White Paper On Alternative Regulatory Options

I. OVERVIEW

Objective

The objective of this report is to provide a discussion including the pros and cons of the three preferred alternative regulatory methodologies explored by the Working Group. Three goals have been enunciated by the Working Group. Remove the disincentives to promote demand side management, reduce contentions between regulators and the Company, and provide the Company the opportunity to earn its allowed return during periods of declining usage.

II. SCENARIO 1

REVENUE STABILIZATION, "UTAH METHOD" OR MARGIN RECOVERY
Annual Rate Cases With Projected Test Years and Quarterly Reviews

The first option is loosely based on methods that have been approved in other states (such as, South Carolina and Alabama). Appendix A shows a detailed procedure for this methodology, along with a hypothetical time line. Appendix B outlines this method as discussed in the Working Group. This method calls for Questar Gas (the Company or QGC) to file annual rate cases using projected test years through the end of the current year. Thus, the test year would typically contain 8 to 12 months of forecasted data. This is similar to the test year used and approved by the Commission in QGC's latest general rate case, Docket No. 02-057-02. The Commission in that case approved the use of year-end rate base, customers, usage per customer, etc. Since this method involves annual rate cases, the use of average rate base for each component in the case results in a fully synchronized test year that would reflect the period of time in which the rates would be in effect.

The Company would file three quarterly results of operations (ROO) no more than 2 months after the end of each quarter. The year-end ROO would be included as supplemental information in the annual rate case. Each ROO would contain all the regulatory adjustments and methodologies approved by the Commission in the previous general rate case. To make these ROOs most comparable to the annual forecast included in the rate case, the use of annualized, period-ending results would be used. In effect, each ROO would provide the actual earnings, on a regulated basis for the Company based on the circumstances existing at the end of each quarter, presented on an annualized basis.

This actual result, in terms of earned Return On Equity (ROE) would then be compared to the most recent allowed ROE approved by the Commission. A band of 1 percent would be allowed around the approved ROE (50 basis points above and 50 basis points below). If the actual ROE falls outside this band, an adjustment to rates would be made to raise or lower revenues sufficient to move the calculated ROE to the midpoint of the band, or the currently allowed ROE. These adjustments, if necessary would be made in the three quarters in between the annual rate cases on a going forward basis.

Through annual filings and quarterly monitoring, the annual rate cases would be streamlined. For this reason, and due to the fact that the quarterly results could adjust rates, the proposed rates in the annual rate cases could go into effect one month after the filing of the case. This can be seen in the time line included in Appendix A.

In addition to the quarterly ROO reports, this methodology would include the use of service quality standards. Another task force established by the Commission in the final order to Docket No. 02-057-02 addressed service quality standards. That task force agreed upon a set of standards by which the Company has been evaluated since the end of that case. While there are currently no incentives or penalties associated with meeting or failing to meet those standards, such incentives or penalties could be incorporated into this methodology.

Incentives could also be incorporated into other components of the case. For example, if the Company can maintain O&M cost increases below the level of inflation, a portion of the saved expenses could be retained by the Company and the remaining portion could be returned to customers. Such incentives can relieve some regulators of fears that the "Utah Method" will result in the failure of the Company to invest in and/or adopt efficiency measures or technological improvements. Such incentives have been successfully incorporated in many other states.

Appendix A provides a potential procedural schedule for implementing the "Utah Method". It is recommended that the methodology be implemented on a "pilot" basis over a period of 3 to 5 years with a review at the end of the pilot to determine if it should be continued. In addition, the methodology would need to start out with a traditional rate case that would establish the methodology, the range of the ROE and any incentives/penalties.

Pros	Cons
• No change to customers' bills • No billing issues • Process is similar to current with more frequent rate cases and Results of Operations • Removes 20-month forecast issue	• More frequent filing may increase contention • May increase work loads for regulators and Company • May require legislation for banded ROE • Collects fixed costs over variable rates

III. SCENARIO 2

RATE DESIGN SOLUTION
Recover DNG Fixed Costs Through Delivery Charges

The second option identified by the on-going task force for further review is based on the use of rate design to solve the problem. This option attacks the problem at its source and, therefore, is more direct, simple and less complex than the annual rate case option outlined in Scenario 1. This scenario does not require a change to the regulatory process. This approach uses delivery charges and/or small volumetric blocks to recover the fixed costs of the Company. This scenario could be implemented with the current regulatory structure, and perhaps between general rate cases, through a rate design case. This scenario would not require extensive review or quarterly updates, reducing the complexity significantly from Scenario 1.

