Exhibit No. ___T (JTS-10T)
Docket No. UG-060256
Witness: Jon T. Stoltz

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

CASCADE NATURAL GAS CORPORATION **Complainant,** **v.** **WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION** **Respondent.**	**DOCKET NO. UG-060256**

REBUTTAL TESTIMONY OF

Jon T. Stoltz

STAFF OF

Cascade Natural Gas Corporation

September 12, 2006

Prepared Rebuttal Testimony of Jon T. Stoltz

Q. Please state your name and address.

A. Jon T. Stoltz, 222 Fairview Avenue North, Seattle, Washington.

Q. Are you the same Jon T. Stoltz who provided direct testimony in this proceeding?

A. Yes

Q. What is the purpose of your rebuttal testimony?

A. My rebuttal testimony covers four major areas. First, I explain why the Company does not agree with several revenue requirement adjustments proposed by Staff, including in particular Staff's methodology for calculating normalized temperatures. Second, my testimony explains why the Company opposes the recommended revisions and/or conditions proposed by the parties in connection with adoption of the Company's proposed Conservation Alliance Plan (CAP) decoupling mechanism. Third, my testimony discusses a number of errors or omissions in the Cost of Service Study developed by NWIGU witness Shoenbeck. (This Study has essentially been adopted by most of the parties as a portrayal of a Commission Basis Cost of Service Study.) Fourth, my testimony comments on the various Rate Spread and Rate Design recommendations made by the parties, including the Company's proposed revisions to Miscellaneous Charges.

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REVENUE REQUIREMENT ADJUSTMENTS

Q. Please identify the revenue requirement adjustments you disagree with.

A. This section of my testimony discusses the following revenue requirement adjustments:

- The Company disagrees with the inclusion of the non-jurisdictional revenues and expenses associated with the merchandizing of gas supplies and associated services to Non-Core customers in the very competitive open marketplace.
- The Company recommends rejection of Staff's proforma adjustment to the revenues of the Special Contract customers.
- The Company opposes Staff's proposed adjustment to Rate Case Expense, and updates our estimate in Exhibit ___(JTS-11).
- The Company presents a detailed analysis explaining why Staff's proposed methodology for calculating the Weather Normalization Adjustment should be rejected in Exhibit ___(JTS-12), Exhibit ___(JTS-13) and Exhibit ___(JTS-14).

In addition to these revenue requirement issues, Barnard discusses Staff's proposed elimination of the Company's proposed low-income assistance funds and Staff's proposed elimination of various proforma adjustments for (1) upgrading the software and hardware associated with the IRP process, (2) upgrading the software of our Gas Management System, and (3) replacing the platform on which we operate the Customer Information System.

Q. Please explain why you disagree with Staff's treatment of Gas Management revenues and expenses.

A. Staff is proposing to include the revenues and expenses associated with Gas Management services in an attempt to pass on the benefits or profits to jurisdictional ratepayers. This is in spite of the Company supplying several responses to Staff's data requests illustrating how the Company has insulated the jurisdictional ratepayers from any of the risk associated with providing this service. The Company's shareholders have always shouldered the business risk of merchandizing gas supplies to non-core customers. Those who shoulder the risk should benefit from any profit that may be derived. In addition, this type of service is traditionally non-jurisdictional across the country.

Q. Please describe the types of risks the shareholders have shouldered.

A. Cascade responded to Staff Data Request No. 205 to "provide all information or support identifying the risks shareholders are absorbing by excluding the management service transactions from regulated operations" with the following:

> The Gas Management supply portfolio is completely separate from the core supply portfolio. The shareholders are exposed to all of the risks associated with the Gas Management supply portfolio. The following describes the major risks:
>
> 1. **Competition**: The margin associated with Gas Management Contracts is not assured or predictable for future periods. All of the Gas Management Contracts are for a finite period of time. Upon expiration of the current contract, the transportation customers have the option to purchase their natural gas commodity from a number of marketers, including Cascade, CMS and others. If Cascade's offer to provide Gas Management Services is not competitive compared to the other marketers, the customers will not sign with the Company.

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2. **Volumetric Risk:** The transportation customers purchasing gas supplies on the open market through the FERC Blanket Marketer Sales Certificates pursuant to FERC Order 547, currently only entertain offers that are purely volumetric. A volumetric deal can be described as a set price for an estimated quantity. The customer will pay a set price for as much or as little gas that the customer actually consumes in a given period. For example, a transportation customer may agree to purchase its needs for the upcoming month at the published 1st of the month price plus transaction costs. The Company must estimate how much the customer will actually consume and arrange to purchase that amount of gas on the open market. If the transportation customer consumes more than the amount purchased, the Company must purchase additional supplies at the market clearing price. If the daily price is above the 1st of the month price, the Company and its shareholders must absorb the difference. If the transportation customer uses less than amount purchased, the Company must sell the excess gas on the open market. If the daily price is less than the 1st of the month price, the Company and its shareholders must again absorb the difference.

3. **Fixed Price Contracts**: Some transportation customers seek a fixed price for their consumption, however, the customer still demands a volumetric deal. The Company and its shareholders are exposed to the over or under consumption scenarios described above with the added risk that the market clearing price for day gas is now compared to the fixed price rather than the1st of the month price. For multiple month fixed price contracts, there is a greater risk of such price disparity with a fixed price contract. The Company and its shareholders must absorb any difference.

