

**BEFORE THE WASHINGTON  
UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,	)	DOCKETS UE-120436 and UG-120437 ( <i>Consolidated</i> )
	)	
Complainant,	)	
	)	
v.	)	ORDER 09
	)	
AVISTA CORPORATION d/b/a AVISTA UTILITIES,	)	
	)	
Respondent.	)	
.....	)	
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,	)	DOCKETS UE-110876 and UG-110877 ( <i>Consolidated</i> )
	)	
Complainant,	)	
	)	
v.	)	ORDER 14
	)	
AVISTA CORPORATION d/b/a AVISTA UTILITIES,	)	
	)	
Respondent.	)	
.....	)	

**FINAL ORDER REJECTING TARIFF FILING, ACCEPTING WITH  
CONDITIONS MULTI-PARTY SETTLEMENT AGREEMENT,  
AUTHORIZING TARIFF FILING, AND REQUIRING COMPLIANCE  
FILING**

1 *Synopsis: The Commission rejects revised tariff sheets filed by Avista Corporation d/b/a Avista Utilities (Avista or the Company) on April 2, 2012, but authorizes and requires the Company to file tariff sheets that will result in rate increases for 2013 of \$13.650 million, or about 3 percent on average, for electric customers and of \$5.300*

*million, or about 3.7 percent on average, for natural gas customers. In addition, the Commission authorizes Avista to return \$4.4 million from the existing Energy Recovery Mechanism (ERM) deferral balance to electric customers to mitigate the 2013 rate increase. These rates, including return of a portion of the ERM deferral balance reducing the 2013 rate increase, are found on the record of this proceeding to be fair, just, reasonable and sufficient. One concern, however, is that we have no absolute assurance that Avista will complete the projects described in its plan for 2013. As a result, we require the Company to file: (1) a progress report on its 2013 calendar year capital expenditures on or before September 30, 2013; and (2) a comprehensive report on the final totals for 2013 capital expenditures on or before March 1, 2014.*

- 2 *Further, the Commission authorizes Avista to file tariff sheets that will result in temporary rate increases for 2014 of \$14.038 million, or about 3 percent on average, for electric customers and of \$1.4 million, or about 0.9 percent on average, for natural gas customers. This Order authorizes the 2014 rates from January 1, 2014, to December 31, 2014, with rates then reverting back to 2013 levels absent any intervening Commission action. This Order also authorizes Avista to return \$9 million to electric customers from the then-existing ERM deferral balance, should funds prove available, to mitigate the 2014 rate increase. While we find that these rates, including the reduction of the 2014 rate increase for electric customers due to the return of a portion of the ERM deferral balance appear to be fair, just, reasonable and sufficient on a temporary basis, justification for our temporary approval lies primarily in Avista's representations that the Company will continue its multi-year capital expenditure program for 2014. Avista did not provide the Commission with a capital expenditure plan for 2014. The Commission thus requires the Company to file: (1) its capital expenditure plan for calendar year 2014 on or before September 30, 2013; and (2) updates on changes in meeting its capital expenditure plan for calendar year 2014 and reports on progress in making such capital improvements on June 1, September 1, and December 1, 2014, respectively, for the previous quarters.*

- 3 *The Commission requires Avista to defer in an account, separate from the ERM accounts, any actual REC sale proceeds above or below the REC sale proceeds included in the base rates of the ERM. At the time of Avista's next filed general rate case, REC sale proceeds should be removed from the base rate in the ERM and recorded in the deferral account established by this Order.*
- 4 *Given the two different attrition methodologies both Staff and Avista employ to arrive at their respective adjustments, and the lack of exploration into the merits of the different approaches, we do not take a position on either but will open an inquiry into this issue to allow for further examination.*
- 5 *With the above additional reporting requirements, we accept and approve with conditions the Multi-Party Settlement Stipulation filed by Avista, Commission Staff, ICNU, NWIGU, and The Energy Project on October 19, 2012.*

### **SUMMARY**

- 6 **PROCEEDINGS:** On April 2, 2012, Avista Corporation d/b/a Avista Utilities (Avista or the Company) filed revisions to its currently effective Tariff WN U-28, Electric Service in Docket UE-120436 and revisions to its currently effective Tariff WN U-29, Natural Gas Service in Docket UG-120437. Specifically, Avista requested an electric rate increase of \$41.0 million, or 9.0 percent, and a gas rate increase of \$10.1 million or 7.0 percent. In addition, Avista filed tariff Schedule 93, which reflects a proposed one-year Energy Recovery Mechanism (ERM) bill decrease, or rebate, to electric customers of \$13.6 million (about 2.9 percent). On April 26, 2012, the Washington Utilities and Transportation Commission (Commission) suspended operation of the tariffs and consolidated the dockets for hearing.

