BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. NORTHWEST NATURAL GAS COMPANY, Respondent.	DOCKET NO. UG-080519
In the Matter of the Petition of NORTHWEST NATURAL GAS COMPANY For an Accounting Order Authorizing Deferred Accounting Treatment of Certain Costs Associated with the Smart Energy Program.	DOCKET NO. UG-080530 *(consolidated)* COMMISSION STAFF'S MOTION FOR SUMMARY DETERMINATION

I. RELIEF REQUESTED

1 Commission Staff moves for summary determination denying Northwest Natural Gas Company's petition for an order authorizing deferred accounting treatment of start-up costs associated with its Smart Energy program. Although Staff opposes the deferral petition, Staff recommends that the Smart Energy tariff be allowed go into effect, unless withdrawn by the Company.

II. STATEMENT OF FACTS

2 Northwest Natural Gas Company ("NW Natural" or "the Company") distributes natural gas. NW Natural's customers burn the natural gas for purposes such as heating and cooking.[1]

3 On March 21, 2008, NW Natural filed tariff pages adding a pilot Smart Energy Program to its Washington service offerings. According to the Company, Smart Energy "is a pilot program that enables NW Natural's residential and commercial customers to offset the greenhouse gas ("GHG") emissions associated with their natural gas use—their 'carbon footprint'—by supporting innovative environmental projects developed by the Climate Trust."[2]

4 On March 24, 2008, NW Natural petitioned the Commission for "an order authorizing the deferred accounting treatment of certain start-up costs associated with NW Natural's Smart Energy™ program up to a total of $79,000."[3] The costs for which the Company seeks deferred accounting treatment are "program start-up costs" that the Company purposely did not include in the product price (*i.e.*, the tariffed rate for the service) "because the Company's market research suggested a price 'tipping point' beyond which customers would be much less likely to participate."[4]

5 Under the tariff, a residential customer voluntarily subscribing to the Smart Energy Program would pay either a flat rate of $6.00 per month or a per-therm rate of $.10486 for the purpose of "offsetting" the carbon emissions associated with the customer's combustion

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[1] Natural gas is regarded as a "cleaner" fossil fuel than coal or oil. However, as with the combustion of any fossil fuel, combustion of natural gas produces carbon dioxide, a greenhouse gas. *See* http://www.naturalgas.org/environment/naturalgas.asp

[2] Petition at ¶ 3.

[3] Petition at ¶ 1.

[4] *Id.* at ¶ 5.

of natural gas supplied by NW Natural. Commercial participants would pay not less than $10 per month. After retaining a portion of the money for administrative expenses, the Company would pass on the remainder of the money to a non-profit entity called the Climate Trust.[5] The Climate Trust would use the money to fund projects that reduce greenhouse gases.[6]

6 The Climate Trust would develop greenhouse gas offset projects on behalf of Smart Energy participants with the first priority for these projects being "to help bring biogas to the region"[7] as a new energy resource.[8] Even if successfully developed, however, Smart Energy program dollars would not be used for the purchase of biogas itself.[9] The "offsets" purchased by NW Natural's customers would not result from any reduction in the amount of natural gas distributed to NW Natural's customers (*e.g.*, through "conservation" within the meaning of WAC 480-90-238(2)(c)). Rather, the offsets would be achieved through the funding of projects to reduce greenhouse gases from other sources (such as methane from animal waste on dairy farms, or the release of carbon dioxide in energy generation).[10]

7 The Company's tariff filing states that implementation of the Smart Energy Program is contingent upon approval of the accounting petition.[11]

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[5] *Id.* at ¶ 3-5.
[6] Customers wishing to purchase carbon offsets through the Climate Trust are not limited to the Smart Energy Program. In fact, customers could achieve more carbon-reducing "bang for their buck" by contributing directly to the Climate Trust and avoiding NW Natural's administrative expense. *See* Thompson Decl., Exh. A (Response to Informal Staff DR 3).
[7] Northwest Natural Gas Company, proposed tariff sheet U.1 (filed March 21, 2008).
[8] Producing biogas from sources such as cow manure reduces a source of the potent greenhouse gas methane—with 23 times more global warming potential than CO^2–by capturing it and burning it for energy. (Methane is also the chief component of fossil fuel natural gas.) *See* Thompson Decl., Exh. A (Response to Informal Staff DR 1).
[9] Thompson Decl., Exh. B (Response to Staff DR 4).
[10] *See* Thompson Decl. Exh. A (Response to Informal Staff DR 1).
[11] Cover letter to March 21, 2008, tariff filing in UG-080519.

