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VIA ELECTRONIC FILING

Steven V. King, Executive Director and Secretary
WASHINGTON UTILITIES &
TRANSPORTATION COMMISSION
1300 S Evergreen Park Drive, SW
Post Office Box 47250
Olympia, Washington 98504-7250

Re: UG-143616 – Investigation of Natural Gas Distribution Infrastructure Expansion
NW Natural’s Comments

Dear Mr. King:

Northwest Natural Gas Company, dba NW Natural (“NW Natural” or the “Company”), submits the following comments in response to the Washington Utility and Transportation Commission’s (“Commission”) Notice of Opportunity to Comment (“Notice”), issued November 25, 2014, in Docket No. UG-143616, an Investigation of Natural Gas Distribution Infrastructure Expansion.

The Commission requested utilities to comment on various methods through which the Commission, or individual companies, could pursue gas infrastructure expansion. The Commission also specifically asked for views about whether such strategies could be accomplished under the Commission’s current authority, through tariffs, rulemaking or policy statements, or whether new legislative authority would be required. Below is the list of potential solutions the Commission provided, followed by NW Natural’s comments.

1. Line Extension Tariffs. Local distribution companies could file revised line extension tariffs to make line extensions more economically viable for new customers to obtain service. Revisions to line extension tariffs could consider different standards for certain underserved areas.

NW Natural believes that revisions to line extension tariffs could significantly increase the amount and accelerate the timing of expansion of the natural gas system in Washington, and that it would be within the Commission's current authority under RCW 80.28.060 to adopt these types of revisions.

In general, utility line extension tariffs are structured to balance two major competing interests: 1) the interest in providing gas service to a new customer, and 2) the interest in recovering the costs of that new service from the new customer over a reasonable period of time. Line extension policies attempt to strike this balance by determining the costs that new customers are required to contribute up-front toward their new service, given the margin estimated to be recovered from usage rates paid by the new customer over a specified number of years.

NW Natural believes there is a spectrum across which line extension policies could reasonably fall. On one end of the spectrum, new customers would be required to contribute very little of the costs of their new service up front, and it would be assumed that the rest of the costs would be collected from them over a long-term horizon in which the customer is expected to continue service. On this end of the spectrum, customer growth and system expansion benefit from the lower up-front costs required of new customers. The utility, however, may be concerned about the long time period over which it will recover its investment in the new service, which can result in decreased earnings in the short term. Additionally, there may be concern on the part of existing customers, who bear some risk that the new customer will not remain a customer long enough to pay the full costs of their service through the margin recovered from that customer.

On the opposite end of the spectrum, new customers would be required to contribute a very large portion of the costs of providing their new service up front, such that they are likely to "overpay" for the costs of their new service if they remain a customer beyond a few years. On this end of the spectrum, customer growth and system expansion would suffer from the high up-front costs affecting the choices of potential customers as to obtaining service. Existing customers, on the other hand, would bear very little risk, and may even stand to benefit from new customers "overpaying" for their new service, with the overpayments from new customers flowing back to offset existing customers' rates. And, utilities may enjoy temporarily increased earnings from higher up front new customer payments that, when coupled with the increased margin from the new customers' rates, exceed the amount that they had to invest to get the new service.

NW Natural's current tariff structure requires new customers to pay up-front for all costs of their new service, to the extent those costs exceed the margin expected to be paid by that customer through rates over the first five years of service. NW Natural characterizes this policy as "five times margin." The five times margin approach falls somewhere in the middle of the spectrum described above. The structure may be somewhat conservative, in that it ensures other customers' rates will not be affected so long as the new customer remains on the system

for at least five years. NW Natural believes that most of its new customers will remain gas customers for a period that is much longer than five years.

If the Commission were to clarify that Washington utilities should consider tariff structures that are more likely to accelerate and increase system expansion, NW Natural would likely seek approval to modify its line extension policy. The modified structure would result in system growth, while still protecting current customers from unreasonable costs or risks associated with system expansion. A competing consideration would be the time period over which the Company feels comfortable recovering the costs of new services.

