Service Date: January 18, 1983

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER of the Application of	)	UTILITY DIVISION
GREAT FALLS GAS COMPANY for	)	DOCKET NO. 82.4.25
Authority to Increase Rates and	)	ORDER NO. 4914a
Charges for Natural Gas Service.	)	

APPEARANCES

FOR THE APPLICANT:

Richard F. Gallagher, Attorney at Law, Church, Harris, Johnson & Williams, P.O. Box 1645, Great Falls, Montana 59401, appearing on behalf of the Applicant

Charles W. Kuether, Attorney at Law, 725 Central Avenue, Great Falls, Montana 59401, appearing on behalf of the Applicant

FOR THE INTERVENORS:

James C. Paine, Montana Consumer Counsel, 34 West Sixth Avenue, Helena, Montana 59620, appearing on behalf of the consuming public of the State of Montana

FOR THE COMMISSION:

Robert Nelson, Staff Attorney

BEFORE:

CLYDE JARVIS, Commissioner and Presiding Officer
GORDON E. BOLLINGER, Chairman
HOWA R D L . ELLIS, Commissioner
THOMAS J . SCHNEIDER, Commissioner

FINDINGS OF FACT

PART A

GENERAL

1. On April 16, 1982, Great Falls Gas Company (Applicant or GFG) filed an application with this Commission for authority to increase natural gas rates by $545,240. At the time of the original filing the Applicant made a motion for interim relief in the amount of $545,240.

2. At its regular agenda meeting held April 26, 1982, the Commission determined that the Company's application patently failed to substantially comply with Commission rules, due to the absence of a system cost analysis for a 12 month historical test year as required in Section 38.5.106, ARM.

3. On May 7, 1982, GFG filed a revised application with this Commission for authority to increase natural gas rates by $1,000,058. The Applicant renewed its motion that the Commission approves the $545,240 increase requested in the initial application on an interim basis.

4. On June 21, 1982, the Commission issued Interim Order No. 4914, which granted additional annual revenues in the amount of $215,901.

5. On September 22, 1982, notice of public hearing was given.

6. On October 19, 1982, at 9:00 a.m. pursuant to the notice, a hearing was held in the Banquet Room of the Civic Center, Park Drive and Central Avenue, Great Falls, Montana. The Commission also held an evening meeting to hear public testimony at 7:00 p.m. on October 19, 1982 at the same location. The hearing was concluded on October 20, 1982.

7. The office of the Montana Consumer Counsel has participated in the proceedings of this Docket since their inception.

8. The Economic Recovery Tax Act of 1981 requires the use of a normalization method of accounting for public utility property to be "recovery property. " GFG has used a normalization method of accounting for at least ten years and the granting of approval to use normalization method of accounting will not affect the rates granted in this case. The Commission approves and requires the normalization of accelerated tax depreciation benefits and investment tax credits on property covered by the Economic Recovery Tax Act of 1981.

PART B

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FUTURE TEST YEAR/PROJECTED VOLUMES

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9. GFG included as a part of its request the concept of a future test period based on projected sales volumes. The Applicant contends that the use of a future test period would base rates on realistic costs and sales volume levels that will be experienced during the first 12 months the new rates are in effect, contain a reasonable allowance to compensate for inflation, and reduce the number of rate cases filed by the Applicant. Implementing such a proposal would require extensive reliance on estimates. The accuracy of some of the estimates which would be relied upon with the use of a future test year, however, are questionable at best.

10. A careful review of several portions of the record in this Docket provides a text-book illustration of the concerns this Commission has with respect to the use of a future test year. The original cost estimate for the new office space was approximately $1,200,000. At the hearing, Mr. Robinson indicated that the final cost would be $1,464,959 (TR., p. 110). The difference between the original estimate and the final cost is 22 percent. The Commission is aware that the numbers for the office project were supplied by people outside of GFG. However, rates based on the original estimate would have been too low.

11. At the hearing, Mr. Geske testified that the Company had experienced a 45 percent increase in premiums for health and accident insurance which was not in the budget (TR., p. 37). Here again, if rates had been set on the basis of the original estimate, they would have been too low .

