

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION
Complainant,

v.

NORTHWEST NATURAL GAS
COMPANY,

Respondent.

DOCKET UG-18____

**NORTHWEST NATURAL GAS COMPANY
Direct Testimony of Zachary D. Kravitz
WASHINGTON ENVIRONMENTAL COST RECOVERY MECHANISM
Exh. ZDK-1CT**

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PER WAC 480-07-160**

December 31, 2018

DIRECT TESTIMONY OF Zachary Kravitz

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I. INTRODUCTION AND SUMMARY

Q. Please state your name and position with Northwest Natural Gas Company (“NW Natural” or “the Company”).

A. My name is Zachary D. Kravitz. My current position is Director of Rates and Regulatory Affairs for NW Natural.

Q. Please describe your education and employment background.

A. I received a Bachelor of Arts degree in English and Government from the University of Texas at Austin in 2005. I received a Juris Doctor degree from the University of Florida in 2008. From 2009 through 2011, I worked at the Ohio Attorney General’s Office in the Labor Relations Division. From 2011 through 2014, I worked in the energy and utility practice at the law firms of Chester, Wilcox & Saxbe, LLC, and Taft, Stettinius & Hollister, LLP in Columbus, Ohio.

I joined NW Natural’s legal department in 2014 as associate regulatory counsel. In 2018, I joined the Rates and Regulatory Affairs department in my current position.

Q. What is the purpose of your testimony?

A. The purpose of my testimony is to present NW Natural’s request for past and future recovery of its environmental remediation expenses related to historic gas manufacturing plants (MGPs) that served the Company’s Washington customers.

Q. Please summarize your testimony.

A. My testimony will describe and support the Company’s proposed environmental remediation cost recovery mechanism for MGPs. As discussed in the Testimony of Andrew Middleton, these MGPs were operated by NW Natural and its predecessors dating back to 1913, consistent with prudent practices of the day. As explained by NW

1 Natural witness Robert Wyatt in Exh. RJW-1T, the environmental remediation costs
2 associated with these MGPs were prudently incurred by the Company pursuant to
3 applicable state and federal law, and by order of governmental agencies, under a
4 statutory framework that governs NW Natural's responsibilities related to remediation
5 of past gas manufacturing operations.

- 6 • My testimony will begin by quantifying the environmental remediation
7 expenses incurred through November 30, 2018 (past environmental
8 remediation expense), as well as the insurance proceeds and other third-
9 party payments collected by the Company to date, that offset those costs. I
10 then describe NW Natural's proposal for recovering both past and future
11 environmental remediation costs. Specific to past environmental
12 remediation expense incurred, NW Natural asks that the Commission: Find
13 that the environmental remediation costs incurred through November 30,
14 2018, were prudently incurred and recoverable in rates; and
- 15 • Order that past environmental costs should be fully offset by the insurance
16 proceeds and other third-party payments received by the Commission to
17 date.

18 Specific to environmental remediation costs incurred in the future (future
19 environmental remediation costs), NW Natural asks that the Commission adopt a
20 recovery framework that:

- 21 • Provides for annual reporting and annual prudency review of future
22 environmental remediation costs, beginning in March 2020;

- 1 • Allows the Company to apply all remaining insurance proceeds and third-
- 2 party payments to environmental remediation expenses;
- 3 • Allows the Company to apply any insurance proceeds or third-party
- 4 payments received in the future to offset then-current environmental
- 5 remediation costs; and
- 6 • Allows the Company to recover prudent remediation costs, as offset by
- 7 applicable insurance proceeds and third-party payments, by tracking these
- 8 costs into rates through the annual PGA filing with a rate effective date of
- 9 November 1 of every year.

