public interest.⁵³

28 In further contrast to Staff, NW Natural claims that the goal of the proposed decoupling mechanism is to alleviate the disconnect between its extensive conservation programs and lost margin resulting therefrom, along with variations in gas consumption due to weather.⁵⁴ NW Natural addresses incremental costs only in response to Public Counsel's position that revenue-per-customer decoupling would result in a windfall for the Company, arguing that Public Counsel "grossly understates" capital costs incurred by serving new customers.⁵⁵

B. Commission Decoupling Policy

⁴⁸ Staff Post-Hearing Brief at ¶ 22.

⁴⁹ NW Natural Post-Hearing Brief at 8.

⁵⁰ *Id.* at ¶ 2.

⁵¹ *See* Liu, Exh. JL-2 at 1 ("Conservation Achievement Goals") (showing that all but one other utility include incremental conservation as part of their respective decoupling programs).

⁵² NW Natural Post-Hearing Brief at ¶¶ 25-32.

⁵³ *Id.* at ¶ 19.

⁵⁴ *Id.*

⁵⁵ *Id.* at 20.

ORDER 06

- 29 In nearly 30 years of cases and orders addressing decoupling, the Commission has consistently focused on the goal of encouraging energy efficiency.⁵⁶ In brief, the Commission first approved decoupling for PSE's predecessor electric company in 1991.⁵⁷ In 1993, the Commission determined that the mechanism was achieving its primary goal of removing disincentives to the company's acquisition of energy efficiency,⁵⁸ but approved discontinuance of the program in 1995, at the company's request.⁵⁹
- 30 A decade later, the Commission initiated a rulemaking inquiry into decoupling, but ultimately decided that it would be more efficient to address decoupling in individual utility rate cases.⁶⁰ Shortly after, in 2007, the Commission rejected a decoupling proposal for PSE's natural gas rates, recognizing that there were other means of promoting conservation programs, and "decoupling is merely one regulatory tool in a larger toolbox of devices we might use to promote greater conservation."⁶¹ A month later, the Commission approved a pilot decoupling program for Avista Utilities' natural gas operations, deciding that the advantages of the proposal outweighed its disadvantages after examining, *inter alia*, the likelihood of increased conservation as a result of

⁵⁶ A thorough history of the Commission's actions and policies on decoupling is found in the Commission's June 25, 2013, order authorizing Puget Sound Energy (PSE) to implement electric and natural gas decoupling mechanisms. See *Petition of Puget Sound Energy and NW Energy Coalition for an Order Authorizing PSE to Implement Elec. And Natural Gas Decoupling Mechanisms and to Record Accounting Entries Associated with the Mechanisms*, Dockets UE-121697 and UG-121705 (consolidated) and *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy*, Dockets UE-130137 and UG-130138 (consolidated), Order 07 at ¶¶ 81-93 (June 25, 2013).

⁵⁷ *WUTC v. Puget Sound Power & Light Company*, Docket UE-901183-T and *In re Petition of Puget Sound Power & Light Company for an Order Approving a Periodic Rate Adjustment Mechanism and Related Accounting*, Docket UE-901184-P, Third Supp. Order (April 1, 1991).

⁵⁸ *Petition of Puget Sound Power & Light Company for an Order Regarding the Accounting Treatment of Residential Exchange Credits*, Docket UE-920433, *WUTC v. Puget Sound Power & Light Co.*, Docket UE-920499, and *WUTC v. Puget Sound Power & Light Co.*, Docket UE-921262 (consolidated), Eleventh Supp. Order at 10 (Sept. 21, 1993).

⁵⁹ *Wash. Utils. & Transp. Comm'n v. Puget Sound Power & Light Co.*, Third Supp. Order *Approving Stipulations; Rejecting Tariff Filing; Authorizing Refiling*, Docket UE-950618, at 6 (Sept. 21, 1995).

⁶⁰ *Rulemaking to Review Natural Gas Decoupling*, Docket UG-050369, Notice of Withdrawal of Rulemaking (Oct. 17, 2005).

⁶¹ *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy, Inc.*, Dockets UE-060266 & UG-060267, Order 08, ¶¶ 53-69 (Jan. 5, 2007).

implementing a decoupling program.⁶² In 2009, the Commission allowed Avista Utilities' pilot program to continue; the company's decoupling proposal did not include the effects of weather or customer growth in the determination of recoverable lost margin.⁶³

31 Although "policy statements are advisory only,"⁶⁴ they help provide context for how the Commission views its regulatory role and authority. Importantly, the Commission's 2010 Decoupling Policy Statement begins by outlining the Commission's statutory framework for approving decoupling mechanisms; namely, RCW 19.285 requires utilities to pursue all available cost-effective conservation,⁶⁵ and RCW 80.28.260(3) allows the Commission to adopt policies to protect utilities from a reduction of short-term earnings that may be the direct result of utility programs to increase the efficiency of energy use.⁶⁶ The Commission discusses and distinguishes three types of regulatory mechanisms in this context: limited decoupling, full decoupling, and specific incentives. The Decoupling Policy Statement defines "limited decoupling" as "a lost margin recovery mechanism [that] would permit the utility ... to recover lost margin due only to the conservation efforts of the utility, including education and informational efforts," and "full decoupling" as a mechanism "designed to minimize the risk to both the utilities and to ratepayers of volatility in average use per customer by class regardless of cause, including the effects of weather."⁶⁷

32 Given that the statutory framework for decoupling is based on utility energy efficiency programs, the Commission expresses a distinct preference for "limited decoupling" over "full decoupling" in the Decoupling Policy Statement. Noting that "adoption of full decoupling gives us some pause,"⁶⁸ the Commission nevertheless allows for its use where appropriate, because, "[b]y reducing the risk of volatility of revenue based on customer

⁶² *In re Petition of Avista Corp. for an Order Authorizing Implementation of a Natural Gas Decoupling Mechanism and to Record Accounting Entries Associated with the Mechanism*, Docket UG-060518, Order 04 (Feb. 1, 2007).

⁶³ *WUTC v. Avista Corporation*, Dockets UE-090134 and UG-090135 (consolidated), Order 10, ¶ 256 (Dec. 22, 2009).

⁶⁴ RCW 34.05.230.

⁶⁵ Decoupling Policy Statement at ¶ 4.

⁶⁶ *Id.* at ¶ 6 n.12.

⁶⁷ *Id.* at ¶ 12.