4. **Supplier Failure**: The Company and its shareholders are exposed to the risk of the supplier going out of business. Although the risk is less if the contract with the transportation customer is a 1st of the month price, the Company would still have to replace the supply with the current market clearing price, which may be more than the 1st of the month price. The risk can be substantial with a fixed price physical contract with the supplier. If the supplier fails, the company must replace the supply at market clearing prices and the Company and its shareholders must absorb the difference.

5. **Financial Institution Failure**: After the Enron debacle, the Company adopted the policy of only providing fixed price Gas Management contracts obtained through swaps with banks and other excellent credit financial institutions. Although the risk is less, it is possible that a financial institution could fail and the Company and its

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shareholders would have to absorb the difference between the market clearing price of supplies and the fixed price embedded in the Gas Management contract.

6. **Transportation Customer Failure**: The greatest risk associated with Gas Management Service is customer failure. The profit associated with this service is normally less than 1% of the retail price. One transportation customer going out of business owing the Company for one, two or three months of Gas Management fees could easily wipeout more than a full year's profit for all of the Company's Gas Management Service contracts.

Q. Could the Company have avoided this issue by forming a non-regulated subsidiary to provide these services?

A. Yes, the Company could have established this business line under an unregulated subsidiary at any time, but that would seem to be an inefficient use of resources in the interests of "form" over "substance." Even under that approach, a rate case issue would remain regarding the proper amount of expenses associated with work performed by the utility employees in support of this function to be assigned to the subsidiary. The Company did not think that forming an unregulated subsidiary would be necessary to properly align the risk and rewards of this business line, given that it is a ratemaking issue involving cost allocations and not a corporate organizational issue. However, if the Commission would prefer to have Cascade's Gas Management business segment under a wholly-owned subsidiary, we are certainly prepared to do so even though we believe this would simply be form over function.

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Q. Do you have any response to the testimony filed by Cost Management Services, Inc. (CMS) with respect to Gas Management Services?

A. The Company does not agree with the characterizations in Lehmann's testimony. In our view, CMS is attempting to eliminate the Company as a competing supplier for these services, and granting the relief requested by CMS, while beneficial for CMS, would be detrimental to our customers' interests. In any event, the issues raised in Lehmann's testimony are the subject of a separate complaint proceeding brought by CMS against Cascade, Docket No. UG-061256, and we will address them in that proceeding.

Q. What is your concern with respect to Staff witness Parvinen's proposed proforma revenue adjustment to reflect the escalation clauses built into the Company's special contracts?

A. I do not believe it is appropriate to pro form these escalation clauses for the automatic adjustments that have or will occur beyond the test period. These automatic escalation clauses are the only opportunity to increase revenues from the special contracts. These clauses were meant to compensate the Company for escalation in operating expenses that occur during the life of the special contracts. Parvinen has indicated that Staff has seen no evidence that the 2006 inflation rate will be substantially different than the inflation rates in 2005. Yet, Parvinen is proposing to adjust revenues to reflect this inflation but is not proposing to adjust the operating expenses that match that inflation. The Commission should reject Parvinen's special contracts revenue adjustment since he has failed to

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recognize offsetting expense factors. It is an obvious violation of the matching principle in ratemaking.

Q. Staff witness Parvinen expressed some concerns with the level of rate case expenses, particularly those expenses associated with amount identified for Cummings. How do you respond to Parvinen's concerns?

A. Parvinen based his concerns upon the Company's original estimate of rate case expenses. At the time of preparing our application, we had to estimate the cost of developing and defending our case. Staff witness Parvinen (page 14, line 17 – page 15, line 2) expressed concern about the rate case expenses associated with Cummings' services indicating that "any of the company witnesses could have provided the same testimony" and "there appears to be no particular expertise this witness brings to the docket at hand." I strongly disagree with Parvinen's assertions and assume that they are made because he is unfamiliar with the services that Cummings has provided to the Company. He has provided a variety of regulatory support services associated with the preparation and processing of the rate case filing, including assessing preliminary filing schedules and Company testimony, researching precedent in other jurisdictions on various ratemaking issues and regulatory mechanisms, and participating in meetings and discussions pertaining to the development and presentation of the rate filing. In fact, the majority of Cummings expenses through July 2006 are associated with these regulatory support services. I believe it is certainly reasonable and less costly for the Company to supplement its small rate department staff

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with outside assistance, as it has in this case, in order to prepare, present, and process a general rate case rather than to hire additional permanent staff for this purpose.

Q. Have you updated the estimated rate case costs?

A. Yes, I have. Exhibit No. ___(JTS-11) revises the Company's estimated rate case costs to $436,804. This estimate includes actual expenditures through August, 2006 plus an estimate of the expenses expected to occur through the completion of the case. One third of the total equals $145,602 and this amount should be replace the original 1/3rd estimate of $166,667 that was included in Exhibit ___(JTS-8).

WEATHER NORMALIZATION METHODOLOGY

Q. Please explain why you disagree with the Weather Normalization Adjustment developed by Staff.

A. I have serious concerns with the Weather Normalization Adjustment put forth by Staff. My concerns include both the development of use per customer per Heating Degree Day (HDD) portion of the analysis and the use of NOAA's published "normals" in establishing the amount of weather normalized therms and resulting revenues for the test period. Staff witness Mariam has introduced a new (to Cascade) Weather Normalization Adjustment methodology to determine the use per customer per HDD coefficients or weather sensitivity

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coefficients in what he calls a more "robust" analysis, which he claims will correct for a statistical problem called autocorrelation or serial correlation.