12. During cross-examination, Mr. Robinson indicated that the inflation adjustment used for this Docket was 9 percent (TR., p. 115). He also admitted, however, that the inflation rate is declining. In this instance, rates based upon the inflation rate estimated by GFG would have been too high .

13. The examples noted above demonstrate the problems that can develop with projections as time passes. This Commission has consistently refused to adopt the future test year concept in past cases. I n this Docket, Mr. Buckley used the historic test year methodology and calculated a cost of service of $2,979,000. Mr. Robinson calculated a cost of service of $2,602,000 using a future test year (TR., p. 101). While Mr. Robinson accounted for some of this difference, it is clear that a historic test year adjusted for known and measurable changes is a reasonable and accurate basis for use in setting utility rates.

14. Mr. Geske in his revised testimony at page 4 stated:

> Another major problem is the refusal of the Commission not recognizing current volumes which reflect the volume shrinkage due to conservation for the period new rates are in effect.

The implication that the Commission has ignored the declining sales of Great Falls Gas is not correct. The present policy of granting interim relief was designed, in part, to address this problem and was supported by GFG. Further, in both the last Docket (No. 81.4.44) and the current Docket, volumes and cost of service have been revised to reflect the most current data. No such revisions have been adopted for other gas utilities regulated by this Commission. These actions represent a clear attempt to provide timely regulatory response to Great Falls Gas.

15. Due to the concerns set forth in Finding of Fact Nos. 10 through 13, the Commission, consistent with past decisions finds that a historic test year adjusted for known and measurable changes is the proper basis for setting rates in this Docket. I n addition to the

reason in Finding of Fact No. 14, projected volumes are not accepted by the Commission due to the rejection of the future test year concept. The use of projected volumes with an historic test year presents a matching problem where projected revenues do not correspond to historic calculations of rate base and expenses. Furthermore, the testimony indicates 1) that historical adjusted volumes are adequate for ratemaking purposes (TR, pp . 209-211), and 2) that calculations of projected volumes are sensitive to the accuracy of equally challenging projections of independent variables such as inflation, housing and future gas and electric prices (See e.g. TR, pp. 160-161).

PART C

ABBREVIATED PROCEEDINGS

16. Mr. Buckley discussed in his testimony at the hearing what GFG could do in terms of alerting the Commission that a substantial change in loads had occurred after a rate case. In the proposed findings supplied by the Applicant a formal abbreviated hearing procedure is proposed. The issue of significant load losses which might occur is not a new one for the Applicant. In recent Dockets, GFG has identified the volumes taken by what is now known as the Simmons Refinery as subject to a possible reduction in load. These reductions, however, were not known with any reasonable degree of certainty. Using the concept of known and measurable changes, the Commission has been and will continue to be willing to consider a significant loss of load when it is experienced by GFG. However, given the present Commission policy with regard to immediate interim relief, no further abbreviation of rate proceedings is deemed necessary.

PART D

NEW OFFICE BUILDING

17. GFG is in the process of remodeling Number One River Park Tower for use as the new corporate headquarters. The expected occupancy date for the new facility is April 1, 1983. Both the Applicant and MCC agreed during the hearing that the new headquarters should not be considered for ratemaking until it is occupied and providing service to the customers of GFG. The Commission agrees with the position of the parties and finds that costs

associated with the new headquarters are not proper for ratemaking at the present time. When the new facility is fully occupied and in service, the Applicant should present all costs associated with the project to the Commission. Examples of data which should be provided include a detailed summary of the cost of the new facility, all expense changes and a revised cost of capital. The cost to be considered should be limited to the $1,464,959 amount contained on the record. The Commission intends to review the data associated with the new headquarters on an expedited basis. No further public hearing on this issue is contemplated by the Commission due to the evidence which al ready exists on the record .

PART E

SALES ADJUSTMENT MECHANISM

18. The Applicant has proposed the implementation of a Sales Adjustment Mechanism (SAM). This account would allow the utility to book, each month, 1/12th of the revenue over the cost of gas authorized in its last general rate case decision, even though the actual billings may be different. The difference between what is booked and what is billed is accumulated in the SAM account and rates are adjusted every six months to adjust this account to a zero balance.

