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BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of Questar Gas Company for a General Increase in Rates and Charges, and other Proceedings

UTAH COMMITTEE OF CONSUMER SERVICES RESPONSE BRIEF

Docket Nos. 98-057-12
99-057-20
01-057-14
03-057-05

The Utah Committee of Consumer Services ("Committee") here files its response brief in these proceedings.

INTRODUCTION

There are three issues before the Commission in this *post-appeal* proceeding:

1. whether QRS management has responsibly met Questar Gas Company's ("Questar Gas" or "utility") burden of proof;

2. whether the Commission's prior evidentiary determination of an insufficient record was a proper and final disposition of Questar Gas' application for rate recovery of its CO_2 gas processing costs; and

3. whether any reasonable and supportable basis exists for a grant of partial rate recovery in

this case.

Consideration of these three issues must be framed by all that has gone before, including: the records of four separate docket proceedings, the Commission's August 11, 2000 Report and Order in Docket No. 99-057-20 (which the Committee appealed to the Utah Supreme Court), and that Court's subsequent ruling in *Committee of Consumer Services v. Public Service Comm'n of Utah*, 2003 UT 29, 75 P.3d 481(cited hereafter as "Court's Decision").

Proper resolution of these issues will implement just and reasonable rates in this case and will underscore a fundamental principle of regulatory law; namely, that in a regulatory proceeding, the public utility has the burden of proof to demonstrate it is entitled to the rate increase it has applied for. It is not the burden of other parties to prove the contrary.

ARGUMENT SUMMARY

QRS management's initial brief fails to cite any evidence that would demonstrate its CO_2 plant remedy decisions were anything other than a case of Questar affiliate interests taking advantage of the exigencies of the moment to further their interests at the expense of the utility and its ratepayers.

The litany of actions discussed in its initial brief all occur in an artificially constrained window of time that begins in the winter of 1997-98 and ends with what QRS management has asserted would have been a customer safety crisis in late 1998 but for either its implemented CO_2 plant remedy or a massive $100 million "expedited reorificing" of customers' gas appliances within the utility's gas distribution system.

Whether utility management acted prudently under the circumstances of the moment, or whether those circumstances were themselves evidence of utility management's prior neglect of utility and ratepayer interests, hangs completely from QRS management's unsupported assertion that the coal seam gas threat to the utility's gas supply was *unforeseeable* prior to the winter of 1997.

QRS management fails to ever explain why, when managing Questar Gas, it was unable to foresee a threat which the Questar Pipeline company it also manages had created and been exacerbating for years.

The Court has already rejected the only record basis for rate recovery QRS management made in these proceedings – the one it again makes in its initial brief:

> [w]hile safety concerns may have necessitated the construction and operation of a CO_2 plant, they do not establish who should bear the cost of these measures.

The Court's Decision directs attention to the fundamental prudence and rate recovery questions which QRS management has steadfastly ignored in these proceedings: how did the coal seam gas threat to the utility's gas supply originally arise and what did utility management do about it prior to the 1998 crisis:

> While the Commission correctly recognized Questar Gas's obligation to ensure the safety of its customers, it incorrectly concluded that this factor provided a near-automatic justification for a rate increase regardless of how the initial threat to safety arose or how the utility sought to alleviate it.

QRS management's initial brief still leaves those fundamental questions

unaddressed despite record evidence showing the threat arose as a direct consequence of Questar Corporation and Questar Pipeline business decisions in the early 1990s, and that earlier effective actions would have jeopardized the profitable business opportunity created as a result of those affiliate business decisions.

QRS management's filings and supporting testimony manifest what has become a recurring regulatory problem: utility management's attempt to foist onto regulatory authorities its burden of proof where conflicting affiliate interests are present. Such actions show they consider their obligations to affiliate interests more important than any obligation they have to the utilities they

manage or to the utilities' ratepayers. Open disclosure of those conflicting affiliate interests would apparently weaken or destroy their case for rate recovery from utility ratepayers, so they file an intentionally incomplete application in the belief such a strategy will net a greater rate recovery than had they forthrightly disclosed their conflicting interests.

QRS management's initial brief cites a Commission's Order in the 1995 US West general rate case ("*US West* proceedings") as legal support for its argument for partial rate recovery. A more relevant aspect of those *US West* proceedings is the Commission's expressed frustration with utility management's failure to provide sufficient evidence with regard to the conflicting affiliate interests that were present to permit an informed Commission rate decision:

> We find no compelling evidence that positive benefits or ratepayer harm are given serious consideration by the Company or its affiliates in the conduct of inter-affiliate business transactions. We find only poor, contractually-based simulations of arms-length transactions negotiated between sibling companies, who are required for all practical purposes to support the parent. Similarly, we find little evidence of competitive bidding. We conclude that USWI's holding company, with its interlocking directorates and common management structure works at cross-purposes to ratepayer interests. Consequently, we affirm our prior assessment, and we will not rely on value studies or RIRs, as presently conceived, in this or future cases, to draw findings on the cost of affiliate transactions . . .

