

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF COLORADO
PROCEEDING NO. 18AL-0305G

IN THE MATTER OF ADVICE LETTER NO. 89 FILED BY COLORADO NATURAL GAS, INC. TO MAKE ADJUSTMENTS TO SERVICE TERRITORY DESCRIPTION, SERVICE AND FACILITY CHARGES, DISTRIBUTION CHARGES AND WEATHER NORMALIZATION TO BECOME EFFECTIVE JUNE 15, 2018

STIPULATION AND SETTLEMENT AGREEMENT AMONGST COLORADO NATURAL GAS INC., THE COLORADO OFFICE OF CONSUMER COUNSEL, AND TRIAL STAFF OF THE COLORADO PUBLIC UTILITIES COMMISSION

COME NOW, Colorado Natural Gas, Inc. (“CNG” or the “Company”), the Colorado Office of Consumer Counsel (the “OCC”), and Trial Staff of the Colorado Public Utilities Commission (“Staff”) (collectively, the “Settling Parties”) and hereby submit this Stipulation and Settlement Agreement (“Settlement Agreement”) for the purpose of resolving all issues which have been raised, or could have been raised, among the Settling Parties in this proceeding.

The Settling Parties respectfully request that the Colorado Public Utilities Commission (“Commission”) approve this Settlement Agreement.

I. Procedural History

1. On May 15, 2018, CNG filed Advice Letter No. 89-GAS with supporting testimony and attachments seeking to increase its rates by \$3.8 million based on a 12-month test year ending on December 31, 2017. CNG’s filing encompassed both Phase I (Cost of Service or Revenue Requirement) and Phase II (Rate Design). CNG filed its Direct Testimony and Attachments with its Advice Letter.

2. By Decision Number C18-0430, mailed June 8, 2018, the Commission suspended the effective date of CNG’s proposed tariff and referred this matter to Administrative Law Judge (“ALJ”) Robert Garvey. The OCC and Staff timely intervened in this proceeding and

subsequently filed Answer Testimony and Corrected Answer Testimony in support of their positions. CNG filed Rebuttal Testimony in accordance with the procedural schedule established by the ALJ.

3. After extensive negotiations, the Settling Parties arrived at this Settlement Agreement, which resolves all issues in this proceeding. The rates described in this Settlement Agreement will go into effect only after a compliance tariff is filed pursuant to a final Commission decision.

II. THE SETTLEMENT AGREEMENT

4. The following section sets forth the negotiated resolution of the disputed issues among the Settling Parties. These agreements are all compromises of the Settling Parties' filed positions and are specifically based on the record in this case, including, but not limited to, CNG's Direct Testimony and Attachments, Staff's and the OCC's Answer and Corrected Answer Testimonies and Attachments, and CNG's Rebuttal Testimony and Attachments. The Settling Parties stipulate to the admission into the record of the pre-filed testimonies and attachments filed by them in support of their respective positions. The Settling Parties submit this Settlement Agreement to the ALJ for his approval and resolution of the issues in this proceeding. The Settling Parties affirm that acceptance of this Settlement Agreement is in the public interest and they will fully support the terms of this Settlement Agreement at any hearing scheduled in this proceeding.

Settlement Terms

A. Return on Equity

5. CNG filed Direct Testimony in support of an 11.90% return on equity ("ROE"). In their respective Answer Testimonies, Staff recommended a 9.75% ROE and the OCC

recommended a 9.60% ROE. In its Direct Testimony, CNG described the business risk attributable to a utility company of its relatively small size. The Settling Parties acknowledge that CNG is one of the smallest of Colorado's regulated natural gas utilities with approximately 22,000 retail customers. The OCC and Staff presented evidence on the risks that the Company faced, that the Commission recently approved a 9.35% ROE for Public Service Company of Colorado-Gas and a 9.45% ROE for Atmos Energy Corporation, and that capital costs have declined over the past five years since CNG's last ROE was authorized by the Commission in 2013. As a result, and for purposes of this Settlement Agreement, the Settling Parties agree that a 10.30% ROE is reasonable for CNG. The 10.30% ROE represents a 65 basis point reduction from CNG's current ROE of 10.95% and is a compromise of the positions the parties put forth in their respective testimonies.

