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Subject: **QGC COS & RATE DESIGN TASK FORCE REPORT**

INTRODUCTION

In January 2003, following the Commission's final order in Docket 02-057-02 in which the COS and Rate Design Stipulation was approved, the COS Task Force, chaired by Darrell Hanson of the Division of Public Utilities, began meeting. The task force has met eighteen times over the past eighteen months to discuss various components of rate design and cost of service including, but not limited to:

- 1- Developing a Cost of Service study in more detail including the allocation bases
- 2- Establishing a value for peaking gas available from IT customers
- 3- Separating the GS-1 rate class into residential and commercial customers
- 4- Modifying the GS-1 rate design
- 5- Studying the amount of the basic service fee
- 6- Qualifications for and design of the FT-1 rate schedule
- 7- Various Transportation rate designs
- 8- Administrative fees and qualifications for transportation service
- 9- Summer/winter rate differentials and other issues related to SNG, DNG, and Commodity components
- 10- "Green tag" compliance incentives

Minutes of each meeting were kept and are attached as Appendix A. Additionally, the Parties agreed to study separately the possible development of a tracker mechanism for

usage per customer. This subject was discussed in four of the meetings towards the end of the Task Force's work.

SUMMARY OF RESULTS AND ACCOMPLISHMENTS

The Division feels that the Task Force meetings were very successful in the sense that many beneficial topics were brought forth and discussed. Not a great deal of consensus was reached on issues where dollars would be shifted from those customers represented by any one particular task force member to those of another. In addition, little consensus was reached on issues that would shift risks to or from QGC. Instead of arguing issues with little chance of resolution, the Division attempted to focus on establishing some basic information that all parties could agree upon as starting points for cost allocation and rate design issues.

The new cost of service study prepared by QGC that breaks cost out by individual FERC accounts is a major accomplishment. In future cases all parties should have a common starting point and can focus on the issues of how various costs should be allocated. Going through the details of how QGC designs the blocks and how the blocks of the GS rates separate the residential and commercial customers was educational to the participants. Overall, the discussions of all of the topics were educational and should eliminate factual mistakes and misunderstandings in future rate cases. One meeting was also held with members of the QGC DSM Task Force in attendance as the issue of QGC's declining average usage per customer was discussed and the ramifications it has on DSM programs.

As discussed in the following, there were a few things that were agreed upon. A lot of education took place. Parties now understand each other's issues better. With the filing of this report, the business of the Task Force is officially concluded, although some of the parties continue to have ongoing discussions on individual issues. Overall the Division feels that the time was well spent with excellent participation by the parties involved and some good things were accomplished as a result of the Task Force meeting over the past eighteen months.

The following is a recap of the results of the discussions for each of the above topics.

1- Development of a new Class Cost-of-Service study (CCOS), including appropriate allocation factors.

This topic was discussed over the course of several meetings. QGC made a presentation that outlined the basic concepts of cost of service and rate design and the various tools available when designing rates. Included was a list of eight criteria of a sound rate structure taken from the book "Principles of Utility Rates" by James C. Bonbright. The eight criteria are commonly referred to as the Bonbright Principles and are a list of conflicting objectives that must be balanced in order to arrive at the most fair and

acceptable cost allocation and rate design. See Appendix A pp 15-16 Seventh Meeting 5-15-03 meeting minutes Attachment 1 for the list quoted by Bonbright.

A new CCOS model that provided rate base, expense and revenue amounts by FERC account was prepared by QGC and reviewed by the Task Force. This model provides significantly more detail than QGC has historically provided. QGC also presented descriptions of the allocation factors used in the model, the basis for using each factor, and which factor is used to allocate each FERC account. Some of the allocation factors, in particular the distribution plant allocation factor, were discussed at length over several meetings. No agreement was reached on the use of specific allocation factors, although it was indicated that there may be some factors that would not be challenged by parties in future rate cases. There was a general consensus of the parties that the use of the QGC revised CCOS model would be the basis of allocating costs in future rate cases.

Examples of the model, using data from the last general rate case, were presented. Included were examples of the model in which a key volumetric allocation factor was varied for sensitivity purposes. This factor is used to allocate costs in categories that show characteristics of both volumetric and demand cost drivers (i.e. compressor station and feeder line costs). The weighting of the factor was varied as follows: 1) 75% demand 25% commodity, 2) 50% demand 50% commodity and 3) 25% demand 75% commodity. A copy of the new CCOS model is attached showing the 50/50 version. See Appendix A ,pp 22-23, Ninth Meeting , minutes of 7-10-03 meeting Attachment # 1.