⁶⁸ *Id.* at ¶ 25.

usage, both up and down, such a mechanism can serve to reduce risk to the company.”⁶⁹ The Commission’s focus, again, is on addressing the volatility of natural gas usage rather than revenue sufficiency. Indeed, rather than encouraging utilities to pursue decoupling as a revenue sufficiency mechanism where costs of serving new customers exceed revenues from new customers, the Commission states that, in that context, “we would consider excluding all or some new customer revenue from the mechanism or some other tool (*e.g.*, modifying a utility’s line extension tariffs) to correct any demonstrated inequity.”⁷⁰

33 **DECISION.** The Commission approves settlements “when doing so is lawful, the settlement terms are supported by an appropriate record, and when the result is consistent with the public interest in light of all the information available to the commission.”⁷¹ The Commission may approve the Settlement, with or without conditions, or reject it.

34 The Commission’s statutory duty is to establish rates, terms, and conditions for natural gas service that are “fair, just, reasonable and sufficient.”⁷² In doing so, the Commission must balance the needs of the public to have safe, reliable, and appropriately priced service with the financial ability of the utility to provide that service. The resulting rates thus must be fair to both customers and the utility; just, in that the rates are based solely on the record in this case following the principles of due process of law; reasonable, in light of the range of potential outcomes presented in the record; and sufficient, to meet the financial needs of the utility to cover its expenses and attract capital on reasonable terms.⁷³

35 We reject the Decoupling Agreement. The Settling Parties have not shown that the proposed decoupling mechanism is tailored to address reductions in short-term earnings that are a direct result of the Company’s energy conservation programs or other usage variation, rather than to recover costs that would be more appropriately recovered through other ratemaking mechanisms. As discussed below, the Decoupling Agreement is

⁶⁹ *Id.* at ¶ 27.

⁷⁰ *Id.* at ¶ 28 n.44.

⁷¹ WAC 480-07-750(1).

⁷² RCW 80.28.010(1); RCW 80.28.020.

⁷³ See generally *Bluefield Water Works & Improvement Co. v. Pub. Serv. Comm’n of W.V.*, 262 U.S. 679 (1923); *Fed. Power Comm’n v. Hope Natural Gas Co.*, 320 U.S. 591 (1944); *People’s Org. for Wash. Energy Res. v. Wash. Utils. & Transp. Comm’n*, 104 Wn.2d 798, 807-13 (1985) (describing rate setting process in Washington).

neither supported by an appropriate record nor consistent with the public interest in light of all the information available to us. NW Natural may, at a later date, make a proposal that properly separates energy usage volatility from revenue imbalance resulting from new customers, as the Commission suggests in the Decoupling Policy Statement.⁷⁴

36 As proposed, the record does not support a finding that the decoupling mechanism is “directly” tied to the Company’s conservation efforts and will not primarily be used to recover incremental costs of service. The Company demonstrates that there is some usage reduction resulting from its conservation programs, and it thus may be experiencing some lost margin, but sales of natural gas are not declining. To the contrary, the Company projects an increase in sales in the next five years.⁷⁵ Thus, the record is insufficient to establish that the decoupling mechanism would be necessary for “reducing the risk of volatility of revenue based on customer usage.”⁷⁶ Nor does the record establish that any lost margin due to usage is proportional to the revenue expected to be recovered under the mechanism as proposed.

37 In addition, it is not Commission policy to use decoupling as an attrition tool. Staff concedes as much.⁷⁷ Decoupling is not designed to be a revenue sufficiency tool for costs and functions poorly as one, in part because it provides no incentive for disciplining costs. Staff states that per-customer O&M expense had a compound annual growth rate of 4.6 percent between 2013 and 2018,⁷⁸ and we find it concerning that the Company’s expenditures on new-customer-related service are increasing so rapidly.

38 In PSE’s 2012 general rate case, PSE’s witness argued for rejecting another party’s proposed decoupling mechanism, stating that “mechanisms such as decoupling do not address [the utility’s] concern that expenses per customer are growing faster than revenue per customer.”⁷⁹ Nor should they. The Commission rejected the decoupling proposal in

⁷⁴ *Id.* The Company would bear the burden of proof to show that the change is just and reasonable. RCW 80.04.130.

⁷⁵ Walker, TR 45:25 – 46:1-2.

⁷⁶ Decoupling Policy Statement at ¶ 27.

⁷⁷ Liu, TR 69:22-25 – 70:1-8.

⁷⁸ Liu, Exh. JL-1T at 8:9-13; *see also* Walker, TR 100:15-19.

⁷⁹ *Wash. Utils. & Transp. Comm’n v. Puget Sound Energy, Inc.*, Docket UE-111048, Order 08, ¶ 434 (May 7, 2012).

that case in light of the company's opposition.⁸⁰ The Commission subsequently approved a decoupling mechanism for PSE in 2013, and approved the continuation of decoupling for PSE in 2017.⁸¹ In the 2017 order approving the continuation of decoupling, the Commission approved a settlement allowing the company to use revenue-per-class decoupling for fixed production costs, and revenue-per-customer decoupling for other costs.⁸² Public Counsel argued against revenue-per-customer decoupling in that case, raising the possibility of "found margin" in an environment of customer growth,⁸³ but the Commission rejected that argument.⁸⁴

39 Both Staff and NW Natural contend that the case at hand is comparable to the Commission's 2017 PSE decision.⁸⁵ It is distinct, however, on both a factual and a legal basis. As a factual matter, Staff concedes that customer growth may be greater for NW Natural.⁸⁶ Thus, the impetus for proposing a per-customer revenue recovery mechanism is more likely to be cost recovery rather than conservation, or other recovery of lost usage. This is an important distinction because our legal basis for rejecting the Settling Parties' decoupling proposal is different as well. The question here is not the appropriate methodology for structuring decoupling for the purpose of addressing the possibility of found margin in a continuing program.⁸⁷ Rather, we are faced with the initiation of a program, proposed in a context of indisputably increasing sales, rather than one, per Commission policy, intended to address usage variation. Our rejection of the Decoupling Agreement is not based on whether there is found margin, but on whether the mechanism proposed is appropriately tailored to the Commission's oft-stated purpose of decoupling: addressing revenue volatility resulting from to usage variations, primarily due to a utility's energy conservation efforts.

⁸⁰ *Id.* at ¶ 453.

⁸¹ *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy, Inc.*, Dockets UE-170033 and UG-170034 (consolidated), Order 8, ¶ 261 (Dec. 5, 2017).

⁸² *Id.* at ¶ 294.

⁸³ *Id.* at ¶ 290.

⁸⁴ *Id.* at ¶ 294.

⁸⁵ *See* Staff Post-Hearing Brief at ¶ 25 and NW Natural Post-Hearing Brief at ¶ 22.

⁸⁶ Staff Post-Hearing Brief at ¶ 26.

⁸⁷ *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy, Inc.*, Dockets UE-170033 and UG-170034 (consolidated), Order 8, ¶¶ 290-91 (Dec. 5, 2017).

