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To: Public Service Commission

From: Division of Public Utilities
Philip J. Powlick, Director
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Marlin H. Barrow, Technical Consultant
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Date: July 12, 2010

Subject: Questar Gas, Docket Nos. 10-057-09 (Pass-Through), 10-057-10 (CET) and 10-057-11 (DSM).

ISSUE:

On June 24, 2010, Questar Gas Company (QGC) filed three applications with the Public Service Commission (PSC).

In Docket No. 10-057-09, QGC asks for approval to increase both the supplier non-gas cost and the commodity rate components of the Company's Utah natural gas rates in order to pass-through an expected total increase in gas costs of $48,323,000. If approved, a typical GS class customer, whose annual usage is 80 decatherms (Dth), will see a $37.48 increase in their annual bill.

Docket No. 10-057-10 is a request to amortize the May 2010 Conservation Enabling Tariff (CET) credit balance of ($3,471,074) (over-collection) in Account 191.9 and adjust the CET component in Block 1 and 2 of the GS class distribution non-gas (DNG) rate. If approved, a typical GS customer, whose annual usage is 80 decatherms, will see a $5.06 decrease in their annual bill.

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Docket No. 10-057-11 is a request to amortize a balance of $36,000,000 in the Demand Side Management (DSM) deferred account 182.4 and adjust the DSM rate component of the DNG rate for the GS rate class. If approved, a typical GS customer, whose annual usage is 80 decatherms, will see a $5.98 decrease in their annual bill.

If all three applications are approved, a typical GS customer, whose annual usage is 80 decatherms, will see a $26.42 increase in their annual bill. All three applications request an effective date of August 1, 2010.

RECOMMEND APPROVAL:

After a preliminary review of all three applications, the Division recommends that all three applications be approved on an interim basis, as filed, with the proposed rates becoming effective August 1, 2010.

DISCUSSION:

DOCKET NO. 10-057-09 COMMODITY AND SUPPLIER NON-GAS COSTS (191 Account)

This filing is based on projected Utah gas costs of $544,678,432. The commodity portion represents an increase of $44,951,000 while the Supplier Non-Gas (SNG) increases by $3,372,000 for a total increase of $48,323,000 for firm sales customers. These results are based on projected gas costs from August 2010 through July 2011.

In this application, QGC is requesting to increase the commodity rate from $4.17/Dth (rounded) to $4.24/Dth (rounded), [1] resulting in a $7,173,000 increase in the base commodity gas costs for firm sales customers as a result of the projected increase in market prices for natural gas expected during August 2010 through July 2011. Adding to the commodity gas cost increase is an increase in the 191 account amortization rate. This rate is increased from $0.00/ Dth, which went into effect June 1, 2010[2] to $0.37/Dth (rounded)[3]. The reason for this increase will be discussed in more detail in the 191 amortization section. The amortization rate increase results

[1] DPU Exhibit 1, lines 11 & 31 for the actual rates.
[2] Docket No. 10-057-05.
[3] DPU Exhibit 1, lines 12 & 32 for the actual rates.

in an increase of $37,778,000 for firm sales customers which, when added to the $7,173,000 increase from market rates, equals the $44,951,000 in commodity gas costs. Interruptible sales customers can also expect an increase of $1,332,000. The Supplier Non-Gas (SNG) base rates also have increased by 3.51%, further increasing firm sales customers SNG costs by $3,372,000.

The net effect of the increase in gas costs to a typical GS customer, assuming an annual usage of 80 decatherms per year, is an average increase in their annual bill of $37.48, an increase of 5.54%, from gas costs in current rates.

Gas Supply

QGC expects a total Utah system requirement of 115.6 million decatherms. Of this, 105.1 million decatherms will meet the projected sales requirement, 5.0 million decatherms is required for gas volume reimbursement for gathering, transportation and distribution fuel use, while 5.5 million decatherms is planned to increase gas storage inventory levels. To supply the Utah system requirement, QGC plans on utilizing 65.4 million decatherms of WEXPRO production, (56.6% of total requirements), at a net projected cost of $269,761,000[4] while purchasing from third party producers another 50.1 million decatherms, (43.4 % of total requirements), for $209,503,000[5]. Transportation and storage costs are projected to be $65,414,000 for an estimated total cost to Utah customers of $544,678,000.[6]

As noted in the filing, and as provided for in QGC's Tariff for Natural Gas Service in Utah, PSCU 400, §2.10, pp. 2-11 through 2-13, these gas costs represent a direct pass through of costs. These costs do not impact the operating profit or rate of return of QGC except for $3,751,000[7], which is the Utah allocation of the pre-tax return on the working storage gas inventory approved by the PSC in Docket No. 93-057-01 and based on the pre-tax rate of return from the weighted cost of capital approved in the Settlement Stipulation in QGC's most recent rate case, Docket No. 09-057-16.