The Commission expressed similar frustration in an earlier US West rate case:

> Upon review of the record, we find that the Company has not met its burden to provide sufficient information to permit us to determine that the affiliate's charges are reasonable for services necessary to the provision of utility services. It is not sufficient for the Company simply to rebut the claims of another party; instead, it has an affirmative obligation.

The evidentiary problem the Commission speaks of exists in this case. QRS management's disingenuous assertion that its actions were prudent without acknowledging the affiliate control and conflicting interests that were present – let alone demonstrating how its actions were prudent *despite*

those factual conditions – makes its regulatory filing little more than pretense.

There is an applicable legal principle available to the Commission in such instances as this that properly and effectively addresses the problem: the utility's burden of proof. Such conduct by a surrogate utility management necessarily undermines the utility's ability to meet its burden of proof. In cases such as this where the issues of affiliate control and conflicting interests are present, the only way utility management can meet its burden of proof is by demonstrating the costs at issue were prudently incurred *despite the affiliate control and conflict of interest that were present*. QRS management clearly did not do that.

QRS management's failure to meet its burden of proof applies to its belated claim to partial rate recovery as well. The same legal principles pertain: (1) the utility has the burden to prove it is entitled to the rate increase it seeks; in order that (2) the Commission can fulfill its duty to make appropriate findings of fact to justify any rate order, including:

> subsidiary findings in sufficient detail that the critical subordinate factual issues are highlighted and resolved in such a fashion as to demonstrate that there is a logical and legal basis for the ultimate conclusions.

The issue here is not the one QRS management attempts to frame in its initial brief; namely, whether the Commission has the power to make a finding of partial prudence or to award partial rate recovery. The issue is whether such a determination is appropriate and supportable from the record in this case. By never explaining how it was allegedly able to represent the utility's interests, while at the same time protecting and furthering Questar Pipeline's conflicting interests in the matter of the coal seam gas threat, QRS management has necessarily left the Commission and opposing parties without any reasonable means to evaluate what, if any, costs should be recoverable in rates.

Had any credible support for partial rate recovery existed in the record, the Commission would have cited it in its earlier order that sought to legitimize partial rate recovery on the rationale the

costs "yielded the required result." The only "record support" the Commission could cite was the debate by the parties over "the likely outcome had FERC considered the issue of who ought to pay to process gas." The Commission, however, effectively negated any value of that discussion with its determination: "we do not find sufficient record support to suggest the probable outcome had the case gone to FERC."

In summary, there is no record support for full or partial rate recovery of the CO_2 processing costs which QRS management assigned to Questar Gas to pay. QRS management's incomplete filings and supporting testimony regarding the critical issues of affiliate control and conflicting interests fall far short of meeting the utility's legal burden of proof.

In addition to implementing just and reasonable rates in this case, a Commission denial of rate recovery will emphasize utility management's burden to demonstrate the costs it seeks to pass on to utility ratepayers are prudent, and just and reasonable, *despite* the conflicting affiliate interests that are evident. It will also affirm a legally binding appellate Court decision that is dispositive of these proceedings.

ARGUMENT

I. QRS MANAGEMENT'S INITIAL BRIEF FAILS TO DEMONSTRATE THAT THE DECISION TO PROCURE GAS PROCESSING WAS PRUDENT.

A. The Applicable Prudence Standard.

QRS management's initial brief invokes the reasonable person prudence standard without ever properly applying it in this case. It correctly states that the standard is an 'objective' one, unburdened by subjective suspicions, that "examines whether a 'reasonable utility manager, under the same

circumstances and acting in good faith would have made the same decision,'" but then forgets the "acting in good faith" part. It further fails to make the pole star linkage between utility management's prudence obligation and the utility monopoly's duty to charge just and reasonable rates and to "operate in such a manner as to give the consumers the most favorable rate reasonably possible."

As explained in the Committee's initial brief, the regulatory prudence standard necessarily assumes that a reasonable person is complying with his or her manager duties – including the duty to forthrightly disclose any conflicting interests. Common sense and generally accepted principles of agency law both say "good faith" is **not** present in circumstances where a manager hides his or her conflicting interests from the decision maker.

The law does **not** attribute a presumption of good faith and reasonableness to cost transactions between corporate affiliates because of any 'subjective suspicion' they were less than arms-length transactions. It presumes those transactions were 'objectively unreasonable,' and imposes a positive burden of proof upon affiliate utility management to demonstrate their reasonableness and prudence *despite* the circumstances that are otherwise presumed to exist. The law expects utility management to be able to convincingly and credibly demonstrate that the utility is entitled to the rate increase applied for whether conflicting affiliate interests are present or not.

By not responding to the issues of affiliate control and conflicting interests after they were credibly raised in the record by opposing parties, QRS management has necessarily fallen under the censure of the presumption of unreasonableness rule mentioned above – a further manifestation of its imprudence and failure to meet its burden of proof.

