Decoupling Through
A Payment Stabilization Mechanism

White Paper
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The February 2005 issue of the AGA American Gas Magazine's cover story is an article entitled **It's Now Easier Being Green**, by S. Lawrence Paulson. This article describes the current status on the natural gas industry very well: Energy efficiency benefits consumers; conservation helps the nation by conserving a valuable domestic resource; and utilities that promote conservation are given high marks by their customers**.** Unfortunately, the old established ratemaking principals create financial impediments for the utility to promote conservation.

The distribution of natural gas to customers is a capital-intensive enterprise. Virtually all of the costs to maintain and operate the distribution system remain constant as changes in volume occur. Other than the costs of the gas supply itself, the only true variable operating cost is associated with odorizing the gas delivered; the more gas delivered, the more odorant injected. However, traditional rate design assigns the recovery of most of these fixed costs to the commodity, or the per therm rate. As such, the utility only receives full recovery of its fixed costs if its customers consume the "normal" amount as established in the last general rate case.

This rate design discourages the utility from doing anything that is going to adversely affect therm sales, including the promotion of conservation. The company's financial responsibilities and corporate citizenship responsibilities are at odds. The utility is forced to choose between conservation and profitability.

It is in the public interest to promote conservation and energy efficiency. Utilities should be encouraged to find ways to overcome current rate design disincentives to promote conservation. The need for doing so was highlighted by the joint statement of American Gas Association and the Natural Resources Defense Council at the summer meeting of the National Association of Regulatory Utility Commissioners. The statement encouraged "innovative programs that reward utilities for encouraging conservation and managing customer bills to avoid certain negative impacts associated with colder-than-normal weather"

Northwest regulators are acting to promote energy efficiency. The Oregon PUC granted Northwest Natural a mechanism to decouple fixed cost recovery from volumetric sales as well as a mechanism to stabilize cost recovery in fluctuating weather. The WUTC conducted a workshop in October 2004 to learn about Northwest Natural's mechanisms, and has opened a rulemaking to investigate decoupling and ways to promote energy efficiency. We at Cascade fully support these efforts as we believe that implementation of a decoupling mechanism is in the best interests of customers, utilities, consumer and environmental advocates, the Commission and its staff, as well as society as a whole.

As Cascade began studying the various alternative approaches to decoupling, we envisioned developing a mechanism that would maximize the benefits to all stakeholder groups. We wanted to sever the relationship between cost recovery and throughput. The model should encourage the promotion of conservation. We wanted to design a program that would be

easy to understand. We wanted a program that could be implemented within our current Customer Information System (CIS). And we wanted a program that would reward our customers for conserving and thereby engage our customers in the pursuit of conservation and energy efficiencies.

We have developed a new payment stabilization mechanism that we believe will provide benefits to all the stakeholders, will be easy to implement and administer, and will be simple to understand. Our new payment stabilization mechanism will produce consistent margin from all customers served under this program. We envision applying the mechanism to all of our residential and commercial customers.

Stabilized Delivery Charge

The mechanism we designed is derived from Cascade's existing Budget Payment Plan process. However, the payment stabilization mechanism is designed to have the margin remain constant, while the gas cost commodity charges follow actual consumption, as it does now. We plan to introduce our mechanism to our customers as the Conservation Rewards Plan. In order to emphasize the importance of conservation, our mechanism calculates each customer's delivery charge per month based upon the lowest annual consumption of the past three-year history.

We are proposing to base the first past-three-year history on the twelve months ended June 30, 2003, the twelve months ended June 30, 2004, and the twelve months ended June 30, 2005, for each and every residential and commercial customer. From this information, we will pick the 12-month ended June period with the lowest consumption and the monthly therms identified from that period will become the "delivery billing units" for the upcoming year. The following is an example of the data that will be used to identify the lowest annual consumption during the most recent three-year period. In this example, next year's monthly delivery charges would be based upon each month of the twelve months ended June 2004, the historical low:

	Historical Therms used		Historical Therms used		Historical Therms used
July-02	10	July-03	8	July-04	12
August-02	8	August-03	10	August-04	11
September-02	10	September-03	8	September-04	12
October-02	40	October-03	38	October-04	45
November-02	80	November-03	62	November-04	55
December-02	120	December-03	100	December-04	120
January-03	130	January-04	180	January-05	170
February-03	140	February-04	145	February-05	140
March-03	80	March-04	70	March-05	80
April-03	50	April-04	30	April-05	55
May-03	20	May-04	25	May-05	20
June-03	15	June-04	10	June-05	10
Total	703	Total	**686**	Total	730