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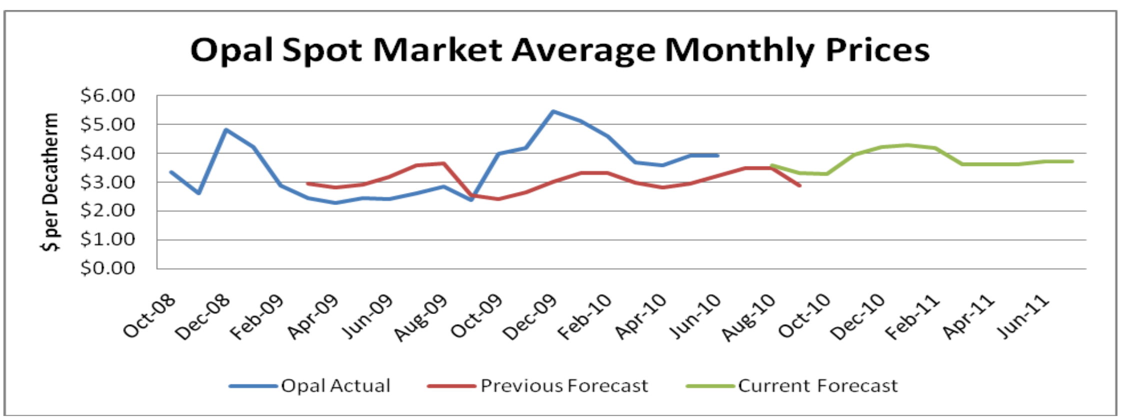
[4] QGC Application, Docket No. 10-057-09, Exhibit 1.5, Line 5 Column E.
5 Ibid, Line 6, Column E.
6 Ibid, Line 14, Column E.
7 Ibid, Line 13, Column E.

Natural Gas Spot Prices

Since the time the PSC approved the last pass-through request, effective October 1, 2009 (Docket No. 09-057-12), actual prices have trended above the previously forecast prices. In this filing, QGC utilizes an average forward looking twelve month forecast spot price of $3.76/Dth compared to $3.04/Dth in the previous filing. Figure 1 below shows the actual first of month spot prices for natural gas at Opal, Wyoming from October 2008 through June 2010 compared to the forecasted prices used in the previous pass-through application in Docket No. 09-057-12, as well as the forecast prices for the August 2010 through July 2011[8] time period used in this application. The Division wishes to point out that from October 2009 through June 2010, actual prices have been higher when compared to the forecast prices that are the bases for setting the rates QGC charges its customers. This divergence of actual prices from forecast is a major reason why QGC is currently under-collected in its 191 account and why this application is requesting to increase the 191 amortization rate that will be discussed below.