B. Questar Regulated Services Management's Initial Brief Fails to Demonstrate its Remedy Decisions were Prudent Despite its Conflicting Affiliate Interests.

QRS management's claim of prudence necessarily hangs from its unsupported argument that,

because the larger-than-forecast growth in coal seam gas production was unanticipated in the winter of 1997, the underlying threat to the utility's gas supply was unforeseeable. (This argument will be further discussed under Section C, below.) Other than that single unsupported argument, it fails to cite any credible record evidence showing the precipitous review and remedy actions it undertook in late 1997 were anything other than the expedient "required result" the Commission previously found them to be.

The Court has made clear that simply recounting the actions taken under the exigencies of the moment to protect customers "do[es] not establish who should bear the cost of [those] measures:"

> [w]hile the Commission correctly recognized Questar Gas's obligation to ensure the safety of its customers, it incorrectly concluded that this factor provides a near-automatic justification for a rate increase regardless of how the initial threat to safety arose or how the utility sought to alleviate it.

QRS management's applications and supporting testimony would have the Commission believe that utility management made its own decisions free and independent of affiliate influence; that there was no conflict between the interests of Questar Pipeline and the utility regarding Questar Pipeline's transport of the coal seam gas on its southern system; and that the only relevant factual information the Commission needed to consider was that there was an impending customer safety crisis in 1998 as a result of higher than forecast coal seam gas production and FERC open access policies. It never mentions its conflicting surrogate management responsibilities, nor does it meaningfully respond to those issues after they were raised in the record by opposing parties.

There are sound regulatory policy reasons behind the established legal principle that a utility's burden of proof in a regulatory proceeding is not merely a prima facie one. The utility is often the only party with the necessary evidence to permit an informed Commission rate decision. Effective utility regulation cannot tolerate utility management's conscious attempts to force a rate decision

while withholding the sufficient and accurate factual information that would permit an informed Commission decision. In failing to ever respond to the affiliate control and conflicting interest issues evident in this case, QRS management has deprived the Commission of the evidence and information needed to make an informed full or partial rate recovery decision.

C.Questar Regulated Services Management's Initial Brief Fails to Demonstrate that Questar Gas Responded to the Threat to its Gas Supply in a Timely Manner.

The Committee's initial brief reviewed the evidence in the record showing that the coal seam gas was a foreseeable threat to the utility's gas supply several years prior to 1997, and that it arose as a direct consequence of Questar Corporation and Questar Pipeline business decisions.

The coal seam gas producers' interest in negotiating with Questar Pipeline for transport of their gas production was clearly to secure a reliable transport to market for the growing quantities of coal seam gas they expected would be produced in the future. Had Questar Corporation and Questar Pipeline not followed through on their negotiated contractual commitments with the producers to accommodate their growing production, those producers would, of necessity, have sought out other transport alternatives. In other words, but for Questar Corporation's use and expansion of Questar Pipeline's southern system in the early 1990s to accommodate that growing coal seam gas production, there would have been no customer safety crisis in 1998 and therefore no need for a CO_2 plant remedy and its attendant costs.

A fundamental prudence issue before the Commission is whether, in light of those Questar corporate decisions and actions, a reasonable and prudent utility management should have foreseen that those actions, and the consequent growth in the quantities of coal seam gas in the southern

system those actions enabled, posed a threat to the utility's gas supply that could grow into the very safety crisis QRS management said it had not anticipated would occur in 1998. The issue is further necessarily framed by the utility's close affiliation with Questar Corporation and its management since the Questar Holding Company structure was formed in 1984, and QRS management's control of Questar Gas and Questar Pipeline since 1995. Those critical facts render absurd any argument that QRS management's utility 'hat' was unaware until the year 1997 of the growing threat to the utility's gas supply which its Questar Pipeline 'hat' created in the early 1990s and was exacerbating in the years thereafter by further expanding Questar Pipeline's southern system to accommodate the gathering and transport of increasing quantities of coal seam gas.

Questar Regulated Services management testified it did not react to the coal seam gas threat until the winter of 1997:

> [p]roduction of coal bed methane began to increase during the winter of 1997-98 and producers forecasted that the volumes from the northern portion of the Ferron Fairway would increase more rapidly than anticipated. QGC determined it could experience a blending problem by the spring of 1999. The Gas Quality Team focused on alternatives to deal with the Btu issue as soon as it became apparent that there could be a blending problem. In fact, production has actually increased at a greater rate than even predicted by the producers.

The effects of QRS management's short-sightedness or intentional neglect are apparent from its own testimony. Its initial brief cites its relief in discovering, in the Spring of 1998, "that CO_2 processing provided a more cost-effective remedy alternative to the expedited re-orificing of customer appliances" it thought would otherwise be necessary. It further testified that its investigation in 1997-98 showed that expedited reorificing "would have cost over $100 million to implement." QRS management's initial brief also cites its record testimony indicating that the options it could consider in the Winter and Spring of 1998 were necessarily limited by its not having discovered the

threat sooner.