The resulting HDD coefficients, however, are significantly larger than the Company's calculation of use per customer per HDD coefficients. The following table shows a comparison of Mariam's coefficients with the Company's. As can be seen from the following Bellingham residential service 503 excerpt from Exhibit (JTS-12), Staff's heat sensitive coefficients are significantly larger in the non-summer months than the Company's heat sensitive coefficients.

Bellingham 503

		Use per cust per HDD Coefficients	Use per cust per HDD Coefficients	
		Staff	Cascade	% Increase
Month	Intercept	16.08991	9.126961	
Oct-04	X Variable 1	0.154853	0.113697	36.20%
Nov-04	X Variable 2	0.179689	0.149687	20.04%
Dec-04	X Variable 3	0.154115	0.128624	19.82%
Jan-05	X Variable 4	0.1734	0.147705	17.40%
Feb-05	X Variable 5	0.138138	0.111345	24.06%
Mar-05	X Variable 6	0.147411	0.116988	26.01%
Apr-05	X Variable 7	0.153345	0.112956	35.76%
May-05	X Variable 8	0.137647	0.081584	68.72%
Jun-05	X Variable 9	0.04426	0.08039	-44.94%
Jul-05	X Variable 10	0.038395	0.106265	-63.87%
Aug-05	X Variable 11	0.039686	0.120641	-67.10%
Sep-05	X Variable 12	0.03868	0.066646	-41.96%

Q. What was the source of information used in Staff witness Mariam's analysis?

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A. Mariam claims to have used the same historical customer counts, therm deliveries and actual HDDs data utilized by the Company in its regression analysis. The Company's analysis produced a high confidence level or R Square factor, mostly in the 0.97 range where 1.0 is perfect. Mariam testified that his autocorrelation revision improved the R Square factors to 0.98. It does not seem logical, however, that an analysis that is supposed to tweak the results for autocorrelation would result in heat sensitive coefficients that are 20% to 70% larger than the Company's results.

Q. How did you test Mariam's analysis?

A. I tested Mariam coefficients in another way. The historical data contains the amount of therms delivered under the actual HDDs. In Exhibit No. ___(JTS-13), for each weather area and for residential rate schedule 503 and commercial rate schedule 504, I have listed the actual therms delivered in Column A. In Column B, I listed the actual customer count. Column C shows the base load per customer as developed by Mariam in his Table Two. Column D is the product of multiplying Mariam's base load per customer times the number of customers and shows the total amount of base load delivered each month. Column E subtracts the base load from the total amount delivered which results in the heat sensitive load actually delivered. Column F lists the actual HDD that occurred in each month, as reported by NOAA. Column G lists the use per customer per HDD coefficients developed by Mariam. Column H multiplies Mariam coefficients by the actual HDDs and by the actual customer count.

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Q. What do you conclude from Exhibit No. ___ (JTS-13)?

A. As can be seen, Mariam's coefficients grossly overestimates the amount of heat sensitive therms that would be sold given actual HDDs. This over statement of heat sensitive therms is particularly pronounced in the heavy heating months of October through May.

Q. What is the impact on assumed therm sales to rate schedules 503 an 504?

A. This review of the impact of Mariam's analyses results in a significant distortion of therms sales to these two rate schedules based upon the actual HDDs we experienced in the test period. The following table shows a comparison of actual therms sold and the amount Mariam's analyses calculates we should have sold under the actual HDD values:

Weather Area	Actual Test Period Sales	Sales Levels Resulting From Staff's Coefficients	Percentage Increase Over Actual
Residential 503			
Bellingham	47,461,391	62,647,603	32.0%
Bremerton	23,003,211	32,229,920	40.1%
Walla Walla	13,162,982	15,248,401	15.8%
Yakima	15,583,732	19,636,285	26.0%
Total	99,211,315	129,762,209	30.8%
Commercial 504			
Bellingham	23,952,157	32,893,267	37.3%
Bremerton	15,799,798	21,737,139	37.6%
Walla Walla	13,205,708	15,264,275	15.6%
Yakima	20,188,969	24,477,088	21.2%
Total	73,146,632	94,371,768	29.0%

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Mariam's analysis thus overstates test period consumption by 30% using actual HDDs. The results of Mariam's analysis does not produce logical results and should not be relied upon to restate the test period regardless of whose "normals" are used to normalize the test period.

Q. Please discuss the concerns you have with using the "normals" as published by NOAA.

A. NOAA calculates the arithmetic mean or average of 30 years of data, whether it concerns temperatures, HDDs, CDD, rainfall, or precipitation. NOAA publishes this arithmetic mean or average as climatic "normals". NOAA publishes an update to this information every ten years. The current version is based upon the period of 1971 through 2000. The climatic "normals" published by NOAA are intended to represent the general climate conditions one might encounter at a given region or city. It should be noted that NOAA has never presented these "normals" as the most likely conditions expected to occur. In fact, NOAA even put a disclaimer in the article entitled "What is "Normal" Temperature?" which Mariam referenced on page 13 in his testimony. The last paragraph of that article states as follows:

> "**Conclusions**
>
> While NOAA's National Weather Service will likely continue to publish "normal" temperature values, one needs to keep in mind that the "normal" is simply an average of all the values. It is possible that not even one of the input values is equal to the computed "normal," and the most commonly occurring values may be significantly separated from the "normal." This further underscores that, although it is *interesting* to know the "normal" or average temperature; it is probably more important to understand the distribution of the

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values used in computing the "normal," which the ranges, standard deviation, variance and frequency distributions can relate."

