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M E M O R A N D U M

To: Public Service Commission

From: Division of Public Utilities
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Energy Section
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Date: February 19, 2009

Subject: Questar Gas, Docket Nos. 09-057-03, 09-057-04, 09-057-05.

ISSUE:

On February 10, 2009, Questar Gas Company (QGC) filed three applications with the Public Service Commission (PSC).

Docket No. 09-057-03 asks for approval to decrease 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 decrease in gas costs of $161,396,000.

Docket No. 09-057-04 is a request to amortize the CET balance and adjust the CET component of the GS-1 DNG Block1 and Block 2 rate class and the CET component of the GSS DNG rate class.

Docket No. 09-057-05 is a request to amortize a balance of $18,267,717 in the Demand Side Management deferred account and adjust the DSM rate component of the DNG rates

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for the GS-1 and GSS rate classes. All three applications request an effective date of March 1, 2009.

On February 10, 2009, the Commission issued the Division separate Action Requests for each of the dockets with an April 13, 2009 due date. On February 11, 2009, the Division filed a memo with the Commission requesting that a hearing be scheduled the week of February 23rd to accommodate Questar's requested implementation date of March 1, 2009. On February 12, 2009, the Commission issued an order scheduling a hearing for February 25, 2009 for all three dockets. This memo constitutes the Division's response to the Commission's three Action Requests in these dockets.

RECOMMEND APPROVAL:

After a preliminary review of all three applications, the Division recommends that all three applications be approved as filed with the proposed rates becoming effective March 1, 2009.

DISCUSSION –Docket No. 09-057-03 (191 Account, Commodity and SNG Costs):

This filing is based on projected Utah gas costs of $578,912,134. The commodity portion represents a decrease of $152,044,000 while the Supplier Non-Gas (SNG) costs decrease is $9,352,000. In this application, the Company is requesting a lower commodity rate, requesting an amortization rate to reduce the over collection of the commodity costs and reducing the current SNG amortization rate to zero.

A typical residential customer, assuming a usage of 80 decatherms per year, will see an average decrease in their annual bill of $127.91 for a decline of 16.53% below the gas costs in current rates. This filing uses a base period of March 1, 2009 through February 28, 2010.

QGC expects total system gas supply requirements of 114.2 million decatherms. To supply these system requirements, QGC plans on utilizing 53.9 million decatherms of WEXPRO production at a net cost of $249.2 million (47.0% of total requirements at an average cost of $4.62/Dth) and purchasing from third party producers, during the winter heating season, another 60.3 million decatherms for $262.4.9 million (53.0 % of total requirements at an average cost of $4.35/Dth). Ninety eight percent of system supply requirement or 104.9 million decatherms is required to meet the projected firm sales requirement of which 96% or 100.8 million decatherms is Utah's firm sales requirement. The remaining 9.3 million decatherms of the 114.2 million supply requirement is for the Company's restoration of Btu value after gas processing and fuel use.