10 **II. PAST ENVIRONMENTAL REMEDIATION EXPENSE INCURRED**

11 **Q. Please provide a high-level description of the environmental remediation costs for**

12 **which the Company is proposing recovery in this case.**

13 A. The costs for which the Company requests recovery in this case are related to NW

14 Natural’s environmental remediation efforts at certain sites impacted by the Gasco

15 MGP (Gasco or the Gasco Plant). NW Natural's predecessor in interest, Portland Gas

16 & Coke Company, owned and operated the Gasco Plant from 1913 to 1956, during

17 which time Gasco produced gas that was used to serve that Company's Oregon and

18 Washington customers. Gasco ceased operation in 1956, and in the late 1960's most of

19 the gasification facilities were dismantled and removed. Over the past decade, NW

20 Natural has been required by state and federal agencies to perform environmental

21 remediation at five sites located on and around the original Gasco plant -- Gasco,

22 Wacker a/k/a Siltronic, Portland Harbor, Tar Deposit, and Central Gas Holdings. These

23 sites are referred as “shared sites” given that the costs of these efforts are allocable to

1 both Oregon and Washington customers. Since 2011, NW Natural has been deferring
2 the Washington-allocable portion of these costs pursuant to Order No. 01 in Docket
3 UG-110199, as well as the insurance proceeds and other third-party payments received
4 by the Company in connection with these costs.

5 **Q. Has the Company been engaged in similar remediation efforts for which it is not**
6 **requesting recovery in this case?**

7 A. Yes. The Company has also been performing similar remediation work at several sites
8 impacted by an MGP plant that did not serve Washinton customers. Those sites are
9 referred to as “non-shared” sites, and the costs of that work are not allocable to
10 Washington customers.

11 **Q. Please describe the insurance proceeds and third-party payments received by the**
12 **Company in connection with its environmental remediation costs at both the**
13 **shared and non-shared sites.**

14 A. In 2008 the Company instituted litigation against several insurance carriers, in order to
15 maximize its recovery and to offset as fully as possible the costs of remediation that
16 would otherwise be borne by its customers. Ultimately the Company received
17 approximately \$152.8 million in insurance and third-party proceeds that offset the
18 environmental remediation costs at both its shared and non-shared sites. The Company
19 may receive additional insurance proceeds and third-party payments in the future. In
20 addition, the Company may receive proceeds from other third-party owners and

1 operators found responsible for contamination of the Portland Harbor Site – known as
2 Potentially Responsible Parties (PRPs) – that would offset remediation costs.¹

3 **Q. What is the total amount spent by NW Natural in performing the remediation**
4 **work at the shared sites?**

5 A. As of November 30, 2018, the Company has spent \$136.2 million on remediation work
6 at the shared sites. Please see Exh. ZDK-2C.

7 **Q. What percentage of the remediation expense incurred at the shared sites related**
8 **to service to Washington customers?**

9 A. Based on historical records, NW Natural estimates that 3.32 percent of its remediation
10 costs assigned to the shared sites are related to Washington customers. This percentage
11 is based on the percentage of gas from the Gasco Plant facility that was sold to
12 Washington customers during the period it was in operation through 1956, when the
13 plant ceased operations. Exh. ZDK-3 provides the calculations that support the
14 3.32 percent figure.

15 **Q. Has the 3.32 percent sharing allocation been approved by the Washington**
16 **Commission?**

17 A. No. In a supplemental UG-110199 petition filed July 17, 2012, the Company proposed
18 to the Washington Commission an allocation of 3.32 percent deferred costs due to
19 historic MGP service in Washington. That petition was not acted upon, and NW
20 Natural was informed by Staff that the Commission would not act upon this request
21 until the Company actually sought rate recovery in Washington.

¹ Please refer to Exh. RJW-1CT, page 8, lines 7-8.

1 **Q. Does the Company continue to propose that Washington customers bear 3.32**
2 **percent of the costs associated with the shared sites?**

3 A. Yes. NW Natural continues to believe the 3.32 percent sharing allocation is appropriate
4 as demonstrated in Exh. ZDK-3.

