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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF INTERMOUNTAIN GAS COMPANY FOR AUTHORITY TO CHANGE ITS PRICES (2006 PURCHASED GAS COST ADJUSTMENT).	)	**CASE NO. INT-G-06-4** **COMMENTS OF THE COMMISSION STAFF**

The Staff of the Idaho Public Utilities Commission, by and through it Attorney of Record, Donovan E. Walker, Deputy Attorney General, in response to the Notice of Application and Notice of Modified Procedure, issued on August 29, 2006, Order No. 30121, submits the following comments.

BACKGROUND

On August 16, 2006, Intermountain Gas Company ("Intermountain; Company") filed its annual Purchased Gas Cost Adjustment (PGA) Application with the Commission requesting authority to place new rate schedules in effect as of October 1, 2006 that will decrease its annualized revenues by $1.6 million (.5%). Application at 2. The PGA mechanism is used to adjust rates to reflect changes in costs for the purchase of natural gas from suppliers, including transportation, storage, and other related costs of acquiring natural gas. *See* Order No. 26019.

Intermountain's earnings will not change as a result of the proposed changes in prices and revenues. Application at 2.

Intermountain Gas seeks to pass through to each of its customer classes a change in gas-related costs resulting from: (1) an increase in costs billed to Intermountain pursuant to the general rate cases filed by Northwest Pipeline Corporation (NPC) and Gas Transmission Northwest Corporation (GTN); (2) benefits included in Intermountain's firm transportation and storage costs resulting from the Company's management of its storage and firm capacity rights on pipeline systems including NPC and GTN; (3) a decrease in Intermountain's weighted average cost of gas (WACOG); (4) an updated customer allocation of gas-related costs pursuant to the Company's PGA provisions; and (5) the inclusion of temporary surcharges and credits for one year relating to gas and interstate transportation costs from the Company's deferred gas cost account. Application at 3-4.

According to its customer notice, if its Application is approved as filed, all residential and commercial customers' unit prices will be essentially unchanged for natural gas used during the next year and the Company's total net revenue will decrease by approximately $1.6 million (.5%). The Company states that despite increases in other energy prices, such as crude oil's 30% increase during the past year, that it expects to be able to manage its natural gas purchases such that it will not need to raise customer prices for this next winter season.

Intermountain Gas proposes to decrease the WACOG from the currently approved $0.73219 per therm to $0.72400 per therm. Application at 5. The Company states that the proposed WACOG includes the benefits to Intermountain's customers generated by the Company's management of significant natural gas storage assets whereby gas is procured during the traditionally lower priced summer season for withdrawal and use during the winter when prices would otherwise be substantially higher. Application at 6. The Company also reports that natural gas prices have been moderated by: historically high levels of natural gas stored in the nation's inventory; natural gas production which has come back on-line in the Gulf of Mexico following Hurricane Katrina; the moderate outlook for the upcoming hurricane season; and price induced increases in domestic natural gas rig counts and production. Application at 5-6. The Company states that although current commodity futures prices dictate the use of a $0.72400 WACOG, it continues to remain vigilant in monitoring natural gas prices and is committed to

come before the Commission prior to this winter's heating season to amend these proposed prices, if the forward prices materially deviate from the $0.72400 per therm. Application at 6.

The Company proposes to include various surcharges, credits, and adjustments in its proposed prices. Application at 7-8. Intermountain has included the elimination of temporary surcharges and credits pursuant to last year's PGA, Case No. INT-G-05-2. Application at 7, Exhibit 4, L. 29. The Company includes a fixed cost collection adjustment pursuant to the provisions of its PGA tariff which provides that proposed prices will be adjusted for updated customer class sales volumes and purchased gas cost allocations. Application at 7, Exhibit 5, L. 24. The Company proposes to pass back to customers the benefits generated from its capacity release agreements through the inclusion of a $3.5 million credit. Application at 7, Exhibit 7. Further, the Company proposes to allocate deferred gas costs from its Account No. 186 balance to customers through temporary price adjustments effective during the 12-month period ending September 30, 2007 as follows: (1) fixed gas costs credit of $3.1 million attributable to collection of interstate pipeline capacity costs and the true-up of expense issues previously ruled on by the Commission; and (2) deferred gas cost debits of $14.1 million attributable to variable gas costs since September 1, 2005. Application at 7-8. Intermountain proposes to collect the balances via the per therm surcharges and credits. *Id.*