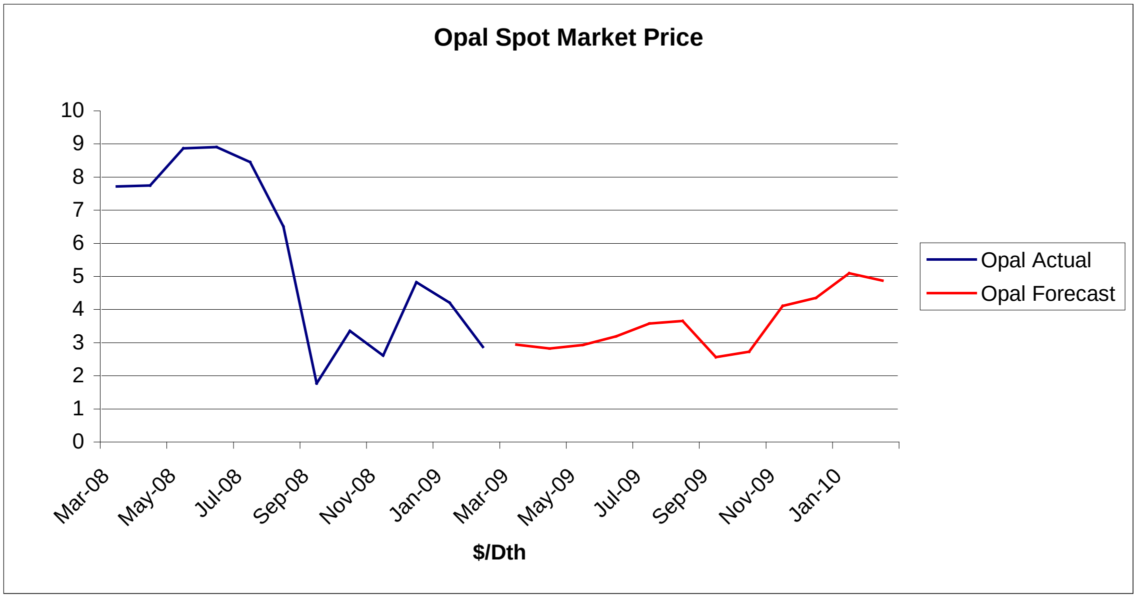
As noted in the filing, and as provided in QGC's Tariff for Natural Gas Service in Utah, PSCU 400, §2.10, pp. 2-11-2-17, these gas costs represent a direct pass through of costs. These costs do not impact the operating profit or rate of return of QGC except for $4.9 million as noted on line 13, column (E) of Exhibit 1.5, 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 using the cost of capital approved in QGC's most recent rate case, Docket No. 07-057-13.

Natural Gas Spot Prices

Since the Commission approved the last pass-through request effective November 1, 2008, there have been additional reductions in the commodity price of natural gas. In the November 2008 filing, the average forecast spot price was $5.20/Dth. This filing utilizes an average forecast spot price of $3.57/Dth, a 31% decline. Figure 1 shows the actual first of month spot prices of gas at Opal, Wyoming from March 2008 through February 2009 along with the forecast prices for March 2009 through February 2010[1]. This chart shows the significant reduction in commodity prices since July 2008. The projections indicate a return to lower and possibly more stable prices in the future.

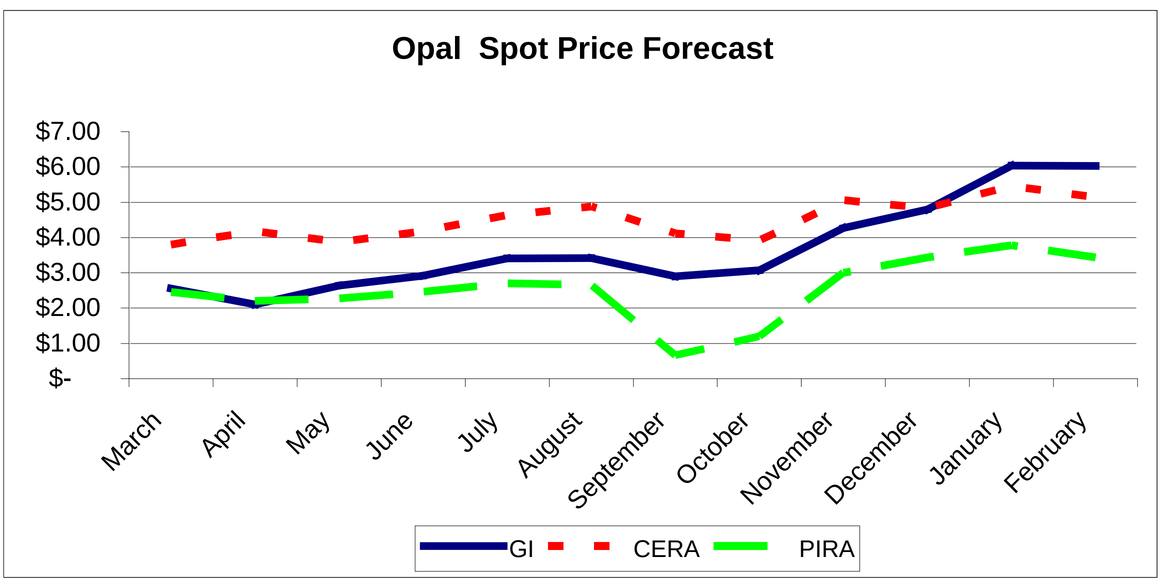
Figure 1

[1] Arithmetic average of GI, CERA and PIRA forecast from March 2009 to February 2010 used in pass-through application Docket No. 09-057-03.