B. Capital Structure

6. In its Direct Testimony, CNG proposed a ratemaking capital structure generally in line with its ongoing efforts to achieve a 55.00% debt to 45.00% equity ratio as set forth in the settlement of its prior rate case, Proceeding No. 13AL-0153G. CNG filed Direct Testimony proposing a capital structure comprised of 44.22% equity and 55.78% debt. In its Answer Testimony, the OCC agreed with the capital structure that CNG proposed in its Direct Testimony. In its Answer Testimony, Staff proposed using CNG's actual capital structure of 42.92% equity, 54.15% long-term debt, and 2.93% short-term debt. While CNG continues to strive to reach its target capital structure, during the 2017 test year, CNG maintained a small amount of short-term debt, primarily associated with the current portion of its long-term debt coming due. Staff testified that the capital structure should include the use of the short-term debt to accurately reflect CNG's current capital structure. Therefore, and for purposes of this

Settlement Agreement, the Settling Parties agree to use CNG’s actual capital structure of 42.92% equity and 57.08% debt, which includes the short-term portion of CNG’s long-term debt.

C. Weighted Average Cost of Capital

7. In its Direct Testimony, CNG presented its long-term debt as having a fixed interest rate. In its Rebuttal Testimony, CNG clarified that some of its debt was issued at a variable interest rate and that CNG had entered into derivative contracts to swap the variable interest rate for a fixed interest rate. The Settling Parties agree to the cost of debt, on both long-term and short-term debt, presented in Staff’s Answer Testimony, which results in a weighted average cost of all debt of 5.51%. The combination of the agreed upon ROE of 10.30%, the agreed upon weighted cost of debt of 5.51%, and the agreed upon capital structure of 42.92% equity and 57.08% debt results in an overall rate of return on rate base of 7.57%.

Table 1: Overall Rate of Return on Rate Base

	<u>Capital Ratio</u>	<u>Cost of Capital</u>	<u>Weighted Cost of Capital</u>
Debt	57.08%	5.51%	3.15%
Equity	42.92%	10.30%	4.42%
Total	100.00%		7.57%

D. Net Revenue Requirement

8. In its Advice Letter, CNG sought to increase its Revenue Requirement by approximately \$3.8 million. In their Answer Testimonies, Staff proposed a Revenue Requirement increase of \$2.7 million, while OCC proposed an increase of \$0.5 million. The Settling Parties agree that the net effect of the agreed upon ROE, capital structure, and other adjustments in this rate case results in an overall Net Revenue Requirement increase of approximately \$2.982 million.

E. Operations and Maintenance (“O&M”) Expenses

9. In its Answer Testimony, the OCC proposed to disallow \$856,944 of CNG’s O&M expenses. In its Answer Testimony, Staff proposed to increase O&M expenses by approximately \$89,000 to account for expenses CNG expects to incur in connection with a multi-year meter testing program it plans to implement later this year. To resolve this issue, the Settling Parties jointly recommend the Commission approve Staff’s O&M expense adjustment of an additional \$89,000. In response to the testimony presented by the OCC that CNG had failed to adequately explain increases in its O&M expenses other than stating that a decline in CNG’s growth resulted in proportionately more expense being allocated to O&M, the Settling Parties agree to disallow \$90,000, which is approximately 10% of the O&M expenses the OCC challenged.

F. Service and Facilities (“S&F”) Charges

10. In its Direct Testimony, CNG proposed modifying its existing S&F charges for its Mountain Division and Eastern Colorado Division. In their Answer Testimonies, Staff and the OCC proposed S&F charges lower than what CNG proposed. In resolution of this issue, the Settling Parties jointly recommend the Commission approve the following S&F charges for residential customers: (1) in CNG’s Mountain Division \$16.00 per month; and (2) in CNG’s Eastern Colorado Division \$14.00 per month. CNG’s S&F charges should remain at current levels of \$27.00 for Commercial and \$40.00 for Large Volume customers in CNG’s Eastern Colorado Division, and will increase to \$50.82 for Commercial customers in CNG’s Mountain Division. Table 2 below shows, for each rate class, the Settling Parties’ proposed S&F charges for CNG’s Mountain Division and Eastern Colorado Division. While CNG asserted its costs associated with its proposed S&F charges had increased, in order to avoid rate shock, and

recognizing that the costs associated with the proposed S&F charges will be recovered in the energy usage rates, the Settling Parties agreed to the increases in the S&F charges shown in Table 2.