As was pointed out throughout the COS Task Force meetings, the source of the disincentive for the Company to support DSM is the use of volumetric rates to collect fixed charges. With the current rate design, whenever customers reduce their usage of natural gas, the Company loses DNG revenue. This situation has been the cause of several of the general rate cases the Company has filed since the late 70's. As customers conserve natural gas, the Company is unable to collect the revenues authorized by the Commission. During periods of rapid decline in usage per customer, the Company has always been forced to file general rate cases. Additionally, supporting Demand Side Management (DSM) will further contribute to the decline in usage, causing the Company to lose revenue and eventually to file another general rate case.

During the task force meetings, information was provided to the group and a discussion ensued concerning the potential level of a higher Basic Service Fee (BSF). One of the conclusions of the task force was that unless the higher Basic Service Fee approaches full recovery of the fixed costs, it does not adequately remove the disincentive for the Company to promote DSM. Using data from Docket No. 02-057-02, the Company calculated what such a charge would need to approach. (See Appendix C.) As can be seen in that appendix, the fixed costs per general service customer, including commercial customers, are $23.48. However, it was pointed out that the charge would not have to be the same for every general service customer. There are legitimate differences in costs to serve an individual apartment in a multi-dwelling building than to serve a separate single family dwelling. Although a full cost-of-service study that separates these customers is required to calculate the actual differences in costs, they can be estimated using the current rate design.

Currently, the average residential customer on QGC's system pays $243.98 per year or $20.33 per month in DNG revenue. For an average customer on the Budget Plan (approximately 1/3 of the customers), there would be no difference in the amount paid each month using the current rate design or a rate design that charged $20.33 per month plus the Commodity and SNG charges for the volume of gas used. For an average customer not on the Budget Plan, the total amount paid for the year would be the same, but the winter bills would be lower with a higher Basic Service Fee and the summer bills would be higher.

In the current QGC system, residential customers are categorized into three types of customers: apartments, mobile homes and single family houses. Looking at a greater detail shows that apartment customers are currently paying $164.86 annually or $13.74 per month in DNG revenues, mobile homes are paying $206.19 annually or $17.18 per month, and single family houses are paying $262.20 annually or $21.85 per month. Through a cost of service analysis, these numbers would be revised to reflect the estimated costs placed on the system by each type of customer. However, this shows the type of variation that could be expected. In addition, through the use of a first block rate of 2 – 3 Dth per month, these basic service fees could be reduced by $3.00 - $5.00 per month.

During the early 1980s, the Company employed a rate design in which the monthly customer charge was over $18.00. This level of fixed charge was not widely accepted at that time. The rate design was eventually changed to the current $5.00 fixed charge and a flat commodity rate for most residential customers. At the time, there were few utility type bills, other than the phone bill, that were paid as fixed charges. Since that time, utility type bills for services such as cell phone, internet access, cable TV, water, garbage, sewer, etc. have commonly included fixed charges. Often, these charges are in the $40.00 range per month. In addition, customers in expansion areas on the QGC system have been paying up to $30.00 per month, in addition to the $5.00 BSF and the volumetric gas charges. In general, these charges have been well accepted. As more customers choose to have bills under the Budget Plan, as may happen with the rising costs of natural gas, the use of different levels of BSF becomes transparent. The introduction of a BSF between $10.00 and $20.00 may be much better accepted today that it was 20 years ago.

This methodology has been implemented in other states. Most recently, the North Dakota Public Service Commission approved this type of rate design in an order issued June 1, 2005. During the course of that case, the parties in the case debated the use of a high fixed charge rate design vs. the traditional low fixed charge, higher volumetric charge rate design. Eventually, the parties in the case stipulated to the higher fixed charge and the Commission adopted the stipulation. Attached as Appendix D and Appendix E are summaries of the views of Excel and the North Dakota Public Service Commission regarding the higher fixed charges. While some of the arguments in these documents do not apply to the QGC situation because the Commission has approved the use of a Weather Normalization Adjustment (WNA) in Utah, many of the arguments do apply and it is instructive to see the result of much debate on this subject in a rate case environment.

As was mentioned above, one of the arguments for the use of a higher fixed charge in other jurisdictions is to counter the effects of colder or warmer than normal weather. This issue was addressed by QGC and the Commission in Docket No. 95-057-02, in which the WNA was approved. One of the advantages of adopting a fixed charge rate design to recover all distribution non-gas cost would be the elimination of the need for the WNA, thereby simplifying the bill calculation and presentation to the customers.

Taking from the North Dakota information and summarizing those points that apply to the QGC situation, the following are arguments for a delivery-charge rate design.

1. Bills would be more stable since a greater portion of the total bill would be fixed each month and not dependent on seasonal variations.