19. One of the reasons GFG proposed the SAM was to reduce the effects of abnormal weather conditions on the operations of the utility. As the Company knows, rates are set on the basis of sales volumes which are normalized for weather. The reason volumes are normalized is to ensure that the effects of unusual weather do not skew the results of operations in the test period. Revenues collected naturally depend on what actual weather occurs. Variations due to weather are a normal risk of providing temperature sensitive utility service just as weather constitutes a risk to other businesses as noted by Dr. Logan:

> There are many people like farmers, ranchers and people who operate businesses that relate to the natural resource industry who are dependent on the climate. They have their revenues and their margin fluctuations depending upon the weather. (TR ., p. 241)

Based upon the evidence on the record, the concept that the SAM mechanism is needed on the basis of reducing volatility from weather is rejected. Further, the concept that weather (which all parties agree is an uncontrollable factor) has prevented the management of Great Falls Gas from managing controllable costs is found to be totally without merit.

20. The conservation which has resulted from audits and zero-interest loans made by the Applicant was characterized as a conflict between consumers and stockholders. The Applicant indicated that adoption of SAM would alleviate this conflict. Mr. Paine asked Mr. Buckley several questions with regard to conservation:

> Q. Now, Mr. Buckley, if the Commission would consider adopting a conservation figure based on the Company's active audits and zero-interest loans, and if it were assumed that this difference did result in a known and measurable change, and assume that conservation would be "X" as applied to sales volumes for the next year, would that type of a rate-making methodology alleviate one of the Company's perceived concerns with regard to conflicts between the shareholders of the Company and the subscribers with regard to a conservation effort?

A. I believe it would.

Q. The conflict would be alleviated and perhaps to every one's continued interest?

A. That's correct.

The Commission accepts the adjustment for conservation as proposed by MCC and supported by GFG. Acceptance of this adjustment removes the "conservation conflict" as an issue in the consideration of SAM.

21. In evaluating a proposal like SAM, the Commission tries to determine what advantages would occur if the system is implemented. During its evaluation the Commission compared SAM to the existing budget billing and found several similarities:

(a) under both programs the customer would not necessarily pay for actual consumption .

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(b) both programs would assign rates based upon fixed billing increments .
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Given the low voluntary participation in the current budget billing program (7 percent), the Commission has serious concerns about implementation of a similar program.

22. Finally, the most serious concern of the Commission 1s the concept of a guaranteed gross margin under SAM. GFG has already had a large portion of risk removed for gas costs through gas tracking proceedings. Now the Applicant seeks a guaranteed gross margin. The Commission must afford utilities the opportunity to earn a fair and reasonable return on their assets. However, this Commission is not inclined to support any ratemaking technique which would guarantee a return. When asked if the cost of equity would be reduced if SAM were adopted, Mr. Geske gave a negative response. In the view of the Commission, if SAM was implemented, a significant downward adjustment in the cost of equity would be required to reflect the reduced risk.

23. For the reasons stated above in Finding of Fact Nos. 18 through 22, the SAM concept is rejected.

PART F

ZERO-INTEREST BALANCING ACCOUNT

24. I n Order No. 4804a the Commission approved a balancing account to account for expenses associated with the provision of zero interest loans.
Expenses reduced by any credits allowed by Montana law were to be accounted for as follows:

> The net amount will be allowed on a uniform cents per MCF basis for the next twelve months, which amount will be adjusted six months later (Order No. 4804a)

The Commission also indicated that GFG should make every attempt to plan its reconciliation applications pertaining to the balancing account to coincide with its general rate applications. The Applicant filed a reconciliation in zero-interest loan this Docket. Exhibit WJF R1 shows a balance in the balancing account of $16,912. The Commission approves the implementation of a charge in the amount of $0.0035 per Mcf. A new filing should be made either in six months or with a general rate case.

PART G

CAPITAL STRUCTURE AND ASSOCIATED COSTS

25. The Applicant and MCC agree and the Commission finds that the cost of equity capital is 14.5 percent, which is the same amount found in Order No. 4804b, Docket No. 81 . 4. 44.