NW Natural notes that it appears that Washington utilities have line extension policies that differ from one another. This likely results from the fact that utilities have different perceptions about the appropriate balance they should strike in terms of encouraging growth, protecting existing customers, and protecting shareholders from diminished returns. It may also result from companies being unclear on what the Commission's expectations are in terms of this balance. Therefore, it would be helpful and appropriate for the Commission to provide guidance on the appropriate balance.

NW Natural believes that the Commission's existing broad authority "to regulate in the public interest . . . the rates, services, facilities, and practices"¹ of public utilities would permit it to adopt such line extension policies, which involve competing interests that the Commission regularly grapples with in fulfilling its statutory mission.

The Commission's Notice also contemplates that different line extension policies could be applied to different areas of a utility's system that are deemed to be "underserved." NW Natural believes that this would be effective in spurring growth in those areas, although such an approach may need to be closely examined to ensure that any preference afforded to an underserved area would not be deemed an "undue preference" in contravention of RCW 80.28.020.

2. Policy Statement. The Commission could issue a policy statement clarifying its policy regarding application of prudence and "used and useful" standards for the recovery of costs for gas infrastructure in selected areas. The policy statement could address or include:

- a. A description of underserved areas in which considerations in the policy statement would apply, perhaps including:**
 - i. Whether the area is a non-attainment area;**
 - ii. Whether any electric energy conserved will assist the state in meeting its target under EPA rules implementing section 111(d); and**
 - iii. The demand for gas service, or the number of potential new customers (residential, commercial, and industrial).**

¹ RCW 80.01.040(3)

- b. A suggested process by which a local distribution company may identify the geographic boundaries of underserved areas.**
- c. A description of the criteria by which the Commission would review the prudence of capital additions in underserved areas and whether they are “used and useful.” The Commission issued a policy statement on renewable energy resources in Docket No. UE-100849 (issued January 3, 2011), addressing the application of the “used and useful” standard.**

NW Natural believes that the approach laid out in this option would make sense and help encourage system expansion in Washington.

The Commission has the authority to clarify its policy regarding the application of prudence and “used and useful” standards for the recovery of costs for gas infrastructure in selected areas, to the extent the policy does not violate existing statutes, rules, or judicial decisions. Likewise, based on the Commission’s policy statement in Docket No. UE-100849, the Commission has the authority to establish criteria for these standards. If the Commission determines that important policy considerations or existing statutes underlie the focus on underserved areas (such as environmental, low-income consumers, or other considerations identified in the Commission’s question), such a policy would have greater legal weight. As such, new legislation would not be necessary to clarify the Commission’s prudence and “used and useful” standards.

3. *Discounted Rates for Low Income Consumers.* RCW 80.28.068 authorizes the Commission to set discounted rates for low-income consumers of electric and natural gas companies. The companies and the Commission could review current low-income tariffs for the local distribution companies and, if appropriate, authorize further discounts for low income consumers. These rates then could serve as part of a strategy for recruiting customers to switch to gas from oil furnaces or woodstoves.

The Commission has the clear discretion, per RCW 80.28.068, to authorize low income discounted gas rates and the subsidized installation of gas mains or service lines. Specifically, RCW 80.28.068 states:

Upon request by an electrical or gas company, or other party to a general rate case hearing, the commission may approve rates, charges, services, and/or physical facilities at a discount for low-income senior customers and low-income customers. Expenses and lost revenues as a result of these discounts shall be included in the company's cost of service and recovered in rates to other customers.

Although such discounted rates may help facilitate system growth, NW Natural notes that low income customers would still need to be able to overcome the first costs associated with the installation of behind the meter natural gas-fired equipment. As such, any program targeted at

low-income installations may need to be in coordination with energy efficiency equipment installation programs or low-income grant programs in order to more fully address the cost barriers that likely exist for low income consumers converting to natural gas.