Calculation Of Billing Unit Rate

After we have identified the base "delivery billing units" for all customers, we sum the total annual volume of billing units by the residential general service rate schedule 503 and commercial general service rate schedule 504.1/ We calculate the revenue requirement of each general service rate schedule by multiplying the margin per customer by the average number of customers in the latest period ended June 30. We then divide that margin requirement by the total "delivery billing units", to derive our delivery billing unit rate for the upcoming year. We picked the 12 months ended June 30, to correlate with the timing of the PGA application. We plan to file the application to update the delivery billing unit rate each year at the same time we file the PGA, with the same effective date. This will allow us the opportunity to notify the customer of final actual rate per delivery billing unit.

By multiplying the average customers reflected in the latest twelve months by the margin-per-customer amount, we reflect the growth that occurred during the year, and our revenue requirement by rate schedule is higher because of it. This provides the Company the incentive to continue to invest in facilities to meet our obligation to serve. The average margin per customer per rate schedule will remain constant between rate cases, but the unit rate to recover that margin will track the annual changes in total "delivery billing units".

Customer Benefits

Individual customers will see monthly "delivery billing units", tailored specifically to their historical low consumption patterns. They will be able to track how their actual consumption is comparing to their individual historical low, and thus, how successfully they are conserving. Additional space on the monthly bill will be devoted to providing a customer an energy efficiency scorecard, conservation messages, and energy saving tips. Every year, a new historical low will be determined for each customer.

In addition to the ability to track individual conservation progress, the customer also benefits from a lower bill in cold winters, as compared to the current rate design. The price of the incremental therms consumed by the customers during colder than normal weather will be reduced by almost 25 percent. Rate relief for our customers will occur exactly when they need it the most - during cold weather. We will provide them with the lowest possible rate, cost of gas only, for those extra therms needed during the coldest months. If it is a warm winter and/or if the customer successfully conserves, he/she will benefit from lower delivery billing units, not just next year but the next three years. The customer should have a sense of

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1/ For customers with insufficient history and newly connected customers, we may calculate first year delivery charges based upon connected equipment and the expected annual gas use by that equipment or we may use actual consumption for both the delivery charges and gas supply charges while the customer is establishing a consumption history.

empowerment toward determining what they pay us for delivering their gas. The customer will pay more during warmer than normal periods under our proposed payment stabilization mechanism than under current rates, but the customers will avoid the cost of the gas supply not needed, and therefore can better afford to pay more. The Company's and our customers' interests will be better aligned; we charge more when the customer can better afford it and charge less when the customer can least afford it.

Comparison With The Decoupling And WARM Mechanisms

The proposed Conservation Rewards payment stabilization mechanism will eliminate the need for two separate systems. We will not need a decoupling mechanism to track usage patterns per customer and a separate weather normalization mechanism to track actual weather compared to normal. The Conservation Rewards Plan will normalize the recovery of fixed charges against changes in customer usage as well as weather fluctuations. One single plan makes sense for a small utility. The proposed mechanism is much simpler to administer than the Decoupling and WARM mechanisms. Most of the individual customers' billing unit data will be obtained directly from Cascade's Customer Information System with no further analysis required. Those accounts requiring analysis can be completed with summer workers or other temporary help. Developing the application and filing for the approval of the Delivery Unit Rate, along with the PGA, is within the capabilities of the existing Regulatory Affairs staff. 2/

Status of Development

We are very excited about this program. We are developing the CIS mainframe programs and exceptions reports necessary for implementation of the mechanism. We are developing and testing these programs and reports based upon the thirty-six months ended September 30, 2004. In addition to developing the proper process for implementation, the data we gather for delivery billing units should provide some interesting comparisons to the actual and weather normalized therm consumption included in FY04. We will continue to analyze this data in depth in the up-coming weeks. We are also drafting the tariff that will regulate this mechanism. We currently anticipate completing this project in time to implement the mechanism this fall, and we certainly hope that stakeholders support our proposal and that regulatory approval is timely.

2/ The implementation and administration processes for our proposed mechanism appear to be much simpler than the Decoupling and WARM mechanisms. Documenting these processes for compliance with the Sarbanes-Oxley Act is anticipated to be achievable with no incremental expense. Auditing the effectiveness of the mechanism should also be much simpler.