Like the previous pass-through filing, the forecast is based on an average of future price projections by three different forecasting entities. Those three entities are Global Insight (GI), Cambridge Energy Research Associates, Inc. (CERA) and the PIRA Energy Group (PIRA). There is a divergence of opinions among the three forecasting services used by QGC as to the prediction of the future spot prices. This is displayed in Figure 2 below.

Figure 2



Because of the disparity between these projections, the use of an average of the three has been recommended and used by QGC in their price forecasts.

Pricing Hedges

The WEXPRO production and QGC's 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 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.

In this filing, WEXPRO production accounts for 47.0% of the gas supply mix at a weighted cost of $4.62/Dth ($4.23/Dth for net QGC production costs and $0.39/Dth for costs associated with gathering the WEXPRO production). The weighted cost of the WEXPRO production has remained relatively flat since the last filing. Based on current spot market prices, the average cost of the WEXPRO production is $0.27 /Dth more than the average cost of purchased gas. If the Opal natural gas spot market sees additional price erosion, the Company may shut-in some WEXPRO production in order to take advantage of the spot market price spread differentials. The Division will monitor these prices to see if the Company can take advantage of those differentials should they occur.

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 mentioned, QGC has developed a gas supply portfolio of 60 million decatherms of purchased gas and 54 million decatherms of company owned production. Of the 60 million decatherms of purchase gas, 19 million decatherms is winter peaking gas. The remaining 41 million decatherms of purchase gas consists of spot market purchases and fixed price contracts. Currently the fixed price contracts have a target goal of between 25% to 33%, depending on future movements in the price of natural gas. 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

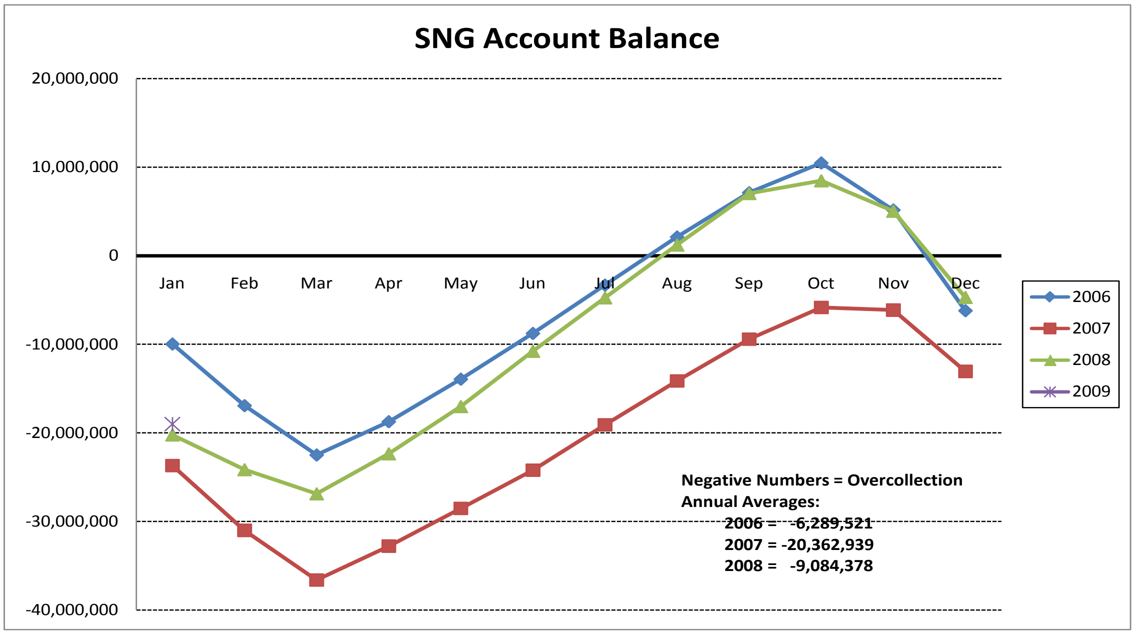
Experience has shown that the natural gas commodity price forecast used by QGC will not exactly match the actual prices as they unfold with time, especially with the market volatility in energy prices that currently exists. This fact is demonstrated by following the monthly commodity balances of the 191 account. At the time of QGC’s last filing in November 2008, the commodity balance was over collected by $11.9 million and the amortization rate was reduced to zero. Since that time, gas prices have continued to decrease more than forecasted and the over collected balance has grown to $60.9 million. Therefore the Company has requested an amortization rate of $(0.61811)/Dth to begin amortizing this balance.