26. The parties have agreed and the Commission finds the Company's overall cost of debt capital is 8.86 percent.

RATE OF RETURN

27. Based on the findings for common equity and long-term debt, the following capital structure and costs are determined appropriate:

Type	Capital Structure	Cost	Weighted Cost
Long-Term Debt	54.8%	8.86%	4.86%
Common Equity	45.2	14.50	6.55
	100.0%		11.41%

PART H
RATE BASE

28. The Applicant and MCC agree that the Applicant's rate base, excluding the new corporate offices, is $6,192,970. The Commission accepts the rate base amount agreed to by the parties.

PART I

REVENUES AND EXPENSES

29. The June 30, 1982 test year adjusted for known and measurable changes, is found by the Commission to be a reasonable period within which to measure Applicant's utility revenues, expenses and returns for the purpose of determining a fair and reasonable level o, rates for natural gas service.

30. Sales volumes are 12 months actual sales adjusted for weather and for an adjustment associated with savings as a result of Applicant's energy audit and no-interest loan program (TR., p. 222). The Commission strongly supports the concept of conservation. In making this conservation adjustment, the Commission is directly reducing the impact of conservation on the stockholders of GFG.

31. MCC proposed that the second year o-f the amortization of interest earned on undistributed proceeds from the Industrial Development Revenue Bonds in the amount of $55,706 be added to test year operating revenues. Since no new evidence on this issue was presented by the Applicant, the adjustment is accepted by the Commission for the reasons set forth in Order No. 4804b.

PART J

REVENUE REQUIREMENTS

32. The Commission finds that Great Falls Gas Company is entitled to $294,292 of additional gross operating revenues as follows (See Schedules 1 and 2):

GREAT FALLS GAS COMPANY - OVERALL COST OF SERVICE

Line No.		12 Months Actual At 6/30/82	Adjustments	Present Rates	Test Period Adjustment	Proposed Rates
1	Operating Revenues	$23,967,234	$ (685,443)	$23,281,791	$ 294,292	$23,576,O83
2	Cost of Service:					
3	Gas Purchased	20,347,796	(601,000)	19,746,796	-0-	19,746,796
4	Other Operation:					
5	Distribution	413,942	87,264	501,206	-0-	501,206
6	Customer Accounts	420,448	113,855	534,303	2,119	536,422
7	Customer Services	117,540	57,980	175,520	-0-	175,520
8	Administrative & General	756,871	151,985	980,856	-0-	908,856
9	Maintenance	188,568	(14,508)	174,060	-0-	174,060
10	Depreciation	325,443	6,060	331,503	-0-	331,503
11	Taxes:					
12	Other than Income	176,964	15,937	192,901	175	193,076
13	Federal Income - Current					
14	(Net-Inv.Cr.)	98,036	(27,219)	70,817	125,253	196,070
15	Federal Income - Deferred	304,125	(234,597)	69,528	-0-	69,528
16	State Income	18,037	(1,319)	16,718	19,710	36,428
17	Total	23,167,770	443,024	22,722,208	147,257	22,869,465
18	Utility Operating Income	799,464	(242,419)	559,583	147,035	706,618
19	Rate Base	6,009,090		6,192,970		6,192,970
20	Rate of Return	13.30%		9.04%		11.41%

SCHEDULE 2

Rate Base	$6,192,970
Recommended Rate of Return	11.41%
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Recommended Return	$ 706,618
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Adjusted Balance Available for Return	559,583
Return Deficiency	$ 147,035
Revenue Deficiency	294,292
Uncollectibles @ .72%	2,119
MCC Tax @ .06%	175
State Taxable Income	291,998
Montana Corporation License Tax @ 6.75%	19,710
Federal Taxable Income	272,288
Federal Tax @ 46%	125,253
Income Available for Return	147,035

PART K
RATE DESIGN

33. The existing GFG rate design features a purely volumetric recovery of all costs of service through an inverted lifeline energy rate. The lifeline rate provides a 25 percent discount on the first 15 MCF per winter month for all firm customers.

34. Both GFG and the MCC attribute a portion of the Company's alleged revenue instability and attrition problems to the existing rate structure. The testimony includes the following dialogue.

Mr. Geske:

> Q. All right. Let me discuss briefly about your perceived problems of revenue volatility. Now, your off-therecord summary did indicate to me one of the primary problems as you see it is with the lifeline rates, or in other words, it has caused the Great Falls Gas Company to be subjected to significant fluctuations in revenue. Is that a fair characterization of your testimony?

