

ORIGINAL

OPEN MEETING



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MEMORANDUM

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Arizona Corporation Commission

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TO: THE COMMISSION 2012 APR 30 P 12: 24

FROM: Utilities Division ARIZONA CORP COMMISSION DOCKET CONTROL

DATE: April 30, 2012

RE: SOUTHWEST GAS CORPORATION - FILING REGARDING THE INCREMENTAL CONTRIBUTION MODEL (DOCKET NO. G-01551A-10-0458)

On January 31, 2012, Southwest Gas Corporation ("Southwest" or "Company") filed, as a compliance item, a document with the Arizona Corporation Commission ("Commission") discussing its modified Incremental Contribution Model ("ICM") used by the Company to evaluate whether new customers need to provide contributions in aid of construction ("CIAC").

Decision No. 70665 (December 24, 2008) in Southwest's previous general rate proceeding required Southwest:

"in its next rate case application, to provide an explanation, with sample calculations and documentation, of how it has been implementing the ICM and Rule 6 tariff provisions."

Southwest provided this documentation in its initial application during Southwest's recently concluded rate proceeding. Upon review of Southwest's initial application, Staff expressed a concern in its testimony that the Company may have been over-collecting CIAC from a certain number of new customers. This issue was addressed as part of the settlement agreement reached in the rate case. The Commission's Decision in the recent Southwest rate case (Decision No. 72723, January 6, 2012) required that:

"Southwest Gas Corporation shall file with Docket Control, as a compliance item in this docket, within 30 days of the effective date of this Decision, a revised ICM model that prevents the Company from collecting contributions in aid of construction that result in an expected ROE, as generated through the ICM model, that is more than 50 basis points above the return on common equity authorized by this Decision. Staff shall submit a recommendation to the Commission within 90 days of SWG's filing of the revised ICM model."

This memorandum is Staff's submittal as required by Decision No. 72723. In addition to Southwest's January 31, 2012 filing, the Company provided Staff with a working copy of the ICM in Excel format. Staff has held subsequent discussions with the Company regarding how the ICM functions and the changes that Southwest made to the model. In essence, the Company has made two adjustments to how the ICM model operates.

The first change is that previously Southwest had included in the costs of providing service to new customers the cost of indirect pressure reinforcement as part of what was collected from the customer. Southwest has indicated to Staff that these costs involve needs that are typically years down the road from when a given project is undertaken. Further, the Company has indicated that the cost of such reinforcement is not specifically attributable to a given project. Thus, Southwest is now proposing to exclude the cost of indirect pressure reinforcement from its ICM calculations. Staff believes this is a reasonable proposal.

Second, the ICM traditionally was manually adjusted after initial inputs to solve toward the goal of the expected Return on Common Equity ("ROE") being within 50 basis points of the Commission's authorized ROE in cases where CIAC are collected. In the handful of examples provided to Staff during the rate proceeding, there were a few that Southwest later identified errors in how it was manually adjusted to solve within 50 basis points of the authorized ROE. Southwest has now adjusted the ICM to automatically solve to within 50 basis points of the authorized ROE. This should avoid possible manual errors which could result in the expected ROE exceeding the authorized ROE by more than 50 basis points.

Staff believes that the two adjustments made by Southwest to the ICM address the concern in the rate proceeding regarding possible collections of CIAC in cases where the expected ROE might exceed the authorized ROE by more than 50 basis points. Staff thus recommends that the Commission accept Southwest's revisions to the ICM model for purposes of compliance with Decision No. 72723.



Steven M. Olea  
Director  
Utilities Division

SMO:RGG:lh\RM

ORIGINATOR: Robert Gray

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**BEFORE THE ARIZONA CORPORATION COMMISSION**

- GARY PIERCE  
Chairman
- BOB STUMP  
Commissioner
- SANDRA D. KENNEDY  
Commissioner
- PAUL NEWMAN  
Commissioner
- BRENDA BURNS  
Commissioner

IN THE MATTER OF THE FILING OF  
SOUTHWEST GAS CORPORATION  
REGARDING THE INCREMENTAL  
CONTRIBUTION MODEL

DOCKET NO. G-01551A-10-0458  
DECISION NO. \_\_\_\_\_  
ORDER

Open Meeting  
May 22 and 23, 2012  
Phoenix, Arizona

BY THE COMMISSION:

FINDINGS OF FACT

1. Southwest Gas Corporation (“Southwest” or “Company”) is engaged in providing natural gas service within portions of Arizona, pursuant to authority granted by the Arizona Corporation Commission (“Commission”).
2. On January 31, 2012, Southwest filed as a compliance item, a document with the Commission discussing its modified Incremental Contribution Model (“ICM”) used by the Company to evaluate whether new customers need to provide contributions in aid of construction (“CIAC”).
3. Decision No. 70665 (December 24, 2008) in Southwest’s previous general rate proceeding required Southwest: “in its next rate case application, to provide an explanation, with sample calculations and documentation, of how it has been implementing the ICM and Rule 6 tariff provisions.”
4. Southwest provided this documentation in its initial application during Southwest’s recently concluded rate proceeding.