2. Customer bills would be simpler, with a single charge for "Delivery Services" instead of up to three charges: a Basic Service Fee, a Charge for gas used, and potentially a revenue stabilization mechanism.

3. A revenue stabilization mechanism (such as that described in Scenario 1 above) would not be required.

4. Over the long term, a BSF charge may generate fewer consumer complaints and questions for both the Commission and the Company, since revenue stabilization type charges or credits are not easily understood and could change on a quarterly basis. Moreover, the customer most likely to complain about a high fixed charge may also complain about an adjustment mechanism that results in a similar fixed billing impact – only in a more convoluted manner.

5. The use of a fixed/variable rate design sends a more accurate cost signal to customers in general and to customers in particular that use natural gas as a backup energy source during peak periods.

6. The Commission would be protected from accusations by customers or the public of complicating bills or attempting to “hide” charges (as with a weather normalization adjustment or the current bifurcated recovery of fixed costs).

7. Frequent rate cases should be avoided because there would be no DNG revenue loss due to declining use per customer over time.

8. Today, consumers have become more accustomed to fixed monthly bills for cable TV, water, internet service, local telephone, and garbage pick-up services, among others. A BSF could be compared to the phone company’s fixed charge for its local wires, while the commodity cost of gas component could be compared to long-distance costs.

9. Since roughly 70% - 75% of a residential bill would still be tied to usage (the commodity cost of gas component), a strong incentive remains for customers to seek ways to conserve energy; however, the change eliminates any disincentives for Questar Gas to actively promote energy conservation by gas customers, since the Company’s delivery revenues would no longer be adversely impacted by declining customer usage.

10. Regulators would be able to audit the Company’s revenues and earnings, as GS-1 DNG revenues would be directly linked to the number of GS-1 customers on the Company’s system.

11. Consumers could be educated about the service/product they are paying for by clearly distinguishing the costs for 1) the natural gas they consume, and 2) the cost to deliver the gas to their homes or businesses. Consumers will better understand the fixed cost nature of the delivery system vs. the variable cost attributes of the commodity gas itself.

12. Revenues are better matched with the associated distribution costs, which is a more efficient pricing methodology. In general, the Company provides each residential customer a standard-diameter main and service line, within a fairly wide range of expected usage. Under current practices, high-usage Residential and Commercial customers effectively subsidize low-usage customers.

13. Most customers (the middle of the bell-shaped usage curve) will not see much of a change in their overall bills, since the Delivery Services charge is primarily a replacement of both the fixed Basic Service Fee and the variable DNG rate. The higher-usage customers should favor this change; it will eliminate the subsidy they are paying and lower their bills. The only group that might complain would consist of the lower-usage customers. But as the previous point explains, some of the lower-usage customers (who are not necessarily low-income) are not currently paying the full cost of their service. In addition, if the cost of service justifies a graduated delivery charge, with lower charges for apartments vs. single family dwellings, this rate design is fair to all customers.

14. Many low-income customers will see their costs reduced. Contrary to common misperception that low-usage customers are also low-income customers, recent studies suggest that personal income level has little predictive relationship regarding gas usage. A poorly insulated or constructed home will need much more gas to heat, and if bills for delivery are based on usage, they will pay more for their service than they would under the traditional rate design.

15. Customer frustration stemming from the use of a decoupling mechanism to address usage-based revenue erosion would be avoided. With a decoupling mechanism rates go up as consumers reduce their consumption.

16. The use of delivery charges is a simpler method (in terms of customer accounting, regulatory effort and billing system changes) to achieve the same objective that decoupling and revenue stabilization mechanisms are designed to address.

Pros	Cons
• Fits under current regulatory environment • Eliminates WNA • Reduces need for future rate cases • Bills more stable, winter bills go down • Bills more understandable • Collects fixed costs with fixed charge • Some low income customers' bills will go down	• May have short-term problem with customer acceptability because of change to customers' bills • Summer bills go up • Potential losses from increased seasonal shut-offs • More complicated for Company to implement than other mechanisms

IV. SCENARIO 3

CONSERVATION ENABLING TARIFF (CET)

The third option identified by the on-going task force for further review is referred to as a Conservation Enabling Tariff (CET). It is loosely based on methodologies that are often referred to as decoupling and that are used in several states around the country including Oregon, Maryland, California and North Carolina. Information for this summary was also gathered from several sources including:

1. A study performed for Pacificorp called the "Demand Side Resource Cost Recovery Collaborative Report", and in particular the "Appendix IV, Final Report – Statistical Recoupling Subcommittee." This report was dated March 31, 1995.
2. "The Theory and Practice of Decoupling", by Joseph Eto, Steven Stoft, and Timothy Belden. This report was dated January 1994.
3. "Decoupling, Conservation, and Margin Tracking Mechanisms – An Overview", by Navigant Consulting, presented in the AGA Rate and Regulatory Issues Audio Conference Series on October 27, 2005.

