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UG-__ – Rate Redesign

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I. Introduction & Summary

Q. Please state your name.

A. My name is Francis P. Ferguson. My position, responsibilities, qualifications, and background are summarized in my Rate Spread testimony, *Exhibit No. ____ (FPF-1)*.

Q. What is the purpose of your testimony?

A. The purpose of this testimony is to describe NW Natural’s (NW Natural or company) proposed rate redesign, to explain why the company is proposing a rate redesign, and to elaborate the steps taken to develop the rate design. Finally, the testimony will describe the proposed rate structure and its impacts.

II. Proposed Rate Redesign

Q. Can you describe the company’s proposed rate design?

A. Yes. NW Natural will create three new rates that will replace all of the company’s current industrial and large commercial schedules. These proposed rates are outlined at *Exhibit No. ____ (FPF-2)*.

Q. Why is NW Natural proposing a rate redesign?

A. The company wants to reduce the number of industrial and large commercial rates schedules from nine to four basic distribution schedules. By reducing the number, it is hoped, the schedules will be easier for customers to use and understand. Further, while the customers do have the final say, it should also promote the use of the most economically rational rate schedule for the customer, making it less likely that a customer will be on a more expensive rate schedule than their load characteristics suggest. Another goal is to send more rational price signals that

1 encourage efficient use of the company's distribution system. NW Natural's new
2 rate schedules achieve this goal by having capacity charges based on peak usage.

3 **Q. What are the revenue effects of the company's proposed rate re-design?**

4 A. Revenue neutrality is an important objective of this rate re-design process. The
5 company does not intend to charge this group of customers more, in total, than it
6 would under the existing rates with the proposed general rate case revenue
7 requirement included; nor does the company intend to collect less than proposed
8 rate case revenue. In contemplating these objectives, the company decided to
9 structure new rates in such a manner as to mimic, as closely as possible, existing,
10 post rate case rate effects, consistent with the objectives of simplifying rates and
11 providing improved price signals. By trying to mimic post rate case charges at
12 each consumption level, revenue neutrality and smaller customer impacts can be
13 more easily achieved.

14 **Q. In what way is the rate design revenue-neutral?**

15 A. The goal of the design process was to minimize the change in margin revenue
16 produced by this group of customers. *Exhibit No. ____ (FPF-3)* shows the margin
17 effects of the design both overall and by rate schedule. Even though most of the
18 rate schedules shown on the table are being eliminated by the rate design, it is still
19 useful to examine the change in margin payments that will be made by various
20 customers on existing rate schedules as the move to the new schedules. The net
21 change in margin payments, after adjustment, is \$620, a change small enough to
22 be regarded as revenue neutral.

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1 **Q. Are the new rates cost based?**

2 A. As there are no customers currently on the new rates, it is difficult to assess what
3 their annual, average and peak day use might be on these new, untested schedules.
4 The lack of customers also makes it difficult to allocate the other elements of a
5 cost of service study to these schedules. Rather than attempting to create a new
6 fully allocated cost study based on phantom customers, the company has decided
7 to construct the new rates in a way that mimics the proposed revenue effects of
8 existing schedules.

9 To the extent that the new rates mimic the existing rates (*i.e.*, provide
10 close to the same cost per therm at each consumption level), it can be argued that
11 the new rates reflect cost of service to the same extent that existing rates do.
12 When the new, redesigned rates have been in place long enough for customers to
13 find their point of repose, it will be possible to craft a more finely tuned analysis
14 of cost of service under the new rates.

15 **III. Summary of Rate Redesign**

16 **Q. Please review the new rates.**

17 A. The company proposes three new rate schedules to replace nine existing
18 schedules. The schedules to be eliminated are:

19 Schedules 4, 11, 21, 22, 23, 55, 90, and 91

20 In their place, the company proposes:

21 Schedules 31, 32, and 33, having the following characteristics:
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Schedule 31

Customer Charge: \$194.13 per month.
First 2,000 therms: \$0.37503 per therm
For all additional: \$0.35450 per therm

Schedule 32

Customer charge: \$1839.75 per month
First 10,000 therms: \$0.15086 per therm
Next 20,000 therms: \$0.12326 per therm
Next 20,000 therms: \$0.09623 per therm
Next 200,000 therms: \$0.05024 per therm
Next 750,000 therms: \$0.03000 per therm
All additional therms: \$0.01415 per therm

Schedule 33

Customer charge: \$38,000 per month
All therms: \$0.00500 per therm

Distribution Capacity Charge:

A distribution capacity charge of \$0.15748 will be applied to firm service on schedules 32 and 33. The charge is paid monthly for each therm of measured peak winter day deliveries with the winter term defined as November through February. The winter (November - February) peak MDDV to which the charge applies remains in place from May 1st to April 30th of the following year, at which time the most recent November-February peak becomes the new MDDV for the upcoming year.

Sales Service:

Customers taking sales service on Schedules 31 - 33 can purchase gas from Northwest Natural either from the company's core portfolio or from an independent gas marketer, if transportation service only is desired.