The Company states that a straight cents-per-therm price decrease was not utilized for the T-1 tariff. Absent Williams' firm transportation TF-1 commodity charge, the proposed decrease in the T-1 tariff is fixed cost related, and since there are no fixed costs recovered in the tail block of the T-1 tariff, a cents-per-therm decrease was made only to the first two blocks of the tariff. Application at 8. Likewise, since the proposed increase to the T-2 tariff demand charge is fixed cost related, a cents-per-therm increase was made to the T-2 demand charge. *Id.* Additionally, the proposed decrease to the T-2 commodity charge incorporates the decrease in the Williams' firm transportation TF-1 commodity charge. *Id.*

STAFF ANALYSIS AND REVIEW

Staff has calculated the impact of the Company's proposal on its customer classes as follows:

Customer Class	Proposed Change in Class Revenue	Proposed Average Change in $/Therm	Proposed Average % Change	Proposed Average Price $/Therm
RS-1 Residential	-20,625	-0.00058	-0.05%	1.2583
RS-2 Residential	-153,330	-0.00100	-0.09%	1.13885
GS-1 General Service	-1,166,345	-0.01209	-1.10%	1.08437
LV-1 Large Volume	-688	-0.00025	-0.03%	0.88869
T-1 Transportation	-268,276	-0.01110	-10.01%	0.09975
T-2 Transportation (Demand)	79,981	0.12103	13.96%	0.98781
T-2 Transportation (Commodity)	-30,575	-0.00169	-25.88%	0.00484
	-1,559,858	-0.00472	-0.47%	0.99758

The overall effect of the proposed changes would be a decrease in the Company's revenue of $1,559,858. The net decrease is comprised of the following items:

PROPOSED PERMANENT CHANGES		
Changes in Weighted Average Cost of Gas (WACOG)	$	(2,356,782)
Removal of Temporary Surcharges		(14,550,684)
Asset Management Agreements		(1,093,942)
Capacity Utilization		(2,316,330)
Increases for Pipeline Transportation		11,294,815
Total Permanent Price Change	$	(9,022,923)
Proposed Temporary Surcharges (Credits)		
2005 PGA Deferrals	$	11,001,232
Pipeline Segmentation		(3,538,166)
TOTAL TEMPORARY SURCHARGES	$	7,463,066
Total Proposed Change	$	(1,559,585)

Staff has reviewed the Company's Application and gas purchase contracts to verify that the Company's earnings will not change as a result of the filing, that the deferred costs are prudent, and to determine the reasonableness of the WACOG request. During the course of the audit, Staff made additional findings that are discussed in detail below.

Effects of the 2005 Hurricane Season

When the Company filed its PGA Application last year, the Company used actual usage data through June 30, 2005 and estimated usage for July, August and September. The 2005-2006 WACOG, with an effective date of October 1, 2005 and using data available as of July 29, 2005, was established through the use of financial derivatives. After the Company made its filing, and before the Commission ultimately issued its final Order in the case, Hurricanes Katrina and Rita struck the gas and oil producing areas of the Gulf of Mexico and the Gulf Coast. The disruption of gas supply in the Gulf of Mexico caused very large spikes in the wholesale cost of natural gas throughout North America. This increase in the prices of natural gas after the hurricanes was not anticipated in the WACOG approved by the Commission and resulted in the Company having to purchase natural gas at prices much higher than had been forecast.

For the two months immediately following Hurricanes Katrina and Rita, September and October 2005, the incremental cost of natural gas was greater than the approved WACOG embedded in the Company's prices by the amount of $11,651,182. The total deferral that the Company seeks to recover in the current filing is $11,001,232. Without the supply disruption from the hurricanes, and the ensuing spike in prices, the Company's forecasts from the 2005 PGA case would have been accurate and deferral balances would have been minimal.

Pipeline Transportation Rate Cases Pending Before FERC

On June 30, 2006, Northwest Pipeline Corporation (NPC) and Gas Transmission Northwest (GTN), the two interstate systems on which Intermountain transports gas, filed general system rate cases with the Federal Energy Regulatory Commission (FERC). The FERC suspended the effective dates of the rate increases until January 1, 2007, subject to refunds to be determined by conditions and outcome of hearings held at the FERC. Intermountain has intervened at FERC in these rate case proceedings. Staff will work with Intermountain to ensure that Intermountain's intervention is aligned with customers' interests.

