State of Utah
Department of Commerce
Division of Public Utilities

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ACTION REQUEST RESPONSE

To: Public Service Commission

From: Division of Public Utilities
Chris Parker, Director
Energy Section
Artie Powell, Manager
Doug Wheelwright, Technical Consultant
Eric Orton, Utility Analyst

Date: May 20, 2013

Subject: Questar Gas, Docket No. 13-057-03 (191 Account Pass-Through).

RECOMMENDATION:

Approve Questar Gas Company's (Company) applications as filed on an interim basis until the audit can be completed.

ISSUE:

On May 2, 2013, the Company filed this application with the Public Service Commission (Commission). On May 3, 2013, the Commission issued an Action Request to the Division of Public Utilities (Division) followed by an Amended Action Request issued on May 6, 2013 specifying "an examination and evaluation of the estimated 10% increase in the Wexpro operator service fee…". This is the Division's response to those action requests; section I discussing the pass-through case and section II discussing the Operator Service Fee (OSF).

I. DISCUSSION OF THE 191 PASS-THROUGH

This filing is based on projected Utah gas costs of $611,127,889[1] for the test year ending May 31, 2014. The application seeks approval to increase the commodity rate components of the Company's Utah natural gas rates by $65,209,000[2] and decrease the supplier non-gas (SNG) cost rate components by $3,775,000[3] for a net increase of $61,435,000[4].

The net unit commodity decatherm (Dth) rate increases from $4.16/Dth[5] to $4.79/Dth[6] for a net increase of $.63/Dth.

Based on current gas cost rates in the GS Rate class, if approved, a typical GS residential customer will see an increase in their annual bill of approximately $47.39 (7.08%)[7].

Utah Gas Supply

For this test year, the Company expects a total Utah system requirement of 111.0[8] million decatherms. Of this, 106.5[9] million decatherms will meet the projected sales requirement; 4.5 (111.0 – 106.5) million decatherms for gas volume reimbursement due to gathering, transportation and distribution fuel and shrinkage. Of the 111.0 million decatherms required, the Company projects supplying 70.6[10] million decatherms (63.6%) using Wexpro production; and 39.6[11] million decatherms (35.7%) purchased from third parties with a net storage of 0.8[12] million decatherms (0.7%).

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[1] Application Page 1, Paragraph 2.
[2] Ibid.
[3] Ibid.
[4] Ibid.
[5] Application, Exhibit 1.6, Page 1, Line 11, Column E.
[6] Application, Exhibit 1.6, Page 1 Line 11, Column D.
[7] Application, Page 1, Paragraph 2.
[8] Application, Exhibit 1.1, Page 19 of 19, total in Column E + Exhibit 1.2 Line 6 Column b + the net of Exhibit 1.4 Page 2 of 3 Line 5 Column B – Line 6 Column B (73,217,730+41,119,222+(12,221,251-11,393,793) * the Utah Percentage (Approximately 96%).
[9] Application, Exhibit 1.6, Page 1,Line 4, Column E.
[10] Application, Exhibit 1.1, Page 19 of 19 total in Column E * Utah Percentage.
[11] Application, Exhibit 1.2, Line 6 Column b * Utah Percentage.
[12] Application, Exhibit 1.4, Page 2 of 3 Line 5 Column B – Line 6 Column B (12,221,251-11,393,793) * the Utah Percentage.

