

**BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION**

In the Matter of

NORTHWEST NATURAL GAS
COMPANY, dba NW NATURAL

Petition for Accounting Order
Regarding Headquarters Lease

DOCKET NO. UG-_____

PETITION

I. INTRODUCTION

- 1 Pursuant to Section WAC 480-90-203(3), Northwest Natural Gas Company dba NW Natural (“NW Natural” or “Company”) hereby petitions the Washington Utilities and Transportation Commission (“Commission”) for an Order authorizing the Company to account for its new headquarters lease transaction on a cash basis for the amounts to be paid for each month of use in accordance with the terms of the lease.

II. BACKGROUND

- 2 In October 2017 NW Natural entered into an agreement with Third and Taylor Office Owner, LLC to lease an office building to be constructed at SW Third and SW Taylor (“250 Taylor”) in Portland, Oregon. Lease commencement is estimated to be in late 2019 or early 2020. The agreement includes a 20-year initial term, with the option of two additional seven year renewals, for a total building rentable area of 179,685 square feet, of which NW Natural’s proportionate share is 100%.
- 3 NW Natural selected 250 Taylor after a multi-phased evaluation of its options for a headquarters location that began in late 2014. The Company conducted a deliberative

process that included seismic research, an evaluation of developer risk, an evaluation of space needs, and a coordinated financial analysis between the Company and external real estate brokers. NW Natural finds that 250 Taylor represents the lowest cost of its finalist options, a vast improvement in seismic resiliency and business continuity capabilities over its existing location, and best suits the long-term needs of its customers and employees.

- 4 Effective January 1, 2019, accounting for lease transactions is prescribed by the Financial Accounting Standards Board (“FASB”) Accounting Standard Codification (“ASC”) No. 2016-02, Leases (Topic 842) (“ASC 842”).¹ This standard prescribes in ASC 842-20-30-1, that upon lease commencement the lessee shall measure both of the following:
1. The lease liability at the present value of the lease payments not yet paid, discounted using the discount rate for the lease at lease commencement (as described in paragraphs 842-20-30-2 through 30-4)
 2. The right-of-use asset as described in paragraph 842-20-30-5.
- 5 ASC 842-20-30-5 describes the initial measurement of the right of use asset, noting that “at the commencement date, the cost of the right-of-use asset shall consist of all of the following:
- a. The amount of the initial measurement of the lease liability

¹ ASC 842 amends FASB ASC, Topic 840, Leases.

- b. Any lease payments made to the lessor at or before the commencement date, minus any lease incentives received
- c. Any initial direct costs incurred by the lessee (as described in paragraphs 842-10-30-9 through 30-10).”

6 Currently, NW Natural’s preliminary calculations result in the recognition of a right of use asset and a lease liability of approximately \$75 million on the lease commencement date under ASC 842. Please see Attachment 1 for a detailed description of ASC 842 and its application to the new lease.

7 Under the FASB standard, subsequent to initial measurement, operating lease expense would be recorded on a straight-line basis over the lease term. The right of use asset and lease liability created upon commencement would be reduced by the operating lease expense and the cash rental payments made over the term of the lease. See the attached schedule (Confidential Attachment 2) for a sample of the accounting journal entries that show how the lease would be accounted for under GAAP assuming the issuance of the regulatory accounting order requested in this filing. The sample entry is the forecasted amount to be recorded in January 2021 and highlights the variance in applying the FASB standard in comparison with the cash basis. Without the requested accounting order, all the entries shown on the schedule would be identical except for the third and fourth entries. The third entry brings the net expense activity to a cash basis using a regulatory asset account. The fourth entry is a mechanical function of total rent expense recognized and a corresponding allocation to capital. This entry

would be different because it is calculated using the amount recognized with the cash versus accrual expense treatment options. As a clarification of some ratemaking considerations, the regulatory asset identified in the third entry would not be included as part of the Company's rate base and would not receive a return.

- 8 Under ASC 842 the lease commencement date is the date on which the lessor makes an underlying asset available for use by the lessee. In our lease arrangement the lessor will make available the underlying asset before we (the lessee) begin operations or make payments under the lease in order for us to construct leasehold improvements to the building. As this is the case, ASC 842 will require expense recognition as early as Q4 2019 as compared to our lease payments which will not substantially begin until September 2020. Without the accounting order, the expense recognition in advance of the first cash payment may otherwise require an application for deferred accounting to ensure matching of costs and benefits.

III. PETITION FOR ACCOUNTING ORDER REQUEST

- 9 For rate making purposes, NW Natural has always included in its regulatory filings recovery of rental expenses based on the actual or forecasted amounts of cash rent paid. Under ASC 842 and NW Natural's current expectations regarding the new lease, the lease commencement date under GAAP may differ substantially from the contractual commencement and/or cash payment commencement. Further, GAAP expense for operating leases is recorded on a straight-line basis using total undiscounted cash flows over the life of the lease while cash payments will be made per

the contract, escalating over time. In order to align the regulatory recovery process with our accounting for this lease, NW Natural requests the Commission issue an accounting order for NW Natural to account for the lease transaction on a cash basis for the amounts to be paid for each month of use in accordance with the terms of the lease. The order will ensure a better alignment between the accounting for this lease with the rate making that has historically been approved for NW Natural lease costs and the basis for which the Company would seek recovery in its next rate case, assuming approval of this accounting order request.

- 10 NW Natural has prepared the attached comparison (Confidential Attachment 3) of estimated expense recognition versus cash spend for illustrative purposes. The numbers are not final amounts and are subject to change as a result of changes in discount rates and timing. In addition, the Company is not asking for cost recovery at this time, but rather intends to include the new lease for a prudence review in our next filed general rate case. If the requested order that would authorize the use of cash payments for recording expenses is approved, then the schedule shows that there would be no difference between cash amounts and net booked expense amounts.
- 11 Pursuant to WAC 480-90-203(3), NW Natural requests to account for the components of its new headquarters lease transaction that are subject to FASB ASC 842 on a cash basis for the amounts to be paid for each month of use in accordance with the terms of the lease.

IV. COMMUNICATIONS

12 Communications regarding this Petition should be addressed to:

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V. CONCLUSION

13 NW Natural respectfully requests that the Commission issue an order authorizing the Company to account for its new headquarters lease transaction as described in this Petition.

Dated this 18th day of October 2019.

Respectfully Submitted,

/s/ Eric W. Nelsen

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