

ITEM NO. 1

**PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: May 31, 2005**

REGULAR X CONSENT _____ EFFECTIVE DATE July 1, 2005

DATE: May 17, 2005

TO: Public Utility Commission

FROM: Deborah Garcia

THROUGH: Lee Sparling, Ed Busch & Bonnie Tatom

SUBJECT: NORTHWEST NATURAL: (Docket No. UM 1194) Requests termination of the Company's propane distribution services and Tariff P.U.C. Or. 23 - Propane Service to Coos County.

STAFF RECOMMENDATION:

I recommend approval of Northwest Natural's petition to terminate propane distribution services and Tariff P.U.C. Or. 23 – Propane Service to Coos County, to be effective July 1, 2005.

DISCUSSION:

On February 1, 2005, Northwest Natural (NWN or Company) filed an application¹ to request authorization to terminate propane service and the associated Tariff P.U.C. Or. 23 – Propane Service to Coos County, effective July 1, 2005. The application was docketed as UM 1194.

Background

Since 1965, NWN has provided propane distribution service to approximately 123 customers in Coos Bay and North Bend utilizing four small Liquefied Petroleum (L.P. or propane) distribution systems. The Public Utility Commission (PUC) granted NWN allocated service territory to serve these customers in Commission Order No. 40972. In

¹ The current Oregon Revised Statutes and Oregon Administrative Rules (OAR) administered by the Public Utility Commission do not have specific application requirements that must be met by an energy utility that requests to abandon service. At Staff's request, NWN's application mirrors (to the extent practicable) the requirements of OAR 860-036-0715 which govern a water utility's request to abandon service.

the Order the Commission noted that NWN planned² to bring natural gas service to the area as soon as the third year after the order was signed. Since that time, the Company conducted numerous studies to assess the possibility of building a natural gas distribution system into Coos County. None of the options were considered financially feasible until the late 1990's when Coos County, with support from the State of Oregon, undertook an economic development project to build a transmission pipeline from the Williams Pipeline Corporation's lateral to serve Coos Bay, North Bend, Myrtle Point, and Coquille.

Coos County negotiated an agreement with NWN that the County-sponsored transmission pipeline would feed natural gas to a NWN distribution system. NWN took the necessary steps³ to begin constructing the initial backbone distribution system. As soon as the agreement was formalized, NWN initiated a strong marketing and community education effort that included radio ads, informational inserts in local newspapers, promotions for special financing and dealer incentive offers, and the development of customer information packets explaining what natural gas is, the benefits of natural gas, and the process to follow to get natural gas installed in a home or business. By the winter of 2004, this effort had resulted in approximately 180 applications for natural gas installations to be completed when the distribution system was operable. Of those applications, 16 were from existing propane customers. At that time, NWN also received verbal commitments to convert from 20 other propane customers.

In November 2004, NW Natural finished construction of the initial backbone natural gas local distribution system in the cities of Coos Bay and North Bend. Included in the construction of the initial backbone distribution system was the construction of main and service piping in the areas where the existing propane service customers are located to enable these customers to readily convert their existing propane service to natural gas. In addition, all propane customers who agreed to convert to natural gas service by May 1, 2005, did not have to pay for the installation of service lines from the service main in the public right-of-way to the customer meter.

² NWN expected to be able to serve a large paper plant at Gardiner, and five other industrial loads in the area indicated they would take gas as soon as it became available.

³ In Order No. 00-274, the Commission granted additional allocated service territory to NWN that was adjacent to the territory granted in 1965. In Order No. 03-236, the Commission approved NWN's request to recover the costs of the backbone distribution system, estimated at \$12M.

Discussion of the Requirements to Abandon Service in OAR 860-036-0715

Copy of contract of other agreement

There is no applicable contract or agreement because the application regards termination of the service and associated tariff. The company does not propose to sell, lease, assign or otherwise dispose of the utility property used to provide the propane service to any other third party.

Affected Propane Service Property

After receipt of Commission approval of the requests in its application, NWN plans to cease using the existing propane distribution facilities. Because of differences in the requirements regarding NWN's distribution system plant, its existing propane system cannot be used to transport natural gas. As stated above, NWN does not intend to sell any part of the distribution system for reasons that include the age of some of the facilities as well as liability concerns. NWN does plan to remove any above-ground components of the existing propane systems, as well as flush and cap the underground piping in accordance with Federal safety standards.

Reason for the Request

NWN owns natural gas local distribution systems in Oregon and Washington. As stated earlier, NWN has always sought to provide natural gas service to the customers in Coos County. Since the completion of the Coos County natural gas pipeline, that service has already commenced. NWN has repeatedly cited reduced costs for all customers as the primary reason for providing only natural gas service. Natural gas customers are in effect subsidizing propane service. Propane customers pay the same rates as natural gas customers although the costs, including the commodity cost of propane, that are associated with the provision of propane service exceed those associated with natural gas service. NWN estimates that the cost to keep the propane distribution system running (barring any unforeseen accidents or plant failures) at more than \$3,000⁴ per month. The additional costs are driven by a number of factors including, the need for separate accounting mechanisms, separate operational expenses due to the provision of a fuel with more inherent safety hazards, and the ongoing separate propane-specific federal training requirements for safety personnel.