5 **Q. Please quantify the deferred shared sites expense as of November 30, 2018.**

6 A. As of November 30, 2018 the Company had deferred \$3.0 million of expenses for
7 remediation efforts at the five shared sites. This amount represents 3.32 percent of total
8 remediation expenses at these sites incurred after January 26, 2011. In accordance with
9 UG-110199 Order 01, interest has not been accrued on these balances. The table below
10 breaks this expense down by each of the five shared sites:

Gasco (a)	\$2,603,422
Portland Harbor	318,131
Tar Deposit	18,093
Siltronic (b)	54,276
<u>Central Service Center</u>	<u>22,906</u>
Total shared sites	\$3,016,828

(a) Includes Uplands, Sediments, Source Control operating costs and insurance litigation costs.

(b) Costs incurred prior to Siltronic project being combined with Gasco Uplands according to an agreement with DEQ.

This amount represents the environmental remediation expense allocable to NW Natural's Washington customers.

11 **Q. Has the Company incurred expenses at the shared sites that are not deferred?**

12 A. Yes. Prior to the filing date of NW Natural's petition seeking an Accounting Order in
13 UG-110199, NW Natural incurred remediation expenses related to efforts at the five
14 shared sites. The portion related to service to Washington customers is \$1.5 million,

1 which represents 3.32 percent of total remediation expenses at these sites. NW Natural
2 is not seeking to allocate to these pre-deferral expenses to Washington customers.
3 However, these pre-deferral expenses are relevant to the Company's request in this
4 case, because we are seeking to apply insurance proceeds and third-party payments
5 allocable to Washington to all of the environmental expenses associated with service
6 to Washington customers.

7 **Q. Please quantify the insurance proceeds and third-party payments that the**
8 **Company proposes to use to offset environmental expenses associated with service**
9 **to Washington customers.**

10 A. As of November 30, 2018, the Company had received a total of \$152.8 million in
11 insurance proceeds and third-party payments related to its remediation expenses at the
12 shared and non-shared sites. NW Natural proposes to use 3.32 percent of these
13 insurance and third-party proceeds to offset the total environmental remediation
14 expense attributable to the shared sites. Using this approach, the Company proposes
15 that \$5.1 million of the total insurance and third party payments received be applied to
16 the the \$4.5 million in environmental remediation expense related to service to
17 Washington customers, as of November 30, 2018.

18 **III. PRUDENCE REVIEW AND TREATMENT OF EXPENSES INCURRED AND**
19 **INSURANCE PROCEEDS**

20 **Q. What treatment does the Company propose for its past environmental expense**
21 **related to the shared sites?**

22 A. NW Natural proposes that all past environmental remediation costs related to the shared
23 sites as of November 30, 2018 be reviewed and found to be prudently incurred. The

1 Company believes the Semi-Annual Report on Environmental Costs² filed with the
2 Commission, and the testimonies of Messrs. Middleton and Wyatt provide substantial
3 record for a determination of prudence of environmental remediation expenses. The
4 Company also requests that the Commission approve NW Natural's allocation to
5 Washington customers of 3.32 percent associated with the shared sites costs.

6 **Q. What treatment does the Company propose for insurance proceeds received as of**
7 **the end of November 30, 2018?**

8 A. NW Natural proposes that the Commission find that 3.32 percent of these insurance
9 proceeds – totaling \$5.1 million – should be used to offset the Company's expense
10 related to service to Washington customers, leaving an insurance balance of \$0.6
11 million.

12 **Q. What treatment does the Company propose for the remaining insurance**
13 **proceeds?**

14 A. NW Natural proposes that the remaining insurance proceeds be applied against shared
15 sites expenses incurred after November 30, 2018, until they are exhausted.
16 Accordingly, all insurance proceeds would be exhausted before the Company would
17 seek to recover any remediation expenses from customers.

18 **IV. WASHINGTON ENVIRONMENTAL COST RECOVERY MECHANISM**

19 **(ECRM) PROPOSAL**

20 **Q. Please summarize your Washington Environmental Cost Recovery Mechanism**
21 **(ECRM) proposal.**

² Per UG-110199 Order 02, this report will be filed annually beginning March 2019.