Q. Is it appropriate to use the NOAA data in the manner relied upon by Mariam in his adjustment?

A. No. While NOAA takes great pains in making sure the data is a homogeneous as possible by adjusting the data set for changes in instrumentation or changes in location, lost or unavailable data or other conditions so that the historical data is as clean as possible, the information remains *historical* data and the arithmetic mean or average calculated from that data is merely that; the average of that data. In these publications of historical data, NOAA is not attempting to produce a product that reflects trends in climatic change and their "normals" were never intended to be used for something as critical as establishing the weather normalized revenue in a utility general rate case. It is my understanding that the National Climatic Data Center is aware that some utility commissions are misinterpreting the published "normals" as the basis for calculating utility revenue requirements. Based upon the National Climatic Data Center and NOAA current Strategic Plan, they are considering developing a new product that would take into account the warmer conditions that are occurring in many regions of the country.

The NCDC's current Strategic Plan describes their new product as follows:

"National Climatic Data Center (NCDC) Strategic Plan

Significant NCDC Pursuits for FY 2005 to FY 2011

Web-based Dynamic Next Generation NORMALS

> Users from a number of economic sectors have petitioned NOAA to develop a new generation of optimal climate normals that can support their respective business needs that require projections on the order of several weeks, months, and years into the future. Industry leaders, such as the American Engineering Society and the American Society of Heating, Refrigeration, and Air Conditioning Engineers (ASHRAE) and the Weather Risk Management Association (WRMA) have indicated that climate variability and customer demands are to the point where the typical 30-year climate normals can no longer adequately support the rapid changes associated with today's national and international business environments. For example, ASHRAE notes that design specifications based on traditional normals were exceeded with alarming frequency during the 1990s and the WRMA use of degree day normals were tied to over $12 billion in contracts in 2002. Implementing a new operational process will provide a more comprehensive generation of dynamically built web-based optimal climate normals easily accessible on a variety of time scales and updated on a regular basis using the most current data. These will be available ondemand through direct web access in spatial grids for metropolitan areas, climate divisions, and geographic regions. Next Generation Climate Normals will make use of past and present climate, as well as future climate scenarios to provide users with a set of probabilistic information related to means, variability, and extremes for a given location, variable, and specific period of time in the future. The robust web access and servicing system will give the user the flexibility to produce information that is application-specific, greatly facilitating the development and use of a wider variety of new normals to support U. S. businesses. These normals will support users in their plans and actions designed to minimize the impacts of unanticipated adverse climate conditions and maximize the benefits of anticipated climate conditions. Applications include energy and water resources management, agriculture, construction, industry and commerce, transportation, and research, as well as government uses, such as forecast verification done by the NOAA."

To my knowledge, this new product is not yet available, however, the mere fact that NOAA is considering adding this product to correct the utilization in rate making is another reason to reject Mariam's methodology.

Q. Do you have any other comments on Mariam's methodology?

A. Yes. It is amazing to me that Mariam was so critical of the "simplistic" least squared regression analysis Cascade uses in developing the use per customer per HDD coefficients

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in its weather normalization methodology (which, by the way, was developed in consultation with Commission Staff members in Cascade's last general rate case). Yet Mariam relies upon the simplest of all statistical tools, the arithmetic mean, in determining what should be considered "normal." Other statistical and dynamical approaches could be used to provide better estimates of future HDD, including excerpting the results of global climate models for the Northwest, as has been done on the UW Climate Impacts Group's web site, http://cses.washington.edu/cig/pnwc/cc.shtml, which indicates a warming rate for the Northwest of 0.3°-1.0°F per decade during the next 50 years.

Q. What are the implications of this warming trend for ratemaking purposes?

A. Based upon the climatic warming we have all noticed in the Northwest and is widely accepted as fact in the scientific community, which can furthermore likely be quantitatively linked, on the decadal timescale, with the continued increase in greenhouse gases,[1] the probability is much greater than 50% that it will be warmer than NOAA's published "normals" in the rate year following the conclusion of this rate case. Dr. Mote's regression analysis of the climatic warming trend is the best available surrogate product for

[1] Mote, P. W. 2003. Trends in temperature and precipitation in the Pacific Northwest during the twentieth century. Northwest Science 77(4): 271-282.
Stott, P.A., 2003: Attribution of regional-scale temperature changes to anthropogenic and natural causes. Geophysical Research Letters, vol 30.

Jones, P.D., et al., 1999: Surface air temperature and its variations over the last 150 years. Reviews of Geophysics, 37, 173-199.

Karoly, D.J., and Q. Wu, 2005: Detection of regional surface temperature trends. Journal of Climate, 18,

establishing normal HDDs for rate making purposes. His analysis produces a product that statistically provides an equal probability of colder than Dr. Mote's normal as the probability that the rate year will be warmer than normal. To provide fair just and reasonable rates, the Commission should adopt the Company's weather normalization methodology along with Dr. Mote's determination of "normals".

CONSERVATION ALLIANCE PLAN

Q. How does the weather normalization issue inter-relate with the Company's proposed Conservation Alliance Plan?

A. While I am on the subject of weather, I would like to provide the Company's view on the removal of the weather component of the Conservation Alliance Plan. Disputes over how to normalize a test period would be minimized if the Commission were to adopt the Company's proposed Conservation Alliance Plan, which includes a weather component as well as a conservation component. Please do not misunderstand me, the weather normalization mechanism used in rate proceedings should be established in a fair and reasonable manner, to avoid unwanted consequences in the decoupling mechanism. Even if the decoupling mechanism only covers conservation, the weather normalization mechanism has significant influence over the measurement of conservation effectiveness. Staff's proposal for a "conservation only" mechanism adopts all the mechanics of calculating conservation and weather margin impacts contained in Cascade's Conservation Alliance

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Plan. The only difference under Staff's proposal would be that the Company would not record, as a deferral, the margin change due to weather variance.