- 40 We agree with Public Counsel that decoupling “is not intended to fully compensate a company for customer growth.”⁸⁸ As NW Natural witness Kyle Walker explains, there are “multiple different types of mechanisms that could potentially be used [to recover costs associated with serving new customers] that maybe are used throughout the country.”⁸⁹ We are not satisfied that decoupling is a suitable mechanism to address this issue. While Staff is correct that, “when we try to use the decoupling mechanism to mitigate the negative impact of conservation of Company volumetric revenue, it is a revenue sufficiency question,”⁹⁰ the revenue sufficiency issue to be addressed is one caused by usage volatility, not new customer costs.
- 41 Our colleague states in his dissent that we do not recognize or consider the new flexible regulatory methodologies that the legislature granted the Commission during the 2019 legislative session, and argues that, contrary to this grant of flexibility, we are restricting our flexibility in this decision. We disagree with this characterization. Decoupling is a flexible tool, but it is not an all-encompassing remedy for all cost-recovery ills. Flexible regulatory authority does not mean the Commission should adopt decoupling for the cost recovery issue facing NW Natural due to new customer growth, with the result that there could be significant cost shifting to existing customers. Flexible regulatory authority does not mean we no longer consider the basic regulatory principles that rates must be fair, just, reasonable and sufficient. In this decision, we find that the settling parties have not met the burden of demonstrating that the rates resulting from approving the Decoupling Agreement would meet this standard, and find that approving the agreement would not be in the public interest.⁹¹
- 42 Finally, we find few disadvantages in rejecting the Decoupling Agreement. While Staff claims that decoupling would address rate case fatigue,⁹² the Decoupling Agreement does not contain a rate case moratorium, so relief from continuous rate cases is not guaranteed.

⁸⁸ Suetake, TR 40:11-13.

⁸⁹ Walker, TR 115:18-21.

⁹⁰ Liu, TR 105:13-16.

⁹¹ The Dissent claims that by rejecting the Decoupling Agreement, the Commission “fails to achieve fair, just, reasonable, and sufficient rates for customers or Northwest Natural.” To the contrary, as we state in our decision on the full Settlement, to which our colleague concurs, we find that the rates for the Company and its customers are, in fact, fair, just, reasonable and sufficient. Rejecting the Decoupling Agreement does not change this finding.

⁹² Liu, Exh. JL-5Tr at 21:19-20.

Nor is there any loss of incremental conservation, as NW Natural does not propose additional conservation efforts as part of the Decoupling Agreement. All conservation efforts offered by NW Natural in this proceeding are required by statute.⁹³ Moreover, the all-party Settlement discussed below, alone, produces rates for the Company that are fair just, reasonable, and sufficient, so the Company will not suffer from unjust rates due to rejection of the Decoupling Agreement.⁹⁴

43 Because we do not implement a decoupling mechanism for the Company, we decline to address, as moot, Public Counsel’s alternative rate-class decoupling proposal.

II. SETTLEMENT

44 As noted above, Commission approval of a settlement agreement is predicated upon the settlement’s lawfulness, adequate evidentiary support, and consistency with the public interest.⁹⁵ Finding that the Settlement, as whole, meets these requirements, we approve the Settlement in its entirety.

45 We discuss each component of the Settlement below.

A. Revenue Requirement and Effective Date

46 The parties agree that NW Natural may implement base rate changes designed to increase its annual revenues from its Washington natural gas customers by \$5,138,531, effective

⁹³ See Settlement at ¶ 20; *Petition of Puget Sound Energy and NW Energy Coalition for an Order Authorizing PSE to Implement Elec. And Natural Gas Decoupling Mechanisms and to Record Accounting Entries Associated with the Mechanisms*, Dockets UE-121697 and UG-121705 (consolidated) and *Wash. Utils. & Transp. Comm’n v. Puget Sound Energy*, Dockets UE-130137 and UG-130138 (consolidated), Order 07 at ¶ 130 (June 25, 2013) (explaining that utilities “face a financial ‘disincentive’ to conservation, which they nevertheless are required by statute to implement to the extent it is cost-effective to do so”).

⁹⁴ See Liu, TR 114:23-25 — 115:1-2 (“if we don’t have decoupling[,] the Company [can] keep the revenue from ... those new customers. And ... those revenue[s] compensate for their cost”); Kravitz *et al.*, Exh. JT-1T at 65:17-19 (“The Parties recommend that the Commission find that the Agreement is in the public interest and would produce rates for the Company that are fair, just, reasonable, and sufficient”) and at 30:3-8 (“Commission must not only assure fair rates to a company’s customers, but also provide a company with rates that will be sufficient to cover its prudently incurred costs and an opportunity to recover a reasonable return on its investment. The Agreement in this case represents the Parties’ best efforts to arrive at an end result that satisfies these requirements”).

⁹⁵ See Contested Issue—Decoupling, *supra*, at ¶¶ 33-34.

with service on and after November 1, 2019.⁹⁶ This is an approximately 7.8 percent overall revenue increase,⁹⁷ or a 12.7 percent increase to margin revenues.⁹⁸ This agreed revenue increase translates to a bill increase, including gas costs, of \$1.81, or 3.7 percent, for an average residential customer on Rate Schedule 2 using 57 therms a month.⁹⁹

47 Although the parties to the Settlement explain that they “took different positions on how to justify the revenue requirement increase,” they agree on certain adjustments, described in section C, below, that they contend justify the agreed-upon revenue requirement.¹⁰⁰ These adjustments are individual reductions to the Company’s initial proposal.

48 In Order 01 issued in this docket, the Commission suspended NW Natural’s proposed tariff revisions, which were to become effective February 1, 2019, for 10 months, *i.e.*, until December 1, 2019, as allowed under RCW 80.04.130(1). The parties describe the Settlement’s proposed earlier effective date for the Company’s new rates as “an integral part of the Agreement and ... one of the tradeoffs among the many concessions made on a variety of issues by the Parties.”¹⁰¹

49 **DECISION.** The revenue increase proposed in the Settlement is reasonable in light of the parties’ agreement on adjustments. Although the parties do not explain how the agreed-upon adjustments result in the proposed revenue increase, the parties’ descriptions of specific adjustments, as well as capital structure and cost of capital underlying the revenue increase proposal, addressed respectively in sections C and B below, provide sufficient reassurance that the proposed revenue requirement is reasonable and adequately supported.

50 We also accept the Settlement’s one-month acceleration of the effective date for new rates. Because all parties agree to the acceleration, no party is prejudiced by the compression of our usual timeline for general rate cases. Staff notes that implementing

⁹⁶ In its initial December 31, 2018, filing, the Company requested a revenue increase of \$8.3 million.

⁹⁷ Kravitz *et al.*, Exh. JT-1T at 10:12-14. In comparison, the Company requested a 12.6 percent increase in its initial filing.