1 A. NW Natural proposes an annual review of the prudence of its future environmental
2 remediation costs allocable to Washington customers. This review would be a part of,
3 and coincide with, a Washington Environmental Cost Recovery Mechanism (ECRM)
4 Regulatory Report filed annually in March.³ Prudent costs would be amortized
5 annually, via a simple cost recovery mechanism, and tracked into the annual PGA filing
6 with a rate effective date of November 1 of that year.

7 **Q. Please summarize NW Natural's Washington environmental remediation cost**
8 **reporting to date.**

9 A. Beginning March 26, 2012 and through March 15, 2018, NW Natural has filed with
10 the Commission semi-annual reports on its deferred environmental expenses and
11 balances.

12 **Q. Please describe NW Natural's reporting requirement beginning March 2019.**

13 A. UG-110199 Order 02 establishes, beginning March 1, 2019, that NW Natural will file
14 with the Commission an annual report on its deferred environmental expenses and
15 balances, "as well as provide a narrative summary along with a timeline summarizing
16 the status of each environmental remediation project."⁴ Per Order 02, the goal of the
17 new reporting requirements is to "assist Commission Staff in monitoring the
18 Company's compliance with its remediation obligations."⁵

19 **Q. What modifications does NW Natural propose for this annual reporting**
20 **requirement?**

³ The report the Company currently files is referred to as the "Semi-Annual Report on Environmental Costs."

⁴ See UG-110199 Order 02, paragraph 4.

⁵ *Ibid*, paragraph 5.

1 A. The annual report process does not specify that the Commission will make a prudency
2 determination based on the report. NW Natural proposes that the annual report process
3 provide that each year, based on the information included in the report, or such
4 additional information that may be requested by the Commission or its Staff, the
5 Commission will determine the prudency of the costs incurred for all Washington
6 allocable shared sites costs over the prior calendar year. The first annual report to
7 include a test of prudency would be the first report to be filed after the rate effective
8 date of this rate case, on March 1, 2020.

9 **Q. What timeline does the Company propose for the prudency review?**

10 A. Beginning March 1, 2020 the Company would submit its first annual report for
11 prudency review, and on March 1 of every year thereafter. The annual report would
12 detail the Company's recorded expenditures for environmental remediation activities
13 at the shared sites since the last month prudently incurred expenses were placed into an
14 account (the "ECRM Account") for deferral, up through the end of the prior calendar
15 year. The recorded expenditures included in the annual report would equate to one
16 year's worth of Washington allocable remediation expenses.⁶ The Company would
17 also report the receipt of any insurance or other third-party proceeds related to its
18 remediation activities during that same time period. Between March 1 and the
19 Company's PGA filing date of each year (usually September 15), the parties,

⁶ For example, the March 2022 report would seek prudency review of remediation expenses incurred from January 2021 through December 2021 for recovery in the 2022-2023 PGA effective November 1, 2022.

1 Commission Staff, and ultimately the Commissioners would have an opportunity to
2 review these costs and receipts to determine that they were prudently incurred.⁷

3 **Q. Will the first annual report following this rate case include environmental**
4 **remediation expenses incurred prior to the preceding 12 months?**

5 A. Yes. Since we propose recovery of costs up through November 30, 2018 in this
6 proceeding, the first annual report with prudency review obligation would include
7 deferred shared sites expenses for December of 2018 in addition to the calendar year
8 2019 expenses. All annual reports thereafter would be based on calendar year
9 expenses.

10 **Q. What cost recovery mechanism does NW Natural propose for costs that are**
11 **deemed prudent after the review period?**

12 A. Once the expenses are determined to be appropriately recoverable in rates through the
13 annual reporting process, we propose that the remediation expenses – net of all
14 available Washington allocable insurance proceeds – be transferred to the ECRM
15 Account. The ECRM Account will be amortized into rates over a one-year period via
16 the proceeding PGA, effective November 1 of that year.