8 NW Natural is already offering its Smart Energy program to its Oregon customers. Washington customers represent about 10 percent of the Company's total customers.[12] The Company received approval from the Oregon Public Utility Commission to defer start-up costs incurred in 2008 of up to $622,000 "for later inclusion in customer rates."[13] The Company estimates that the Washington start-up costs for the Smart Energy program will total $79,000 for 2008 and 2009 combined.[14]

III. STATEMENT OF THE ISSUE

9 Whether Washington law supports authorization of a deferral for the purpose of allowing the Company an opportunity to recover, through general rates, costs associated with the Smart Energy program that exceed revenues received from customers subscribing at the tariffed rate.

IV. EVIDENCE RELIED UPON

10 This motion is based on the Declaration of Jonathan Thompson, counsel for Commission Staff and:

1. The Company's responses to Staff's informal data requests 1 through 5, attached to the Declaration of Counsel for Commission Staff as Exhibit A;

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[12] Petition at ¶ 6, 8.

[13] *Id.* at ¶ 6; A copy of the Oregon Public Utility Commission's Order No. 07-383 (Aug. 31, 2007) is attached for the convenience of the bench. Also attached is a copy of an Oregon Staff memo dated August 15, 2007, stating:

> Staff's counsel has advised that the Commission generally does not have statutory authority to impose the costs of a voluntary program on all customers, unless the utility can demonstrate that there are utility related benefits for non-participating customers. Although the legislature has granted the Commission specific authority for similar programs through a few specific statutes—such as tree planting and portfolio options (SB 1149)—that specific authority has not been granted for the type of program the company is proposing in Advice No. 07-04. Alternatively, the Commission has general authority under ORS 756.040 to authorize cost recovery for the purpose of establishing adequate service at just and reasonable rates.

[14] *Id.* at ¶ 7.

2. The Company's response to Commission Staff's Data Request No. 4, attached to the Declaration of Counsel for Commission Staff as Exhibit B;

3. The Company's response to Commission Staff's Data Request No. 5, attached to the Declaration of Counsel of Commission Staff as Exhibit C;

4. The pleadings and other documents already on file in this matter.

V. LEGAL AUTHORITY

11 This motion is made pursuant to WAC 480-07-380(2)(a), which provides that "[a] party may move for summary determination of one or more issues if the pleadings filed in the proceeding, together with any properly admissible evidentiary support (*e.g.*, affidavits, fact stipulations, matters of which official notice may be taken), show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law."

A. Although the Commission does not decide prudency and recovery in rates in approving deferral of costs, the Commission should deny NW Natural's petition on the grounds that the Company's rationale for deferring Smart Energy start-up costs—*i.e.*, eventual recovery of those costs in rates charged for other services—is contrary to Washington law.

12 A "deferred cost" is one that has been paid by the company but is postponed for inclusion in rates until a future period.[15] A utility must seek prior permission from the Commission before booking such costs.[16] Permission is given prospectively, from the date the petition was filed, and not retroactively.[17]

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[15] Goodman, Saul Leonard, *The Process of Ratemaking*, Public Utility Reports, Inc., p. 321 (1998).
[16] *Re Puget Sound Power and Light Company*, Docket UE-920433, Eleventh Supp. Order, 147 PUR4th 80, 119 (Wash. UTC Sept. 21, 1993).
[17] *Re the Petition of PacifiCorp d/b/a Pacific Power & Light Company*, UE-020417, Third Supp. Order, pp. 7-8 (Sept. 27, 2002).

13 The creation of a deferred cost is basically to accommodate the company, such as to protect it from adverse financial effects of regulatory lag, and to give it the later opportunity to recover the deferred charges. However, it is improper to assume that having met the criteria for deferred charges that the company is automatically entitled to recovery of the full amount in rates.[18] As the Commission stated in addressing an accounting petition by PSE:

> We emphasize that the question of accounting treatment and the question of recovery in rates are separate and distinct questions. The first question -- accounting treatment -- can be answered without the necessity for a detailed record because there is no inherent risk to ratepayers in doing so. That risk is not present precisely because the second question -- rate treatment -- will be answered only after the development of a detailed record. If PSE seeks to recover these costs in future rates, the Company will bear the burden to prove that such recovery is proper. Other parties will have the opportunity to contest whatever proof the Company offers, and to offer their own evidence and argument concerning how we should treat these costs for ratemaking purposes.[19]

The Commission will typically allow the company to charge deferred costs on its books of account subject to the company's initially absorbing the cost until it can mount a general rate case or other occasion for presenting specific proof of the reasonableness (and prudence) of including these costs in rates. Thus, the deferral is allowed prior to a rate case (or other