Removing the link between revenues and usage as a concept can be very simple. In implementation, however, such a program or tariff can be very complicated. The mechanism in use by Northwest Natural Gas in Oregon is an example of a methodology that is more complex. For purposes of a pilot program, the Company prefers a mechanism modeled after what Northwest Natural Gas later proposed in their Washington jurisdiction after they had some experience with the Oregon method and a current proposal by Southwest Gas Company in their Arizona jurisdiction. In both of these proposals, a revenue per customer adjusting mechanism was put forth.

As was stated in the DSR Collaborative Report,

> ". . . there are essentially only two types of decoupling currently in operation: Electric Revenue Adjustment Mechanism (ERAM) decoupling and Revenue Per Customer (RPC) decoupling. Decoupling under an ERAM mechanism breaks the link between revenue and sales by predetermining allowed future revenue based on a future test year. Rates are subsequently adjusted to ensure that the utility earns neither more nor less than this predetermined level of revenue. . . . Decoupling under an RPC mechanism allows future revenues to grow in proportion to customer growth instead of sales. . . . Decoupling removes the disincentive of lost sales associated with investment in [DSM]. . . . Since revenue [per customer] is fixed under decoupling and not profit, utilities maintain the same incentive to cut costs in between rate cases as exists under current regulatory practice."

CET Method

There are a multitude of variations on how this mechanism could be designed and implemented. This scenario attempts to keep it as simple and straight forward as possible. This methodology would apply to only the General Service class of customers (residential and small commercial). By including the larger commercial and industrial customers, a level of complexity would be added to this process that is not necessary. The Demand Side Management programs are typically directed towards the residential and small commercial customers. After gaining experience with the pilot program, the mechanism could easily be expanded to include other customer classes if desired.

The CET methodology first calculates the allowed GS revenue per customer by month. On an on-going basis, the actual revenue per customer each month is compared to the allowed and any difference, higher or lower, is booked into a balancing account that is then amortized periodically over the volumetric portion of the rates. The algebraic formula for the accrual portion of this methodology can be illustrated as follows:

Authorized Revenue per Customer per month: $RPC^{Auth\ 1\text{-}12} = Rev^{Auth\ 1\text{-}12} / \#\ Cust^{Auth\ 1\text{-}12}$

Actual Revenue per Customer per month: $RPC^{Actual\ 1\text{-}12} = Rev^{Actual\ 1\text{-}12} / \#\ Cust^{Actual\ 1\text{-}12}$

Monthly Accrual to Balancing Account: $RPC^{Auth\ 1\text{-}12} * \#\ Cust^{Actual\ 1\text{-}12} - Rev^{Actual\ 1\text{-}12}$

The amortization is accomplished by calculating the percentage change to Block Rates as the Cumulative Balancing Account balance divided by the forecast block revenue for the future 12 month period. The percentage is applied to block rates and the rate change is contemplated to be implemented contemporaneous with pass through rate changes.

While this mechanism ensures that the revenue per customer is maintained between rate cases, it does not ensure that the return earned by the Company is maintained. For one thing, the mechanism does not address the expense side of the earnings equation. For this reason the Company continues to have the incentive to operate efficiently and adopt technological improvements whenever possible. Second, maintaining the current revenue per customer does not necessarily ensure that the costs of serving additional customers are being recovered.

The following table illustrates how this methodology would have been used at the end of the last general rate case, Docket No. 02-057-02. This table shows the calculation of the allowed revenue per customer per month given the final revenue requirement and GS customers included in the final order. The allowed revenue per customer shown in column C would remain unchanged until the next general rate case and would be compared each month to the actual GS DNG revenue per customer to arrive at the amount over- or under-collected to be booked into the balancing account. Appendix E to this report shows how this methodology would have operated in the time since the last rate case.