Q. What is the importance of a reasonable weather normalization mechanism?

A. I have prepared Exhibit No. ___ (JTS-14) to illustrates the importance of a reasonable weather normalization mechanism in a decoupling mechanism. The decoupling mechanism currently proposed by the Company divides the monthly change in margin that occurs into two parts, weather related consumption variance and conservation-related. This exhibit compares how this separation would occur under Cascade's weather normalization mechanism and under Mariam's mechanism. Schedule 1 Page 1 of 1 shows the weather and conservation margin variance under both weather normalization mechanisms for the estimated impact over the next three years. The point is, Mariam's proposed weather heat sensitive coefficients essentially *triple* the magnitude of both the weather and conservation margin variance.

Q. Does this have implications on the level of adjustments that could be necessary?

A. Yes. Those parties suggesting limitations on the amount of surcharge that could be passed through annually based their recommendations on Cascade's calculations. I believe they would need to reconsider those annual cap suggestions if the Commission were to adopt Mariam's weather mechanism, which obviously skews the results.

The Commission should consider the above described consequence on the measurement of conservation effectiveness as another reason to reject Mariam's weather normalization methodology.

Q What is the Company's position on the need for an annual ceiling on the rate impact of the Conservation Alliance Plan?

A. The Company generally agrees with attempting to limit the impact of the rate changes on customers. Such limits, however, must be carefully considered. The limit should not discourage the pursuit of conservation. My experience tells me that an effective cap can be modeled after the accepted practices in Purchased Gas Adjustment applications. In PGA proceedings, the utilities change the amortization of their deferrals to two years or longer if the rate impact of a one year amortization is too large. There is no set threshold in the PGA process, but I cannot recall a situation where the amortization period was disputed. I do not believe the parties would have difficulties in determining a reasonable amortization period within the decoupling mechanism under a similar regime.

The Company proposed such a clause in its proposed Conservation Alliance Plan. I recommend that the Commission acknowledge that the selection of length of the amortization period is adequate protection against rate shock.

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Q. Do you have concerns with some of the other suggestions associated with the implementation of a decoupling mechanism?

A. Yes. Steward is recommending excluding new residential customers from the decoupling mechanism because new customers use less per year than existing customer. However, she recommends including new commercial customers because they consume more the existing customers. Somehow, she testifies that excluding new customers will provide incentives for the Company to pursue higher efficiencies in the new home market, because once built, it will be years before DSM opportunities will be available from this group of customers. Steward has it backwards. Excluding new customers preserves the disincentive for the Company to promote conservation to these customers. If they are excluded from the mechanism, in will be in the Company's best financial interest for these customers to consume as much gas as possible. To maximize the opportunity to achieve higher energy efficiency in new homes is a good reason to include new customers in the decoupling mechanism.

Excluding new customers in the decoupling mechanism would also unduly complicate the tracking process. The Company would have to somehow flag the new accounts and separate their billing information from existing customers.

New customers would have to pay the surcharge resulting from the decoupling mechanism but would not be the recipient of any of the conservation programs.

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The Company's line extension policy could be greatly simplified if all new customers had the same margin per year value of the test period's margin per customer.

For all of these reasons, the Commission should reject Steward's proposed exclusion of new residential customers.

Q. How does the company respond to Weiss' proposal of Conservation thresholds and the proposed performance chart?

A. The company disagrees with the proposal offered by NW Energy Coalition witness Weiss for conservation thresholds and a complex performance chart, for several reasons. First of all, Cascade does not have the size of staff that PSE does in order to support the level of conservation Weiss is indicating. As indicated in Barnard's rebuttal testimony, Cascade's additional utility-sponsored conservation programs would most likely be delivered through independent third party vendors. Weiss' testimony indicates that the utility should need to spend as much as "Cascade would have spent to implement the lost conservation" (Weiss at page 21, lines 17 &18). It appears that Weiss assumes that the utility has some embedded conservation costs in its rates. That is not the situation, however, in the case of Cascade. Additionally, he indicates that if the Company does not hit the targets, that a third party vendor would need to be hired to implement the programs. To the extent the Company

already plans to implement conservation programs through a third party, it would be fair to assume that Weiss' concerns are unwarranted.

Second, the Company is also concerned with Weiss' suggestion that the Company should be penalized for under achievement of the conservation targets and merely achieving the base targets warrants no additional recovery. While Cascade can offer programs and promote conservation, we cannot force customers to accept our programs. Under Weiss' proposal, the Company could meet all of its implementation commitments and still not be allowed to fully recover the declining use per customer if the declines do not exceed a 150% of the "stretch" goal. Customers have a choice whether to implement conservation or not. The Company can only be responsible for promoting it and even with extensive incentive programs and marketing could not guarantee that it would be able to achieve the targets. Additionally, all ratepayers benefit to the extent that customers implement and invest in conservation without a utility-sponsored program. Under the current methodology, when the utility provides an incentive program, the costs associated with the program are deferred and passed on to all ratepayers through the tracker mechanism. To the extent that customers chose to invest in conservation without a company-sponsored program, that individual customer benefits from lower utility bills. This also benefits all other ratepayers that do not or more importantly cannot participate in a program as they currently subsidize those ratepayers that do participate. Therefore, the Company believes that the promotion of conservation goes beyond merely offering utility sponsored programs. Just because usage

declines for reasons other than a utility sponsored program, does not mean that the utilities shareholders should need to suffer.