1 **Firm Sales:**

2 Customers choosing firm service will be required to pay (upstream) demand
3 charges associated with delivering gas into the company's distribution system.
4 These customers can elect to pay upstream demand charges either on a rolled in
5 basis at the currently tariffed \$0.12942 per therm of firm deliveries, or as a winter
6 peak day MDDV demand charge (Peak Demand Option) of \$1.85 per therm of
7 daily peak load per month. Customers on schedules 32 and 33 who opt for the
8 Peak Demand Option will be required to have a company-approved demand
9 meter. Customers selecting the Peak Demand Option on Schedule 31 will have
10 the option of installing a company approved demand meter, or accepting the
11 MDDV as the highest metered monthly usage during November through February
12 divided by 30.4 and that result divided by 0.7. In addition, customers taking firm
13 sales service on Schedule 32 will pay a storage for firm service charge equal to
14 \$0.20415 per therm of MDDV as measured in the November through February
15 period. As Schedule 32 is fully unbundled, a specific charge is necessary to
16 assign cost for storage service to only those customers electing firm service.
17 Transporting customers do not receive any automatic benefit from storage
18 capacity.

19 **Interruptible Sales:**

20 Customers wanting interruptible sales service will pay a per therm demand charge
21 of \$0.01559 cents per therm. This is the currently tariffed interruptible sales
22 service demand charge.

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1 **Q. Please explain the distribution capacity charge.**

2 A. The distribution capacity charge attempts to assign a price to customers'
3 distribution system, peak day demand. Current rates make no effort to price
4 distribution demand, yet peak deliverability is something that the company must
5 build facilities to meet, and it is the thing most likely to become scarce as loads
6 grow. Logically, it needs to become an element in customer gas utilization
7 planning and actions. The charge itself, \$0.15748, is equal to one half of the
8 distribution capacity charge of \$0.010355 at the one hundred percent load factor
9 developed by Dr. John Hanson in his ongoing analysis of Oregon distribution
10 costs. The \$0.15748 is computed as $(0.5 \text{ times } \$0.010355 \text{ times } 365)/12$ which is
11 one half the cost of one therm at one hundred percent load factor paid in monthly
12 installments. The distribution capacity charge attempts to measure the cost of
13 maintaining the system at a firm capacity level over time given the addition of
14 new, firm customers and load. While the study is based on Oregon experience, it
15 does not allocate costs to Washington, but rather serves as a proxy to measure the
16 cost of providing firm service over time. The results of the study should be an
17 excellent indicator of the cost of providing firm service because there is no reason
18 to believe these costs are any different for Oregon than for the system as a whole,
19 or for Washington alone.

20

1 **Q. Have you determined the impact of the proposed rates on the bills paid by**
2 **the customers involved?**

3 A. Yes, I have. The results of the proposed rate design are shown in *Exhibit No.*
4 *____ (FPF-4)*. The various schedules will see the average revenue changes shown
5 in the table below. These changes are calculated on total bills including demand
6 and commodity in order to better see the comparison between schedules and to
7 more accurately reflect the change in total energy bills those customers will
8 experience.

9

| Schedule | Bill Effect |
|-------------------|-------------|
| 3 | -0.9% |
| 4 | -3.3% |
| 11 | -5% |
| 21 | 4.8% |
| 22 | 14.3% |
| 23 | -17.3% |
| 55 | -0.6% |
| 90 | -2.4% |
| 91 | 1.2% |
| Special Contracts | -1.1% |

10

11 **Q. Does the rate design provide any benefits for high load factor customers?**

12 A. Yes, it does. The maximum daily delivery volume (MDDV) based upstream
13 demand payment mechanism benefits non-heating season and high load factor
14 customers. A customer with no usage in November through February will
15 register a zero winter peak MDDV. As such, this customer will pay no upstream
16 demand charges and no distribution capacity charge—reflecting the fact that this
17 customer places no peak period burden on the system. This will provide

1 significant benefits to the off peak, seasonal gas user. In addition, any customer
2 having a high load factor will benefit from the MDDV option. At the proposed
3 rate of \$1.85 per therm of peak MDDV per month, a customer using 1 therm a
4 day, every day, would pay 1.85 every month for an annual demand bill of \$22.20.
5 This customer will have used 365 therms in the course of the year for a per therm
6 demand charge of \$0.06082. A space heating customer, on the other hand, using
7 no gas for one quarter the year (and one therm per day when he did use gas)
8 would use 274 a year therms and pay \$34.46 in annual demand charges at the rate
9 of \$0.12942 cents per therm. Obviously, the higher load factor customer gets a
10 much lower per therm rate using the peak MDDV method of paying both
11 upstream and distribution demand charges under the company's proposed rate
12 design.

13 **Q. What will happen to the existing rates?**

14 A. The new rates, schedules 31, 32, and 33, will replace existing rate schedules 4, 5,
15 11, 21, 23, 55, 90, and 91.

16 **Q. What will happen with the existing special contracts?**

17 A. The existing special contracts will remain in effect through the term of the current
18 contracts, and will carry forward in accordance with the terms of those
19 agreements. If customers want to move to one of the new rates, they would be
20 welcome to do so once their current contract has expired.

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IV. Transition to New Rates

Q. How will the transition to the new rates be done?

A. A transition plan is being developed, but it is anticipated that customers will receive at least two direct mail pieces with at least one explaining the rate redesign and providing an analysis of the new rate options based on the customer's historical load. Those customers that do not self select will be moved to the most economical rate based on their historical load. It is further anticipated that the typical three month cancellation period will be waived for a time during the transition period.

Q. Does this conclude your direct testimony?

A. Yes, it does.