Calculation of Allowed Revenue per Customer

	Month	(A) GS-DNG Revenues \1	(B) Utah GS Customers	(C) Allowed Rev/Cust
1	Jan	$32,610,091	725,526	$44.95
2	Feb	$27,371,599	725,343	$37.74
3	Mar	$21,945,654	724,607	$30.29
4	Apr	$14,756,548	723,001	$20.41
5	May	$9,303,854	721,092	$12.90
6	Jun	$7,891,373	720,765	$10.95
7	Jul	$7,586,194	719,478	$10.54
8	Aug	$7,685,653	720,791	$10.66
9	Sep	$9,384,057	724,506	$12.95
10	Oct	$13,255,759	728,654	$18.19
11	Nov	$22,394,098	736,266	$30.42
12	Dec	$31,515,464	740,556	$42.56
13	Total / Average \2	$205,700,345	725,882	

\1 Excludes Service Initiation Fees

\2	Docket 02-057-02 final	719,344	GS-1
	year end customers used	6,538	GS-S
	to calculate final order.	725,882	

One of the advantages of this method over that presented in Scenario 2 is that the current rate design could be maintained and future rate designs can reflect Commission ordered methodologies. Customers would see very little change in the calculation of their bills. In addition the use of the graduated BSF would continue to allocate the collection of costs to different sizes of customers while maintaining a volumetric component of the bills.

Statistical Recoupling Method

The statistical recoupling mechanism, addressed by the report of the Statistical Recoupling Subcommittee, is a further refinement and complication of the CET methodology. Instead of maintaining a fixed revenue per customer between rate cases, the recoupling mechanism uses econometric models to estimate, based on economic variables, prices, weather, customer growth, etc., what the revenue per customer should be for the current period. That value is then compared to the actual revenue per customer to arrive at the amount to be booked into the balancing account. Everything else in the methodology remains the same. While the Company is not opposed to the recoupling methodology, the simpler, more direct approach of the RPC is preferred for the pilot program. The recoupling is an improvement that could easily be added at a later time, if desired.

ERAM Decoupling Method

The use of the ERAM type of decoupling, as is used in Oregon and California, usually includes the use of formulas, indexes, efficiency measures, etc. to compensate for the growth in

customers between rate cases. Again, the Company believes that the complexity of these mechanisms is not necessary to meet the goals of implementing a decoupling mechanism. More complex does not necessarily mean better.

Preferred Method

Appendix F presents a summary of how the proposed CET methodology would have worked had it been implemented at the end of the Company's last general rate case (Docket No. 02-057-02). In that case, rates were made effective at the end of 2002. The total revenue requirement in that case for the General Service classes (GS-1 and GSS) amounted to $205,700,345 and was based on year-end rate base and year-end customers. To arrive at the monthly revenue per customer for use in the CET, the monthly revenues are divided by the number of customers used in the rate case. In Column G of Appendix F, you can see how the balancing account would change from month to month over this period, including the amortizations. On Line 3 you can see that the balance after the first three months following the order in Docket 02-057-02 shows an over collection of $1,537,602. This is the result of the average usage per customer in 2003 being greater than the usage per customer used in the rate case calculations. As expected, a rising usage per customer would result in an over collection and a reduction of rates over the amortization period. Column F shows the monthly impact of having the balance amortized every 6 months over the volumes expected over the succeeding 12 month period.

Interest should be calculated on the over- or under-collection in the balancing account just as they are currently calculated on the 191-Account balance. That is, a 6% annual rate of interest is calculated on the over- or under-collected balance.

Pros	Cons
• No change to customers' bills • No billing issues • Easy to implement • Will reduce need for future general rate cases based on revenue losses • Rate adjustments may mitigate other rate changes	• Collects fixed costs over variable rates • May increase need for future general rate cases based on expense increases • Rate adjustments may compound other rate changes

APPENDIX A
Revenue Stabilization Administrative Procedure

Proposed Methodology

The filing of a rate case would be the beginning in initiating the revenue stabilization option. In the initial rate case, the methodologies would be approved that would be used in the quarterly ROO reviews and the subsequent annual rate cases during the pilot period. For example, a pilot program could be established that would last for 3 years. The methodologies used could include the test year determination, the forecasting and allocation methodologies, the standard set of adjustments and the time frames for filing and implementing rates.

This scenario follows the test year and forecasting methodologies used in the Company's latest general rate case, Docket No. 02-057-02. The test year could be made up of some historical and some forecasted information. However, the test year could be comprised of average test-year information with known and measurable adjustments, rather than the year-end data that was used in that case.

The key to this option is the review period in which the projected test year used in the case is compared with actual results. This comparison would be made in the three quarterly ROOs filed by the Company between annual cases. The reviews would identify variations in revenues, expenses and rate base from those forecasted in the case and would calculate a fully-adjusted, annualized, actual ROE earned by the Company for the period ending that quarter. In other words, the ROO would use the year-end information as was used in Docket No. 02-057-02. However, because the ROO would not be a forward looking analysis, it would be most appropriate to compare with the forecasted test year used in the annual rate case. The methodology would also provide the ability for the Commission to approve adjusted rates for deviations from forecasted rates that caused the Company to under- or over-earn for the period. It is important to include these provisions in order to provide protection for the customers and the Company from significant, unexpected gains or losses in revenues or expenses. Without such a mechanism, it may be difficult for the parties to reach agreement on the rate case forecasts, and would certainly cause the process to be much more contentious.

