Agenda Date: January 12, 2017
Item Number: A2

Docket: UG-161268
Company: Puget Sound Energy

Staff: Jason Ball, Regulatory Analyst
Kyle Frankiewich, Regulatory Analyst

Recommendation

Take no action and allowing Rule No. 6 – Extension of Distribution Facilities to replace Rule No. 7 in tariff WN U-2.

Background

In 2014, the commission opened Docket UG-143616 to investigate expanding natural gas distribution infrastructure. Several modifications to line extension policies were proposed including changes to existing line extension policies. In February, 2016 the commission approved a change to Avista Corporation's (Avista) natural gas line extension policies consistent with some of the finding in Docket UG-143616. In August, 2016 Cascade Natural Gas Corporation (Cascade) was authorized by the commission to implement the same methodology change presented by Avista earlier in the year.

During the fourth quarter of 2016, Puget Sound Energy (PSE) worked with commission staff to develop a new line extension policy consistent with the findings of Docket UG-143616 and the filings by Avista and Cascade. On December 6, 2016, PSE filed a tariff revision implementing a new Rule No. 6 – Extension of Distribution Facilities (Rule No. 6). Rule No. 6 simplifies PSE's tariff for extending natural gas service to new customers and changes the methodology for calculating customer margin allowances.

Discussion

Change in Allowance Methodology
PSE proposes using a newer methodology for calculating credits provided to customers for new line extensions; such credits are referred to as margin allowances. The Perpetual Net Present Value (PNPV) methodology produces the maximum line extension allowance that is economically-viable for the company. Staff has supported this method in previous tariff filings for both Avista and Cascade.[1]

[1] Additionally, literature supports the use of this method. See *Line Extensions for Natural Gas: Regulatory Considerations*, by Ken Costello. February 2013, National Regulatory Research Institute at 20.

The PNPV method it simpler to calculate and relies on information from recent rate cases. The anticipated revenue from the customer[2], divided by the authorized rate of return, results in the net present value of the customer's presence on the system. This metric is a good proxy for the financial break-even point of adding new customers to the system.[3]

PSE's current line extension allowance methodology is far more complex to calculate. Under the current Rule No. 7, margin allowances are calculated using a discounted cash flow calculation contained in an excel spreadsheet. Referred to as the "Facilities Investment Analysis" or FIA Model, certain assumptions around the annual therms (estimated using square footage for residential customers) produces a semi-unique margin allowance for each customer. Switching to the PNPV method simplifies this process and clarifies line extension policies for new customers.

Housekeeping
PSE proposes to replace Rule No. 7, the current line extension policy, with the new Rule No. 6. However, this requires modification of additional schedules and rules to reflect the updated references and procedures. Further, Rule No. 7 would still apply to customers who received a line extension under that Rule.

Conclusion

PSE's proposal aligns its natural gas line extension policies with the current policies of other investor owned utilities in Washington. Further, it implements the recommendations discussed in Docket UG-143616 and encourages more widespread adoption of natural gas throughout PSE's service territory.

Recommendation

Take no action and allowing Rule No. 6 – Extension of Distribution Facilities to replace Rule No. 7 in tariff WN U-2.

[2] The anticipated revenue from the customer is the annual revenue from the basic charge plus the decoupled revenue per customer, after "backing out" the rate of return component. The company earns a rate of return on the line extension when the line extension is added to rate base.

[3] A key assumption in this methodology is that the recovery period approaches infinity. Mathematically, this is approximate to the book life of distribution assets,usually around 30 to 50 years. See Dockets UG-152394 and UG-160967 for a more robust discussion of this approach.