Table 2: Monthly S&F Charges

Mountain Division		Eastern Colorado Division		
Residential	Commercial	Residential	Commercial	Large Volume
\$16.00	\$50.82	\$14.00	\$27.00	\$40.00

G. Over-collection of Prior Rate Case Expenses

11. As a result of its last rate case, CNG’s incurred recoverable rate case expenses that were amortized over three years. At the end of this amortization period, CNG agreed to file a tariff with the Commission that, when implemented, would act as a negative rider to stop the collection of the rate case expenses. CNG inadvertently failed to file this tariff to stop collecting the rate case expenses and, as a result, over-collected the expenses. After settlement negotiations in this proceeding, CNG agrees that the amount of over-collected rate case expenses will accrue interest (at its previously authorized cost of capital) and the net amount shall be applied against the rate case expenses incurred in this proceeding. At this time, the amount of over-collected rate case expenses following CNG’s 2013 rate case proceeding is approximately \$189,160, plus interest of \$10,917, and totaling \$200,077. CNG agrees to true-up its rate case expenses from this proceeding and collect the actual rate case expenses, as adjusted for prior over-collections, through rates that result from the Commission order in this proceeding. CNG agrees to amortize over three years its actual rate case expenses in this proceeding less the amount of over-collected prior rate case expenses *plus* interest and implement a negative rider when the net rate case expenses have been fully amortized to terminate collection of the rate case expenses. For

purposes of this proceeding, CNG's current rate case expenses total approximately \$360,000.

By settling this proceeding, CNG's rate case expenses will be less than they would have been had the case been fully litigated. This reduction in rate case expenses is in the public interest and provides support for the Settlement Agreement proposed here. Therefore, CNG agrees that it shall only recover its actual rate case expenses, but in no event shall the amount of recoverable rate case expenses exceed \$400,000.

H. Weather Normalization

12. In its Direct Testimony, CNG sought to implement a weather normalization adjustment to the test year ("WNA adjustment") using a rolling 30-year average of heating degree days ("HDD") to normalize its annual gas balance for rate case purposes. CNG also sought to implement a real-time WNA mechanism ("WNA mechanism") that would have updated each month using a 30-year rolling HDD average, and allowed the Company to adjust revenues on a monthly basis for all non-summer months via a designated rider, depending on how a month's actual weather compared to the month's "normal" weather, as defined by the HDD average.

Historically, CNG has used a semi-static 30-year HDD average computed by the National Oceanic and Atmospheric Administration to normalize its annual gas volumes for weather. Staff recommended that CNG use a rolling 20-year HDD average for normalizing its annual gas volumes for weather, so as to better account for a trend of declining HDDs over time. For purposes of this settlement, the Settling Parties agree to Staff's proposed 20-year rolling HDD average when calculating the WNA adjustment.

Staff further recommended using regression analysis to calculate the relationship between HDDs and gas demand. In its Rebuttal Testimony, CNG agreed that Staff's approach is a more

precise way to weather normalize customer usage. The Settling Parties agree to use Staff's regression-based methodology for weather normalization calculations.

Both Staff and OCC opposed CNG's proposed WNA mechanism. As such, CNG agrees to withdraw its request to implement a real-time WNA mechanism.

I. Tax Cuts and Jobs Act ("TCJA")

13. In order to benefit CNG's customers, the Settling Parties agree it is appropriate for CNG to resolve the TCJA impacts promptly via this proceeding. For purposes of this settlement, CNG agrees to amortize its unprotected excess accumulated deferred income taxes ("ADIT") (a regulatory asset) over 12 years and to amortize its protected excess ADIT (a regulatory liability) using the Average Rate Assumption Method ("ARAM") over 44 years. CNG's collection of unprotected excess ADIT and its return of protected excess ADIT will essentially offset each other over the next 12 years and be revenue-neutral. While the protected ADIT amortization period is based upon the useful lives of certain assets, the amortization period for unprotected ADIT is not prescribed or associated with useful lives prescribed for protected assets.

In June of 2018, in Proceeding No. 18L-0379G, CNG implemented a \$1.4 million annual customer rate reduction to account for the reduction in its federal corporate income tax rate from 35% to 21% as a result of the passage of the TCJA.

With these actions, the Settling Parties agree that CNG has fully resolved the TCJA impacts for the benefit of its customers.