⁹⁸ *Id.* at 6:11-13. In comparison, the Company requested a 20.5 percent increase to margin revenues in its initial filing. *Id.*

⁹⁹ *Id.* at 10:16-18.

¹⁰⁰ *Id.* at 11:18-21.

¹⁰¹ *Id.* at 8:16-18.

rates on November 1 would prevent the Company's customers from experiencing back-to-back rate changes, given that customers will also experience a rate change on that date due to the Company's annual PGA. We also appreciate that the proposed compression of the initial timeline in the context of this case is minimal enough to give the Commission sufficient opportunity to thoroughly consider and decide all matters at issue in this docket.

B. Capital Structure and Cost of Capital

51 The Parties agree to a capital structure of 49 percent equity, 50 percent long-term debt, and 1 percent short-term debt. The Settlement's proposed return on equity is 9.40 percent, the cost of long-term debt is 5.066 percent, and the cost of short-term debt is 2.186 percent. The overall Settlement ROR is thus 7.161 percent.¹⁰²

52 In its initial filing, NW Natural proposed an ROR of 7.63 percent, with an ROE of 10.3 percent and a capital structure comprising 49.5 percent equity, 49.5 percent long-term debt, and 1 percent short-term debt.¹⁰³ In NW Natural's last general rate case, which the Commission decided over 10 years ago, the Commission allowed a capital structure of 50.74 percent equity and an ROR of 8.40 percent, with an ROE of 10.10 percent.¹⁰⁴

53 **DECISION.** The capital structure and ROE proposed in the Settlement is reasonable. The equity capital structure agreed to in the Settlement is similar to that which the Company proposed, and the cost of capital is within a range the Commission has adopted recently for other regulated natural gas utilities.¹⁰⁵ The Settlement's adjustments to the

¹⁰² Settlement at ¶ 5.

¹⁰³ Initial filing cover letter at 2-3.

¹⁰⁴ *Wash. Utils. & Transp. Comm'n v. Nw. Natural Gas Co.*, Docket UG-080546, Order 04, ¶ 59 (Dec. 26, 2008).

¹⁰⁵ In July 2018, the Commission approved an all-party settlement establishing a capital structure of 49 percent equity, an ROE of 9.4 percent, and an ROR of 7.31 percent for Cascade Natural Gas Corporation. *Wash. Utils. & Transp. Comm'n v. Cascade Natural Gas Corp.*, Docket UG-170929, Order 06, ¶ 58 (July 20, 2018). In April 2018, the Commission authorized a capital structure of 48.5 percent equity, 48.6 percent long-term debt, and 2.9 percent short-term debt, with an ROE of 9.5 percent and 7.5 percent ROR for Avista Corporation. *Wash. Utils. & Transp. Comm'n v. Avista Corp.*, Dockets UE-170485 and UG-170486, Order 07, ¶¶ 111-12 (April 26, 2018). Similarly, for Puget Sound Energy, the Commission approved a multiparty settlement with a 48.5 percent equity capital structure and 9.5 percent ROE, with a 7.6 percent ROR, in December 2017. *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy*, Dockets UE-170033 and UG-170034, Order 08, ¶¶ 83, 94 (Dec. 5, 2017).

Company’s proposed cost of capital reduced the Company’s initially-filed revenue requirement by \$1,166,217. In light of the parties’ agreement and because there is no evidence to indicate otherwise, we conclude that the Settlement’s proposed cost of capital and capital structure is consistent with the public interest.

C. Miscellaneous Adjustments

54 The parties explain that the agreed-upon revenue requirement reflects downward adjustments to the Company’s initially filed revenue requirement in the following eight categories:

Category	Description	Amount
Revenue and Gas Costs	Demand Side Management savings removed from usage-per-customer calculations.	\$113,035
Bonuses	Bonus adjustment recalculated using a five-year average and excluding the long-term portion of the Company’s executive compensation program.	\$271,144
Payroll	Reduction to payroll O&M expense, including payroll overhead.	\$87,414
Miscellaneous O&M	O&M expense reduced by \$250,000.	\$260,844
ISWC	Reduced to \$972,715 through re-categorization of certain accounts.	\$1,027,567
Allocation Factors	Washington allocation factors corrected. ¹⁰⁶	\$123,042
Post-Test Year Plant Additions	The following plant additions identified in the Direct Testimony of	\$107,326

¹⁰⁶ On April 15, 2019, the Company filed updated workpapers for witness Kevin McVay reflecting corrected Washington allocation factors, which were provided to the parties in the Company’s supplemental response to Staff Data Request No. 43. The parties state that all further adjustments in the case have been calculated from this update. Kravitz *et al.*, JT-1T at 13:10-11.

	Joe S. Karney, Exh. JSK-1T, were excluded from rate base: Network Control Systems (“NCS”) Tech Refresh, NCS Tech Refresh Microwave, Lacamas Regional Gate Station, Mist Standby Generator and Mist Fiber Network.	
Non-Plant Excess Deferred Income Taxes (EDIT)	Non-Plant EDIT removed from Deferred Taxes included in rate base.	\$16,924

55 **DECISION.** The downward adjustments to the Company’s initially filed revenue requirement described above appear to be appropriate, both individually and as a whole. These adjustments account for approximately two-thirds of the Settlement’s overall decrease from the Company’s initial filing. The treatment of non-plant EDIT and ISWC accounting methodology are further discussed in sections F and H below, respectively.

D. Rate Spread and Rate Design

56 Under the Settlement, the total revenue requirement increase of \$5,138,531 will apply on an equal percent of margin basis across all rate schedules; the Company will perform a second adjustment within Rate Schedules 41 and 42, such that sales and transportation margin rates in those two Rate Schedules receive the same percentage increase.¹⁰⁷ The Company will continue to apply its revenue requirement on an equal percent of margin basis across all rate schedules in its annual filings.¹⁰⁸

57 The parties agree to an increase in the customer charge for Residential Rate Schedule 1 from \$3.47 to \$5.50 and in the customer charge for Rate Schedule 2 from \$7.00 to \$8.00.¹⁰⁹ The parties to the Settlement also accept the increases to the customer charges proposed in the Company’s initial filing for the following schedules: Commercial Rate

¹⁰⁷ Settlement at ¶ 15.

¹⁰⁸ Kravitz, TR 118:2-11.

