

ITEM NO. 1

PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: August 8, 2006

REGULAR X CONSENT _____ EFFECTIVE DATE _____ N/A _____

DATE: July 26, 2006

TO: Public Utility Commission

FROM: Judy Johnson

THROUGH: Lee Sparling and Ed Busch

SUBJECT: OREGON PUBLIC UTILITY COMMISSION STAFF: Request to open an investigation into the earnings of Cascade Natural Gas.

STAFF RECOMMENDATION:

Staff requests the Commission to: (1) summarize investigate the rates of Cascade Natural Gas (Cascade or CNG) under ORS 756.515; (2) conclude the information contained in staff's public meeting memo provides sufficient grounds to warrant a hearing be held on the reasonableness of the rates; and (3) order that a statement be issued to Cascade notifying it of the hearing and that a notice setting a pre-hearing conference be issued as well.

DISCUSSION:

On April 19, 2006, in Order No. 06-191, the Commission approved a Stipulation between Cascade, Commission staff, Citizens' Utility Board, NW Energy Coalition, Natural Resources Defense Council, Community Action Directors of Oregon, Oregon Energy Coordinators Association, and Northwest Industrial Gas Users. This Stipulation included a decoupling mechanism consisting of two deferral accounts, one to track changes in margin due to variations in weather-normalized usage and another to track changes in margin due to weather that varies from normal. As part of the Stipulation, CNG agreed that if requested by the Commission no later than December 31, 2007, Cascade would agree to submit a general rate filing to Oregon no later than April 1, 2008. The Stipulation did not contain any provision whereby staff was precluded from reviewing and challenging the reasonableness of CNG's rates during the term of the agreement.

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After reviewing Cascade's Rate of Return (ROR) and Return on Equity (ROE) for previous years, staff concludes that Cascade should be brought in for a general rate case. Staff finds that Cascade has had excessive earnings for the past several years and that with the company's latest regulatory-adjusted ROR and ROE, these over earnings will continue on a forward-looking basis absent a rate reduction. Below are listed the RORs and ROEs for the last 10 years based on Cascade's Results of Operations, which are filed annually by the company. These figures reflect typical regulatory adjustments to actual operating income and rate base (such as normalizing for weather). The 2005 results also include several additional adjustments, identified by staff's recent audit of CNG's books, which are necessary to provide an accurate assessment of Cascade's current earnings situation.

Year	ROR	ROE
2005	10.46%	13.64%
2004	10.11%	12.12%
2003	9.98%	11.88%
2002	10.19%	12.27%
2001	7.10%	5.56%
2000	13.20%	17.77%
1999	12.17%	15.96%
1998	9.92%	12.04%
1997	9.88%	11.40%
1996	11.15%	14.24%

Staff believes that the historically high RORs and ROEs, coupled with Cascade's 2005 results of operations, are sufficient to warrant the Commission holding a hearing regarding the reasonableness of Cascade's rates. Based on our preliminary review, staff further believes that customers' rates could be lowered by as much as \$2.309 million, which is 3.3% overall. This assumes an authorized return on equity of 9.25%. To illustrate the sensitivity of staff's recommended rate decrease to the recommended return on equity, staff also ran the revenue requirement model assuming a 9.75% return on equity. This resulted in a decrease in revenue requirement of \$2.048 million, which is 2.9% overall. The results of the sensitivity analysis demonstrates that when assuming a 50 basis point premium to staff's recommended cost of equity, the recommended rate reduction is reduced 0.4%.

PROPOSED COMMISSION MOTION:

The Commission: (1) summarily investigate the rates of Cascade under ORS 756.515; (2) conclude that the information contained in staff's public meeting memo provides sufficient grounds to warrant a hearing be held on the reasonableness of the rates; and

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(3) order that a statement be issued to Cascade notifying it of the hearing and that a notice setting a pre-hearing conference be issued as well.