J. Quality of Service Plan (“QSP”)

14. CNG and Staff agree it is essential for both parties to collaborate to build a QSP and develop performance metrics that are appropriate for CNG and its customers. The Settling Parties agree that, within six months after the effective date of any final decision in this proceeding, CNG will file a QSP, QSP metrics, and appropriate obligations with the Commission in a separate proceeding. In advance of the filing, the Settling Parties will work in good faith toward reaching a consensus. The Settling Parties anticipate that a Commission-approved QSP will afford ongoing annual evaluations of the approved QSP and QSP metrics along with an opportunity for interested parties to comment on QSP reports filed in such separate proceeding.

K. Other Issues

15. The Settling Parties desire to resolve two other issues by this Settlement Agreement. First, CNG commits to seek Commission approval before entering into any financial derivatives, including interest rate swaps, in connection with its future financing transactions. CNG has previously obtained Commission approval for all debt financings and considered debt-related derivatives, including interest rate swaps, to be within management’s discretion for converting previously-approved variable-rate debt to fixed-rate debt¹.

Second, CNG commits to provide all of its O&M expenses by Federal Energy Regulatory Commission (“FERC”) account in its annual report filing with the Commission.

III. GENERAL TERMS AND CONDITIONS

16. Through active pre-hearing investigation and extensive negotiations, the Settling Parties have negotiated the agreements set forth in this Settlement Agreement resolving enumerated, contested and disputed issues in this proceeding in a manner the Settling Parties

¹ Examples of previously approved Commission financing are Proceeding Nos. 10A-501SG and 12A-898SG.

agree is just and reasonable and in the public interest. This Settlement Agreement reflects a compromise in settlement of those issues among the Settling Parties in this proceeding. The Settling Parties further agree that reaching an agreement by means of negotiations, stipulations and/or settlement rather than through litigation is in the public interest and supported by the Commission, pursuant to Rules 1407 and 1408 of the Commission's Rules of Practice and Procedure. This Settlement Agreement is intended to comply with the provisions of Rule 1408.

17. The Settling Parties agree to present, to support and to defend this Settlement Agreement before the Commission and in the courts. They further agree to present testimony and exhibits in the evidentiary hearing in this proceeding for the purposes of obtaining the Commission's approval of this Settlement Agreement. At any such hearing, the Settling Parties agree that all pre-filed testimony and exhibits filed by the Settling Parties in this docket shall be admitted into evidence without cross-examination by the Settling Parties of each other's witnesses on the issues resolved by this Settlement Agreement. This Settlement Agreement shall not become effective until the Commission issues a final order addressing the Settlement Agreement. In the event the Commission modifies this Agreement in a manner unacceptable to any Settling Party, that Settling Party may withdraw from the Settlement Agreement and shall so notify the Commission and the other Settling Parties in writing within ten (10) days of the date of the Commission order. If a Settling Party timely exercises its right to withdraw from this Settlement Agreement, this Settlement Agreement shall be null and void and of no effect in this or any other proceeding.

18. The Settling Parties agree the Commission's approval of this Settlement Agreement shall constitute a determination that the Settlement Agreement represents a just, equitable and reasonable resolution of the disputed issues resolved herein.

19. The Settling Parties agree that this Settlement Agreement represents a negotiated settlement that they believe is in the public interest with respect to the various matters and issues enumerated herein, for the sole purposes of the settlement of the matters agreed to in this Settlement Agreement. The Settling Parties shall not be deemed to have approved, accepted, agreed to, or consented to any concept, theory or principle underlying or supposed to underlie any of the matters provided for in this Settlement Agreement, other than as specifically provided for herein. Notwithstanding the resolution of the issues set forth in this Settlement Agreement, none of the methods or principles herein contained shall be deemed by the Settling Parties to constitute a settled practice or precedent in any future proceeding.

This Settlement Agreement may be executed by counterparts and by facsimile or electronic copies of signatures all of which when taken together shall constitute the entire Settlement Agreement with respect to the matters herein.

IV. CONCLUSION

For the reasons stated above, Colorado Natural Gas, Inc., the Colorado Office of Consumer Counsel and Trial Staff of the Colorado Public Utilities Commission respectfully request that the Commission enter an Order approving this Stipulation and Settlement Agreement, with the finding that the Commission's approval of this Stipulation and Settlement Agreement represents a fair, just and reasonable resolution of any and all disputes in this proceeding as to those issues.

DATED this 10th day of October 2018.

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