Figure 1

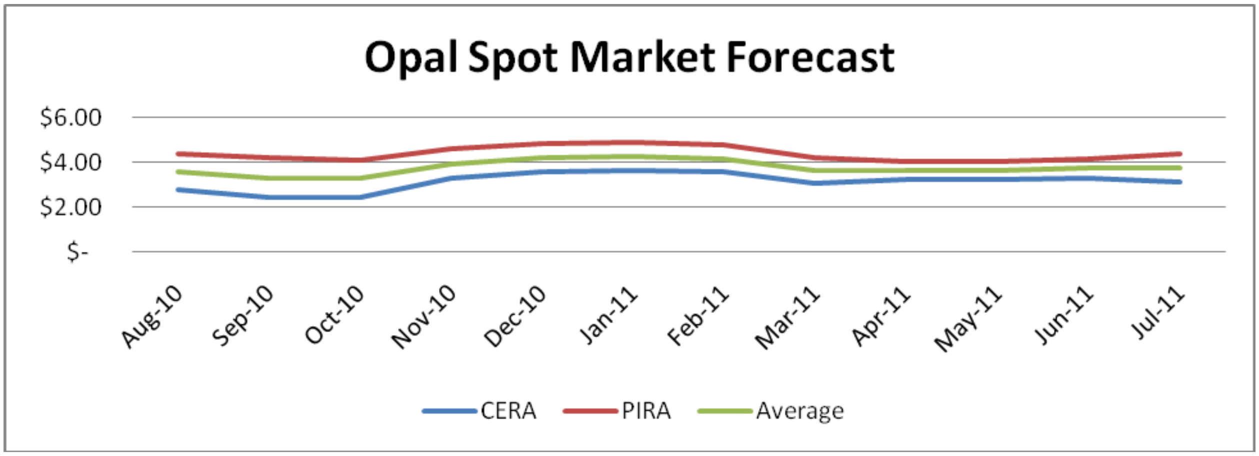


The price forecast in this filing is based on an average of future price projections by two different forecasting entities. Those two entities are Cambridge Energy Research Associates, Inc. (CERA) and PIRA Energy Group (PIRA). The two price forecasts for CERA and PIRA are

[8] Arithmetic average of PIRA and CERA forecast from August 2010 to July 2011 used in pass-through application Docket No. 10-057-09.

displayed in Figure 2. As shown in the chart in Figure 2, there is some disparity between the two forecasting entities, which may be more indicative of some uncertainty on future price expectations in the Rocky Mountain region for the next twelve months.

Figure 2



Pricing Hedges

The WEXPRO production and QGC's gas storage practices play an important role in QGC's plan to "hedge" against natural gas price volatility while meeting their overall supply plan. These practices generally allow QGC to keep WEXPRO production flowing during the summer months to meet summer demand and to inject into storage for later use during the winter months. The use of storage gas minimizes the need to purchase gas in the winter. As previously mentioned, the Utah allocated WEXPRO production is 65.4 million decatherms or 56.6% of the gas supply mix. The weighted cost of this production is $4.12/Dth[9] which is a decrease of $0.93/Dth or 11.0%, since the last filing in Docket No. 09-057-12. Based on current spot market prices, the average net cost of the WEXPRO production is $0.06 /Dth less than the projected average cost of $4.18/Dth[10] for purchased gas.

[9] QGC Application, Docket No. 10-057-09, Exhibit 1.4, Line 5, Column E.
[10] QGC Application, Docket No. 10-057-09, Exhibit 1.4, Line 6, Column E.

QGC further attempts to manage gas price volatility, and thereby “hedge” or mitigate customers’ exposure to that volatility, by continuing its planned purchase program. For this filing, as previously discussed, in addition to the 65.4 million decatherms of company owned production, QGC has developed a Utah gas supply portfolio of 50.1 million decatherms. Of the 50.1 million decatherms of purchased gas, 13.4 million decatherms are for winter peaking gas. The remaining 36.7 million decatherms of purchase gas consists of spot market purchases and fixed price contracts. Currently, depending on future movements in the price of natural gas, the fixed price contracts have a target goal of 30% of the winter base load requirement. An additional $2,000,000 is included in this filing to allow QGC to purchase price-capped supply contracts. However, the price of such caps is currently too high to be cost-effective. The extra $2,000,000 provides the company with the option to act if and when capped contracts prices move downward. These approaches were developed through continued meetings with regulators to provide updated information regarding this planned “hedging” program and current expectations in the gas market.

Amortization of Existing 191 Account Balance

Experience has shown that the natural gas commodity price forecast used by QGC will not exactly match the actual prices as they unfold with time, especially with the market volatility in energy prices that has existed in the past, as shown in Figure 1 above. This fact is demonstrated by following the monthly commodity balances of the 191 account. In the September 2009 forecast, in Docket No. 09-057-12, there existed an over-collected balance of $24,880,000 and as a result of this, QGC established, with PSC approval, a 191 amortization credit rate of ($0.24106)/Dth. However, as illustrated in Figure 1, actual gas prices have increased above forecasted spot market prices (or gas cost currently being collected in rates) such that in May 2010, in order to begin to mitigate the effect of this increase in actual gas costs, in Docket No. 10-057-05, the PSC authorized QGC to remove the ($0.24106)/Dth credit from rates, effective June 1, 2010. Since that time, there has continued to be an under-collection such that in this

Docket, QGC is requesting to increase the 191 amortization rate from $0.00/Dth to $0.37/Dth (rounded) to begin amortizing a $37,777,000 under-collected May 2010 balance.