As demonstrated above, the fact that coal seam gas production increased faster than forecast in a particular calendar quarter in no way demonstrates that the underlying threat to the utility's gas supply was not foreseeable years earlier, or that a prudent utility management would not have responded much earlier by at least investigating the threat to determine how it could likely further develop, what reasonable remedy options might exist, and what the lead-time was to implement those possible remedies.

QRS management's prudence claim is further undermined by its testimony that it would have been unwise for Questar Gas or Questar Pipeline to "have made operational changes or expanded their systems" based upon "speculation that the volume of gas from the Ferron Fairway could be substantial at some point," when it had already implemented operational changes on Questar Pipeline southern system to accommodate further coal seam gas production growth.

It is highly unreasonable to think that a prudent and independent utility management, aware not only of the "speculation" of growing coal seam gas production but also of Questar Corporation's and Questar Pipeline's expansion of Questar Pipeline's southern system to accommodate the transport to market of growing coal seam gas production, would not have promptly raised its concerns in a remonstrance to the pipeline company upon whose transport of the bulk of the utility's gas it was vitally dependent, demanding that Questar Pipeline agree to protect the utility and its ratepayers from any consequent harm that transport might cause. It is also unreasonable to think, had Questar Pipeline not agreed to remedy any materializing harm at its cost, that a prudent and independent utility management would not have promptly gone to the FERC for a cost allocation decision.

Initiating an action before the FERC in the early 1990s would have allowed plenty of time for an orderly, even protracted, proceeding before the FERC where the opposing issues and interests of

the parties could have been completely aired and considered.

QRS management repeatedly testified of the "risk" and uncertainties in how the FERC might allocate remedy costs. In reality, the *downside* of that risk was no worse an outcome than the cost *certainty* QRS management sought to burden ratepayers with in these proceedings. And, there was a big upside to that risk: the FERC may well have allocated *no* remedy costs to Questar Gas. In short, QRS management's actions in not timely making a demand upon Questar Pipeline to remedy the coal seam gas threat, and, in the event such a demand was not productive, promptly initiating a FERC proceeding, were highly affiliate-interest oriented failures to respond and highly imprudent from a utility management perspective. In the words of the Court:

> Questar Gas's decision not to seek a cost allocation determination from FERC, given the possibility that FERC might have imposed the entire cost on producers rather than on ratepayers, raises further questions regarding the utility's fidelity to its obligations to its customers.

D. Questar Regulated Services Management's Initial Brief Fails to Demonstrate that a CO_2 Plant Paid for by Ratepayers Was a Reasonable Remedy under the Circumstances.

Pages 20-47 of QRS management's initial brief is a detailed summary of the options QRS management stated that it and its Gas Quality Team considered in addressing a solution to the impending customer safety crisis in the winter of 1997-98.

QRS management's initial brief attempts to show that any resort by utility management to the provisions of Section 13.5 in the applicable gas transportation agreement between Questar Gas and Questar Pipeline was doomed to failure because of QRS management's expert's assessment that Section 13.5 does not mean what it says. Had utility management responded in a timely manner to the threat, Section 13.5 could have easily provided at least one legal lever for the utility to assert a claim before the FERC that either Questar Pipeline or the coal seam gas producers should bear the

costs to remedy the threat.

All that aside, however, *even if* the CO_2 plant remedy was the appropriate remedy for reasons of time constraint or otherwise, the plant was constructed, and is owned and operated by a Questar Pipeline subsidiary. Questar Pipeline could just as easily and quickly have paid for its construction and operation. Beyond its unsupportable assertion that the coal seam gas problem was a FERC phenomenon that affected Questar Pipeline just as it did Questar Gas, QRS management has not bothered to provide any justification why it did not seek to impose the costs of the CO_2 plant remedy upon Questar Pipeline. As the record shows, that is really where any remedy costs belong.

E. QRS Management's Initial Brief Fails to Demonstrate that the 1998 Carbon Dioxide Extraction Agreement was Not Imprudent on its Face.

The 1998 Carbon Dioxide Extraction Agreement has been a major issue since the beginning of these proceedings. QRS management's application in Docket No. 98-057-12 sought Commission approval for that agreement, yet the record shows there never was an "agreement" in any meaningful sense. There was only a QRS management allocation of the benefits of CO_2 plant ownership and operation to Questar Pipeline and allocation of the associated cost burden to the utility and its ratepayers. QRS management claims that agreement was a prudent transaction for the utility and its ratepayers. That claim presupposes that QRS management legitimately and adequately represented and protected the utility's interests in the transaction. Given the conflicting interests disclosed in the record, it simply is not reasonable to believe that ever happened.

Moreover, the correctness of that transaction presupposes the correctness of allocating ownership and operation of the plant to Questar Pipeline. The only evidence QRS management offered in the record to justify such an allocation of benefits was the statement:

> Questar Gas does not own or operate transportation or processing facilities upstream of its city gates. In addition Questar Pipeline has field personnel who are located in the vicinity of the CO_2 plant.

