Agenda Date:	July 15, 2010
Item Numbers:	A2 and A3
Dockets:	UG-100847 and UG-100860
Company Name:	Cascade Natural Gas Corporation
Staff:	Rick Applegate, Regulatory Analyst – Energy Ann LaRue, Regulatory Analyst – Energy

Recommendation

Issue an order authorizing the transfer of property requested by Cascade Natural Gas Corporation in Docket UG-100860 to sell its Seattle general office and granting the approval of the petition for accounting treatment of the gains associated with the sale. This authorization for transfer of the property is subject to the accounting treatment proposed by Cascade Natural Gas Corporation in Docket UG-100847.

Discussion

On May 14, 2010, Cascade Natural Gas Corporation (Cascade or company) filed a petition seeking approval under WAC 480-143-120 of an agreement for the transfer of the company's general office buildings and land located at 222 Fairview Ave N and 230 Fairview Ave N in Seattle to Touchstone Corporation for $9.2 million ($1.8 million in cash and a promissory note with a principal value of $7.4 million).[1] The general office currently supports both Oregon and Washington natural gas operations. Under RCW 80.12.020 and WAC 480-143-120, a public service company must secure commission approval prior to completing the sale of a property necessary or useful in the performance of its duties to the public. WAC 480-143-170 also requires that the transaction be in the public interest and that, if it is not, the commission shall deny the application. Cascade acquired 222 Fairview in 1957 and 230 Fairview in 1986. Approval of the transfer will enable Cascade to advance its corporate integration plans by allowing the company to move many general office functions to a newly constructed facility built to Leadership in Energy & Environmental Design (LEED) standards in Kennewick, Washington. Cascade states that had it not elected to sell the general office and relocate to a newly constructed LEED certified facility in Kennewick, it would face significant renovation costs.

Also on May 14, 2010, Cascade filed an accounting petition in Docket UG-100847 requesting depreciation accounting treatment of the gains from the sale of the Seattle general office. The company will record the sale of the property, retirement of the building, and deferral for the gain for the sale of the land with the following journal entries:

[1] Numbers presented on an unallocated basis (i.e. combined Oregon and Washington operations).

Account	Debit	Credit
Cash	1,248,000[2]	
Notes Receivable	7,400,000	
Utility Plant – Land		696,777
Gain on Sale of Land		904,864
Accounts Payable - Tax Liability		2,596,395
Accumulated Depreciation – Building		4,449,964
Buildings & Improvements		6,561,328
Accumulated Depreciation – Building	6,561,328	
Gain on Sale of Land	904,864	
Accumulated Depreciation		904,864

The accounting petition filed in Docket UG-100847 provides an adequate explanation of the treatment of the gains from the office sale and the property transfer petition filed under WAC 480-143-120 in Docket UG-100860 contains all elements required under that rule.

Share of Gain on Sale

The proposed sale will generate significant value in excess of the facilities' current book value. Based on the equitable sharing principles of *Democratic Central Committee v. Washington Metropolitan Transit Comm'n*[3], the company must share a portion of the gain on the sale (i.e.,

[2] Equals $1.8 million less transaction costs of $552,000.
[3] 458 F. 2d 786 (D.C. Cir. 1973), *reh den, cert den,* 415 US 935 (1973); As this commission stated in its Second Supplemental Order, Order Approving Sale with Conditions (Centralia Coal), at ¶ 48, Docket Nos. UE-991255, UE-991262, UE-991409 (March 2000):

> A number of Commissions have applied the equitable-sharing principles of *Democratic Central* to justify a sharing of gain. See, for example, *Power & Light Co. v. State Corp. Comm'n of Kansas*, 5 Kan. App. 514, 529, 620 P.2d 329 (1980) (where the court, on review, reversed the Kansas commission's decision granting 100% of the gain from sale of a utilities headquarters building, and instructed the commission on remand to take into account the equities due to both the ratepayers and stockholders); *In the Matter of the Application of Southern California Gas Company for Authority pursuant to Public Utilities Code Section 851 to sell and lease back its*

the appreciation of the building above net book value) with Washington customers for the sale to be in the public interest.

After transaction costs and taxes, the $9.2 million sale price will yield net proceeds of $6,051,605. Because the Seattle general office currently has a net book cost of $2,763,729, Cascade would have realized significant earnings and free cash from the transaction had the company not replaced the general office and not proposed depreciation accounting treatment of the gains.

Under the company's accounting petition, Cascade will credit the gains from the sale to accumulated depreciation. This treatment reduces the company's rate base in excess of the current book value of the property and leaves the company's 2010 net operating income unaffected by the sale. While this does not return to the ratepayers in cash any of the difference between the net sale price and the net book value, it does allocate the benefits of the sale to the ratepayer in the form of a lower rate base and future reductions in depreciation expense. Accordingly, staff recommends approval of the sale subject to the accounting treatment proposed in the company's accounting petition.

Integration Plan

In 2009, Cascade's parent corporation Montana-Dakota Utilities Co. (MDU) announced that four MDU companies including MDU, Cascade, Great Plains Natural Gas Co., and Intermountain Gas Co will streamline operations. These plans include the sale and relocation of Cascade's Seattle office, consolidation of five call centers into two, elimination of customer walk-in traffic at all offices for MDU, Great Plains and Intermountain, and the termination of some ancillary services. At the time of the announcement, MDU estimated that the streamlining would result in a work force reduction of an estimated 130 employees across the utility group in eight states in the first nine months.

As part of MDU's streamlining strategy, Cascade's relocation from Seattle to Kennewick represents an effort to move company operations closer to its customer base and to occupy a more central location with respect to the company's service territory. While Cascade serves about 250,000 residential, commercial, industrial and transportation customers in 96 communities in Washington and Oregon, the company's service territory does not include the

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Headquarters Property in Los Angeles, California Decision No. 90-11-031, Application No. 87-07-041, 118 P.U.R.4th 81 (where the California commission ordered a sharing between shareholders and ratepayers of the gain on the sale of a company's headquarters building); *Central Maine Power Company*, Docket No. 99-155, Maine Public Utilities Commission, Public Utilities Reports Fourth, Slip Opinion, August 02, 1999 (where the Maine commission "ruled" that the ratepayers were entitled to recover the gains on the sale of right-of-way property, but then shared the gains 90/10 between ratepayers and shareholders). See also David W. Wirick, *State Public Service Commission Disposition of the Gain on Sale of Utility Assets,* National Regulatory Research Institute 94-17(1994).

Seattle area. Some operations currently located in the Seattle general office will move to other existing locations, such as Bellingham.

The proposed sale agreement allows Cascade to remain in the Seattle office until the Kennewick facility becomes operational. Following Cascade's move, the Seattle general office will no longer be necessary or useful to perform its public duties.

Conclusion

Staff recommends approval of Cascade's petition in Docket UG-100860 to sell the Seattle general office subject to accounting treatment proposed by the company in Docket UG-100847. Approval will enable Cascade to advance its integration plans by allowing the company to move many general office functions to a newly constructed LEED facility in Kennewick, Washington.