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[18] *See, e.g., Business and Prof. People for the Pub. Int. v. Illinois Commerce Comm'n,* 146 Ill.2d 175, 585 N.E.2d 1032, 1058-59 (1991);

[19] *In re Petition of Puget Sound Energy, Inc., for an Order Authorizing Temporary Deferred Accounting,* Docket UE-011600, Order Granting Accounting Petition ¶ 9 (Dec. 28, 2001); *WUTC v. PacifiCorp d/b/a Pacific Power & Light Company,* UE-050684, Order 04, UE-050412, Order 03, at p. 111 (April 17, 2006); *see also,* WAC 480-109-050(4). On the other hand, Statement of Financial Accounting Standards (FAS) No.71, Financial Accounting Standards Board, p. 3 (Dec. 1982) states:

> An enterprise shall capitalize all or part of an incurred cost that would otherwise be charged to expense if both of the following criteria are met:
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> a. It is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for ratemaking purposes.
> b. Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs. . . .

occasion such as a purchased gas adjustment[20]) as a stop-gap remedy pending further consideration of whether the expense should be allowed.[21] The company may be allowed to book carrying charges on the deferrals. If the Commission finds, either at the time of the petition or when the company seeks recovery, that the balance of the deferred account should be spread forward over a period of years, it will define an amortization period and the account will be written off or amortized in equal installments over the defined period.[22]

14 Although the Commission does not decide recovery in rates in the context of approving an accounting order, the Commission may deny a petition for an accounting order when the company has failed to establish a well-supported basis for deferral accounting treatment.[23] The basis asserted by Northwest Natural in its petition for an accounting order is that the rates it will charge customers who choose to participate in the Smart Energy program cannot exceed $6.00 per month (or $.10486 per therm) without passing a "tipping point" (beyond which customers would be much less likely to participate).[24] Therefore, the Company proposes to establish a deferral to set the stage for it to recover at some future time, through rates charged to general ratepayers for other services, the program start-up costs in excess of the revenue to be recovered from Smart Energy participants. For the reasons set forth below, that rationale is flawed as a matter of law and contrary to Washington state policy applicable to analogous voluntary programs that are offered under tariff by electric utilities. As such, the Company's petition for an order authorizing a deferral of these costs should be denied.

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[20] *Re Cascade Natural Gas Corp.*, UG-051135, Order No. 1 (August 31, 2005).
[21] Goodman, Saul Leonard, *The Process of Ratemaking*, Public Utility Reports, Inc., p. 323 (1998).
[22] *See Re Puget Sound Power and Light Co.*, 147 PUR4th 80, 119 (Wash. UTC 1993).
[23] *Re PacifiCorp d/b/a Pacific Power and Light Company*, Docket UE-020417, *WUTC v. PacifiCorp d/b/a Pacific Power & Light Co.*, UE-991832, Sixth Supp. Order/Eighth Supp. Order, pp. 14-15 (July 15, 2003).
[24] Petition at ¶ 5.

B. The Commission lacks authority to allow the Company to recover, in rates charged for other utility services, costs associated with a program in which customers may voluntarily purchase greenhouse gas credits to offset their individual "carbon footprint."

15 It is important to note that customers purchasing greenhouse gas offsets under the Smart Energy program would not actually purchase either gas or a conservation service, but would instead make a voluntary contribution to fund projects to reduce the release of greenhouse gases from other sources (such as methane from animal waste on dairy farms) as a means of "offsetting" the carbon dioxide released by the customer's combustion of natural gas supplied by NW Natural. Although it is possible, and perhaps even likely that gas distribution companies may be required to meet emissions standards with the option of purchasing greenhouse gas credits or offsets, they are not presently required to do so. And there is debate over whether such a regulatory scheme should hold a gas distribution company responsible for its customer's emissions.[25]

16 Staff believes NW Natural is to be praised for anticipating and readying itself for the possibility of such regulatory requirements in the future. However, because gas companies are not required by law to contribute money to projects designed to reduce greenhouse gas emissions by third parties (or to sequester carbon already in the atmosphere), the Company's election to do so is akin to a charitable contribution. As such, the Company may not recover expenses associated with that contribution from general ratepayers who have not volunteered the use of their money for this purpose. The Washington Supreme Court, in *Jewell v. WUTC,*[26] held that the Commission lacks statutory authority to allow a regulated utility to recover its charitable contributions as an expense for purposes of ratemaking. In

[25] Thompson Decl., Exh. C (Response to Staff DR 5).
[26] 90 Wn.2d 775 (1978).