¹⁰⁹ *Id.*

Schedule 1 to \$7.00; Commercial Rate Schedule 3 to \$22.00; Industrial Rate Schedule 3 to \$22.00; and Residential Heating Dry Out Rate Schedule 27 to \$9.00.¹¹⁰

58 **DECISION.** The rate spread and customer charges proposed under the Settlement are approved and adopted for purposes of this Order, consistent with our July 20, 2018, decision in Docket UG-170929.¹¹¹ In that Order, the Commission held that applying revenue changes on an equal percentage margin increase or decrease to each schedule is a reasonable compromise that maintains the status quo during the pendency of the Commission’s cost of service rulemaking. We similarly conclude here that reserving this issue “until the conclusion of the rulemaking docket is reasonable because the rulemaking and associated policy statement will provide significant guidance for all regulated utilities that will impact how cost of service studies are performed.”¹¹²

E. Environmental Remediation

59 NW Natural’s predecessor companies operated five sites located in and around Portland, Oregon, and federal and state agencies have directed the Company to undertake environmental remediation associated with those sites.¹¹³ The Company began to incur costs associated with this environmental remediation activity in 2003 and will continue to do so over the next decade.¹¹⁴

60 The Settlement requires the Company to establish an Environmental Cost Recovery Mechanism (ECRM) and allows it to recover certain environmental remediation costs allocable to Washington customers, including those costs in rates each year on November 1, following a review process.¹¹⁵

¹¹⁰ Kravitz *et al.*, JT-1T at 14:7-11.

¹¹¹ See *Wash. Utils. & Transp. Comm’n v. Cascade Natural Gas Corp.*, Docket UG-170929, Order 06, ¶ 66 (July 20, 2018).

¹¹² *Id.* at ¶ 65. The Cost of Service Rulemaking in Dockets UE-170002 and UG-170003 is currently in the CR-101 phase. The Commission hosted technical workshops on December 3, 2018, February 21, 2019, and February 22, 2019, to discuss cost of service studies. The Commission has solicited comments from interested persons on the cost of service templates filed in the dockets on August 30, 2019. Those comments are due December 6, 2019.

¹¹³ See generally Wyatt, Exh. RJW-1CT.

¹¹⁴ Kravitz *et al.*, JT-1T at 41:6-11.

¹¹⁵ Settlement at ¶ 18.

- 61 The costs that may be recovered through the ECRM are limited to 3.32 percent of those environmental remediation costs that are allocable to both Washington and Oregon customers. The 3.32 percent Washington allocation factor also applies to insurance proceeds related to those sites, which will also be allocated to Washington customers. The Company will not recover environmental remediation expense incurred prior to the filing date of the accounting petition approved by Order 01 in Docket UG-110199¹¹⁶ or offset those costs with insurance proceeds;¹¹⁷ however, Order 01 allows NW Natural to defer subsequent Washington-allocable costs, as well as the insurance proceeds and other third-party payments received by the Company in connection with these costs. Order 01 prohibits the Company from accruing interest on the environmental remediation expense deferral.¹¹⁸
- 62 Under the Settlement, the Company will make an annual ECRM tariff adjustment filing on or before July 15 for rates effective each November 1. The filed ECRM rate will collect prudent expenditures deferred during the previous calendar year, less that year's allocation of insurance proceeds.¹¹⁹ The first ECRM rates will go into effect on November 1, 2020, for expenses deferred July 1, 2019, through December 31, 2019.
- 63 The parties to the Settlement agree that the Company will apply insurance proceeds to entirely offset deferred remediation expenses incurred between February 1, 2011, through November 30, 2018, subject to a review of the prudence of those expenditures in the Company's July 15, 2020, ECRM tariff filing. Similarly, expenses deferred during the period of December 1, 2018, through June 30, 2019, will be offset entirely with insurance proceeds, subject to a review of the prudence of those expenditures in the Company's July 15, 2020, ECRM tariff filing.

¹¹⁶ In Order 01, the Commission authorized deferred accounting for environmental remediation costs, other than costs incurred prior to the initial filing in the docket. *In the Matter of Nw. Natural Gas Corp., For an Accounting Order Authorizing Deferred Accounting Treatment of Certain Costs Associated with Env'tl. Remediation*, Docket UG-110199, Order 01, ¶ 12 (June 30, 2011). The petition in Docket UG-110199 was filed January 26, 2011, but the Company did not defer any expenses prior to February 1, 2011. Kravitz *et al.*, JT-1T at 15:14-16.

¹¹⁷ Kravitz *et al.*, JT-1T at 41:17-19.

¹¹⁸ *Id.* at ¶¶ 11-12.

¹¹⁹ The annual environmental remediation deferral amount in the ECRM Account would be collected from all customers on an equal percent of margin basis. Kravitz *et al.*, JT-1T at 18:14-17.

- 64 The Company will amortize the remaining balance of insurance proceeds over the 10.5-year period of July 1, 2019, through December 31, 2029; the amortization for the sub-period of July 1, 2019, through December 31, 2019, is a six-month, pro rata share of the remaining balance of insurance proceeds. Any additional insurance proceeds and third-party payments will be added to the remaining balance of insurance proceeds and amortized over the remaining years in the 10.5-year amortization period.
- 65 There is a soft cap on annual revenue increases under the ECRM: once the insurance proceeds have been fully used to offset deferred expenses, ECRM rates may not result in an increase to the Company's Washington normalized revenues by more than one percent per year. If amortization of the prior year's deferred amounts over a one-year period would cause an increase to the Company's Washington normalized revenues by more than one percent, then the deferred amounts exceeding the one percent cap will be amortized over the next three years, beginning with the next year's Purchased Gas Adjustment tracking period. In that case—if amortization of an annual deferral balance exceeds one year—the Company will assess interest on the balance at its cost of long-term debt, as set in the Company's most recently approved general rate case.¹²⁰ No interest accrues on the deferral balance if it is amortized over one year or less.
- 66 If NW Natural receives additional insurance proceeds or third-party payments after the 10.5-year amortization of the remaining insurance proceeds, the Company will propose a new amortization schedule in its first prudence review filing following receipt of the insurance proceeds or third-party payments. If recoveries from insurance providers or other third-party payments allocable to Washington more than fully offset shared site expenses such that a negative deferral balance accrues, the amount would be amortized over one year and the deferral balance in the ECRM Account would be returned to customers coincident with the PGA filing effective November 1 of the year immediately following the negative deferral balance year.¹²¹
- 67 While not described in the body of the Settlement, in the joint testimony supporting the Settlement, the parties state that the proposed ECRM will modify existing annual reporting requirements for NW Natural.¹²² The Company currently files an annual report

¹²⁰ Kravitz, TR 118:17-19.

¹²¹ Kravitz *et al.*, JT-1T at 20:8-17. The Commission may alternatively allow a credit balance to be carried to the next PGA filing. *Id.* The Settlement eschews discussion of negative deferral balances, which are addressed only in the all-party joint testimony in support of the Settlement.