Supplier Non-Gas Costs (SNG):

In contrast to the volatility seen in the commodity gas costs, the SNG costs are relatively stable and predictable since those costs are set by contractual rate agreements. Therefore, as mentioned in the Company’s application in paragraph 13, the current SNG amortization rate is proposed to be zero with the anticipation that in future filings, the SNG costs will be amortized on an annual basis beginning with the fall pass-through filing. The Company anticipates that by the fall pass-through filing, the current $19.0 million over collected SNG balance will naturally be reduced without an amortization rate due to the relatively stable SNG costs. The Division believes there may be some merit in setting the SNG amortization rate only once a year in order to facilitate more overall rate stability.

As can be seen in Figure 3, there is a cyclical pattern in the balance of the SNG account.

Figure 3



During the summer months when sales volumes are low, an under collection in the SNG cost balance is likely to occur requiring an increase in the SNG amortization rate with the fall pass-through application. During the winter months when sales volumes are high, an over collection is likely to occur requiring a subsequent reduction in the SNG amortization rate in the following pass-through application in the spring. This cyclical pattern in the account balance, therefore, causes excess volatility in the SNG amortization. Setting the SNG amortization rate once annually with the fall pass-through, when the account balance is relatively small, may provide for more stable rates over the year.

Rate Details: Exhibit 1a shows a summary of the SNG and commodity rate changes proposed in this application. As shown in the attached Exhibit 1a Line 34, the summer rates are reduced by $1.55714/Dth and $1.61706/Dth for the winter rates. If the Commission approves these pass-through rates, a typical GS-1 customer will see a decrease in their annual bill of $127.91 (Col E,Line 56) exclusive of the CET and DSM amortization rate changes pending before the Commission.

The Division requests the rate decrease be granted on an interim basis until the Division can complete an audit of the entries into the CET 191.9 account. After the completion of that audit, the Division will issue a memo to the Commission with its recommendation on making the revised rate permanent.

DISCUSSION –Docket No. 09-057-04:

The application in this docket requests to amortize $ 446,884 in the CET deferral account which is the balance in Account 191.9 as of January 31, 2009. If approved by the PSC, a typical residential customer, assuming a usage of 80 decatherms per year, will see virtually no change in their annual bill from this request.

The Division has verified the calculation of the amount of $446,884 as the balance showing in Account 191.9 as of January 31, 2009 however, the actual financial statements for January 2009 have not been released by the Company at the time of this filing in order to verify this balance on the Company's balance sheet. The sales volumes used to calculate the CET amortization rates are the same sales volumes used in the 191 pass-through application in Docket No. 09-057-03. This application reflects an incremental increase of $11,389 in the CET balance from the amount previously requested in Docket No 08-057-24.

Rate Details: As shown in the attached Exhibit 1b Line 35, the CET amortization rates reflected in the tariff sheets filed with this application reflect a very minor increase from the rates currently in effect (.0022% for GS-1 Winter 1st Block and .0021% for GS-1 Summer 1st Block). The incremental increase in the GS-1 DNG Block 1 rate is $0.00017/Dth for the summer rate and $0.00020/Dth for the winter rate (Exhibit 1b, Line 34). If the Commission approves this filing, this increase will calculate, for a typical GS-1 customer, an increase in their annual bill of $0.00 (Exhibit 1b, Col E, Line 56) exclusive of the 191 gas cost pass-through and DSM amortization rate increases pending before the Commission.