Jewell, the Court based its conclusion on the fact that the Commission is directed to regulate in the public interest the rates of all persons supplying any utility service, and that the Commission is to set rates that are fair, just, reasonable, and sufficient to allow the company to render prompt, expeditious, and efficient service.[27] The Court stated: "There is nothing in the statutory scheme which directs that the telephone company must be a good corporate neighbor or that it is entitled to rate charges for contributions which result in improving the image of the corporation."[28] The Court further stated:

> The commission's orders demonstrate how far it has strayed from its statutory function. Those orders state, in part, that charitable contributions are 'socially appropriate, indeed mandatory Company expenses.' Further, 'all businesses in the state of Washington are expected to, and in fact do, support social and charitable institutions through contributions.' The Commission is not the keeper of the social conscience of the citizens of this state. The arbitrary and capricious nature of its orders is simply proved by its conclusions that (1) it is socially appropriate, indeed mandatory, that the contributions be made and that (2) all businesses are expected to, and in fact do, make charitable contributions. The commission may be accurate in its statements, but that does not mean it has statutory authority to order telephone users to make involuntary contributions.[29]

The Court also found that "[t]hat which is involuntarily removed from the telephone subscribers' pockets is more akin to a tax than a charitable contribution."[30] Here, though participation is voluntary, any shift in the programs costs would be analogous to the forced charitable contributions in *Jewell*.

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[27] *Id.* at 775 (citing RCW 80.01.040 and RCW 80.36.080). (Although the Court was referring to statutes pertaining to telecommunications companies, the same could be said based on the statutes pertaining to gas companies. *See* RCW 80.01.040 and RCW 80.)
[28] 90 Wn.2d at 777.
[29] *Id.* at 777, 778.
[30] *Id.* at 781.

17 Similar concerns were behind the Washington Supreme Court's 2007 ruling in *Okeson v. City of Seattle*.[31] In *Okeson*, a group of Seattle City Light customers brought a class-action lawsuit against the City of Seattle, arguing that payments City Light made for greenhouse gas offsets were "illegal because they lack sufficient nexus to the utility's statutorily prescribed purpose, which is to supply people with electricity."[32] In order to meet a self-imposed policy of meeting electric energy needs with no net increase in greenhouse gas emissions, the City (coincidentally based on proposals solicited and evaluated by Climate Trust) had entered into a series of agreements to pay other entities (such as King County Metro, Washington State Ferries, and a Dupont plant in Kentucky) to use cleaner fuels and, in return, to receive credit for the resulting greenhouse gas reductions.[33] According to a City Light press release, the contracts made Seattle City Light "the first large electric utility in the country to effectively eliminate its contribution to harmful greenhouse gas emissions into the environment."[34] The Court first analyzed the relevant statutory authority of city utilities in Washington and concluded that the statute does not specifically authorize city utilities to pay other entities to reduce their greenhouse gas emissions, nor is that authority necessarily or fairly implied in or incident to the powers expressly granted by the Legislature.[35] The Court found that the greenhouse gas offsets served a general governmental purpose and not a proprietary, utility purpose.[36] In essence the Court's conclusion was that the cost of such programs could be borne by taxpayers but not in rates paid for utility service.

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[31] 159 Wn.2d 436.
[32] *Id.* at 444.
[33] *Id.* at 441, 442.
[34] *Id.* at 442.
[35] *Id.* at 447-450.
[36] *Id.* at 450-453.

18 Shortly after the Court's decision in *Okeson*, the Legislature amended the statutory authority of the various publicly-owned (city and town, county, and public utility district) electric utilities so as to provide the statutory authority that the Court in *Okeson* found lacking.[37] The legislation states: "The legislature finds and declares that greenhouse gases offset contracts, credits, and other greenhouse gases mitigation efforts are a recognized utility purpose that confers a direct benefit on the utility's ratepayers." Although the Legislature's pronouncement is seemingly broad, the Legislature did not specifically amend the statutes pertaining to investor-owned utilities, despite the fact that the *Okeson* Court's analysis could apply equally to the statutes under which the Commission regulates the rates and services of electric or gas companies.[38] (The Legislature did, however, in the same legislative session, authorize electric utilities to purchase, under limited circumstances, "verifiable greenhouse gases emissions reductions" from other electric generating facilities within the Western interconnection as a means of meeting new greenhouse gases emissions performance standards for electric generating resources).[39] Thus, there remains a significant question as to whether an investor-owned utility may recover in general rates the cost associated with the purchase of greenhouse gas offsets that are not incurred as a result of a regulatory requirement. "Where a statute specifically designates the things or classes of things upon which it operates, an inference arises in law that all things or classes or things omitted from it were intentionally omitted by the legislature . . . ."[40]

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[37] 2007 Wash. Laws, ch. 349.
[38] Compare former RCW 35.92.050, discussed at 159 Wn.2d 445, 446 with RCW 80.28.010, .020.
[39] RCW 80.80.040 (13).
[40] *Silver Firs Town Homes, Inc. v. Silver Lake Water District*, 103 Wash. App. 411, 421 (2000) (holding that the UTC regulates only investor-owned water utilities and not municipal corporations because municipal corporations are not specifically listed among the entities to which commission regulation extends.)