¹²² *Id.* at 17:10-22, 18:1-2.

on March 1 regarding its deferred environmental expenses and balances. Under the ECRM proposal in the Settlement, the annual report would be filed on July 15 of each year and would include information to support a prudency review of the costs incurred for all Washington allocable shared site costs over the prior calendar year, beginning with the report filed on July 15, 2020. The annual report would describe Washington allocable expenditures for environmental remediation activities at the shared sites, as well as the receipt of any insurance or other third-party proceeds related to its Washington allocable remediation activities during the same time period.

68 **DECISION.** We approve the ECRM proposed in the Settlement, as discussed above. Thus, Order 01 and Order 02 in Docket UG-110199 are superseded where in conflict with the ECRM provisions of the Settlement adopted in this Order.

69 We note the discrepancy of accruing interest on deferral balances amortized for a period of longer than one year, but not accruing interest on insurance proceeds amortized over 10.5 years. Interest accrued on the latter could benefit customers. While, as NW Natural argues,¹²³ no interest accrues on expenses amortized within a year, which could benefit the Company, those expenses are recovered quickly on an annual basis. However, understanding that the Settlement is a cohesive sum of compromises, we approve the ECRM as proposed, including all interest terms.

F. Effects of Tax Cuts and Jobs Act of 2017

70 The Settlement incorporates the effects of the Tax Cuts and Jobs Act (TCJA), enacted on December 22, 2017, which lowered the federal corporate income tax rate from 35 percent to 21 percent, effective as of January 1, 2018.¹²⁴ The new 21 percent federal income tax rate is reflected in the revenue requirement increase agreed to by the parties to the Settlement.¹²⁵ The two other issues resulting from the TCJA are the appropriate regulatory treatment of the benefit associated with a lower tax rate during the interim period of January 1, 2018, through October 31, 2019, and the recalculation and regulatory treatment for the benefit from the net decrease in NW Natural's accumulated excess

¹²³ Kravitz, TR 120:14-18.

¹²⁴ An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018, Pub. L. No. 115-97, 131 Stat. 2054 (2017).

¹²⁵ Kravitz *et al.*, JT-1T at 21:12-15.

ORDER 06

deferred income taxes, or EDIT, recorded upon enactment of the TCJA, which the Company is currently deferring.

- 71 Regarding the interim period benefit, the Settlement provides for an interim period benefit of \$2.1 million, to be reflected as a reduction in customer rates through a tariff rider and amortized over a one-year period beginning on November 1, 2019.¹²⁶ NW Natural will develop separate tariff riders to credit the interim period deferral and Plant EDIT, discussed below. The parties to the Settlement explain that the \$2.1 million interim period benefit is a “black box” consensus and does not reflect agreement among the parties as to the correct methodology for calculating the interim period over-collection.¹²⁷
- 72 The Settlement also addresses Plant EDIT and non-Plant EDIT balances recorded as of the enactment of the TCJA. Under the Settlement, non-Plant EDIT is set to zero, *i.e.*, with no collection from or benefit to customers.¹²⁸ Plant EDIT allocated to Washington customers is \$14.592 million, before gross-up for taxes; it will be amortized in accordance with federal normalization rules and credited to customers as a reduction to customer rates through a tariff rider effective for a five-year period. The initial annual amortization will be \$400,000 before any applicable income tax and revenue sensitive tax gross ups are applied, or \$528,000 after reflecting the gross-up factor.¹²⁹
- 73 **DECISION.** We approve and adopt for purposes of this Order the Settlement’s proposed incorporation of the effects of the TCJA in NW Natural’s proposed rates. The Settlement appropriately applies the new federal income tax rate to effective rates, and timely returns the agreed-upon interim period benefit. We accept the parties’ removal of non-Plant EDIT as a reasonable compromise of the parties’ settlement positions and the Settlement’s Plant EDIT treatment as consistent with federal law.

G. Energy Conservation

¹²⁶ *Id.* at 21:16-19; Settlement at ¶ 19.

¹²⁷ Settlement at ¶ 19.

¹²⁸ *Id.* Setting the non-Plant EDIT to zero will translate as a loss to the Company’s regulated books of accounting. Kravitz, TR 123:4-9.

¹²⁹ The Settlement revenue requirement includes a 1.5-year amortization of \$600,000 related to Plant EDIT. NW Natural will make a subsequent filing before the end of five years to revise the separate tariff rider to reflect the Plant EDIT amortization for the next subsequent five-year period. NW Natural will be revisiting Plant EDIT amortization every five years.

- 74 Regarding the Company's energy conservation program, the Settlement requires the Company to make the following filings: (1) a conservation tariff adjustment, each year, effective November 1, by September 15; (2) an annual conservation plan by December 1 of each year, describing anticipated demand-side management (DSM) activities for the upcoming calendar year and how the plan will help the Company achieve its annual conservation target; (3) an annual conservation report, by June 1 of each year, describing the DSM program's targets and gas savings achieved, and comparing actual expenses and forecasted expenses for the previous calendar year.¹³⁰ NW Natural will hold Energy Efficiency Advisory Group (EEAG) meetings quarterly, replacing the quarterly and semi-annual reports currently required under the Company's tariff; the Company must provide drafts of annual reports, annual plans, and all tariff adjustments to the EEAG for review at least 20 calendar days prior to filing.¹³¹
- 75 Regarding the content of the energy efficiency plans, the Settlement requires the Company to identify and acquire all available cost-effective conservation, identified in the Company's energy efficiency plans, and to use a total resource cost test, where available, to determine the cost effectiveness of the conservation program. NW Natural must conduct an independent conservation potential assessment (CPA), projecting the 20-year conservation potential, every two years, which must be prepared by a consulting firm and inform the Company's integrated resource plan (IRP) and be filed along with the Company's IRP. NW Natural must also propose an annual conservation target and demonstrate that it represents acquisition of all available cost-effective conservation resources.¹³²
- 76 The Settlement adjusts the Company's conservation cost recovery mechanism to allow for contemporaneous recovery of expenses, with rates effective November 1 through October 31 of each year collecting forecasted expenses for that period plus the prior period deferral balance.¹³³ The prior period deferral balance, in turn, consists of the difference between the forecasted amounts and actual expensed amounts for that period.

¹³⁰ Settlement at ¶ 20. The parties to the Settlement agree to exclude the Company's industrial customers from the terms and conditions of this energy conservation section of the Settlement. Nor will this provision of the Settlement affect the operations of NW Natural's low-income weatherization program. *See Kravitz et al.*, JT-1T at 63:21-23.

¹³¹ *Id.*

¹³² *Id.*

¹³³ No interest will accrue on these deferral balances. *Kravitz et al.*, JT-1T at 44:8-11.