Changes in rates would only be on a "going forward" basis, thereby avoiding the issue of whether this method includes retroactive ratemaking. If it is determined that legislation is necessary to allow the review and subsequent rate adjustments, the parties could jointly approach the legislature with such legislation.

Hypothetical Time Line:

April 1, 2006	The Company files a complete rate case. The test year is a forecast of all rate case items for calendar year 2006 and is based on average rate base, customers and revenues. Return on equity (ROE) and capital structure are fully contested and it is requested that the Commission issue an order regarding these issues that would include a range in which the Company may earn. The order would include a methodology for the Company to adjust rates each quarter if the actual ROE for the 12 months ending that quarter are higher or lower than this range.
August 1, 2006	Rates from the full rate case go into effect through a stipulation of revenue requirement issues. Cost allocation and rate design issues could continue to be contested and implemented at a later date, if necessary.
September 1, 2006	Company files ROO for period ending June 30, 2006. Rates are adjusted up or down if the fully adjusted ROE for this time period falls outside the range established in the rate case.
December 1, 2006	Company files ROO for period ending September 30, 2006. Rates are adjusted up or down if the fully adjusted ROE for this time period falls outside the range established in the rate case.
April 1, 2007	The Company files a forecasted 2007 rate case. As in the previous year, the case is based on calendar year 2007 and is based on average rate base, customers and revenues. Also included in this filing is the ROO for period ending December 31, 2006. Since there have been several reviews between cases, this rate case is merely an update using the ordered adjustments from the previous case and forecasted information through the end of the year.
May 1, 2007	Rates from 2007 rate case go into effect.
June 1, 2007	Company files ROO for period ending March 31, 2007. Rates are adjusted up or down if the fully adjusted ROE for this time period falls outside the range established in the rate case.
September 1, 2007	Company files ROO for period ending June 30, 2007. Rates are adjusted up or down if the fully adjusted ROE for this time period falls outside the range established in the rate case.
December 1, 2007	Company files ROO for period ending September 30, 2007. Rates are adjusted up or down if the fully adjusted ROE for this time period falls outside the range established in the rate case.
On-going	The schedule continues as outlined above.

DRAFT – 11/23/2005

APPENDIX B
ALTERNATIVE REGULATION

1. Annual Forecasted Test year
   - O&M
   - Rate Base
   - Revenues
     i. Usage per Customer
     ii. Customers

2. Service Quality Standards

3. Quarterly True-Up

4. Banded ROE

5. Incentives

APPENDIX C
Example of Graduated Basic Service Fees by Customer Type

Questar Gas Company – Utah Jurisdiction
Current Distribution Non-Gas Contribution
From Docket No. 02-057-02

		Yearly	Monthly
1	Typical GS-1 (115 Dth)	$295.81	$24.65
2	GS-1 & GSS (Residential, Commercial, Industrial)	281.78	23.48
3	GS-1 (Residential Only)	243.98	20.33
	GS-1 Residential (Apartment, Mobile Home, Single Family)		
4	Apartment	$164.86	$13.74
5	Mobile Home	206.19	17.18
6	Single Family	262.20	21.85
7	Total	$243.98	$20.33

APPENDIX D
Benefits of Fixed Monthly Charge

Northern States Power Co. d/b/a Xcel Energy
Gas Utility – State of North Dakota
Benefits of a Single Residential Fixed Monthly Charge
for Natural Gas Delivery Services

