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To: Public Service Commission

From: Division of Public Utilities
Irene Rees, Director
Energy Section
Artie Powell, Acting Manager
Marlin H. Barrow, Utility Analyst

Date: May 6, 2005

Subject: Docket 05-057-02, Approval of Questar Gas Company's Firm Transportation Agreement with PacifiCorp.

ISSUE:

On March 4, 2005, Questar Gas Company (QGC) filed with the Utah Public Service Commission (PSC) an application for an order approving an Agreement for Firm Transportation to PacifiCorp's Lake Side Generating Facilities (Agreement) between QGC and PacifiCorp. On March 16, 2005, the direct testimony of Barrie L. McKay, in support of the Agreement was filed with the PSC. On May 5, 2005, QGC filed with the PSC, a First Addendum to the Prepared Direct Testimony of Barrie McKay as well as a First Amendment to the Agreement.

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RECOMMEND APPROVAL:

The Division recommends that the Commission approve the Agreement as amended.

DISCUSSION:

The Division began reviewing the Agreement soon after it was filed with the PSC. In the course of this review the DPU asked for clarification of several issues through data requests, which QGC has responded to in a timely fashion.

One of the data requests questioned the impact on QGC's customers if PacifiCorp exercised an early buy-out option as contained in the Agreement (Exhibit #2 Section 2.6(a) of March 16th filing). An investigation of that question led QGC to the conclusion that should PacifiCorp exercise an early buy-out option, QGC customers could be negatively impacted in the cost of service. This led the parties to renegotiate some sections of the Agreement. The renegotiated sections of the agreement were filed with the PSC on May 5th as Exhibit A to the First Addendum to the Prepared Direct Testimony of Barrie L. McKay. Mr. McKay explains the reasons for the changes to the Agreement in his testimony. The Division concurs with those reasons.

The Agreement (Exhibit #2 of March 16th filing), in Section 1.1 miss-stated the miles the main extension of 20 inch steel pipe will require. The correct number of approximate miles is 7.2, which is the basis for the costs estimates and which is correctly shown in exhibit #3 of the filing as well as in Mr. McKay's testimony on line 27 of page 2. The existing Feeder Line #85 will continue to serve the Cedar Fort area, which is west of the proposed Kern River tap, with gas supplies coming from Kern River. One concern of the Division's was the potential of the Cedar Fort customers incurring a higher gas commodity cost due to the Kern Index Price, which is usually higher than the QPC Index price. QGC management states this will not be the case due to segmentation, which will allow QGC to supply Company-owned production and purchased gas to the Cedar Fort area at existing subscribed capacity on Kern River and because the backhaul rate QGC pays to Kern River is equal to the credit QGC receives from QPC for volumes transported on ML 104.

The customers in the Cedar Fort area currently are paying an extension area charge (EAC) to cover the cost of extending FL #85 to serve the area. ($30 / month for fifteen years as established in Docket #99-057-05) Mr. McKay has testified that approximately 5.5 miles of FL #85 that is east of the proposed Kern River tap will be dedicated to the PacifiCorp Lakeside service. These 5.5 miles of 12" pipe has an estimated remaining book value of $1,099,000. QGC estimates approximately 1 mile of the 5.5 miles is currently being used to serve the Cedar Fort area with an estimated book value of $209,000. [5523 ft. (approx 1mile) / 29040 ft. (approx 5.5 miles) = 19.02% * $1,099,000=$209,000]. This $209,000 will be charged to the Lake Side project and will be subtracted from the balance in the Cedar Fort EAC account.

Currently, the Cedar Fort EAC is slightly lagging behind the initial estimate of the required time period to recover the costs. At the present rate per customer and assuming no additional growth, QGC estimates this reduction will bring the EAC recovery time back in line with the original fifteen year estimate. If additional growth is experienced in the Cedar Fort area, this amount of time could be further reduced.

As stated by Mr. McKay in his testimony, there are **five areas** where the terms of this contract between QGC and PacifiCorp differ from QGC FT-1 tariff.   The **first area** is Section 2.5 of the Agreement, Take or Pay. Rather than require an up-front contribution in aid of construction, QGC and PacifiCorp have agreed to a schedule of minimum payments. The schedule of payments, as shown on page 5 of the Agreement, is based on the estimated cost of $13,411,870 for the project and is designed to recover the projected cost of service over the depreciable thirty-year life of the project. In the original agreement, the actual amounts of the minimum payments were to be based on the actual final costs of the project as discussed in Section 1.6 of the Agreement. But in the amended filing, in Exhibit A of Mr. McKay's addendum to his testimony, Section 1.6 was amended to an agreed final cost which will not exceed $13,411,870, exclusive of environmental and right of way costs, which will be paid by PacifiCorp.