77 A cumulative deferral balance of approximately \$5.25 million, as of October 31, 2019, will be amortized over a four-year period, November 1, 2019, through October 31, 2023. Interest will accrue on this balance over the amortization period at the current interest rate published by the Federal Energy Regulatory Commission. This \$5.25 million balance comprises a \$2.84 million balance deferred from January 1, 2018, through February 28, 2019, and a \$2.41 million balance projected for March 1, 2019, through October 31, 2019.

78 **DECISION.** We approve the changes to the Company's energy conservation tariffs proposed in the Settlement. The proposed changes to the conservation program bring it into alignment with other regulated companies' conservation reporting timing and requirements. Amortizing the \$5.25 million deferral balance over a four-year period addresses rate volatility that could otherwise result from amortizing the balance over a shorter period. Nevertheless, instating a shorter deferral period for cost recovery of conservation expenses is also appropriate because it minimizes the need for unnecessary interest expense and recovers costs from customers likely to have caused them.

H. ISWC Accounting Methodology

79 The Settlement provides for an investor-supplied working capital (ISWC) accounting methodology for the Company to use in its Commission Basis Reports (CBR), requiring the Company to place average of monthly average account balances into one of four categories and categorizing the amounts by state or as non-operating. The ISWC methodology requires, *inter alia*, the Company to assign balance sheet accounts, on an average of monthly average basis, into one of four categories (Current Assets, Current Liabilities, Average Invested Capital, and Total Investment), then categorize Total Investment into sub-categories between states (Washington and Oregon) and non-operating.

80 **DECISION.** We approve and adopt this requirement of the Settlement for purposes of this Order.

I. Special Contract Feasibility Study

81 The Settlement requires the Company to conduct an updated economic feasibility study for its special contracts within three years after November 1, 2019. Staff explains in the joint testimony supporting the Settlement that the Company has been unable to locate the original study, and that the relevant contract has been effective on a month-to-month basis for the past 20 years. Staff thus affirms that an updated study is needed to verify

that the special contract rates continue to be fair, just, and reasonable, and states that a three-year period for completing the study is appropriate.¹³⁴

82 **DECISION.** We approve the economic feasibility study update requirement, including allowing a three-year period for completion, accepting it as a reasonable compromise of the parties' positions for the purposes of settlement.

J. Interruptible Customers' Gas Usage

83 The Settlement requires the Company to track the unauthorized gas use of interruptible customers during curtailments.

84 **DECISION.** In the joint testimony in support of the Settlement, Staff explains that the Company currently tracks usage during curtailments, but that the Settlement memorializes the practice to ensure its continuity and consistency.¹³⁵ We approve of this development because it is necessary to enforce the Company's interruptible service tariffs.

K. Low-Income Bill Assistance Program

85 The Settlement provides for several changes to the Company's Gas Residential Energy Assistance Tariff (GREAT) Program, including the establishment of an Advisory Group for the program by September 1, 2019.¹³⁶ The Advisory Group, comprising key stakeholders, will meet for the first time by November 1, 2019, and will hold subsequent meetings at least quarterly until December 31, 2020, and at least twice a year after January 1, 2021. The Settlement sets out goals for the Advisory Group, including keeping customers connected to natural gas service; providing assistance to more customers than are currently served; to lower the energy burden of GREAT Program participants; and to collect data necessary to assess GREAT Program effectiveness and to inform ongoing policy discussions. The Advisory group will present an action plan to improve the GREAT Program by July 1, 2020.

86 NW Natural will work in consultation with the Advisory Group to produce a low-income evaluation study to assess the need for low-income assistance among the Company's

¹³⁴ *Id.* at 50:6-12.

¹³⁵ *See id.* at 50:13-22.

¹³⁶ Settlement at ¶ 24.

Washington customers, including low-income weatherization, and to identify ways to improve the GREAT Program to better align with the goals of the Advisory Group. The Company agrees to not seek recovery of the costs of the low-income evaluation study from customers.¹³⁷

87 **DECISION.** The Advisory Group and the Company’s low-income evaluation study are both welcome advances. Staff explains that funding for the GREAT Program has been underutilized in recent years, and that the number of households receiving GREAT benefits has been flat.¹³⁸ The Company thus will collaborate with the Advisory Group to “more effectively deliver benefits to qualifying customers.”¹³⁹ We thus find that the Settlement’s proposed changes to NW Natural’s GREAT Program are in the public interest and approve them.

88 We have reviewed the Settlement and supporting evidence and conclude that the resulting rates, terms, and conditions are fair, just, reasonable, and sufficient. The Settlement terms are lawful, supported by an appropriate record, and consistent with the public interest in light of all the information available to the Commission. We therefore approve the Settlement without conditions.

FINDINGS OF FACT

89 Having discussed above in detail the evidence received in this proceeding concerning all material matters, and having stated findings and conclusions upon issues in dispute among the parties and the reasons therefore, the Commission now makes and enters the following summary of those facts, incorporating by reference pertinent portions of the preceding detailed findings:

- 90 (1) The Commission is an agency of the State of Washington vested by statute with authority to regulate rates, rules, regulations, practices, and accounts of public service companies, including natural gas companies.
- 91 (2) NW Natural is a “public service company” and a “natural gas company” as these terms are defined in RCW 80.04.010 and these terms are otherwise used in Title

¹³⁷ *Id.*

¹³⁸ Kravitz *et al.*, JT-1T at 45:6-8.

¹³⁹ *Id.* at 45:8-10.

80 RCW. NW Natural is engaged in Washington State in the business of supplying utility services and commodities to the public for compensation.

- 92 (3) On December 31, 2018, NW Natural filed with the Commission revisions to its currently effective Tariff WN U-6 for natural gas service provided in Washington. NW Natural requested authority to increase annual revenues by \$8.3 million, *i.e.*, a 12.6 percent increase to overall base rates.
- 93 (4) NW Natural, Staff, Public Counsel, AWEC, and TEP entered into a Settlement to resolve all but one issue in this proceeding, which they filed with the Commission on May 23, 2019.
- 94 (5) The Settling Parties, comprising all parties but Public Counsel, entered into a Decoupling Agreement that proposed a decoupling mechanism for NW Natural, which they filed with the Commission on May 23, 2019.
- 95 (6) The parties to the proceeding reserved for hearing the issue of whether the Commission should implement a decoupling mechanism for NW Natural, and if so, whether the decoupling mechanism should use a per-rate class or per-customer methodology for calculating annual revenue recovered.
- 96 (7) NW Natural's Washington customer base is projected to increase by more than 22 percent in the next five years.
- 97 (8) The decoupling mechanism proposed in the Decoupling Agreement would primarily serve to recover incremental costs of serving new customers.