Additionally, it is interesting that Staff has proposed removal of the advertising dollars the Company requested for additional conservation promotion. Cascade still believes that customer education is a viable means of achieving conservation savings, without burdening ratepayers further with the costs of utility sponsored incentive programs. The problem is these types of programs are difficult to measure their success.

The Commission should reject Weiss' suggested targets and recovery thresholds.

Q. Should the Commission include the deferral of margin loss due to weather in the Decoupling mechanism?

A. Yes. Weather is certainly one item that is beyond the utility's control. Under traditional rate designs, variation in weather is the source of multi-million dollar swings in earnings. When weather is colder than the "normal" established in the utility's last rate case, customers pay too much for the delivery of their gas supply and the utility has a financial windfall. When weather is warmer than the "normal," customers pay too little for the delivery of their gas supply and the utility does not recover all of its fixed cost. Many state commissions have already recognized this fact and have approved weather normalization mechanisms, sometimes combined with a conservation decoupling mechanisms, but often as

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a separate mechanism. It is likely much easier for the utilities and the commission staff to jointly establish a reasonable process for normalizing a test period for weather, if the financial impact of weather variances is mitigated through a weather decoupling mechanism. The simple fact is rate theory is attempting to ensure utilities on average to not over earn or under earn due to weather. That is the reason we spend so much time attempting to predict the appropriate future weather and ensure the volumes associated with this weather are also appropriate. Inclusion of a weather component to the Conservation Alliance Plan simply forces that issue by ensuring this occurs. However, it is still in everyone's best interest we utilize the correct assumptions for future weather as have been outlined by Dr. Mote.

Q. Staff witness Steward indicated that including weather in the decoupling mechanism may increase rate volatility for customers. Are there opportunities to minimize rate volatility for customers?

A. Yes. Steward was referring to the situation where large balances are accumulated during a warmer than normal winter and amortized during the next year. If the amortization year is colder than normal, then customers would be paying more because of the colder weather and would be paying the surcharge associated with the previous year's deferrals. Cascade's filed proposal included one alternative for reducing such volatility. Our proposed Conservation Alliance Plan would establish baseline rates based upon warmer than normal weather at the first annual CAP rate update. In this manner, the weather component of the

decoupling would almost always create credits to customers rather than charges. However, Steward's recommendation to eliminate the annual update of the baseline margins per customer would eliminate the opportunity to set the baseline rates upon warmer than normal weather, unless it is done in setting rates in this general rate case. If the Commission approves the inclusion of weather in the decoupling mechanism, the Commission should either allow the annual resetting of baseline margins per customer or require the establishment of baseline margin per customer in this rate case to be based upon warmer than normal weather so that this rate volatility mitigation can be implemented.

COST OF SERVICE STUDY

Q. Please comment of the status of the Cost of Service Study.

A. Due to the difficulties in trying to determine whether Cascade's filed Cost of Service study met the standard of a Commission basis Cost of Service study, the NWIGU witness Shoenbeck replicated Dickey's model in an excel spreadsheet. Through this process, Shoenbeck was then able to identify several areas of Dickey's study that departed from a "Commission Basis" study. Shoenbeck filed his version of a Commission Basis Cost of Service Study as Exhibit No. ___ (DWS-3). Most Parties have adopted Shoenbeck's study as a Commission Basis Cost of Service Study. Cascade agrees that Shoenbeck's Exhibit No. ___ (DWS-3) comes closer to producing a Commission basis study, but it does contain two areas of allocation that are incorrect.

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Q. What allocations are incorrect under Schoenbeck's study?

A. The first area is the allocation of A&G and other operation expenses to the Special Contracts 901. The second area concerns the therm sales levels used as throughput in the study. Since Shoenbeck's excel spreadsheet is so much easier for the parties to follow, the Company has elected to use his excel spreadsheet in its submittal of its rebuttal Cost of Service Study exhibit rather than asking Dickey to rerun his model.

Q. Please explain why A&G and other allocated expenses should not have been assigned to the Special Contracts 901.

A. All of Cascade's Special Contracts were approved by the Commission pursuit to WAC 480-80-143. All of the customers served on Special Contracts had legitimate by-pass alternatives available to them. WAC 480-80-143, Section 5 (c) specifically prescribes that the revenues derived from Special Contracts recover, at a minimum, the direct expenses associated with providing the service, as follows:

> "(5) Each application filed for commission approval of a contract must:
> (c) Demonstrate, at a minimum, that the contract charges recover all costs resulting from providing the service during its term, and, in addition, provide a contribution to the gas, electric, or water company's fixed costs;"

In our view, Section (5) (c) applies not only at the initial Commission consideration for approval of the Special Contract, but Cost of Service Studies filed subsequently in general rate applications should also be based upon this Section (5) (c), and only the expenses and rate base directly attributable to providing the Special Contract service should be allocated

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to that group of customers in a Cost of Service Study. Exhibit ___(JTS-15) is Cascade's rebuttal Cost of Service Study that removes the A&G costs assigned to the Special Contract 901 group. Shoenbeck's study still assigns some expenses that are not direct expenses or allocated based upon direct rate base. I did not remove those expenses, although full compliance with Section (5) (c) would require that removal. This improved assignment of cost demonstrates that the Special Contract 901 group continues to meet the requirement of WAC 480-80-143, Section (5) (c), including demonstrating that the Special Contracts continue to provide a contribution toward the Company's fixed cost.