The Division requests the rate increase be granted on an interim basis until the Division can complete an audit of the entries into the CET 191.9 account. After the completion of that audit, the Division will issue a memo to the Commission with its recommendation on making the revised rate permanent.

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 12-month Utah Jurisdictional GS DNG revenue, through January 2009 is approximately $225,093,000. The 12 month rolling CET accrual limit is 5% of this amount which is approximately $11,255,000. Total actual 12 month rolling CET accruals through January 2009, is a credit of $857,000. The rolling 12-month amortization limit is 2.5% which is approximately $5,627,000 through January 2009. The amount to be amortized, per this request, is $446,884. The rolling 12 month amount amortized through January 2009 is $2,017,000. The amounts deferred into the CET account, the amount requested for amortization, and the total amount amortized all fall well within these limits.

DISCUSSION –Docket No. 09-057-05:

This application requests an increase in the DSM amortization rate to amortize the January 2009 DSM balance of $18.3 million. If approved by the PSC, on a stand-alone basis, a typical residential customer, assuming a usage of 80 decatherms per year, will see an average increase in their annual bill of $3.99 or 0.52% from those rates currently in effect.

The Company reports that $18.1 million dollars was spent in 2008 on the DSM programs with 42% of that total or $7.7 million in the ThermWise Weatherization Rebates program. Of this $7.7 million, $5.9 million was for rebates paid to customers for attic insulation additions. January 2009 saw an additional $2.1 million in attic insulation expenditures. The Division is pleased with the promotion of and the level of participation by customers in the offered DSM programs. However, the Division does have some concern about the allowed rebate incentives in the attic insulation offering because it has been reported that some insulation companies are promoting this service as a "no cost to the customers" opportunity when combined with the Rocky Mountain Power rebate incentives. The Division is planning on meeting with both Questar and Rocky Mountain Power to discuss this matter.

Rate Details: This is an increase of $4.4 million from the previous request in Docket No. 08-057-25 which will increase the total DSM amortization rate to $0.20259/Dth. This rate is derived by dividing the requested $18.3 million amount to amortize by total projected sales volumes of the GS-1 and GSS rate classes used as a basis in the 191 pass-through application in Docket No. 09-057-03. As shown in Exhibit 1c Line 34, the incremental rate increase is $0.04996/Dth for both the winter and summer rates GS-1 and GSS DNG rates. This will increase a typical GS-1 customer's annual bill by $3.99 or 0.52% (Exhibit 1c, Cols E and F, Line 56).

If approved by the Commission, with a DSM amortization rate of $0.20259/Dth, a typical GS-1 customer using 80 decatherms on an annual basis will pay $16.21 a year for DSM programs, irrespective of whether or not that customer actually participates in any DSM programs.

The Division requests this rate increase be granted on an interim basis. The Division will conduct an audit of DSM expenditures through January 2009. After the completion of that audit, the Division will issue a memo to Commission recommending whether or not the requested DSM amortization rate should become permanent. The Division will continue to perform audits on the DSM accrual accounting entries on a going forward basis and report to the Commission any adjustments that may need to be made based on its findings.

The Division notes that the tariff sheets filed as Exhibit 1.4 in the Company's application are exclusive of the rate changes requested in Docket Nos. 09-057-03 and 09-057-04.

SUMMARY AND CONCLUSION:

Exhibit 1d, Line 34 shows the net decrease of all three applications on the rates of the GS-1 and GSS rate classes. Line 56 shows that a typical residential customer whose annual usage is 80/Dth will see a net decrease in their annual bill of $123.90 or 16.01%. Exhibit 1e provides a component reconciliation of all of the filings as they relate to a typical customers annual bill.

Last spring saw a dramatic increase in the spot price of natural gas followed by an unusual and unanticipated decline in prices during the summer and fall months. 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 prices will become more stable. The Division still 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. The Division continues to urge Questar 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.

As always, the Division will continue to monitor the published monthly index prices[2] and compare them to the prices used in this pass-through filing to see if any trend develops which may warrant an out-of-period filing by QGC.

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

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