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A. In general, yes, but I think it's the structure of the lifeline that is causing a lot of it. The fact that the discount rate, we are selling 15 cents per MCF below cost, is one of the biggest distorting factors. (TR. pp. 11, 12)

Mr. Buckley:

A. ... But to me it certainly appears that the problems that the Great Falls Gas has been encountering is not with the use of historic volumes associated with weather or historic test years adjusted for known and measurable changes, but I think it should be pretty obvious that it has to be related very, very strongly with the rates on the inverted rates. (TR. p. 210)

35. The primary objections to the existing rate structure appears to be the relationship between the resulting discount rate and the cost of purchased gas. In that the discount rate is less than the cost of gas, GFG maintains that the Company's ability to earn its "margin" becomes highly sensitive to weather conditions. Both GFG and MCC recommended that the discount rate at least reflect the cost of gas. In addition, GFG summarily concludes that the Commission's rejection of SAM necessitates a monthly service charge of $5.

36. The existing "lifeline/volumetric" rate structure has as its genesis Docket No. 6618 -- a contested proceeding featuring volumes of testimony and exhibits addressing solely the subject of natural gas rate design. The Commission is hesitant to substantially revise the existing structure absent testimony (See e.g. TR. p. 274) empirically demonstrating: 1) improved revenue stability (long-run as well as short-run) resulting from alternative structures, 2) cost of service supporting proposed revisions, and 3) billing frequencies and billing comparisons contrasting the relative customer impacts resulting from proposed rate structures.

37. The Commission rejects the GFG concept of a $5 service charge in that the proposal is not supported by calculations of cost, improved long-run revenue stability, or customer impact.

38. However, in that the existing 25 percent discount was established to reflect a reasonable discount ra1:her than an empirical result, the Commission finds appropriate the GFG and MCC proposals to "peg" the discount rate at the Company's cost of purchased gas.

39. The cost of purchased gas is to reflect the Montana Power Company's Firm Utility Gas Contract rate modified to 13.28 PSIA and a 2.98 percent Company use and unaccounted for

factor. On a test year basis, the resulting rate decision features roughly a 20 percent discount:

0-15 MCF, Winter	$4.050/MCF
Ail other MCF	$5.060/MCF

40. One rate structure element not addressed by the parties that warrants discussion is the size of the discount block. The declining average consumption per customer suggests that the size of the discount block -- 15 MCF -- should possibly be reexamined. Such proposal, however, must be accompanied by billing frequency information demonstrating the frequency of various volumes per customer, as well as affect on revenue stability and customer monthly bills.

CONCLUSIONS OF LAW

1. The Applicant, Great Falls Gas Company, is a "public utility" within the meaning of Section 69-3-101, MCA.
2. The Commission properly exercises jurisdiction over the Applicant's rates and operations pursuant to Title 69, Chapter 3, MCA.
3. The revenues and rate structure authorized by the Commission are just, reasonable and not unjustly discriminatory.

ORDER

THE MONTANA PUBLIC SERVICE COMMISSION ORDERS THAT:
1. Great Falls Gas Company shall file rate schedules which reflect an annual revenue increase of $294,292 for natural gas service, based on the test period ending June 30, 1982.

2. The increased gas revenues authorized herein shall be distributed according to the direction contained in the rate design portion of this order. The lifeline discount rate is to be set at the cost of gas, as specified in Finding No. 39.

3. Rate schedules shall include a charge of $0.0035 per MCF to reflect the cost of the zero interest loan program, pursuant to Finding No. 24.

4. Applicant shall file revised schedules incorporating the changes in its rate schedules approved herein. The schedules shall become effective for service rendered on and after January 17, 1983.

5. All motions and objections not ruled upon at the hearing are denied .

DONE IN OPEN SESSION at a meeting of the Montana Public Service Commission held the 17th day of January, 1983 by a vote of 3-0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

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THOMAS J . SCHNEIDER, Chairman

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HOWARD L. ELLI S . Commissioner

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CLYDE JARVIS, Commissioner

ATTEST:

Madeline L. Cottrill
Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be flied within ten days. See 38.2.4806, ARM.