In its filing, Intermountain's proposed prices are weighted to account for the January 1, 2007 effective date of the proposed price increases. Though the outcome of the proceeding is uncertain until a final order is issued by FERC, an increase in transportation costs is likely given that rates charged by these two pipeline corporations were set over ten years ago. However, the

sizes of the proposed increases are large and there is a significant difference between the NPC and GTN increases, in both the amount and the reasons for the increases. NPC has requested increases of approximately 42% over the current tariff due primarily to operational and maintenance issues. GTN has requested rate increases of over 70% due primarily to decreased demand resulting from competing pipelines with lower tariffs. Intermountain Gas' interstate transportation costs are heavily weighted toward the NPC pipeline. The Company has estimated the dollar impact of the interstate pipelines' cost increases to be $11,294,815 for the 2006-2007 gas-year. Approximately 80% of this increase is from the proposed NPC price increase and the balance from the GTN and Canadian (due to exchange rate changes) transportation cost increases. Since the increases are subject to possible negotiation between the pipelines and their customers (including Intermountain Gas) and are subject to FERC approval, it is reasonable to expect that the approved transportation price increases may be lower than those requested by the pipelines.

The weighting methodology used by the Company to determine the annual impact of the January 1, 2007 interstate pipeline rate increases on the total cost of service is appropriate. The methodology aligns the transportation increases with the Purchased Gas Cost Adjustment during the PGA year in which the increases occur. The methodology will also promote price stability to customers by limiting the amount that would have been deferred until the 2007 PGA filing. Rather than the Company deferring until next year the entire effect of the increase, the Company will only have to true-up any differences between the Applications filed by GTN and NPC and the final order to be issued by FERC. Given the uncertainties in the natural gas markets and IGC's current Application with minimal price changes, Staff believes that measures to defray future deferrals will serve in the best interest of ratepayers.

Staff recommends that, in the event that the FERC approved rate increases are significantly lower than those in the proposed Intermountain tariffs, the Commission reserve the right to re-open the approved tariffs that result from this proceeding.

Weighted Average Cost of Gas (WACOG)

The Company's requested WACOG of $0.72400 per therm is a decrease of approximately 1.19% from the $0.73219 WACOG currently included in Intermountain's rates. The current WACOG was approved last year in Order No. 29875 and has been in effect since October 1, 2005. The chart below provides a five-year history of the annual WACOG. Though the requested

WACOG is virtually left unchanged in the current filing, the chart reflects the volatility of the natural gas market during this period.

Year	WACOG	Percentage Increase/(Decrease) From Prior Year
2001	$0.35295	n/a
2002	$0.32000	(9.34)
2003	$0.47500	48.44
2004	$0.55492	16.83
2005	$0.73219	31.95
2006	$0.72400	(1.19)

Last year's WACOG of $0.73219 per therm was based on forward gas prices for the Company's supply sources as of the date of the Company's 2005 PGA filing. While actual gas prices varied greatly throughout the year, the WACOG estimates were fairly reflective of market rates through most of the PGA year. The result is a nominal balance in the Company's deferral accounts for the twelve months ended June 30, 2006 and a small decrease in customer rates for the coming year.

The Company's proposed WACOG of $0.72400 per therm is slightly less than that which could be justified when applying the forward prices available as of June 30, 2006 to the purchases that are yet to be made. The Company has taken the aggressive stance that they can deliver the natural gas yet to be purchased for a lower price than the forward prices indicate. Given that all natural gas needed for Intermountain's storage has already been purchased at favorable prices, that the resulting affect of the Company's aggressive forward purchasing plan on the WACOG is small and that the risk is placed on the Company rather than the consumer, Staff believes that the deviation from use of the NYMEX pricing is acceptable in this case.

