

**PUBLIC UTILITY COMMISSION OF OREGON
ADMINISTRATIVE HEARINGS DIVISION REPORT
PUBLIC MEETING DATE: November 5, 2002**

REGULAR _____ **CONSENT** x **EFFECTIVE DATE** _____ **NA** _____

DATE: October 18, 2002

TO: John Savage

FROM: Ed Busch through Terry Lambeth and Lee Sparling

SUBJECT: AR 449: Open a rulemaking to amend OAR 860-022-0070(7) to enable continuation of the annual earnings review mechanism for gas utilities.

STAFF RECOMMENDATION:

I recommend opening a rulemaking to remove the current OAR 860-022-0070(7). This deletion will allow the earnings review established for gas utilities under OAR 860-022-0070 to continue.

DISCUSSION:

OAR 860-022-0070 established procedures and standards for reviewing gas utilities' earnings prior to making changes to rate resulting from changes in base gas costs in the purchased gas adjustment mechanism. Specifically, the rule established a simplified earnings review to be held each spring for each gas utility; if the utility's earnings are above a specified earnings threshold, revenues would be shared with customers before passing through base gas cost changes. OAR 860-022-0070(7) states:

The earnings review mechanism established under the terms of this rule will be effective for four years, with earnings reviews conducted in 1999 counting as the first year. The mechanism will be reviewed for potential extension after the fourth year.

The earnings review conducted during spring 2002 was the fourth year of the earnings review mechanism. Based on Staff's review of how the mechanism has worked for the past four years, we believe the earnings reviews under OAR 860-022-0070 should be continued. The earnings reviews provide a reasonable balance between allowing pass-through of prospective base gas cost changes and ensuring that substantial over-earnings are shared with customers. Additionally, staff believes that the spring earnings

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reviews over the past four years have been accomplished smoothly and absent the contentiousness sometimes experienced in previous years (when their structure was less well defined and they were conducted as part of the PGA filings).

Deleting the current OAR 860-022-0070(7) would enable the earnings review mechanism to continue.

PROPOSED COMMISSION MOTION:

Rulemaking docket AR 449 should be opened to consider adoption of the proposed removal of the existing OAR 860-022-0070(7).

AR449.doc

860-022-0070

Procedures and Standards for Reviewing Gas Utility Rates in the Context of the Purchased Gas Adjustment Mechanism

(1) The purpose of sections 1 through 7 of this rule is to ensure that earnings of a natural gas utility local distribution company (“gas utility” or “LDC”) with a purchased gas adjustment (“PGA”) mechanism are not excessive prior to passing through prudently incurred base gas cost changes in rates through a mechanism which is fair to all parties and efficient to administer. For purposes of this rule, earnings are excessive only if a gas utility does not share with its customers past revenues related to earnings that exceed an earnings threshold determined by the Commission.

(2) Prudently incurred base gas cost changes will be included in rates through tracking filings, subject to the Commission’s review of gas cost purchasing practices at the time of those filings.

(3) A separate, simplified earnings review will be conducted on an annual basis independent of and in advance of the PGA filings. The purpose of such an earnings review is to determine whether the gas utility’s earnings are above an earnings threshold so as to require some sharing of revenue with customers before passing through base gas cost changes. The purpose is not to make a forward-looking, permanent change in rates.

(4) In an earnings review conducted under this rule, it is reasonable for PGA base gas cost changes to be passed through into rates if, in circumstances when the gas utility’s earnings in the prior year were above an earnings threshold determined in section 5 of this rule, revenue representing a percentage of earnings in that year above that earnings threshold is shared with customers.

(5) The standards to be applied in an earnings review under this rule for each LDC are as follows:

(a) Test year: The test year for the earnings review will be the calendar year immediately prior to the year in which the PGA filing is made, unless otherwise specified by the Commission.

(b) Normalization and adjustments: The test year results will be adjusted with a predetermined list of rate-making adjustments equivalent to those applied in the gas utility’s most recent general rate proceeding.

(c) Earnings threshold: There will be no revenue sharing required for years when a gas utility’s return on equity from utility operations in Oregon is lower than the earnings threshold determined by the Commission for each LDC. Neither this value nor any of the components implied in establishing it will be precedential in a general rate case involving any Oregon public utility.

The Commission will update the value for the earnings threshold annually for each LDC, pursuant to a mechanism established by order of the Commission for each LDC, to reflect changes in conditions in the capital markets. Upon a showing of good cause, the Commission may consider other relevant factors in addition to changes in conditions in the capital markets.

(d) Sharing percentage: The amount of revenue in a test year representing a specified percentage of the earnings above the earnings threshold will be shared with customers. The Commission by order will determine the sharing percentage for each LDC.

(e) Deferral and amortization: Any revenue determined for the gas utility for a test year under section 5(d) of this rule will be deferred as of December 31 of the test year. The balance in the deferred account will accrue interest from that date at the LDC's rate of return on rate base determined in its last general rate case. Interest will continue to accrue at this rate during the amortization period, which will begin on the date of the next PGA rate change and extend for twelve months. The Commission by order will determine the method for allocating amounts to be amortized among customer classes.

(6) Each LDC will file test year results of operations by May 1. Any person may request to be placed on a list to receive all such earnings review filings at the time they are submitted to the Commission or may request a copy of individual filings. Any person wishing to participate as a party shall so notify the Commission and other parties via letter. Commission staff will complete its review and distribute summary conclusions by June 10 to all parties. Staff will present the results of the earnings review at the first regular public meeting in July; alternatively, if issues are unresolved among all parties, a settlement conference including all parties will be conducted. By August 1, the parties will file position statements with the Commission on unresolved issues, if needed. The Commission will issue its decision on unresolved issues, if any, by September 15. Unless otherwise directed by the Commission, each LDC will file its annual gas cost tracking filing by October 15, including amortization of credit amounts in the deferred account, if any, resulting from the earnings review.

~~———— (7) The earnings review mechanism established under the terms of this rule will be effective for four years, with earnings reviews conducted in 1999 counting as the first year. The mechanism will be reviewed for potential extension after the fourth year.~~

(78) Application of earnings reviews conducted under this rule to amortization of deferred gas costs: The results of the earnings review conducted under this rule will be applicable to amortization of deferred gas costs if the LDC has a risk sharing mechanism for variations in commodity gas costs, as defined in the PGA tariff, that allocates less than 33 percent of the risk to the LDC. An earnings review will not be applicable to amortization of deferred gas costs if the LDC assumes at least 33 percent of the responsibility for commodity cost differences in the risk sharing mechanism. The Commission may modify this requirement if it authorizes an alternative incentive mechanism relating to variations in gas costs for an LDC.

Stat. Auth.: ORS Ch. 183 & 757
Stats. Implemented: ORS 757.210 & 757.259
Hist: PUC 1-1999, f. & ef. 4-21-99 (Order No. 99-284)