Supplier Non-Gas Costs (SNG):

In contrast to the volatility seen in the price of natural gas, the SNG costs are relatively stable and predictable since those costs are set by contractual rate agreements. Therefore, in Docket No. 09-057-03, QGC proposed and the Division supported, setting the SNG amortization rate annually beginning in each fall pass-through. QGC projects total SNG costs, in this filing, to be $100,107,000.[11] At current rates, SNG revenues that would be collected are projected to be $96,492,000.[12] QGC is still projecting that by this fall, the current over-collected balance in the SNG portion of the 191 account will be ($245,000).[13] Therefore, QGC is requesting a 3.51%[14] increase to the SNG base summer and winter rates as shown in DPU Exhibit 1, line 29 due mainly to the increase in gathering expenses associated with the WEXPRO production. The SNG amortization rate will be trued up in the fall pass-through application.

191 Account Rate Details:

Lines 27 through 33 of DPU Exhibit 1 shows a summary of the SNG and commodity rate changes proposed in this application for the GS Rate Schedule while lines 7 through 13 show the current GS rates. Netting the changes requested from the current rates results in an increase in the GS commodity rates of $0.44/Dth (rounded) for both the summer and winter. The GS SNG rates increase by $0.02/Dth (rounded) in the summer and $0.04/Dth in the winter. Based on these new rates, a typical customer, whose annual usage is 80 decatherms, will see an estimated increase in their annual bill of $37.48 which is a 5.54% increase in annual gas costs.

[11] Exhibit 1.6, page 2 of 3, Line 1 of Application in Docket No. 10-057-09.
[12] Ibid, Line 4.
[13] Ibid, Line 2.
[14] Ibid, Line 7.

DOCKET 10-057-10: CONSERVATION ENABLING TARIFF (CET)

Unlike the SNG and commodity rate changes in Docket No. 10-057-09 that affect the rates for all firm sales customers, the rate changes requested in Docket No. 10-057-10 affect only a component of the distribution natural gas (DNG) rates of the GS rate class. This Docket requests that the PSC approve the request for QGC to begin amortizing an over-collected balance of ($3,471,000) in the CET deferral account, which is the balance in Account 191.9 as of May 31, 2010. This request is a net decrease of ($5,328,000) over the previous amount of $1,857,000 requested in Docket No. 09-057-13. If approved by the PSC, a typical GS rate class customer, assuming an annual usage of 80 decatherms per year, will see a decrease in their annual bill of $5.06 or a 0.75% change.

The Division has verified the amount of ($3,471,000) as the credit balance showing in Account 191.9 as of May 31, 2010 from QGC's financial statements. The sales volumes used to calculate the CET amortization rate are the same sales volumes used in the 191 pass-through application in Docket No. 10-057-09.

Rate Details: The CET amortization rates reflected in the GS tariff sheets filed with this application have changed for both blocks 1 and 2 of the summer and winter rates. The incremental decrease in the GS DNG Block 1 rate is $(0.06)/Dth (rounded) for the summer rate and $(0.07)/Dth rounded for the winter rate.

CET Stipulation Cap Review: The Commission's order in Docket No. 05-057-T01 changed the measure of the CET accrual and cap limits from total GS revenues to GS DNG revenues. The rolling 12-month Utah Jurisdictional GS DNG revenue, through May 2010 is $232,443,000. The 12 month rolling CET accrual limit is 5% of this amount which is $11,662,000. Total actual 12 month rolling CET accruals through May 2010, is a credit of ($4,485,000). The rolling 12-month amortization limit is 2.5% which is $5,881,000 through May 2010. The amount to be amortized, per this request, is a credit of ($3,471,000). The amounts deferred into the CET account and the amount requested for amortization all fall well within these limits.

Per the stipulation reached in Docket No. 09-057-16, QGC last general rate case, the CET is no longer considered a pilot program.