CONCLUSIONS OF LAW

98 Having discussed above all matters material to this decision, and having stated detailed findings, conclusions, and the reasons therefore, the Commission now makes the following summary conclusions of law, incorporating by reference the pertinent portions of the preceding detailed conclusions:

- 99 (1) The Commission has jurisdiction over NW Natural, the other parties, and the subject matter of this proceeding.
- 100 (2) The Commission has an independent obligation to determine whether the Settlement is lawful, supported by the evidence, and consistent with the public interest.

- 101 (3) The rates, terms, and conditions in the Settlement are fair, just, reasonable, and sufficient.
- 102 (4) The Commission should approve the Settlement without condition.
- 103 (5) The Commission adopted decoupling under RCW 80.28.260(3) as a policy in appropriate cases to protect utilities from a reduction of short-term earnings that may be the direct result of utility programs to increase the efficiency of energy use.
- 104 (6) Decoupling is not a mechanism intended for recovery of incremental costs of serving new customers.
- 105 (7) The parties to the Decoupling Agreement have not shown that the proposed decoupling mechanism is tailored to address revenue volatility due to variations in energy usage, rather than primarily to recover costs associated with serving new customers.
- 106 (8) The parties to the Decoupling Agreement have not shown that the Decoupling Agreement is in the public interest in light of all of the information available to the Commission.
- 107 (9) The Commission should reject the Decoupling Agreement.
- 108 (10) Because the Commission does not implement a decoupling mechanism for NW Natural in this Order, Public Counsel's alternative rate-class decoupling methodology is moot.

ORDER

THE COMMISSION ORDERS:

- 109 (1) The Commission approves the Joint Settlement Agreement, which is attached as Exhibit A to, and incorporated into, this Order, and adopts the Joint Settlement Agreement as its final resolution of the issues in this docket that it addresses.
- 110 (2) The Commission rejects the revisions to Northwest Natural Gas, d/b/a NW Natural's Tariff WN U-6 filed on December 31, 2018. Northwest Natural Gas, d/b/a NW Natural, must file tariff sheets in compliance with this Order no later than five business days prior to the tariff sheets' stated effective date.

- 111 (3) The Commission rejects the Partial Multiparty Settlement Agreement on Decoupling.
- 112 (4) The Commission requires that Northwest Natural Gas, d/b/a NW Natural, make a filing, no later than September 30, 2024, to reflect plant excess deferred income tax amortization for the subsequent five-year period.
- 113 (5) The Commission retains jurisdiction to enforce the terms of this Order and delegates to the Executive Director and Secretary the authority to confirm compliance with this Order.

Dated at Olympia, Washington, and effective October 21, 2019.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DAVID W. DANNER, Chairman

ANN E. RENDAHL, Commissioner

NOTICE TO PARTIES: This is a Commission Final Order. In addition to judicial review, administrative relief may be available through a petition for reconsideration, filed within 10 days of the service of this order pursuant to RCW 34.05.470 and WAC 480-07-850, or a petition for rehearing pursuant to RCW 80.04.200 and WAC 480-07-870.

Concurring and Dissenting Opinion of Commissioner Balasbas

- 1 I agree that approval of the Joint Settlement Agreement is in the public interest and fully support Part II (Paragraphs 43 through 87) of Order 06. However, I respectfully disagree with my colleagues' decision to reject the Partial, Multi-Party Settlement Agreement on Decoupling (Decoupling Agreement). The evidence in the record clearly supports a finding that the Decoupling Agreement is in the public interest, and I support its approval. Conversely, rejecting the Decoupling Agreement fails to achieve fair, just, reasonable, and sufficient rates for customers or Northwest Natural. Today's decision also sends the wrong signal about how the Commission plans to use new statutorily authorized flexible ratemaking tools obtained from the 2019 legislature.
- 2 The Commission regulates in the public interest by ensuring rates are fair, just, reasonable, and sufficient.¹⁴⁰ While arguably not a perfect ratemaking mechanism, decoupling as applied in this instance effects just results. Northwest Natural, through its oral testimony at the evidentiary hearing and in its post-hearing brief, clearly demonstrated that increased conservation and efficiency spending over the past 10 years has led to lower sales revenues (*i.e.* lost margin).¹⁴¹ The Company also showed how the cost to serve new customers is higher than any additional revenue collected.¹⁴²
- 3 My colleagues' decision fails to fully consider the Company's unique circumstances of higher than average growth and longer than average time between general rate cases. The 2010 Policy Statement on decoupling clearly allows for the mechanism to help a Company recover lost revenues between general rate cases due to lower sales from any source.¹⁴³ This makes decoupling an effective revenue sufficiency tool regardless of the reason with the practical effect in this case serving to help the Company recover costs that would otherwise remain unrecovered. My colleagues argue that decoupling is not the right mechanism to recover costs to serve new customers. On the contrary, the Decoupling Agreement produces a fair outcome that is consistent with the guidance

¹⁴⁰ Order 06, ¶ 34.

¹⁴¹ Northwest Natural Post Hearing Brief on Decoupling, ¶ 30.

¹⁴² *Id.* ¶ 43.

¹⁴³ Docket U-100522 Report and Policy Statement on Regulatory Mechanisms, Including Decoupling, To Encourage Utilities to Meet or Exceed Their Conservation Targets, ¶ 27. Emphasis added.

provided in the Policy Statement. Staff, AWEC and TEP all agreed with this fair outcome through their support of the Decoupling Agreement. Just because a Policy Statement does not address an issue does not make it a basis to reject a well-structured proposal that serves the public interest.

4 Further, the proposed decoupling mechanism looks nearly identical to other gas utility decoupling programs the Commission has already approved and includes more than adequate ratepayer protections.¹⁴⁴ Rejection of the Decoupling Agreement can only be construed as a statement that the Company does not deserve the same treatment as other gas utilities the Commission regulates.

5 I also find troubling that, in our first rate case decision since the legislature authorized more flexible ratemaking authority for the Commission,¹⁴⁵ my colleagues have chosen to restrict our flexibility.

6 The Commission spent significant time and effort to convince the legislature we needed more flexible ratemaking authority in statute after it was limited by a 2018 Division II Court of Appeals decision. Rejecting the Decoupling Agreement for what effectively amounts to semantic reasons and disallowing a flexible approach to the Company fairly recovering costs for new natural gas customers completely undermines arguments made during the 2019 legislative session. Indeed, the Commission should embrace its new flexibility as we move forward with implementing the complex and ambitious package of energy legislation enacted earlier this year. Rejecting simple and sensible settlements such as the Decoupling Agreement is antithetical to this goal.

JAY M. BALASBAS, Commissioner

¹⁴⁴ Partial, Multi-Party Settlement Agreement on Decoupling, ¶ 4.

¹⁴⁵ Engrossed Second Substitute Senate Bill 5116, Section 20 (RCW 80.04.250).

Exhibit A