

**BEFORE THE WASHINGTON STATE UTILITIES AND TRANSPORTATION
COMMISSION**

Rulemaking to Review Natural Gas
Decoupling

DOCKET NO. UG-050369

PRELIMINARY COMMENTS OF
PUBLIC COUNSEL

**PUBLIC COUNSEL'S PRELIMINARY COMMENTS REGARDING GAS
DECOUPLING;**

COMMENTS ON CASCADE WHITE PAPER

May 10, 2005

INTRODUCTION: THE PURPOSE OF DECOUPLING

There are two primary purposes of decoupling revenues from sales volumes. Decoupling reduces risks and associated capital costs for the utility allowing the benefits to be passed on to ratepayers. Second, by eliminating the disincentives for utility investment in energy efficiency that results when profits are linked to sales volumes, energy efficiency efforts can be advanced.

Because of the reduction of risk to the utility, decoupling mechanisms must include an explicit adjustment to the cost of capital to reflect the shift of risk to ratepayers. This risk shifting element of decoupling has been widely recognized in the professional literature. This is an essential element of any decoupling proposal, and in order to be fruitful, any discussions of decoupling must include a commitment to recognize and quantify this impact.

Decoupling proposals should also identify the energy efficiency programs that a company would intend to offer if the decoupling mechanism were approved. Incentives for utility investment in energy efficiency are the most important justification for decoupling discussed by decoupling advocates (see, e.g., testimony of NRDC and NWECA in Puget Docket UE-011570).

ALTERNATIVE DECOUPLING MECHANISMS AND THE CASCADE WHITE PAPER

The workshops will provide an opportunity to review and evaluate a variety of theoretical and actual examples of decoupling mechanisms. Some initial observations, prompted by Cascades' White Paper, are discussed below.

The Cascade White Paper does not provide much detail about how the proposed decoupling mechanism will work. Cascade's White Paper is silent on energy efficiency programs and on a cost of capital adjustment. Due to the lack of detail, the exact components of the decoupling mechanism proposed in Cascades White Paper are open to interpretation. Two alternative interpretations, which we term "True Decoupling" and "Fixed-Variable" rate designs, are discussed below. Cascade can clarify its proposal at the workshop, but Public Counsel takes the opportunity to make some observations about the two possible interpretations.

Alternative 1: A "True Decoupling" Mechanism

In a general rate case, Cascade rates would be set as they are now, with a customer charge to recover meter reading and billing costs, a delivery charge per therm of natural gas, and a gas supply charge to cover purchased gas expenses. The current rate design, simplified to remove fractions, is:

Customer Charge:	\$5.00
Delivery Charge:	\$.22/therm
Gas Charge:	\$.69/therm

Each year, at the end of the year, the Commission would compare actual sales volumes to projected test year sales volumes (with, we assume, some adjustment for customer count), and adjust the delivery charge to collect under-recoveries or to rebate over-recoveries. New rates would be set for the ensuing year. Assuming 10% deviation in sales volumes (up or down), the

result would be:

	10% Increase in Sales	10% Decrease in Sales
Customer Charge	\$5.00	\$5.00
Delivery Charge	\$.198/therm	\$.242/therm
Gas Charge	\$.69/therm	\$.69/therm

Under this approach, customers would see approximately the same incremental cost per therm for gas that they now see (+/- 2%), and incentives to conserve in response to price would be unaffected.

A true decoupling mechanism has a number of details that would need to be resolved, and we should not underestimate the complexity of resolving those details. Commission orders regarding Puget's Periodic Rate Adjustment Mechanism (PRAM), in effect from 1990 to 1995, contain a rich discussion of some of these issues. The basic principle, however, is to allow the utility to recover its delivery costs independent of sales volumes through a periodic true-up mechanism to recover or rebate deviations from allowed levels. While the details are important, they do not affect this underlying principle.

Alternative 2: A "Fixed-Variable" Rate Design

Some language in the White Paper suggests that Cascade is proposing something more akin to a fixed/variable rate design, with a fixed monthly charge to recover all delivery costs independent of sales volumes and a gas charge per therm to recover only gas supply costs. If this interpretation is accurate, the proposed rate design would look something like one of the following:

Option One

Customer Charge	\$25.00
Delivery Charge	None
Gas Charge	\$.69/therm

Option Two

Customer Charge	\$5.00
Delivery Charge, First xxx therms/year, individually calibrated for each customer based on low-year usage	\$.50
Delivery Charge, Additional Therms	\$.02
Gas Charge	\$.69/therm

This approach would prevent any revenue attrition to Cascade from variation in sales volumes, but would also provide customers a strong incentive to use more gas. The incremental rate per therm of gas would be about 25% lower than under traditional cost-based rate designs. Assuming an elasticity factor of -.3, the expected result would be approximately a 7% - 8% increase in natural gas consumption. This is not consistent with a fundamental purpose of decoupling --- to foster a greater commitment to energy efficiency, rather than an incentive for greater consumption.

The first option above would be particularly detrimental to implementation of the State Energy Strategy, which calls for expansion of natural gas to additional customers, particularly low-use multi-family customers. A fixed/variable rate design that is not customer-specific would essentially make natural gas service uneconomic for an entire class of small-use customers. The second option would leave gas service attractive to customers, but would implement a scheme whereby increased usage would be attractive. Neither is an acceptable outcome of any rate design discussion, much less a decoupling discussion.

CONCLUSION

We look forward to participating in the Commission's decoupling workshop. We offer these initial comments because we believe discussions will be most productive if they begin with the basic principles behind decoupling and the essential components of a decoupling mechanism.