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State of Utah
Department of Commerce
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Division of Public Utilities
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Memorandum

To: Public Service Commission

From: Division of Public Utilities
Irene Rees, Director

Energy Section
Judith Johnson, Energy Manager
Tom Peel, Technical Consultant

Date: May 25, 2004

Subject: In the Matter of the Application of Questar Gas Company for an Accounting Order Regarding Treatment of Transmission Line Safety Compliance Costs - Docket No. 04-057-03

ISSUE:

On April 21, 2004, Questar Gas Company (the Company) filed an application with the Utah Public Service Commission (Commission) for a **deferred accounting order**.

The Company is required to comply with the new federal requirements of the Pipeline Safety Improvement Act of 2002 (the Act), enacted December 17, 2002, and the Final Rule regarding "Pipeline Integrity Management in High Consequence Areas" (Final Rule), effective January 14, 2004. The new requirements are expected to provide benefits, such as, safety, reliability, and public confidence in gas transmission.

The Company seeks authorization to establish an account (regulatory asset) to defer **unfunded** costs which will start in 2004. The Company proposes to defer costs until January 1, 2007 or until the next general rate case, whichever is sooner. If a rate case is not filed before

January 1, 2007, the Company intends to begin amortizing these costs over a five-year period beginning January 1, 2007.

The Act and the Final Rule apply to gas transmission pipelines for both interstate pipelines and local distribution companies.

RECOMMENDATION:

The Division recommends approval of the Company's request for a deferred accounting order for costs associated with the federal Pipeline Act and Final Rule. The Division's recommendation is based on the fact that these federal requirements were unforeseen and extraordinary in that incremental costs will be incurred that are not part of normal operations. The Company must comply with the mandated federal requirements. Although an estimate, an annual expense impact of $2 to $5 million is significant to Questar Gas.

Approval of the requested accounting treatment for cost deferral will not impact current rates nor does it determine future rate making treatment. The resolution of appropriate cost recovery will be decided in the Company's next general rate case. At that time, the regulatory asset will be subject to a thorough examination in terms of the appropriateness of the costs, allocations, and amortization period. In the unlikely event that the Company fails to file a general rate case prior to January 1, 2007, the Company should begin a five year amortization in 2007, as proposed in its application.

BACKGROUND:

As a result of high-profile accidents in Bellingham, WA (1999) and Carlsbad, NM (2000), Congress prescribed a major enhancement of the requirements pertaining to pipeline integrity in "High Consequence Areas" (HCAs), when it re-authorized the Pipeline Safety Act in 2002. This resulted in the most significant and complex Department of Transportation (DOT) code change ever.

The new federal requirements under the Act and the Final Rule require gas transmission pipeline operators to perform ongoing assessments of pipeline integrity, to improve data collection, integration, and analysis, to repair and remediate transmission (feeder) lines as necessary and to implement preventative and mitigative actions.

Among the many conditions of the Act and Final Rule is the requirement that the Company identify feeder lines in HCAs. The Company estimates between 400 - 800 miles of its 1,400 miles of Utah feeder lines will be classified as being in HCAs. The HCA designation is based on population density criteria. Once the HCAs have been identified, the Company must perform risk analyses and prioritize pipeline segments on the basis of potential threats.

The Company must begin baseline assessments by June 17, 2004. At least Fifty percent of baseline assessments must be completed by December 17, 2007 and 100% by December 17,

2012. Company feeder lines in HCAs must be reassessed every seven years.

To comply with the new federal requirements, the Company expects to incur significant costs for initial program development, staffing, technology, data management, pipeline integrity assessments, remedial repair work, and additional preventive maintenance and mitigative measures.

As a first-time program, the Company does not have sufficient experience nor cost data to accurately forecast the costs required to comply with this program. The Company estimates costs to range from $2 to $5 million annually. The amount of remedial work resulting from the assessments is unknown at this time.

Shared costs that would be subject to allocation, between Questar Gas and Questar Pipeline, would include initial program development, staffing, and technology and data management. Costs associated with integrity assessments, remedial work, preventive maintenance, mitigative measures would be "direct" assigned to each Company. The majority of costs, as much as two-thirds of the high-end estimate, are anticipated to be associated with the pipeline integrity assessments and remedial work.

New hardware and software to comply with the new requirements will be capitalized. The Company is not seeking to defer these costs. The annual licensing fees, however, would be deferred.

In the case of pipeline integrity assessments and remedial work, the most economically feasible method is "direct" assessment, because much of the distribution system is not amenable to internal inspections. Direct assessment involves excavation of sections of feeder lines for visual inspection. The costs of remedial work does not include the costs of a system replacement that might be required. Any system replacement costs will be capitalized as plant in service and not subject to deferral.

DOT estimates a cost impact of $5 billion nationally over the next 20 years. Questar estimates costs in the range of $50 million over a 10 year baseline as a result of satisfying the new federal requirements.

The purpose of the deferred accounting order is to address the issue of dealing with unfunded costs resulting from new federal requirements.

cc: Committee of Consumer Services, Eric Orton
C. Scott Brown, Colleen Larkin Bell, Questar Gas Company
Barrie McKay, Questar Gas Company