Witness OCS – 1SR

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

IN THE MATTER OF THE APPLICATION OF QUESTAR GAS COMPANY TO INCREASE DISTRIBUTION RATES AND CHARGES AND MAKE TARIFF MODIFICATIONS	)))))))))	**Docket No. 13-057-05** **Surrebuttal Testimony of** **Danny A.C. Martinez** **on behalf of the** **Office of Consumer Services**

January 7, 2014

Q. WHAT IS YOUR NAME, YOUR OCCUPATION AND YOUR BUSINESS ADDRESS?

A. My name is Danny A.C. Martinez. I am a utility analyst for the Office of Consumer Services (Office). My business address is 160 E. 300 S., Salt Lake City, Utah 84111.

Q. DID YOU FILE DIRECT TESTIMONY IN THIS PROCEEDING?

A. Yes. I am the same person that filed direct testimony on the behalf of the Office on October 30, 2013.

Q. WHAT IS THE PURPOSE OF YOUR SURREBUTTAL TESTIMONY?

A. My surrebuttal testimony responds to issues addressed in the rebuttal testimony of Ross Ford on behalf of the Utah Home Builders Association ("HBA") and Reed Ryan on behalf the Utah Asphalt Pavement Association ("UAPA"). The specific issues I will address are:

- HBA's objection to Questar's ("Company") cost sharing proposal for extending service to new homes and businesses.
- UAPA's objection to the Company's proposal to change from the monthly market index price to the weighted average cost of gas ("WAGOG") for gas commodity pricing in the Interruptible Service (IS) class.

Q. DOES THE OFFICE HAVE CONCERNS ABOUT THE TIMING OF THE TESTIMONY FILED BY THE UAPA AND THE HBA?

A. Yes. The UAPA and the HBA introduced new issues on the record in the rebuttal phase of this proceeding that should have been properly raised in direct testimony. Both Mr. Ryan for UAPA and Mr. Ford for the HBA indicated that their testimony was in rebuttal to the originally filed Company case. (See Ryan Rebuttal lines 47 - 53 and Ford Rebuttal lines 27 – 32.) The direct testimony phase of the case is the proper place to rebut issues raised by the Company in their initial filing. Therefore, raising these issues in the rebuttal phase of this case is untimely and procedurally out of order. Parties such as the Office will not have the benefit of reviewing the Company's response prior to formulating its final position on the issues. This deprives the Commission of the full benefit of three rounds of pre-filed testimony on these issues.

<u>Rebuttal of the Home Builders' Testimony</u>

Q. WHAT IS THE CLAIM OF THE HBA?

A. On behalf of the HBA, Mr. Ford has asserted that the Company's cost allocation proposal for extending service to new homes places a greater burden on customers with smaller than average homes and/or homes with relatively small lots (See Ford Rebuttal at lines 103 – 106.) Later Mr. Ford states that lower-income customers who generally live in lower-end homes will be adversely affected by the Company's proposal. (See Ford Rebuttal at lines 116 – 118.).

Q. WHAT CONCERNS DOES THE OFFICE HAVE WITH THE HBA's POSITION?

A. The Office has the following concerns with the HBA's position:

1. The HBA has not provided evidence demonstrating a correlation between short service line lengths and lower income home buyers;
2. The HBA has provided inconsistent cost information when comparing the current service line installation cost allocation system to the Company's proposed service line cost allocation system;
3. The HBA's analysis indicates a very small dollar impact per new home, thus it appears that the HBA is more concerned with maintaining the current benefit for home builders than protecting new homebuyers; and
4. Mr. Ford's assertion fails to recognize the key ratemaking principles of cost causation and fairness.

No Demonstration of Correlation

Q. DID HBA PROVIDE EVIDENCE TO SUBSTANTIATE ITS CLAIMS THAT QUESTAR'S PROPOSED CHANGES CAUSE DISPROPORTIONATE HARM TO SMALLER HOMES AND LOWER INCOME FAMILIES?

A. No. Mr. Ford provided no evidence in his rebuttal testimony demonstrating that lower-end homes are directly correlated with shorter service lines or that lower-income customers would be adversely affected. Specifically, the Office asked the HBA to provide any studies that demonstrate the correlation between service line length and home size and/or income levels. In response, the HBA stated it "relied on the experience and observations of its members with significant knowledge of the residential construction industry in forming its opinions." (See HBA responses to OCS Data Request 1.4 and 1.5, attached as Exhibit OCS – 1SR 1.0). The HBA did not provide any reports, studies, analysis or any other evidence supporting its opinion. Therefore, the HBA does not have any substantive evidence to offer that demonstrates shorter service lines correlate to lower income home buyers.