19 *Jewell* and *Okeson* both address the use of rates paid for utility services, and not the the use of *voluntary* payments from customers. Thus, a tariffed "service," whereby individual customers may make voluntary contributions—with no subsidy from general rates—to offset the greenhouse gas emissions resulting from their own activities, would seem to avoid *Jewell's* prohibition on recovery of charitable contributions in rates for a utility service. Likewise, a voluntary program that did not rely on general revenues would avoid the fault that the *Okeson* court found with Seattle City Light's purchase of greenhouse gas offsets using rates paid for utility service. The problem arises when general ratepayers are forced to make an involuntary contribution to the program. But that is precisely the objective of the deferral sought by the Company.

C. State policy prohibits the shifting of program costs to non-participants.

20 The Legislature has authorized various mechanisms intended to address social and environmental objectives through utility rates and service offerings. For example, the Commission is authorized "upon request of an electric or natural gas company" to approve rates at a discount for low-income customers and to include resulting lost revenues in rates recovered from other customers.[41] As another example, gas, electric, and water companies are authorized to file conservation service tariffs with the Commission and to include in ratebase all bondable conservation investment.[42] Under RCW 80.28.300, gas and electric companies are authorized to request donations from their customers to support urban forestry, which the companies may use to support and complete projects consistent with model evergreen community management plans and ordinances. The question presented

[41] RCW 80.28.068.
[42] RCW 80.28.303.

here is, where no specific authority is provided for a program of this type, may the Company offer the program through its tariff, and if so, under what conditions?

21 The statute that is of particular relevance to NW Natural's request in this case—because it mandates electric utility programs very closely analogous to the program NW Natural seeks authorization to implement—is RCW 19.29A.090. Under that statute, each electric utility is required to offer its customers the opportunity to purchase "qualified alternative energy resources." The electric utility may provide this service either through resources it owns or contracts for, or by purchasing credits through a clearinghouse or similar system. The rates, terms, and conditions of these offerings by investor-owned electric utilities must be approved by the Commission and are set out in tariff. Importantly, however, "[a]ll costs and benefits associated with any option offered by an electric utility under this section must be allocated to the customers who voluntarily choose that option *and may not be shifted to any customers who have not chosen such option.*" (Emphasis added.)

22 It stands to reason that if the Legislature has *required* electric utilities to offer individual customers the opportunity to make voluntary payments for the additional cost of generating resources that do not release greenhouse gases, then a gas utility should be allowed to offer, through its tariff, a voluntary program with a similar objective. But if RCW 19.29A.090 is to be relied on as evidence that state policy allows for the offering of such voluntary programs under tariff, then the limitations imposed by the Legislature must be taken into account as well. The key restriction, for purposes of the instant petition for an accounting order, is that program costs must not be recovered from non-participants. The Washington Supreme Court's *Jewell* and *Okeson* decisions suggest, even setting aside the analogy to RCW 19.29A.090, that this same restriction is required for the Smart Energy

program, at least until investor-owned gas distribution companies are subject to regulations that require or authorize them to purchase greenhouse gas credits as a means of meeting emissions standards.

23 Because the rationale of the requested deferral is to provide a vehicle for recovery of Smart Energy program costs from customers other than program participants, the Commission should deny the Company's petition. Staff does not oppose the Company's proposal to offer the Smart Energy program under tariff, but simply opposes the deferral of costs not otherwise recovered through the tariffed rates. Although the Company concedes that the rates contained in its Smart Energy tariff may not be sufficient to cover all program costs (depending on subscribership), the Company may either make a new tariff filing increasing the rate or it may absorb the deficiency. The Commission should allow the tariff to go into effect unless it is withdrawn by the Company.

VI. CONCLUSION

24 For the foregoing reasons, the Commission should deny Northwest Natural Gas Company's petition for an accounting order authorizing deferral of certain startup costs associated with its Smart Energy program, but allow the Smart Energy tariff amendment to go into effect, unless withdrawn by the Company.

DATED this 18th day of July, 2008.

Respectfully submitted,

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