Not only is such testimonial evidence inadequate to support such a capital asset allocation, it was effectively rebutted by Division witness testimony, which also demonstrated the fallacy of QRS management's argument that, since Questar Pipeline competitively bid construction of the plant, the affiliate disclosure requirements concerning competitive bidding were complied with:

> Q Does the fact that QTS bid out the design and construction of the plant alleviate the affiliate problem?
>
> A No. But this does illustrate something important. QGC could have done exactly what QTS did. There is no need for the unregulated affiliate in the middle.
>
> Q What about the argument that QGC does not have in house expertise and the affiliate does?
>
> A I don't believe that argument has merit. The decision to have QTS build the plant was influenced by the larger interests of Questar Corporation. My experience is that Questar Corporation moves people between companies within the corporation to accomplish what it wants done. The necessary expertise could have been provided to QGC. To me it is obvious that Questar Corporation saw overall corporate advantages to setting it up the way they have proposed.

The Commission's August 11, 2000 Report and Order in Docket No. 99-057-20 termed the prudence of the 1998 Carbon Dioxide Extraction Agreement "the most troubling question." It may be a troubling question, but the imprudence is clear.

F. QRS Management's Initial Brief Fails to Cite any Contemporaneous Documentary Evidence to Support its Assertions that it Was Acting in the Interests of the Utility and its Ratepayers.

The utility's burden of proof to demonstrate its entitlement to a rate increase surely means that

burden must be met with more than after-the-fact assertions and untimely analyses. QRS management never supported its assertions and argument with any contemporaneous documentary evidence. The pipeline studies it said were conducted at the time a remedy was being considered, the analysis of Section 13.5 of the transport agreement between the utility and Questar Pipeline, the propane injection study it said it conducted at the time a remedy was being considered, its purported analysis of FERC decisions at the time the remedy was being considered – are all unsupported by any contemporaneous documentary evidence. The only documentary evidence QRS management offered to back up its study assertions were after-the-fact analyses made at the time it filed its application for rate recovery. As Division witness Hanson testified:

> I found that the decision making process was lacking a credible or sufficient written analysis, similar to a bid analysis, that is usually part of a capital budget process. Without such a document it is impossible to determine that the choice to enter into a CO_2 removal contract was prudent . . .
>
> The Division's investigation revealed that specific options were discarded without any written explanation . . . Further, no inquiries were made of the staff of the Federal Energy Regulatory Commission (FERC) to determine if something could be done. Nor was any legal review of FERC cases done where any written record was kept . . .

The issue here is not whether QRS management was being forthright in its assertions, but once again, whether it has properly and adequately met its burden of proof. The issue becomes even more acute when one considers QRS management's numerous testimonial assertions that 'Questar Gas considered,' 'Questar Gas decided,' 'Questar Gas concluded,' etc. The reality, of course, is QRS management undertook those purported "Company" actions while at the same time managing and furthering the business of Questar Pipeline. Where are the corporate records and minutes or any contemporaneous written documentation that would lend tangible support to QRS management's otherwise unsupported assertions that it was acting at the time for and on behalf of the utility and its

ratepayers and not for and on behalf of Questar Pipeline and Questar Corporation? QRS management's inability or unwillingness to provide such contemporaneous documentation to support its assertions is itself a demonstration of imprudence in addition to further not meeting its burden of proof. It belies QRS management's claim that "[t]he evidence on the record compels the conclusion that all of the CO_2 removal costs were prudently incurred."

II. THERE IS NO FACTUAL BASIS IN THE RECORD THAT WOULD SUPPORT A COMMISSION GRANT OF PARTIAL RATE RECOVERY OF THE CO_2 PROCESSING COSTS.

The initial briefs of the Division and QRS management argue that partial rate recovery in the form of Commission approval of the CO_2 Stipulation is appropriate in this case. Any award of partial rate recovery must be supported by adequate evidence from the record every bit as much as an award of full recovery does. In either case, the Commission must find and cite sufficient persuasive evidence for its rate recovery decision.

The Division's argument for partial rate recovery is based upon the assumption that utility ratepayers received some new benefit from the CO_2 plant remedy by continuing to receive a safe gas supply. The matter of some new benefit accruing to utility ratepayers as a result of the CO_2 plant remedy is loosely implied but never addressed by the Division or QRS management. If utility ratepayers' entitlement to a safe gas supply is a utility obligation as QRS management asserts, and if utility management negligently allowed that safe gas supply to be jeopardized through years of inaction in the face of a growing threat, as the Committee's initial brief has demonstrated, how is utility management's belated correction of its neglect a new benefit to ratepayers that they should share the cost of? The law generally requires those whose negligence causes harm to others to pay

the costs to correct the harm.

The record shows the only reason precipitate action had to be taken in 1998 was because timely action was not taken earlier by utility management. The record further shows utility management never remonstrated to Questar Corporation or Questar Pipeline, whose business decisions directly caused the threat to the utility's gas supply.