Data Inconsistencies

Q. DID THE OFFICE FIND ANY ERROR IN HBA's ANALYSIS?

A. Yes. As presented in Mr. Ford's Exhibit UHBA 1.3, there is a discrepancy in the total cost numbers for the two cost allocation methods. Specifically, Mr. Ford utilizes a fixed $506 for Questar internal costs at all service line lengths. The calculation should have varied by service line length using the Company's internal cost per foot of $9. For example, the internal costs for a 10-foot service line would be $90, not $506. Therefore, Mr. Ford misrepresents the internal costs and miscalculates the total costs of the service line installations in his Exhibit UHBA 1.3.

Q. HOW DOES THIS TOTAL COST DISCREPANCY IMPACT THE ANALYSIS OF THE COMPANY'S PROPOSAL?

A. By relying on the total cost information contained in Exhibit UHBA 1.3, Mr. Ford distorted the costs under the Company's cost allocation method. This results in a bias in the numbers when comparing the current cost allocation method to the Company's proposed method. The HBA's data is unreliable for purposes of making an accurate cost comparison between the current system in place and the Company's proposal. The HBA's faulty analysis belies the underlying purpose of the Company's proposal, which is to assign service line costs on an equitable cost per foot basis at all service line lengths.

Impacts of Home Builders' Calculations

Q. BASED ON THE HBA'S ANALYSIS OF THE COMPANY'S PROPOSAL, WHAT IS THE TOTAL AVERAGE IMPACT PER NEW HOME?

A. Setting aside the concern with the HBA analysis and assuming that individual developers are able to pass along the full amount of the cost increase in the sales price of the home, the total average impact would be quite modest. The new customer installing an average service line of 46 feet would pay $750.16. Assuming a 30-year fixed mortgage at a 5% interest rate, an increase of $750.16 would result in an increase of $4.03 dollars per month in mortgage costs. New customers with service lines less than 46 feet would pay less than $4.03 in monthly mortgage costs.

Q. IS THIS IMPACT SIGNIFICANT?

A. No. According to Mr. Ford's rebuttal testimony at lines 215 – 217, 70% of all service lines installed in 2012 were less than 35 feet. It is unlikely that $4.03 or less per month would make a significant difference in the decision to purchase a new home. The HBA has not provided any evidence to show how this increase on average "will have a deleterious effect on the housing market generally and particularly at the lower end of the new home market." (See Ford Rebuttal lines 223 – 225.)

Q. WHAT QUESTIONS ARE RAISED BY THE RESULTS OF THE HBA ANALYSIS?

A. Since the HBA's analysis shows such a small dollar impact per new home, the HBA concerns may not be specifically for new home owners. Instead, the HBA appears to be more interested in protecting the current benefits enjoyed by its members.

Key Ratemaking Principles

Q. PLEASE EXPLAIN HOW THE ALLOWANCE FOR SERVICE LINE EXTENSIONS WORKS UNDER THE CURRENT COST ALLOCATION METHOD.

A. Under the current method, existing customers provide a dollar contribution to the service line installations for new homes. This formulaic calculation attempts to share costs between existing and new customers on a 50/50 basis by providing a fixed dollar allowance towards the cost of installing a new service line. Regardless of the size of a service line and income of a home buyer, a fixed amount is provided towards the cost of installing a new service line.

Q. DOES THE CURRENT METHOD RESULT IN THE APPROXIMATELY 50/50 SHARING OF NEW SERVICE LINE COSTS BETWEEN EXISTING AND NEW CUSTOMERS?

A. No. While the current method divides costs 50/50 in aggregate, the impact on individual new service lines is quite disparate. According to HBA Exhibit 1.3, in 2012 existing customers contributed 74% of the installation costs for new homes with service lines less than 35 feet. In fact, any new home requiring a service line 20 feet or less was actually not assessed any installation costs. These costs were recovered entirely from existing customers.

Q. ARE CUSTOMERS WITH LONGER SERVICE LINES DISADVANTAGED UNDER THE CURRENT COST ALLOCATION SYSTEM?

A. Yes. Since the allowance is a calculated fixed amount, customers with longer line lengths are paying a greater percentage of costs compared to customers with shorter service line lengths.