DOCKET NO. 10-057-11 DEMAND SIDE MANAGEMENT AMORTIZATION (DSM)

This application requests a decrease in the DSM amortization rate to amortize an estimate of $36,000,000 which is the DSM budget for 2010. The actual May 2010 DSM balance is $33,420,000. If approved by the PSC, a GS customer, assuming an annual usage of 80 decatherms per year, will see an average estimated decrease in their annual bill of $5.98 or a 0.88% decrease from those rates currently in effect.

The sales volumes used to calculate the DSM amortization rate are the same sales volumes used in the 191 pass-through application in Docket No. 10-057-09.

Figure 3 shows a history of the DSM 182.4 account through May 2010.

Figure 3

Utah DSM Account 184.2

(000)

	Beg Bal	Costs	Int	Amort	End Bal
2007	$ (1,300)	$ 7,413	$ 87	$ (620)	$ 5,580
2008	$ 5,580	$ 18,076	$ 714	$ (6,620)	$ 17,750
2009	$ 17,750	$ 47,449	$ 2,156	$ (26,853)	$ 40,502
2010 *	$ 40,502	$ 15,063	$ 824	$ (22,969)	$ 33,420
Total	$ (1,300)	$ 88,001	$ 3,781	$ (57,062)	$ 33,420

* As of May 31, 2010

As of May 31st, 41.8 % of the $36,000,000 budget has been spent. On June 30th, QGC sent a letter to the PSC notifying them that two programs, the ThermWise Appliance and ThermWise Builder programs, have reached 55% of their budgeted amounts. At the end of March, they were at 36% and 28% respectively. The annualized May year-to-date expenditure would be $36, 151,000. In light of this information, the Division feels it is reasonable, at this time, to base the amortization rate on the 2010 budget rather than the actual balance in the DSM account, as has been done in the past.

Rate Details: This is a decrease of $6,928,000 from the previous request in Docket No. 09-057-14, which will decrease the total DSM amortization rate from $0.45/Dth to $0.38/Dth (rounded), a net of decrease of $0.07/Dth (rounded).

SUMMARY AND CONCLUSION:

DPU Exhibit 1, Line 56 , Columns B,C,D and E shows the net increase of all three applications on the rates of the GS class's summer and winter rates. DPU Exhibit 2 combines the effect of all three applications and shows that a typical GS rate class customer whose annual usage is 80/Dth will see a net increase in their annual bill of $25.81 or 3.81%. This is the net result of the $(11.65)[15] reduction to a customer's annual bill as a result of the changes to the DNG rates off-set by the increase of $37.46 from the changes to the SNG and commodity rates.

Even though current spot market price projections in Figure 1 show the price of natural gas remaining relatively stable over the next twelve months, circumstances beyond QGC's control can and do cause spikes in these prices and, as shown in Figure 2, there is some disparity in the forecasting entities regarding the projection of future prices. With the current state of the overall economy, it is difficult to predict exactly what effect the current economic conditions will have on the volatility of natural gas prices. It is hoped that prices will remain stable, but, as history has shown, that hope can diminish very rapidly. The Division wishes to emphasize the need for customers to become even more energy efficient. The current DSM programs offered by QGC through the ThermWise campaign provide an excellent opportunity for customers to become more aware of ways they can become more energy efficient. Those GS customers that do take advantage of the DSM programs will be able to mitigate, to some degree, the effects of price spikes in natural gas. The Division continues to urge QGC to use its customer education and DSM funds to educate consumers on how they can reduce their gas usage on an ongoing basis in order to reduce consumption and mitigate the impact of possible future price increases.

[15] Includes the effect of the Low-Income tariff requested in Docket No. 10-057-08.

As always, the Division will continue to monitor the published monthly index prices[16] and compare them to the prices used in this pass-through filing to see if any trend develops that may warrant an out-of-period filing by QGC.

The Division supports and recommends that the rate changes requested in these three applications be approved by the Commission on an interim basis until the Division can complete an audit of the entries into the respective accounts associated with these applications. After the completion of those audits, the Division will issue memos to the Commission with its recommendation on making the revised rates permanent.

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[16] Published monthly in Platts "Inside FERC's Gas Market Report."