1. Residential customers would no longer overpay for the cost of gas delivery service in colder than normal winters and underpay in warmer than normal winters;
2. Bills would be more stable since 24.1% of the total bill would be fixed each month and not dependent on changes in weather or usage patterns (versus 8.4% currently):
3. Customer bills would be simpler, with a single charge for "Delivery Services" instead of up to three charges: a Basic Service Charge, a Distribution Charge, and potentially a revenue stabilization (partial decoupling) mechanism;
4. Eliminates altogether the need for revenue stabilization mechanisms (such as Xcel Energy's proposed Partial Decoupling Rider or MDU's Distribution Delivery Stabilization Mechanism [DDSM]), which are more difficult to explain to customers, result in regularly changing adjustments (positive and negative), create the potential for error, and may be burdensome to implement and maintain;
5. Over the long term, a single Residential Delivery Services charge should generate fewer consumer complaints and questions for both the Commission and the Company, since decoupling riders and DDSM type charges or credits are not easily understood and will change each month. Moreover, the customer most likely to complain about a high fixed charge may also complain about an adjustment mechanism that results in a similar fixed billing impact – only in a more convoluted manner;
6. Would send better economic signals to customers who request to use Xcel Energy natural gas service only as a backup energy source during peak periods, thereby creating higher costs for other Xcel Energy natural gas customers
7. The Commission would be protected from accusations by customers or the public of complicating bills or attempting to "hide" charges (as with an adjustment mechanism or the current bifurcated recovery of delivery services costs);
8. Should extend the length of time between gas rate cases because there would no delivery services revenue loss due to declining use per customer over time.
9. Today, consumers have become more accustomed to fixed monthly bills for cable TV, internet service, local telephone, and garbage pick-up services, among others. A fixed Delivery Services charge for Xcel Energy's local gas pipes would be comparable to the phone company's fixed charge for its local wires (while the wholesale Cost of Gas component would be comparable to long-distance costs);
10. Since roughly 75% - 80% of each residential bill would still be tied to usage (the Cost of Gas component), a strong incentive remains for customers to seek ways to conserve energy; however, the change eliminates any disincentives for Xcel Energy to actively

promote energy conservation by gas customers, since the Company's delivery revenues would no longer be adversely impacted by declining customer usage;

11. Company earnings in North Dakota would not be as unpredictable as a result of abnormal weather swings. It would also be easier for the Commission to audit the Company's revenues and earnings, as residential regulated delivery revenues would be directly inked to the number of residential customers on the Company's system;
12. Would mitigate the impact of "Budget Billing" true-ups on customer bills because less of the bill would be subject to the variations of weather and its subsequent impact on usage;
13. Helps to educate consumers about the service/product they are paying for by clearly distinguishing the costs for 1) the natural gas they consume, and 2) the delivery of the gas to their homes or businesses. Consumers will better understand the fixed cost nature of the delivery system vs. the variable cost attributes of the commodity gas itself. Consumers will also better understand the component of their bill that Xcel Energy is responsible for.
14. Provides a better match of revenue with the associated distribution costs, and is therefore a more efficient pricing methodology. In general, the Company provides each residential customer a standard-diameter pipe, regardless of their expected usage. Under current practices, high-usage Residential customers effectively subsidize low-usage customers;
15. Most customers (the middle of the bell-shaped usage curve) won't see much of a change in their overall bill, since the Delivery Services charge is primarily a replacement of both the fixed Basic Service Charge and the variable Distribution Charge. The small group of high-usage customers should favor this change; it will eliminate the subsidy they are paying and lower their bills. The only group that might complain would consist of relatively few low-usage customers, since their bills will rise significantly on a percentage basis (although only $4-6$ dollars per month more than the more traditional Option A rate design). But as the previous point explains, low-usage customers (whom are not necessarily low-income) are not currently paying the full cost of their service;
16. Many low-income customers will see their costs reduced. Contrary to common misperception that low-usage customers are also low-income customers, recent studies suggest that personal income level has little predictive relationship regarding gas usage. A poorly insulated or constructed home will need much more gas to heat, and if bills for delivery are based on usage, they will pay more for their service than they would under the monthly Distribution Charge;
17. Avoids customer frustration stemming from the use of a partial decoupling mechanism to address usage-based revenue erosion, whereby surcharges only get larger the more consumers reduce their consumption.
18. Represents a much lower cost method (in terms of customer accounting and billing system IT changes) to achieve the same objective that real-time partial decoupling and DDSM mechanisms are designed to address.

APPENDIX E
Excerpt From The North Dakota PSC Order Regarding Fixed Charge

NOTE: In the following excerpt from the North Dakota order, there are references to Option A and Option B. In this case, Option A refers to a rate design option that was proposed in the case in which the traditional approach of using a relatively small customer charge or Basic Service Fee is coupled with volumetric rates to recover the utility's fixed costs (this is consistent with Questar Gas' current rate design). Option B is a rate design proposed in the case, and ultimately agreed upon through stipulation, that uses a high monthly fixed charge to recover the utility's fixed costs. This concurring opinion expresses, from the Commission's point of view, the benefits of the high fixed charge option.

CONCURRING OPINION
Commissioner Tony Clark

June 1, 2005

Northern States Power Company
Natural Gas Rate Increase
Application

Case No. PU-04-578

Advocacy staff and Xcel Energy have proposed two settlement options for the commission to consider in this case. In deciphering whether option A or B is best for consumers, option B wins in a landslide. Average residential rates will be lower under option B than under option A. The new billing format will decrease the price volatility in winter gas bills. It ends unfair rate discrimination against customers living in older homes. And it helps lower the chance that we will hear another rate case in the near future.