Q. Does Cascade have the ability to require Special Contract customers to provide fuel-in-kind for distribution system lost and unaccounted for gas?

A. No, none of the Special Contracts currently contains such a provision. This is an item of expense that was overlooked in the early 1990s when most of the Special Contracts were negotiated. It is an item we will include in our negotiations as these contracts come up for renewal.

Q. Have you reflected the cost of Cascade providing the fuel lost during distribution to the Special Contract group in Exhibit ___(JTS-15)?

A. Yes, I have included $822,516 for the cost of Cascade providing the fuel lost during distribution in this Cost of Service exhibit.

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Q. How have you treated the cost of Cascade providing the fuel lost during distribution to the other transportation customers served on Rate Schedules 663 & 664 in Exhibit No. ___(JTS-15)?

A. Following discussions with NWIGU, the Company is proposing a number of modifications to the rate design of rate schedules 663 & 664. Included in these modifications is the provision that will require rate schedules 663 & 664 customers to provide fuel-in-kind gas supplies to cover the gas lost during distribution. Since the customers will be providing this supply, Cascade will not have to incur the expense. I have therefore removed the cost of lost and unaccounted for gas in this Cost of Service study.

Q. You also indicated that this cost of service study corrects the therm sales levels used as throughput. Please describe the correction that is required.

A. Some of the components of expense and rate base are allocated to the various rate schedules based upon throughput. One of the restating adjustments is the weather normalization adjustment. My Exhibit No. ___(JTS-6) results in an additional 1,804,351 therms on a weather normalized basis to residential service 503 and an additional 1,653,651 therms on a weather normalized basis to commercial service 504. These restated therm levels are reflected in the throughput numbers contained in the Exhibit No. ___(JTS-15) Cost of Service Study.

However, Mariam calculated different weather normalized therms in his Exhibit No. ___(YKGM-2), in which he indicates that residential 503 therms should be increased by 5,862,710 and commercial 504 therms should be increased by 4,439,798 therms. Mariam did not file a cost of service exhibit but instead included a Revenue To Cost Ratio Table, based upon his cost of service study in his testimony as shown on page 23. It does not appear that Mariam reflected his own weather normalization therm adjustments in his throughput numbers when he developed his cost of service study.

RATE SPREAD AND RATE DESIGN

Q. Various Parties have addressed Rate Spread issues in their testimony. Please describe the Company's concerns with these various recommendations.

A. Public Counsel witness Lazar recommends that any increase granted in this rate case be spread as an equal percentage of margin. Such a rate spread proposal completely ignores the results of the Commission Basis Cost of Service Study. Certain rate schedules are shown to provide revenues far in excess of cost. The application of an equal percentage of margin will perpetuate this unjust situation. The Commission should reject the equal percentage of margin approach.

NWIGU witness Shoenbeck recommends a one third movement toward full Cost of Service rates, including a $2,000,000 reduction for Rate Schedule 663. Staff witness Steward rejects Cascade's equal rate of return (full Cost of Service) rate spread and also

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rejects the concept of equal percentage of margin, as illustrated by the Company and proposed by Lazar. Steward recommends a partial movement toward Cost of Service rates. Steward's recommendation ranges from no increase for Rate Schedule 663 to 125% of the average increase to rate schedules 503 and 541. The Company understands that the Commission usually considers more than just the Cost of Service results in determining the appropriate rate spread. The Company believes that the ultimate goal of rate spread should be the achievement of cost-based rates. If the Commission decides not to achieve full Cost of Service rates in this proceeding, the Company recommends a partial movement toward Cost of Service rates along the lines recommended by Shoenbeck, even if that partial movement results in a decrease for some rate schedules. It would take many rate case decisions and perhaps decades before Cost of Service rates could be achieved if "no increase" is the maximum allowable relief available for those services that are subsidizing other rate schedules.

Q. Please comment of the various Rate Design proposals recommended by the various Parties.

A. Staff witness Steward recommends a modest increase in the Basic Service Charge of residential Rate Schedule 503 and commercial Rate Schedule 504 because each of these schedules would be included in the decoupling mechanism. Steward accepts the Company's proposed increases in the Basic Service Charge of the other rate schedules. The

Company believes Steward's approach and recommendations are reasonable and we are willing to accept her recommendations.

Public Counsel witness Lazar, NW energy Coalition witness Weiss and The Energy Project witness Eberdt all recommend the retention of the current residential $4.00 Basic Service and an inverted rate design. The Company does not agree with these recommendations. Almost all of the Company's costs are fixed costs, even though the Commission has traditionally only reviewed the cost of meter reading and billing in the establishment of Basic Service Charges. If the Basic Service Charge recovers more than meter reading and billing, the Company's line extension policy will be adjusted to reflect that part of the investment to serve the customer will be recovered through the basic charge. Lastly, the Company's proposed increase in Basic Service Charges still leaves the majority of the fixed costs to be collected through the volumetric rate.