Utah Gas Costs

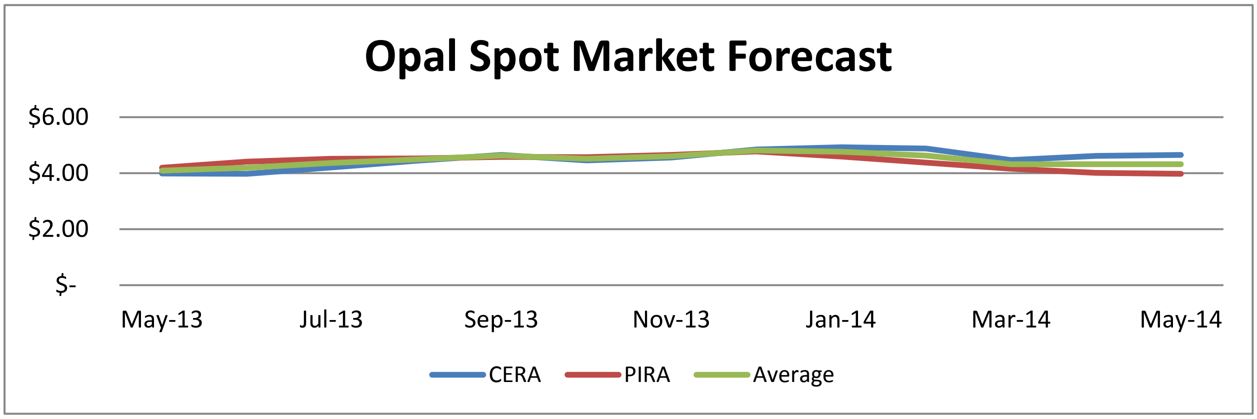
For the test year, the Company expects to spend $611,127,889[13] in total. Wexpro's production has a net projected cost of $338,877,663[14] at an average rate of $4.80/Dth[15]. The purchased gas cost from third parties has a projected cost of $187,788,766[16], with an average rate of $4.74/Dth[17]. With the recent increase in the forecast market price for natural gas, the price difference between Wexpro production and market purchases has been significantly reduced. In addition to the commodity cost, transportation costs were $65.6 million and added $0.58 to the cost per Dth for a projected customer price of $5.74/ Dth.[18]

Natural Gas Spot Prices

Since the time the Commission approved the last pass-through request, (Docket No. 12-057-08), actual prices have turned and are now trending upward from the previously forecasted prices. In this filing, the Company utilizes an average forward looking thirteen month forecast spot price of $4.47/Dth[19]. 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 displayed in Figure 1. This shows a relative consensus on the stability of natural gas prices through May 2014 by these two forecasting entities. What prices actually turn out to be, could be dramatically different from these forecasts.

13Application, Exhibit 1.5, Line 14, Column E.
[14] Application, Exhibit 1.5, Line 5 Column E.
[15] Application, Exhibit 1.4, Page 1, Line 5, Column D.
16 Ibid, Line 6, Column E.
[17] Application, Exhibit 1.4, Page 1, Line 6, Column D.
[18] Application, Exhibit 1.4 Page 1, Line 10, Column D
[19] Arithmetic average of PIRA and CERA forecast from May 2013 through May 2014.

Figure 1



Volatility Hedges

Historically, the Wexpro production and the Company's gas storage practices play a critical role in the plan to "hedge" against large spikes in natural gas price volatility while meeting the overall supply plan. These practices generally allow the Company to keep Wexpro production flowing during the summer months to meet summer demand and to inject gas into storage for later use during the winter months. The use of storage gas reduces the need to purchase gas in the winter months when the price is expected to be higher.

The Division is aware that the percentage of Wexpro production is continuing to increase and may be approaching the point where its summer production may be more than summer demand and storage injection can take. This situation may be remedied by the Company procuring more storage, shutting in wells for use only during the winter heating season, or by some other means. The increased Wexpro production increases costs to customers as long as Wexpro gas is more expensive than market gas. The Division will monitor closely the effects of the increased Wexpro production and report to the Commission as necessary.

In the past, the Company also attempted to manage gas price volatility, and thereby "hedge" or mitigate customers' exposure to price volatility (called "stabilization costs"). The Company typically targets 20% to 30% of the winter purchase requirement as a target to either purchase fixed priced gas contracts or change variable priced contracts to fixed price contracts. In this current filing the Company has chosen not to include any stabilization costs, thus effectively mitigating the increase by approximately $2 million.

Supplier Non-Gas Costs (SNG)

In contrast to the volatility that often is seen in the price of natural gas on the spot market, the SNG costs are relatively stable and predictable since these costs are set by contractual rate agreements and tariffs. These costs are associated with gathering and processing the Wexpro gas from the well heads to market hubs, transporting the gas from market hubs to city gates and storing the gas for later withdrawal during the winter months. Because of the stability in these costs, in Docket No. 09-057-03, the Company proposed and the Division supported, setting the SNG amortization rate annually. That annual amortization rate was last set in Docket No. 11-057-08 at $0.000/Dth and maintained in the most recent pass-through docket (12-057-08), likewise, the Company chose not to amortize any balance in this filing keeping the rate at zero.