Even if the threat to the utility's gas supply was not foreseeable prior to the winter of 1997, QRS management has provided no credible explanation why the CO_2 plant remedy should not have been implemented at Questar Pipeline's expense since it caused the threat and is the party owning and deriving the revenue benefit of that capital asset.

QRS management's initial brief argues for partial rate recovery in the guise of having the Commission re-approve the CO_2 Stipulation:

> The $5 million per year approved in rates represented approximately 68% of the Company's estimated annual CO_2 removal costs. This amount represented a reasonable and prudent settlement of the amount of CO_2 removal costs to be appropriately recovered in rates – a reasonable compromise taking into consideration the risks and uncertainties that all parties must account for in litigation.

There is certainly policy support in the law for settlements as a means of avoiding otherwise costly litigation. However, the CO_2 Settlement was never supported by parties representing the interests of residential customers and small business customers – a group that constitutes a substantial majority of the utility customers affected. The fact that the CO_2 Stipulation did not achieve the desired objective of avoiding costly litigation, but instead contributed to it, is better support for the likelihood that the settlement was **not** fair and reasonable than it is for any argument that the Commission should approve it now. That aside, the law still requires that Commission make its own determination regarding the justness and reasonableness of any recommended rate. The fact

that the rate is the product of a compromise settlement does not alter that obligation.

In addition to its argument that the stipulated partial rate recovery represents a reasonable compromise settlement, QRS management seeks to justify partial rate recovery on prudence grounds:

> Given the unrebutted testimony on the prudence of the Company in assessing the heat-content problem, the uncontested testimony on its prudence in constructing the CO_2 plant in the manner it did and the testimony on the unacceptable risk of gambling on a timely and favorable outcome had the Company sought to shift costs for the CO_2 removal at the FERC, there is substantial evidence on the record for the Commission to find that CO_2 removal costs were prudently incurred in their entirety. Recovery of the lesser stipulated amount is, therefore, clearly reasonable and appropriate.

Aside from the illogic that, because 100 percent recovery is just, something significantly less is also just, this reasoning has a further fatal flaw: there is substantial unrebutted and uncontested testimony in the record regarding the issue of QRS management's prudence, but that evidence shows QRS management was imprudent, not prudent, in its role as surrogate utility management.

The conclusion the Commission earlier expressed in its August 11, 2000 Report and Order, that the record is insufficient to permit a determination whether affiliate interests influenced the selection of options prior to 1998, is correct in making clear QRS management failed to provide a sufficient record that would permit a determination that the utility's gas processing costs were prudently incurred. It is an accurate assessment of the box QRS management has constructed for itself in these proceedings. By engaging in the pretense that affiliate control and conflicting interests do not exist, it renders impossible the task of demonstrating its CO_2 plant remedy decisions were prudent.

In light of QRS management's failure to address its conflicting affiliate interests and responsibilities, the best face the utility's settlement partner in the CO_2 Stipulation, the Division, could put on the utility's actions in its testimony at the time of the CO_2 Stipulation settlement is QRS

management “was not entirely prudent.” While the Division has advanced its “not entirely prudent” rationale as its policy position for supporting the CO_2 Stipulation settlement, that position is at odds with the prior testimony Division witnesses put into the record. For example, Division witness Hanson testified concerning the several failings by QRS management that prevented him from determining that QRS management’s actions were prudent:

> I investigated the process that Questar Gas Company (QGC) went through in evaluating other alternatives to resolve or deal with the low BTU problem on the southern system. I found that the process was influenced by affiliate relationships in a way that was detrimental to the interests of Utah customers. I indicated that the standard for determining prudence should be whether or not a reasonable person (1) looking out for the interests of QGC and its customers, and (2) with the information available at the time, would have made the decision to contract for the Castle Valley Plant. I found that the decision making process was lacking a credible or sufficient written analysis, similar to a bid analysis, that is usually part of a capital budget process. Without such a document it is impossible to determine that the choice to enter into a CO_2 removal contract was prudent . . .
>
> The Division’s investigation revealed that specific options were discarded without any written explanation . . . Further, no inquiries were made of the staff of the Federal Energy Regulatory Commission (FERC) to determine if something could be done. Nor was any legal review of FERC cases done where any written record was kept . . .
>
> . . . New facilities were required to transport the growing volumes from the coal bed methane area. Transportation contracts with producers of the coal seam gas were contingent on the completion of new facilities. QPC could have said “We don’t have room for your gas” or they could have said, “We will build facilities to take your gas if you will help us with the gas quality needs of our major customer.” Answers to data requests indicate that they never discussed the quality problem with the producers.
>
> In the earlier case there was a discussion of other options that required the construction of physical facilities. Most of these were discarded because the low BTU problem became an emergency and a solution was needed quickly. This time constraint may have been avoided with a more timely recognition of the problem . . .