17 **Q. How do you propose to spread the amortized expense across rate schedules?**

18 A. The annual environmental remediation deferral amount placed in the ECRM Account
19 would be collected from all customers by applying a percentage of the costs to each
20 class that is equal to the percentage of margin that is paid by that class as of that PGA
21 year.

⁷ The Company proposes a prudency review cut-off date about two weeks prior to the PGA filing date, or September 1 annually.

1 **Q. How will the Company treat negative deferral balances?**

2 A. It is possible that in some future year, recoveries from insurance providers or other
3 third-party payments allocable to Washington will more than fully offset shared sites
4 expenses. NW Natural proposes amortizing the amount over one year and returning
5 the deferral balance in the ECRM Account to customers through the PGA filing
6 effective November 1 of the year immediately following the negative balance year. A
7 credit balance may be carried, however, to the next PGA filing if it is determined by
8 the Commission that the credit balance is best used to offset future expected
9 environmental site remediation costs not yet recorded in the deferral account, or for
10 such other reasons as the Commission may approve.

11 **Q. Please explain why you believe that the proposed ECRM will benefit customers?**

12 A. The proposed ECRM will allow for the environmental remediation expenses to be
13 recovered over time, as they are incurred, instead of allowing large deferral balances to
14 accrue between the Company's rate cases. This approach will better match costs and
15 benefits and will improve generational equity.

16 The mechanism would also accommodate uncertainty regarding future
17 recoveries and costs by adjusting the amount of recoveries in the future to reflect costs
18 as they are incurred, net of any available insurance recoveries or other third-party
19 payments. The mechanism also allows for recovery to be based on actual costs,
20 avoiding the over- or under-recovery that would result from basing collections strictly
21 on a forecast of costs or receipts.

22 **V. IMPACTS OF THE ECRM PROPOSAL ON CUSTOMER RATES**

23 **Q. What will be the impact of the ECRM proposal on customer rates at the effective**

1 **date of this rate case?**

2 A. There will be no impact on customer rates due to this proposal at the time new rates go
3 into effect with this rate case. There will be no impact because the deferred remediation
4 expenses will be offset by Washington allocated insurance proceeds. The net balance
5 of insurance proceeds would be \$0.6 million.

6 **Q. When will the ECRM proposal, if approved, begin to affect customer rates?**

7 A. This proposal would not impact customer rates until the first PGA filing after the
8 effective date of this rate case. This would be the filing for the 2020-2021 PGA year.
9 The Company expects that shared sites remediation expenses allocated to Washington
10 will achieve a net positive balance for the first time in the latter half of 2019.

11 **Q. Please summarize the estimated impact of the ECRM proposal on customer rates
12 beyond the rate case effective date.**

13 A. During the first year this mechanism is in effect beyond the effective date of this rate
14 case, the impact to rates beginning the 2020-2021 PGA year will be minimal due to the
15 availability of insurance proceeds to off-set much of the remediation costs in 2019.
16 We anticipate that residential and small commercial rates would rise by 0.4 percent in
17 that PGA year relative to current rates. Anticipating the rate impact in future years can
18 be difficult because the annual remediation costs and third-party recoveries are not
19 generally smooth year-to-year, but we expect beginning the 2021-2022 PGA year and
20 through at least the 2024-2025 PGA year the rate impact to residential and small
21 commercial customers will be between 0.6 percent and 0.7 percent in each year relative
22 to current rates.

- 1 **Q.** Does this conclude your testimony?
- 2 **A.** Yes, it does.

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VI. LIST OF EXHIBITS

Exh. ZDK-2.....	Redacted Total Environmental Remediation Spend and Insurance Recoveries
Exh. ZDK-2C.....	Confidential Total Environmental Remediation Spend and Insurance Recoveries
Exh. ZDK-3.....	Derivation of State Allocation of Environmental Deferrals