4. Advertising Rule Changes. Current rules prohibit cost recovery of promotional advertising by local distribution companies (WAC 480-90-223). The Commission could consider revising this rule to permit cost recovery of such advertising when it is directed toward encouraging connection to gas in under and unserved areas.

WAC 480-90-223 currently prohibits the collection of costs for “promotional advertising,” and defines “promotional advertising” in such a way that would likely capture the types of advertising described by the Commission. Thus, in order for the Commission to implement such a revision to the rule, the Commission would be required to conduct a rule-making proceeding in compliance with RCW 34.05.310 through 34.05.395.

While this is an interesting idea and NW Natural would support it, by itself recovery of promotional advertising would likely not result in significant system expansion, given that the advertising itself would not address the consumers’ first cost barriers associated with the conversion to natural gas from another fuel. Such an approach to advertising costs could, however, be an effective part of a more integrated approach to removing cost barriers for new customers, and communicating those programs to customers.

5. On-Bill Financing. RCW 80.28.065 authorizes local distribution companies to offer on-bill financing for energy conservation measures. The Commission seeks comments on whether local distribution companies are interested in pursuing on-bill financing as an option for customers to finance line extensions over a longer period of time than current tariffs allow.

RCW 80.28.065 allows a utility to carry the repayment charges on a customer’s energy bill when the funds borrowed are used to cover the installed cost of a conservation measure. Although NW Natural may be supportive of the option described by the Commission, it is not clear if the installation of a gas main and service line would qualify as part of the installed cost for financing under this statute. NW Natural believes that the Commission could reasonably interpret the law as applying, if it determined that replacing existing non-gas fired-heating equipment with high efficiency natural gas-fired equipment was a cost effective method of attaining energy conservation.

The Company supports the development of financing options for customers to convert to natural gas. The first cost barrier could be significantly mitigated or removed if low interest loans with flexible underwriting criteria were made available to prospective customers.

When NW Natural has looked into this type of program in the past, we found that the primary challenge is in finding a third-party financial institution that is interested in financing these

types of consumer loans without having the utility secure the loan portfolio. Additionally, if the loans are secured against the customer's home, the utility then must comply with a number of federal financing laws that may create significant additional compliance and administrative costs that the utility may not be able to support. Ideally, an on-the-bill payment program would need to be a tariffed service that can be structured so as to fall outside of the federal financing laws.

Additionally, we believe it would be important that any type of financing program for a substantial investment include an authorization for utilities to disconnect for nonpayment of such financing (in order to protect other customers), and it would be necessary to revise the existing rules around prior obligations as well.

6. *Infrastructure Fund.* To the extent that installation of new infrastructure would result in incremental tax revenues (such as public utility taxes), the incremental revenues could be used to secure bond financing for some of the infrastructure.

NW Natural would support the Commission promoting expanded infrastructure projects through tax increment financing. The Washington legislature approved this type of "Community Revitalization Financing" in Chapter 39.89 of the Revised Code of Washington. The purpose of Chapter 39.89 is to "finance public improvements that are designed to encourage economic growth and development in geographic areas characterized by high levels of unemployment and stagnate employment and income growth." RCW 39.89.10. The local government that would benefit from incremental tax revenue resulting from utility franchise or privilege taxes could seek bond approval to support the expansion of gas service into Washington state communities pursuant to Chapter 39.89 of the Revised Code of Washington. If the Commission sought to expand tax increment financing beyond geographic areas marked by unemployment and stagnate income growth, it would likely need a legislative action expanding the tax increment financing for public utility infrastructure projects.

7. *Pilot Rules.* To the extent it may be necessary to develop different policies for different geographic locations, or to experiment with one or more methods or strategies discussed in this notice, it may be useful to adopt "pilot rules" under the Administrative Procedure Act, which authorizes such rules. RCW 34.05.310(2)(b); 34.05.313.