Xcel appears entitled under the law to an increase of some amount. Even advocacy staff acknowledges such by virtue of the proposed settlement that is before us. Under the settlement the commission is approving, the increase will only be about $1 a month averaged over the course of a year for a typical Xcel customer. While no one likes even a small rate increase, it should be noted that regulated rates have been exceptionally stable for Xcel. Over the past 20 years, there will have now been two rate decreases and two rate increases that essentially net each other out. (I only wish the unregulated cost of gas was as stable. For this, federal policy makers should be ashamed for their lack of attention. But I digress.)

The most noticeable change being implemented is that billing formats have been substantially improved in a way that most customers will appreciate. It is an accepted ratemaking principle that fixed, non-usage sensitive costs should be recovered through fixed charges and variable, usage sensitive costs should be recovered through variable charges. Unfortunately, regulators and utilities across the country have too often drifted from sound economics in favor of less than straightforward ways of implementing utility rates. A common

trick for hiding rate increases is to incorporate the increase into volumetric (usage-based) charges. I applaud this commission, its staff and Xcel for providing an option that does not fall into this trap. It is, however, easy to see why some regulators and utilities find such schemes so appealing. Volumetric charges are hard to understand. They are calculated in fractions of cents and are based on usage, so it is difficult for consumers to ever know when and how their rate has increased. It is a perfect solution for those wanting to deflect and obscure the attention of the general public.

But political expediency for regulators and utilities carries a heavy price for consumers. Moving these fixed costs into variable charges does not mean that consumers pay any less. In actuality, they pay just as much over the course of time as they would if sound decisions were implemented. (Under Option A, they would pay more.) Instead, when fixed costs are recovered through usage, consumers have the burden of paying for most of the costs of the distribution network when they can least afford it, in the middle of winter. This is especially painful for consumers in a northern state like ours. Residential gas usage is relatively stable in sunbelt states, therefore recovering distribution costs via the volume of gas used may not be so offensive, because the costs will naturally be spread throughout the year. Indeed, irrational usage-based charges might even be somewhat tolerable where usage is somewhat consistent throughout the year. Electricity usage, for example, is becoming much less seasonable for most utilities. But in North Dakota, we know all too well that natural gas usage surges during our coldest months. This means that any usage based gas charge, such as proposed in settlement option A, will be paid for disproportionately when usage is the highest, and when the unregulated cost of the gas is also highest. When gas distribution costs are nearly all fixed regardless of usage, I cannot fathom why consumers should be asked to pay more during cold weather as opposed to warm. The option the commission is selecting will be preferred by a majority of consumers, by far. Helping to mitigate the extreme price volatility of winter gas bills will be welcomed by consumers. While the total monthly bill will be only a few dollars higher for most consumers during the warmest months, it is estimated to reduce an average January bill by over $25. (It should be noted that the cost of gas itself will still be a usage based charge, which is entirely appropriate for obvious reasons. For this reason, consumers' bills will still be more expensive when gas usage is the highest, and consumers will still have the incentive to conserve energy.)

Placing fixed costs in usage-based charges can also add a significant burden to those living in older homes – often our senior citizens and those on fixed incomes. I formerly represented north Fargo in the legislature. That portion of the city is a prime example of why inappropriately applied usage charges can discriminate against these customers. Legislative District 44 is one of the most established residential districts in the state. The residences within it are overwhelmingly single family homes, and most of them have been there for some time. Older homes tend to be less well insulated than newer homes. They typically also have furnaces which cannot compare to the super-high efficiency furnaces now standard in most newly constructed homes. The distribution costs associated with these homes are no more than of any other home on the network. (In fact, a strong case can be made that they cost less due to a variety of factors.) Yet irrationally recovering fixed, non-usage sensitive costs through usage-based charges, such as under option A, requires these customers to shoulder an unfair portion of the cost of the distribution network. Option B ends such unjustifiable subsidies and discrimination.

Finally, by selecting option B, the Commission is, hopefully, reducing the chance that we will be holding another rate case soon. Cost recovery via usage creates utility company revenue streams that fluctuate based on the technological efficiency of the equipment using the natural gas, as well as seasonal weather fluctuations. Such uncertainty benefits neither consumers nor the utility, because there is a negligible ability for any single party to control them. Because the utility company has more certainty as to what its revenue stream will be, efficient planning that benefits both consumers and the utility is enhanced.

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Tony Clark, President