Q. DOES THE COMPANY'S PROPOSED COST ALLOCATION METHOD REPRESENT A REASONABLE SOLUTION TO THE CURRENT SITUATION?

Yes. The Company has developed a cost-based allocation method that charges an equal per foot cost for new service lines, which if adopted would eliminate the unintended current windfall for new customers with shorter service lines. Under the Company's proposal, all new customers will pay for the external costs of installing a service line. This means that, regardless of the length of the line, all new customers will pay a <u>cost-based</u> share of the external installation costs. Existing customers will continue to be responsible for covering the internal costs of the new service lines. The Company's proposal represents a cost-based method that maintains a similar split of service line installation costs between existing and new customers, and results in a more equitable treatment among new customers with differing service line lengths.

Q. PLEASE SUMMARIZE THE OFFICE'S REBUTTAL OF THE HOMEBUILDERS.

A. The HBA has not adequately supported its claims. The HBA neglected to provide any evidence to demonstrate a correlation between short service lines and low-income customers and included inconsistent data in its analysis. Setting aside these deficiencies, the HBA's own analysis shows a very small dollar impact on affected customers. This raises questions about whether the HBA is concerned about protecting the interests of new homeowners or more interested in preserving a cost allocation method that generates benefits currently enjoyed by its members. Lastly, the HBA's proposal to retain the current allocation method is contrary to the fundamental ratemaking principles of cost causation and fairness. These key principles are the cornerstones upon which this Commission has relied on in making cost allocation decisions in rate proceedings over many years. It is important that the Commission follow these ratemaking principles in order to render an informed, evidentiary-based decision on this issue.

UAPA- Commodity Pricing Method

Q. WHAT IS THE UAPA'S POSITION ON COMMODITY PRICING?

A. Currently, the Company uses the monthly market index for gas commodity pricing for the IS class and the WACOG for all other classes. The Company has proposed changing the pricing method for the IS Class to the WACOG so that all customers are treated uniformly for the commodity portion of the rate structure. The UAPA opposes the Company's proposal.

Q. DOES THE OFFICE AGREE WITH UAPA'S POSITION REGARDING THE COMPANY'S PROPOSAL?

A. No. The WACOG is used for commodity pricing for all other customer classes. Allowing the IS class to have different commodity pricing represents poor policy, sends improper price signals to IS customers, and creates inter-class subsidies.

Q. HOW DOES CHANGING THE MONTHLY MARKET INDEX PRICE CURRENTLY USED FOR THE IS CLASS TO THE WACOG PREVENT INTER-CLASS SUBSIDIES?

A. The gas supplied to all customer classes, including IS customers, typically reflects a combination of market purchased gas and Wexpro gas. The present differential between the monthly market index and the WACOG creates a windfall for the IS class. The windfall is created because all other customers are subsidizing the commodity costs of the IS class. The Office's position is that this type of subsidy should not be part of the Company's rate structure. Rates should properly reflect cost causation, not arbitrage opportunities.

Q. MR. RYAN INDICATES THAT THE MONTHLY MARKET INDEX METHOD HAS BEEN USED FOR THE PAST 10 YEARS (RYAN REBUTTAL LINES 81 – 82). DOES THIS JUSTIFY CONTINUING TO USE THIS PRICING METHOD?

A. No. Mr. Ryan's preference to continue to use a method simply because it was used in the past does not justify retaining a pricing method that creates differential treatment for one class and results in inter-class subsidies. Absent the Company's proposed change to the WACOG method, all other customer classes will continue to pay for a single customer class' commodity cost advantage. The change to the WAGOG method is necessary so that IS customers, like all customer classes, pay commodity costs based on the actual costs paid by the Company for gas supplies.

Q. The UAPA APPEARS TO SUGGEST THAT BECAUSE OF THEIR STRONG SUMMER LOAD PROFILE ASPHALT COMPANIES SHOULD PAY LESS FOR MARKET GAS DURING THE SUMMER (SEE RYAN REBUTTAL LINES 85 -88.) WHAT IS YOUR RESPONSE?

A. The load profiles of asphalt companies do not change what the commodity prices are to serve them. These companies should pay the actual costs incurred by the Company to serve them, which would be accomplished by assigning these customers the WACOG. UAPA members are free to evaluate whether it would be advantageous for them individually to switch from IS to TS service and procure their own gas supply from the market.

Q. WHAT IS THE OFFICE'S RECOMMENDATION RELATED TO THE COMPANY'S PROPOSED CHANGE TO THE WACOG PRICING METHOD?

A. The Office recommends that the Commission approve the Company's proposed change in commodity pricing method for the IS class from the monthly market index to the WACOG. Approving this change will provide a uniform commodity pricing method for all customer classes and eliminate further commodity pricing subsidies.

Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?

A. Yes.