For illustrative purposes, the present values shown in Column D of Exhibit 5 of the Agreement are based on receiving 12 equal monthly payments equal to the minimum payment amount for each year. The Division, in a data request, asked for a cost of service study based on the minimum payment schedule.

This study showed the revenue stream, as shown in Column B, page 5 of the Agreement, exceeded the cost of service in every year except years eleven and sixteen. As discussed in Mr. McKay's testimony on page 5, lines 134-140, a levelized fixed cost rate of this project is equal to 14.937% or $1,930,906, (based on a final cost of $13,411,870). Years eleven and sixteen are the first years where the minimum required payment stream, as shown in the exhibit on page 5, steps down below this levelized fixed cost rate of $1.9 million. Because of this, in these two years and only in these two years, the projected cost of service slightly exceeds the required minimum payment. In all other years the required minimum payments exceed or equal the projected cost of service for the project. For the life of the project, the net present value of the minimum payments over the cost of service, discounted at 9.64%, is about $1.7 million, indicating that the customers of QGC will not incur any costs of this project based on the given assumptions.

The **second area** is in the calculation of the fuel reimbursement. The tariff requires a fuel reimbursement based on a fixed percentage of 1.5% of volumes transported. Under this agreement, PacifiCorp will take custody of the delivered gas at the Kern River Tap and any redelivers by QGC to customers along FL #85 will be subtracted from the metered volumes of PacifiCorp's custody meter.

The difference between the custody volumes, after subtracting out the redeliveries to QGC customers, and the metered volumes at the Lakeside Facility will be the responsibility of PacifiCorp. There are limits built into the agreement to protect

PacifiCorp from letting this difference become too great. Under this method, current QGC customers will not be liable for any fuel reimbursement on this portion of feeder line #85.

The **third area** of difference is in the assignment of capacity rights. Under this agreement, PacifiCorp has the right to assign its capacity rights to any other industrial user as long as that industrial user uses the gas for electrical generation at the Lake Side property. PacifiCorp has capacity rights for up to 190,000 Dth per day of delivery. This capacity is more than what is needed for the current generating requirements of PacifiCorp, based on the current design of the Lake Side generating unit.

The intent of this provision is to give PacifiCorp the right to assign to any third party generators this capacity if PacifiCorp desires to let some other party build a second generating unit at the site rather than PacifiCorp build one.

The **fourth area** deals with PacifiCorp's priority in the event of an emergency. Under current tariff provision's, in the event of an emergency, firm transportation customers can be restricted after interruptible customers have their volumes interrupted. Because PacifiCorp nominates its volumes on Kern River and takes custody of those volumes at the new FL#85 Kern River tap, those volumes would have very little impact on helping QGC meet any emergency needs on the QGC distribution system. Because of this and also because PacifiCorp is serving the public need, PacifiCorp has first priority over all other firm transportation customers in emergency curtailment situations.

The **last difference** is giving PacifiCorp the right to receive potential credits beginning in the eleventh year of the agreement when PacifiCorp's annual usage exceeds the minimum volume requirements. The amount of the credit is the difference between the calculated minimum payment and 14.937% of the project cost ($1.9 million), which, as discussed earlier, is the levelized fixed cost of the project.

The minimum payment PacifiCorp is paying during the first ten years of the project is greater than the levelized payment amount of $1,930,906 ($13,411,870 * 14.937%). Because of this, when PacifiCorp's annual usage exceeds the minimum volume requirements in years 11-30, a credit shall be granted to PacifiCorp based on the difference between the $1.9 million levelized amount and the minimum payment requirement. Based on the assumptions in this project, the maximum amount of this credit will not exceed $260,000 in years 11-15 and $618,000 in years 16-30. Because PacifiCorp's minimum payments, during the first ten years of the project, exceed the levelized cost payment requirement, this credit option provides PacifiCorp some assurance that overall minimum payments they make are more in line with the levelized cost rate of the project.

Based on the information furnished through data requests, analysis of the assumptions used in the cost of service model and follow up questions, the Division is satisfied that QGC's existing customer base will not be subsidizing the costs of this project and PacifiCorp's minimum payment requirement, in lieu of an up-front contribution in aid of construction payment, as required by QGC's current tariff, are in line with the QGC's cost of service projections. The Division feels this agreement is in the public interest and recommends the Public Service Commission approve the agreement.

Cc: Barrie McKay, Manager Regulatory Affairs, Questar Gas Company
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