The Company projects total SNG costs to be $93,672,262.[20] At current rates, SNG revenues that will be collected are projected to provide $97,447,293[21] leaving an over collected balance of $3,775,031.[22] Therefore, a 3.89%[23] decrease from the current total SNG rates will adjust for this over collection.

The reduction in the SNG rate is partially due to the reduction in storage costs in the Ryckman storage field. In the afternoon of April 20, 2013 a pressure valve malfunctioned causing a fire at the facility which forced the field to shut down until repairs are made. This event temporarily eliminated the storage costs for that field.

[20] Application, Exhibit 1.6, Page 2 of 3, Line 1.
[21] Ibid, Line 4.
[22] Ibid, Line 5.
[23] Ibid, line 7.

As in the past, the Company also projects to incur transportation and storage services at an estimated cost of $84,461,460[24].

II. OPERATOR SERVICE FEE

Section III-5 of the Wexpro Stipulation and Agreement outlines the concept and components of the OSF. The three parts of III-5 (a, b and c) outline that;

a) Wexpro "… will bill the Company for the services it performs and for the use of the facilities it has installed to produce the Company's natural gas, natural gas liquids and oil";

b) References the reader to Exhibit E for cost-of-service charges and

c) Dictates that Wexpro "…will be entitled to an additional 8% (r+8.00)" return or recovery on its investment in gas wells.

Exhibit E lists six parts of the OSF. These parts are:

1) Operating Expenses,

2) Depreciation,

3) Amortization and Depletion,

4) Taxes,

5) Returns, and

6) Costs, Expenses and Investment.

The $30.2 million ($315,627,797-$285,465,564=$30,162,233) mentioned in the May 6, 2013 Amended Action Request is made up of the changes in these costs included within these six components. The specific drivers for this increase in this instance are; Taxes (specifically Production Taxes) and the After Tax Adjusted Return ($12.3 and $11.0 million respectively). The other contributing costs are Depreciation and O&M/G&A ($4.2 and $2.4 million respectively). The increased costs are derived from the increased production from Wexpro and the increase in the forecast market price.

[24] Application, Exhibit 1.5 Lines 14,5 and 6 (611,127,889-338,877,663-187,788,766=84,461,460).

As mentioned above, Wexpro production increased by 4,851,000 Dth(7%) and market price by \$1.42/Dth (43%). The \$30.2 million increase in OSF from the previous pass-through filing is primarily due to the increase in taxes, return in investment and depreciation.
The other component of the increase is O&M/G&A.

One of the OSF areas the Division has monitored has been the Wexpro O&M/G&A costs which are passed onto the Company's customers. These expenses are manageable to some extent by Wexpro, and should be tightly controlled. Although these costs increased in this filing by \$2.4 million in total, as a percentage of cost per decatherm produced, the costs have decreased.

CONCLUSION: With the continued uncertainty of the local, national and international economy, the ever-present threat of increased regulation on hydraulic fracturing, and the continued increasing production of Shale gas in many parts of the country, it is difficult to predict what effects these conditions will have on the volatility of natural gas prices. For Utah customers, much of the volatility in gas costs is mitigated by the Wexpro production. As always, the Division will continue to monitor the published monthly index prices[25] and compare them to the prices used in these pass-through filings to see if any trend develops that may warrant an out-of-period filing.

The Division recommends that the rate changes requested in Docket Nos. 13-057-03 be approved by the Commission. The proposed rates should be approved on an interim basis until the Division can complete its audit. After the completion of the audit, the Division will issue a memo to the Commission with its recommendations on making the rate changes permanent.

As noted in the filing, and as provided for in the Company'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 the Company except for

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

$3,977,130,[26] which is the Utah allocation of the pre-tax return on the working storage gas inventory approved by the Commission 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 the Company's most recent rate case, Docket No. 09-057-16.

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26 Application, Exhibit 1.5, Line 13, Column E.