1           5.       Upon review of Southwest's initial application, Staff expressed a concern in its  
2 testimony that the Company may have been over-collecting CIAC from a certain number of new  
3 customers. This issue was addressed as part of the settlement agreement reached in the rate case.

4           6.       The Commission's Decision in the recent Southwest rate case (Decision No. 72723,  
5 January 6, 2012) required that:

6           "Southwest Gas Corporation shall file with Docket Control, as a compliance item  
7 in this docket, within 30 days of the effective date of this Decision, a revised ICM  
8 model that prevents the Company from collecting contributions in aid of  
9 construction that result in an expected ROE, as generated through the ICM model,  
10 that is more than 50 basis points above the return on common equity authorized  
11 by this Decision. Staff shall submit a recommendation to the Commission within  
12 90 days of SWG's filing of the revised ICM model."

13           7.       In addition to Southwest's January 31, 2012 filing, the Company provided Staff  
14 with a working copy of the ICM in Excel format.

15           8.       Staff has held subsequent discussions with the Company regarding how the ICM  
16 functions and the changes that Southwest made to the model. In essence, the Company has made  
17 two adjustments to how the ICM model operates.

18           9.       The first change is that previously Southwest had included in the costs of providing  
19 service to new customers the cost of indirect pressure reinforcement as part of what was collected  
20 from the customer. Southwest has indicated to Staff that these costs involve needs that are  
21 typically years down the road from when a given project is undertaken. Further, the Company has  
22 indicated that the cost of such reinforcement is not specifically attributable to a given project.  
23 Thus, Southwest is now proposing to exclude the cost of indirect pressure reinforcement from its  
24 ICM calculations. Staff believes this is a reasonable proposal.

25           10.      Second, the ICM traditionally was manually adjusted after initial inputs to solve  
26 toward the goal of the expected Return on Common Equity ("ROE") being within 50 basis points  
27 of the Commission's authorized ROE in cases where CIAC are collected. In the handful of  
28 examples provided to Staff during the rate proceeding, there were a few that Southwest later  
identified errors in how it was manually adjusted to solve within 50 basis points of the authorized  
ROE. Southwest has now adjusted the ICM to automatically solve to within 50 basis points of the

1 authorized ROE. This should avoid possible manual errors which could result in the expected  
2 ROE exceeding the authorized ROE by more than 50 basis points.

3 11. Staff believes that the two adjustments made by Southwest to the ICM address the  
4 concern in the rate proceeding regarding possible collections of CIAC in cases where the expected  
5 ROE might exceed the authorized ROE by more than 50 basis points.

6 12. Staff has recommended that the Commission accept Southwest's revisions to the  
7 ICM model for purposes of compliance with Decision No. 72723.

8 CONCLUSIONS OF LAW

9 1. Southwest is an Arizona public service corporation within the meaning of Article  
10 XV, Section 2, of the Arizona Constitution.

11 2. The Commission has jurisdiction over Southwest and over the subject matter of the  
12 rate application and the subject matter discussed herein.

13 3. The Commission, having reviewed the filing and Staff's Memorandum dated  
14 April 30, 2012, concludes that it is in the public interest to accept Southwest's revisions to the  
15 ICM model for purposes of compliance with Decision No. 72723.

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ORDER

IT IS THEREFORE ORDERED that Southwest Gas Corporation's revisions to the ICM model be and hereby are accepted for purposes of compliance with Decision No. 72723.

IT IS FURTHER ORDERED that this Decision become effective immediately.

**BY THE ORDER OF THE ARIZONA CORPORATION COMMISSION**

CHAIRMAN

COMMISSIONER

COMMISSIONER

COMMISSIONER

COMMISSIONER

IN WITNESS WHEREOF, I, ERNEST G. JOHNSON, Executive Director of the Arizona Corporation Commission, have hereunto, set my hand and caused the official seal of this Commission to be affixed at the Capitol, in the City of Phoenix, this \_\_\_\_\_ day of \_\_\_\_\_, 2012.

\_\_\_\_\_  
ERNEST G. JOHNSON  
EXECUTIVE DIRECTOR

DISSENT: \_\_\_\_\_

DISSENT: \_\_\_\_\_

SMO:RGG:lh\RM

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