Effect of Application on Propane Customers

Approval of this application requires that propane customers find an alternative source for energy. Based on the particular needs of the customer, the options, as may be available from local dealers or contractors, include conversion to electric, propane, wood, coal, pellet stoves, heating oil, or natural gas. The customers will be responsible

⁴ The higher commodity cost of propane is not included in this amount.

for the cost of converting or replacing their appliances and in some instances bearing the cost of construction to install or modify piping or wiring inside the customer-owned structure. Customers converting to alternative propane service will be responsible for paying a supplier to install a propane tank on the customer's property.

Benefits of Application Approval

All customers benefit from this application because it eliminates, as mentioned earlier, the added costs for managing and maintaining the L.P. system, including the rate subsidies that exist between the cost of propane fuel and the rates actually paid by the propane service customers.

Outreach and Customer Education

To its credit, NWN has made a tremendous effort to ensure that propane customers receive ample notice and information about the Company's proposal to terminate propane service. NWN also worked closely with local low-income assistance agencies to explore the kind and amount of assistance available to help defray conversion costs for low-income customers. Southern Oregon Coast Housing (SOCH) was able to provide funds for several propane customers' conversions to natural gas. Unfortunately, SOCH is currently out of funds, but has good reason to believe the additional grants it has applied for will be available soon to help other low-income customers convert to natural gas service.

In addition to the general outreach to Coos County citizens regarding the availability of natural gas that was outlined earlier in this memo, NWN planned and implemented targeted contacts to propane customers. During the first week of February 2005, immediately after filing the application in question, NWN sent by direct mail a notice of intent to request termination of propane services as of July 1, 2005, and a page of probable customer questions and answers (Q&A). In addition, NWN mailed copies of the letter and Q&A to the homeowner of record, if different from the customer stated on the account. Staff worked closely with NWN on the contents of both the letter and Q&A. A copy of each was attached to NWN's application as Exhibits B and C. In the letter, NWN offered to meet personally with customers either at the NWN office or at the customer's residence to discuss the process or available options. On two separate occasions, NWN has also called all customer and/or homeowners who are undecided about which fuel source they will choose, to offer information or answer questions.

Discussion of Other Issues

On March 14, 2005, Staff mailed a letter to each propane customer and homeowner of record, inviting them to an open house hosted by Staff that would include representatives from NWN and SOCH. The purpose of the open house was to provide

a forum for customers to have their questions and concerns addressed on an individual basis. Approximately 30 people attended the open house that was held at the Coos Bay Public Library on March 29, 2005, from 6:30 to 8 p.m.

At the open house, one customer who said she was attending so that she could sign an agreement to convert to natural gas ended up not signing. She declined to sign the agreement when she found out she would be responsible for the conversion costs including the conversion of her appliances. She said her income was too low and she would not be able to afford the costs. She left the open house unsure of whether she would be able to afford to convert to any other fuel source.

Staff took complaints from two customers. The first was from a customer who had already made plans to convert to natural gas, but wished to speak on behalf of low-income customers. His view was that regardless of the cost, NWN should provide propane service indefinitely because some people simply could not afford to convert to another fuel source. The other complaint was over a company decision to remove a propane tank located on the customer's property, rather than selling it to the customer.⁵

In a discussion held after the open house, NWN and Staff examined the possible alternatives available to low-income propane customers unable to afford the cost of conversion. NWN generously came forward with a plan offering financial assistance to those customers who wish to continue using propane. For customers who meet the same income guidelines as used by the Low Income Energy Assistance Program to determine eligibility for its program, NWN will solicit bids, arrange for installation, and pay up to \$500 for the placement of a propane tank and any necessary connections. Currently, three dealers offer propane service in the Coos Bay/North Bend area. Staff's research revealed that most conversions to an alternative propane supplier should cost much less than \$500, so any eligible customer should be able to have their conversion costs paid in full by NWN's program. NWN has sent a letter and application to all propane customers outlining the above program.

As of May 17, 2005, of the 114 current propane customers, 75 have already signed agreements with NWN to convert to natural gas; 8 customers have reported they have plans to convert to another fuel source; and 31 customers are undecided. Of the 31 undecided customers, approximately half of them have made verbal agreements with NWN to convert to natural gas.

⁵ In reply to Staff's investigation, NWN stated that its decision, based on the advice of its legal department, was due to the age of the tank, the exposure (salt air near the ocean), and the potential to be held liable (regardless of the contract language) for future problems, due to NWN's status in the sale as a "merchant."

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Although it is unusual for an energy utility to request permission to terminate service, in this instance it appears to be the correct choice. Now that natural gas is available to the citizens of Coos County, it would be unreasonable to ask the rest of NWN's natural gas customers to continue subsidizing the Coos Bay/North Bend propane service. NWN has done an outstanding job of assisting customers as they transition to another fuel source, and with the addition of NWN's low-income conversion assistance program, Staff's concerns have been answered. Staff recommends the Commission approve NWN's application.

PROPOSED COMMISSION MOTION:

NW Natural's petition to terminate propane distribution services and Tariff P.U.C. Or. 23
– Propane Service to Coos County be approved.