Independent of the hurricane related supply issues effecting natural gas pricing, world unrest and subsequent instability of energy supply and delivery, supply and demand fundamentals has continued to affect the price of natural gas purchased by Intermountain Gas in 2006. In spite of the lack of storms in the Gulf of Mexico and the fact that, entering the spring of 2006 North American storage facilities were at record high levels, there has been little mitigating effect on the volatility of natural gas prices. Natural gas spot prices have varied from lows below $4.00 to highs above $9.00. During this period, Intermountain's substantial storage capacity has allowed

them to take advantage of lower prices when they have occurred by hedging the entire storage season's purchase at a favorable price early in the summer. This ability to fill storage at a fixed price along with other hedging strategies discussed below will allow the Company to file changes to lower the WACOG.

RISK MANAGEMENT AND GAS PURCHASING DECISIONS

The Company's contracts for physical gas supplies are typically based on the first-of-month index price. As part of the short-term hedging strategy, the Company has the opportunity to convert the first-of-month price to daily pricing. This decision is based on the market fundamentals reviewed by the Gas Management Committee when the daily pricing is expected to decrease during the month. Additional financial hedge opportunities are also evaluated with the same process.

During the 2005–2006 PGA year, the Company converted from first-of-month index price to daily pricing several times throughout the year, with an overall effect of increasing the Company's gas procurement expenses by $4,372,066. With each conversion to daily pricing, there is a risk that prices will increase beyond expectations. In prior years, the Company's hedging transactions provided significant benefits to ratepayers. However, during the current PGA year, the Company was required to make cash settlements to its suppliers because the monthly versus daily pricing did not meet the Company's expectations. The bulk of these cash settlements were due to the extreme volatility in prices following the 2005 hurricane season, when the Company converted to daily pricing as fundamentals suggested daily prices should decline.

In addition to the storage hedge to provide supply and price stability for the 2006-2007 PGA year, the Company has now hedged winter flowing gas requirements based on normal winter projections. This strategy will lock the price of 90% of the expected winter needs with multiple financial contracts on gas contracts from the three supply basins of Sumas, Rockies and AECO.

The Company and Staff continue to evaluate the risk management guidelines within the "Gas Supply Risk Management Program"[1] to manage the risk and price volatility to customers. The Company's documentation of its market evaluations and market fundamentals continues to

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[1] The objectives of Intermountain Gas Company's Gas Supply Risk Management Program are to (a) help ensure adequate gas supplies, transportation and storage are available for its customers; (b) mitigate the adverse impact that significant price movements in the natural gas commodity can have on the Company's supplies, customers and other operations; and (c) minimize the credit risk inherent in the implementation of certain price risk reducing strategies.

improve. The market expertise and experience of the Company and its purchasing agent are extensive and they will provide the background to evaluate the current guidelines and expand the Gas Supply Risk Management Program as the Company and Staff continue to meet on this topic.

CONSUMER ISSUES

The customer notice and press release were included in Intermountain's Application. The Application was received on August 16, 2006. Staff reviewed the customer notice and press release and determined they were in compliance with the requirements of IDAPA 31.21.02.102. The customer notice was mailed with Intermountain's cyclical billings beginning August 17, 2006 and ending September 15, 2006. Customers were given until September 20, 2006 to file comments. The Commission had received no written comments from customers as of the comment deadline.

Although no rate increase is a welcome announcement, natural gas rates have nearly doubled since the year 2000. Because of this, meeting energy needs continues to challenge many customers whose income has not kept pace with rising energy costs. Because so many customers still struggle to make ends meet, Staff would like to remind qualified customers to take advantage of the energy assistance available through the federally-funded Low Income Home Energy Assistance Program (LIHEAP) and non-profit fuel funds such as Project Share in southwestern Idaho and Project Warmth and Helping Hand in southeastern Idaho. For more information on these programs, customers may call the nearest Community Action Partnership (CAP) agency, Intermountain Gas Company, the Idaho Public Utilities Commission, or for other community resources call the 2-1-1 Idaho Care Line.

RECOMMENDATION

After a complete examination of the Company's Application and gas procurements for the year, Staff recommends the following:

1) That the Commission accepts the Company's Application and filed tariffs reducing the Company's annual revenue by $1,559,858.

2) That the Commission reserves the right to reopen any approved tariffs as a result of the FERC pipeline increases being less than what the Company has included in the Application.

Respectfully submitted this 20th day of September 2006.

Donovan E. Walker
Deputy Attorney General

Technical Staff: Harry Hall
Donn English
Marilyn Parker

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 20TH DAY OF SEPTEMBER 2006, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF,** IN CASE NO. INT-G-06-04, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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