Q. Why do you oppose the inverted rate proposal?

A. Inverted rates likely do not provide increased price signals to customers. Lazar offered no evidence that residential customers base their consumption decisions upon the cost of the next therm. Cascade believes that the majority of the residential customers receive their price signals from that portion of the bill that says "Pay This Amount." When the total bill is too high, the customers decide to upgrade the equipment or to turn the thermostat down a little more and put on another sweater or blanket. In addition, inverted rates will likely cause undo harm on lower

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income customers. These customers do not have the financial resources to properly equip their homes to reduce or eliminate wasteful use of natural gas. The overly simplistic view that inverted rates cause the Company's revenue deficiency to be placed on larger users of natural gas who are affluent is misplaced. Many low income customers consume higher than average therms due to their inefficient homes. Inverted rates could do more harm than good. The Company's proposed Conservation Alliance Plan, which will align our interest with that of our customers, will likely be much more effective in helping our customers minimize the amount of natural gas they use than the price signals associated with an inverted rate design. I believe most environmental and consumer advocates would agree that the best conservation opportunities are in the low-income rental dwellings. A Conservation Alliance Plan that allows Cascade to work with other groups to figure out how to capture that conservation opportunity has to be more important than inverted rates.

Once the Conservation Alliance Plan has had a chance to help all customers who are desirous of conserving this precious resource, revisiting some logical form of inverted rates may make sense in the future.

Q. What about the rate design proposals for Schedules 663 and 664?

A. As indicated earlier, the Company is proposing a number of modifications following discussions with NWIGU and other interested Parties concerning the rate design of transportation rate schedules 663 and 664. Under a compromise rate design proposal, rate

schedules 663 and 664 would be consolidated into one rate schedule with a 15 cent/month demand charge and four declining block rates We believe NWIGU has also agreed to the Company's proposal of having transporters provide fuel in kind under the Company's rolling/annual assessment method. In turn, the Company will eliminate the 50,000 therm restriction for balancing, essentially providing the same balancing service that is available from Northwest Pipeline.

Shoenbeck has also requested a "volumetric firming charge" as an alternative to the 15 cent/month demand charge. The Company is willing to consider such an alternative provided there are safeguards in the alternative volumetric firming charge that prevents the customer from receiving firm service without fully paying for it. The Company is required to have adequate facilities available to provide firm service 365 days per year. The volumetric firming charge should not allow the customer to avoid paying for those facilities. However, we believe that a properly designed volumetric firming charge can be a viable option to the demand charge.

Q. Please summarize the differences between the Company's proposed miscellaneous service charges and the recommendations of Commission Staff.

A. There are only five differences between the charges originally proposed by the Company and those proposed by Staff. Staff recommends that the disconnection fee be increased to $15 rather than $25 as proposed by the Company; that the After Hours Reconnection fee be increased to $75 rather than the Company's proposed $100; that the proposed tampered

meter charge be modified from the proposed flat fee of $175 to an actual costs for the individual occurrence; and that the Late Fee that the Company originally proposed at 1.5% on outstanding balances of greater than $100, with a minimum $4 charge be modified to be a 1% fee that is applied to all outstanding balances and excludes a minimum fee. Additionally, Staff recommends the Commission reject the Company's proposed fees for Short Notice Utility Locate Services and Equipment Service Calls.

Q. What is the Company's position regarding Staff's proposed revisions to the Company's miscellaneous service charges?

A. Based on Staff's responses to the Company's data requests 72 and 73, it appears that Staff does not challenge the development of the Company's costs to provide these services. The Company therefore believes that its original proposal of $25 for disconnection and $100 for After Hours reconnection fees should be approved as originally filed. The Company agrees with Staff's proposal to modify the tampered meter charge from a flat fee to an actual costs basis as reflected in the proposed tariff language included in Parvinen's testimony at page 24 lines 14 through 16.

Q. Does the company agree with Staff regarding the proposed changes to the Late Fees?

A. Not entirely. The Company can accept Staff's proposal to apply 1% to all balances over 30 days as opposed to the 1.5% originally filed. However, the Company also believes that a minimum late fee should still apply. The Company believes that at a minimum this fee

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should be $1.00, which, as indicated in Parvinen's testimony, is consistent with the level currently authorized for NW Natural. The Company believes a minimum charge of $1.00 is appropriate as it will assist in recovering the costs associated with the mailing of disconnection and urgent notices to these customers who do not chose to pay their bills in a timely manner.

Q. Do you agree with Staff regarding their assessment of safety issues surrounding the Short Notice Locate fee and Equipment Service Call?

A. The Company accepts Staff's position on the Short Notice Locate Fee and will continue to provide this service free of charge to those who request it. However, the Company does not agree with Staff's position on the Equipment Service Call Fee. It is important to note that the Company did not propose to charge for safety related calls, such as gas odors or carbon monoxide investigations as indicated in the Company's response to Staff Data Request No. 173. However, when customers need help with appliance functionality, and there is no safety concern, the Company believes it is appropriate for the customer to pay for that expense, rather than all other ratepayers. Again, the Company believes that no party is disputing the calculation of the cost, but rather who should pay for that cost.

Q. How do you address the concerns of Public Counsel, NW Energy Coalition, and the Energy Project who all propose that these increases be rejected?

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A. The Company strongly disagrees with their position and believes that, at a minimum, the Commission should accept Staff's proposed service charge structure. Each of these parties claim that it will produce additional hardship on low income customers. None of them, however, provided any evidence that the Company's calculation of costs to provide these services is incorrect. If the Commission were to adopt their proposal and reject the proposed increases in these costs, Cascade would continue to have the lowest charges for these services and would be burdening all other ratepayers with the costs associated with performing these functions. We believe this goes against the cost causation principal and that the Commission should reject their proposal to keep the existing fee structure the same.

Q. Does this complete your rebuttal testimony?

A. Yes, it does.

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