> In my testimony in the earlier docket I concluded that the decision to build the Castle Valley Plant was based on what was best for Questar Corporation and not on what was best for Utah customers.

Division witness Olson's expert conclusion was:

> [W]ith respect to this hearing record, my view is that QGC has been imprudent in its gas supply activities and is now asking to be bailed out by the Commission . Further, it is clear to me that the affiliate relationship between Questar Gas and Questar Pipeline is not beneficial to Utah ratepayers.

There is certainly no support from Committee testimony that QRS management's actions should only suffer the mild censure that they were "not entirely prudent," nor did the Commission review of the case produce any such conclusion in its August 11, 2000 Report and Order.

The only methodology the Commission found in the record to support its approval of partial rate recovery in its August 11, 2000 Report and Order, was the admittedly impossible attempt to determine what costs might have been assigned to the utility and its ratepayers had the controversy gone to the FERC for resolution. The Commission admitted the attempt was impossible because: "we do not find sufficient record support to suggest the probable outcome had the case gone to the FERC."

The Commission nevertheless expressed the methodology this way:

> The Division confronts this uncertainty in a different way by focusing on the probable consequences of alternative FERC decisions ranging from assigning full cost recovery to producers, assigning these costs, because of the characteristics of its system, to QGC, and alternatives in between. This is a useful way to consider the uncertain outcome of a case that would have been vigorously contested. The Division analysis, which we have summarized above, leads it to recommend recovery of 50 percent of gas processing costs. We therefore find record support for a conclusion that a significant share of the cost recovery burden would have been a QGC, and therefore a local-distribution customer, responsibility.
>
> On this basis, we further conclude that the Stipulation reasonably resolves

> the gas processing cost recovery dispute. The Company testifies that the settlement, which allows it to recover but 68 percent of the costs of gas processing, is reasonable. From its point of view, there is value in ending a two-year old dispute. . . [T]he Division argues the tradeoff to permit recovery of a greater portion of the costs but to cap the recovery at a maximum and to mitigate the risk ratepayers bear by limiting the applicable period to five years is both worthwhile and reasonable.
>
> We conclude that the Stipulation offers a fair and reasonable settlement of the cost recovery issue. We accept the Stipulation.

While the Division's recommendation might provide support for the Commission's "required result" rationale that was subsequently rejected by the Court, it provides no support for a rate recovery determination based upon a finding of prudence or partial prudence. In fact, the Division's mutually exclusive conclusions that QRS management's decisions were "not entirely prudent" and "appear to be influenced by affiliate relations **more than** the financial interests of its customers" [emphasis added], would be, or should be, the kiss of death to any such attempt. A conclusion that utility management's actions were dictated more by affiliate relations than the financial interests of its customers is a conclusion of severe imprudence because it demonstrates that management was working contrary to the fundamental duty the utility has to "operate in such a manner as to give the consumers the most favorable rate reasonably possible."

Just because partial rate recovery in light of a finding of less than complete management prudence may be appropriate in some cases does not mean such an outcome is appropriate in this case. Had QRS management been forthright and factual in its filing, there might be some fair and justifiable reason to allow partial rate recovery despite the conflicting interests and control involved. But that is not the case here.

QRS management's filings intentionally hide its conflicting interests and management responsibilities and Questar Pipeline's and Questar Corporation's causal roles in the threat to the

utility's gas supply. Its assertion that the threat was the result of FERC open access rules was intentionally deceptive and misleading.

Moreover, it has not produced any contemporaneous documents and records that in any way support its claim that the decisions at issue were even "utility" decisions taken in the best interests of the utility and its ratepayers. It has offered no credible evidence to show the threat to the utility's gas supply was unforeseeable before the winter of 1997. It has offered no credible explanation why utility management did not make a timely demand upon Questar Pipeline to remedy at the pipeline's cost any materializing harm to the utility's gas supply, or why it did not initiate a timely action before the FERC.

As discussed above under Section A of Argument I, the Commission has for over a decade labored with the impossibility of attempting to order just and reasonable rates under circumstances where a utility management with conflicting interests refuses to provide the Commission the information necessary to make an informed rate decision. That unfortunate condition will continue so long as the benefit such management and its parent company derive from so acting outweighs the pain of less than full rate recovery.

The tool for the Commission to wield to correct that unacceptable condition is the utility's legal burden of proof. Where it has not been met, the Commission should let the consequence be suffered rather than trying to find some partial rate recovery alternative without the evidence necessary to support it.

The Committee respectfully submits that equity and fairness do not support rate recovery of **any** utility CO_2 processing costs in this case. There is no ratepayer benefit conferred by those costs, as all reasonable analysis of the record shows that, had utility management reacted promptly to the threat to the utility's gas supply posed by Questar Corporation's and Questar Pipeline's business

decisions, there would likely have been no remedy costs to utility ratepayers. In any case, the CO_2 plant remedy confers no new benefit; it merely restores a ratepayer right to a safe gas supply that affiliate decisions and utility management neglect put at risk.