NW Natural agrees that it may be appropriate for pilot rules to be established as the Commission works to determine the appropriate approach to system expansion.

8. *Local Construction Costs and Impact Fees.* The Commission seeks data or specific examples from local distribution companies concerning the specific costs companies or their customers have experienced when constructing or expanding gas distribution infrastructure including impact fees and the costs of other local requirements.

Jurisdictional fees and access restrictions can burden new customers with incremental and sometimes excessive costs, which may make the upfront cost of service prohibitive. Construction permits for a typical gas conversion job average around \$180 in the City of Vancouver. In cases where customers are required to contribute for service, this permitting fee alone would add an additional contribution of approximately \$230 when grossed up for taxes.

A larger barrier exists when utility construction access is denied because of a paving moratorium. Below are some typical scenarios, which NW Natural hopes may help illuminate the relevant issues for the Commission.

Typically, paving moratoriums last 3 to 5 years, but they can be extended by jurisdiction.

If we identify a moratorium prior to installing a new service, then the job is measured, and if we are unable to identify an alternate route, the incremental costs associated with the moratorium are passed on to the consumer. In most cases the consumer declines to move forward with the installation because these costs are prohibitive.

In some cases, a consumer and the utility agree to a new service installation before the utility knows that a moratorium is in effect. Although it is the Company's practice to inquire about the existence of a moratorium of the consumer, the requesting consumer also may not know that there is a moratorium in effect in their neighborhood. NW Natural does not currently have a means to reflect moratorium areas in its mapping system because the local jurisdictions often do not communicate their moratorium decisions.

In the instances where a new service is agreed to before the existence of a moratorium is known, the utility may not become aware that a moratorium is in effect until it finishes the permitting process (which, depending on the jurisdiction, could take 1 to 3 weeks). In some instances, by the time we discover that a moratorium is in effect, the consumer may have already begun making the interior changes needed to accommodate the equipment installation. In this case, the utility must mobilize resources to find an alternate route for providing service, which may include a service double off from a nearby neighbor, or the need for specialty equipment (e.g. an expensive drill operation) – and possibly a main extension from a different street. This then not only increases the cost of providing service, but typically extends the time to provide service an additional 4 to 6 weeks. For commercial applications this may also include performing the work at night.

NW Natural offers these examples of recent experience to highlight that local jurisdictional requirements often add significant costs and complexity to new service installations and system expansions.

9. *Concurrent Construction Projects.* The Commission seeks comments on how it might assess the economic feasibility of expanding natural gas service concurrently with other utility infrastructure or construction projects

NW Natural believes that it is important for the Commission to view utility investments in the context of all factors that bear on the economics of those investments. As the Commission notes, in certain instances, the timing of other utility infrastructure or construction projects may make it economic for a gas company to coordinate a project with those projects, even though the timing of the gas company's project would otherwise be later. While allowing a utility to make such determinations clearly would be in the interest of customers (because it would take advantage of more favorable economics), utilities can sometimes be concerned about whether such investments would be viewed as "used and useful" if accelerated. For this reason, it would be useful for the Commission to clarify that investments that are accelerated in order to take advantage of favorable economics are used and useful in providing utility service.

10. *Other Strategies and Methods.* Interested parties should submit comments to the Commission concerning any other strategies or methods that would be useful to consider in taking action or developing rules to expand natural gas infrastructure to unserved and underserved areas in Washington.

NW Natural believes that capital cost recovery mechanisms are an important tool that the Commission should consider to encourage the expansion of natural gas infrastructure. To the extent that gas utilities are able to recover their investments in a timely manner, NW Natural believes that they will make those investments. As is the case with safety-related system investments, NW Natural believes a cost tracking mechanism would also be appropriate for infrastructure expansion projects.

NW Natural appreciates the opportunity to comment in this docket. Please contact Jennifer Gross at (503) 226-4211, extension 3590, if you have questions regarding our comments.

Thank you.

Sincerely,

/s/ Mark R. Thompson

Mark R. Thompson