The Committee questioned the validity of the QGC sampling size used to determine allocation factors. The Committee desired to see a study done where QGC would identify all the facilities used by a 100% of the non-GS-1 customers, to try and determine the exact costs associated with these customers. The Committee felt such a study would remove any questions about the appropriate allocation factors used. QGC felt that there sampling methods gave a good representation of the facilities being used by various customer classes. QGC felt that the additional costs and time involved would not produce any different significant results. This is an area in which no resolution was reached and will be looked at by the Committee in future rate cases.

2- The value of peaking gas available from IT customers during periods of interruption, for consideration in the class cost-of-service methodologies for allocation and rate-design purposes.

After a presentation by both the Company and Industrial representatives and following extensive discussion it was generally agreed that the value of the peaking gas made available during interruptions should be recognized in the CCOS and a provision to do so was incorporated in the QGC CCOS model. However, the Company, Committee and Industrials had different valuation methods and ideas.

3- Possible separation of the current GS-1 residential and commercial customer class into separate classes.

This topic was discussed in the August 20, 2003 meeting after which the Committee made a request for additional data. QGC has provided requested data, which is being reviewed by the Committee. The Committee has made additional data requests, has received that data and is currently reviewing the data. The discussion centered on two points: 1) how to define commercial vs. residential and 2) whether the cost/usage characteristics of the two are sufficiently different to justify separate rate classes. No concrete recommendation regarding the separation of these customers into two rate classes was proposed.

4- Modification of the current GS-1 rate design.

The subject of modifying the GS-1 rate design was discussed over the course of several meetings. QGC presented data on the development of cost curves from the results of the CCOS model and presented some options regarding the GS-1 block rate designs. There was a consensus of the task force participants that the cost curves are an analytical starting point for future discussions regarding the design of block point breaks, basic service fee levels and rate levels in the blocks. There were no specific agreements on any type of modifications.

5- The amount of the basic service fee.

QGC presented information suggesting that the national average for the basic service fee is around \$8.00 per month. There was general consensus that QGC's current basic service fee of \$5.00 per month for GS-1 customers with a Category 1 meter is below cost of service. There was no consensus of what this fee should be.

6- Qualification for and design of the FT-1 rate schedule.

Issues for designing an FT-1 (anti bypass rate schedule) would include making sure that variable costs are covered and that the revenues collected from the rate would contribute as much as possible towards overall fixed costs without risking the loss of potential customers that would help cover those costs. The Committee asked QGC to provide some information on the FT-1 class cost of service, which the company provided on May 3rd. The Committee hasn't had time to review the material but indicated that it will review the material outside the context of this task force and bring up any issues or findings in the next general rate case that QGC files

7- Transportation rate design, including transportation service for smaller customers.

This subject was discussed in the April 28, 2003 and May 4, 2004 meetings. The discussions centered around the high load factor requirements that prevent many customers who may desire transportation services from being able to obtain those services. The Company is in the process of looking at options to redesign the transportation rates and is seeking input in the transportation rate design from industrial customers.

8- The amount and applicability of administrative fees, criteria for qualification and demand charges for transportation service.

Topic was discussed in meetings on August 20, 2003 and May 4, 2004. The group discussed how the fee levels were determined, the allocation of costs among different accounts, the barriers that exist for a customer to move to the IT schedule and the perceived inequity that exists between the transportation and interruptible sales rate schedules. The need for maintaining balance in revenue stability, administration fees and volumetric rates was a main topic of discussion. QGC and industrial customers have agreed to hold additional meetings to further discuss issues on this topic.

9- The DNG summer/winter rate differential and issues related to supplier non-gas cost and commodity rate design.

This topic was presented in the 11th meeting on October 7, 2003 along with other issues relating to block rate design. Consensus was reached that this differential is a tool to help match the rate design with the cost curves and that the company should continue to evaluate summer / winter differentials when designing rates.

10- Possible compliance incentives to be offered in connection with the Company's "green tag" program for inspecting natural gas appliances.

There was little interest and minimal discussion on this topic.

Additionally, the Parties agreed to study separately the possible development of a tracker mechanism for usage per customer.

Although not listed under the tasks for the Cost Allocation / Rate Design Task Force, the order also directed the parties to address the issue of declining usage per customer. The Task Force discussed this issue in the meetings held on December 16, 2003, January 21, 2004, February 11, 2004 and March 11, 2004. No specific consensus was reached but the Task Force felt it was important to continue discussions in this area into the future after the Task Force concludes.

Appendix A contains the minutes taken in each of the eighteen meetings that were held by the Task Force.