III. RESPONSES TO CERTAIN STATEMENTS IN QRS MANAGEMENT'S INITIAL BRIEF.

Statement 1:

> In *Committeee of Consumer Services v. Public Service Comm'n of Utah ("Decision")* the Utah Supreme Court held that CO_2 removal costs may be included in rates only if the Commission finds that such costs were prudently incurred."

Reply: What the Utah Supreme Court actually said was:

> If the record had permitted, the Commission could have carried out its initial obligation to review the prudence of the CO_2 plant contract and its terms, holding Questar Gas to its burden of establishing that its decision to enter into the contract and the costs it agreed to were prudent and not unduly influenced by its affiliate relationship with Questar Pipeline. *Since the Commission found that no such record was or could be made available, it should have refused to grant a rate increase that included CO_2 plant costs. We therefore overturn the Commission's decision to accept the CO_2 Stipulation and to grant the rate increase proposed therein.* [Emphasis added].

There is no statement or inference anywhere in the Court's Decision that these proceedings were being remanded to the Commission for it to proceed with a prudence determination. The Court concluded that the Commission had already determined the record would not permit that determination to be made. Statement 2:

> (The most likely outcome of a FERC proceeding given the substantive merits of the case, particularly given that Questar Gas was the only Questar Pipeline customer that required CO_2 removal from gas that was in all respects compliant with Questar Pipeline's FERC-approved tariff) [was that Questar Gas would be 'responsible for all CO_2 removal costs'].

Reply: This is nothing more that QRS management's assertion in the record. The Commission

concluded, on p. 35 of its August 11, 2000 Report and Order in Docket No. 99-057-20:

> . . . [W]e do not find sufficient record support to suggest the probable outcome had the case gone to FERC.

QRS management's own Responsive Brief to the Committee's Opening Brief on Appeal to the Utah Supreme Court similarly concluded on pp. 21-22:

> What would have been the outcome if the Company had first petitioned the FERC to declare who had cost responsibility? Not unreasonably, and despite extensive expert testimony on all sides of the question . . ., the Commission concluded that this was a speculative matter, and that it was impossible to answer with any certainty.

Statement 3:

> The motives of Questar Pipeline are irrelevant to a determination of the prudence of Quesetar Gas.

Reply: The motives of Questar Pipeline are very clearly relevant when the issue is conflicting affiliate interests and the same controlling affiliate interest is managing both the utility and Questar Pipeline.

Statement 4:

> Although the Committee speculated that Questar Gas should have anticipated the heat-content problem and taken action to address it sooner, it provided no analytical support for that speculation.

Reply: There is ample record support for the speculation of Committee and Division witnesses that QRS management could have responded sooner to the threat to the utility's gas supply. See pp. 15-20 of this brief for some of that record support. It is QRS management's assertion that it could not have responded sooner that is unsupported in the record.

Statement 5:

> Thus, there is no dispute that Questar Gas was prudent in arranging for the design, construction and operation of the CO_2 plant built by its affiliate Questar Transportation Services.

Reply: There certainly is a dispute in the record regarding that entire matter, and why QRS

management had Questar Gas contract with Questar Transportation Services for gas processing services when it could have just as easily arranged for the construction and operation of the plant itself. [See p.7 of the April 1, 1999 Direct Testimony of Division witness Darrell S. Hanson, Docket No. 98-057-12.] Moreover, there is no evidence in the record that Questar Gas "arranged" for design, construction and operation of the CO_2 plant.

CONCLUSION

QRS management's task in these prudence proceedings was to demonstrate it was prudent in having Questar Gas contract with a Questar Pipeline subsidiary for CO_2 gas processing services. Because of the affiliate control and conflicting affiliate interests evident in the record, QRS management's necessary burden of proof was to demonstrate those decisions were prudent *despite* the affiliate control and conflicting affiliate interests that existed. It has fallen far short of ever meeting that burden. In fact, it consciously avoided ever meaningfully addressing those issues.

As a consequence, its application for rate recovery of the utility's CO_2 processing costs necessarily fails for want of sufficient proof. That same want of proof affects any proposal for partial rate recovery in this case. The record demonstrates QRS management was highly imprudent in how it responded to the coal seam gas threat to the utility's gas supply. Its actions were controlled by conflicting affiliate interests and management responsibilities to protect and further Questar Pipeline's business opportunity in gathering and transporting the coal seam gas that was causing the threat to the utility's gas supply.

The evidence is missing from the record that would support any Commission grant of rate recovery in this case. The proper and necessary Commission decision is the one it has essentially already made in its August 11, 2000 Report and Order: QRS management failed to provide a sufficient record that would permit a Commission determination of full or partial rate recovery.

Respectfully submitted this 21st day of May, 2004.

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CERTIFICATE OF SERVICE

I certify that I mailed or hand-delivered the foregoing **UTAH COMMITTEE OF CONSUMER SERVICES RESPONSE BRIEF** this ____________ day of May, 2004.

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