7 On May 14, 2012, the Commission entered Order 03/08<sup>1</sup> consolidating Dockets UE-120436 and UG-120437 with the second phase of Avista's 2011 general rate case, Dockets UE-110876 and UG-110877, which specifically addresses the issue of electric decoupling for the Company.

8 **PARTY REPRESENTATIVES:** David J. Meyer, Vice President and Chief Counsel for Regulatory and Governmental Affairs, Spokane, Washington, represents Avista. Simon J. ffitch, Senior Assistant Attorney General, and Lisa W. Gafken, Assistant Attorney General, Seattle, Washington, represent the Public Counsel Section of the Washington State Attorney General's Office (Public Counsel). Donald T. Trotter and Michael A. Fassio, Assistant Attorneys General, Olympia, Washington, represent the Commission's regulatory staff (Staff or Commission Staff).<sup>2</sup>

9 Melinda J. Davison and Joshua D. Weber, Davison Van Cleve, P.C., Portland, Oregon, represent the Industrial Customers of Northwest Utilities (ICNU). Ronald L. Roseman, Attorney, Seattle, Washington, represents The Energy Project. Chad M. Stokes and Tommy A. Brooks, Cable Huston Benedict Haagensen & Lloyd LLP, Portland, Oregon, represent the Northwest Industrial Gas Users (NWIGU). Todd True, Earthjustice, Seattle, Washington, represents the NW Energy Coalition (NWEK).

10 **COMMISSION DETERMINATIONS:** The Commission finds, on the basis of the evidence presented, that consideration of attrition in setting rates for 2013 is appropriate. However, the attrition is caused substantially by Avista's ongoing capital investment program, and we have no absolute assurance that Avista will complete the projects described in its plan for 2013. As a result, we require the

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<sup>1</sup> The dual order number is the result of consolidation.

<sup>2</sup> In formal proceedings, such as this, the Commission's regulatory staff participates like any other party, while the Commissioners make the decision. To assure fairness, the Commissioners, the presiding administrative law judge, and the Commissioners' policy and accounting advisors do not discuss the merits of the proceeding with the regulatory staff, or any other party, without giving notice and opportunity for all parties to participate. *See* RCW 34.05.455.

Company to file a progress report on 2013 calendar year capital expenditures on September 30, 2013, as well as final totals for 2013 capital expenditures on or before March 1, 2014.

- 11 While we find the arguments of some of the settling parties persuasive that attrition will continue into the very near future, including the 2014 calendar year, we are basing our temporary approval of the 2014 rates on the Company's representations of these continued capital investments. The Commission, thus, requires Avista to file: (1) its capital expenditure plans for 2014 on or before September 30, 2013; and (2) reports describing any changes to its 2014 capital investment plan as well as its progress in fulfilling that plan on June 1, September 1, and December 1, 2014, respectively, for the preceding quarters.<sup>3</sup>
- 12 The record evidence supports a finding of attrition in the near term; however, we refuse to endorse either of the different attrition methodologies employed in this case. Instead, we will take the issue up in a subsequent inquiry to explore the issue further. The Commission accepts the remainder of the Multi-Party Settlement Stipulation (Settlement), including the stipulated return on equity (ROE) and capital structure; noting, however, that the overall trend for ROEs has been edging downward.

## MEMORANDUM

### **I. Background and Procedural History**

- 13 On April 2, 2012, Avista filed revisions to its currently effective Tariff WN U-28, Electric Service in Docket UE-120436, and revisions to its currently effective Tariff WN U-29, Natural Gas Service in Docket UG-120437. The proposed tariff revisions bore an effective date of May 3, 2012. Avista proposed a general rate increase of

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<sup>3</sup> We recognize that non-fuel operations and maintenance costs contribute to Avista's attrition, and, while we are not seeking any reporting on these expenses at this time, we may require additional reports in 2014.

\$41.0 million, or 9.0 percent, for electric customers and \$10.1 million, or 7.0 percent, for natural gas customers. The Company also requested approval of a one year ERM bill decrease for electric customers in the amount of \$13.6 million, or approximately 2.9 percent. On April 26, 2012, the Commission suspended the proposed tariff revisions and consolidated the two dockets.

14 Avista's initial request was based on a test year ending December 31, 2011, with pro forma adjustments into 2013. The filing also included proposals for the following:

- An attrition adjustment, based on Dr. Mark N. Lowry's analysis, which proposed to cure a perceived revenue deficit of \$21.6 million in 2013.<sup>4</sup>
- An overall rate of return of 8.25 percent.<sup>5</sup>
- A return on common equity of 10.9 percent.<sup>6</sup>
- A capital structure consisting of 48.4 percent equity and 51.6 percent debt.<sup>7</sup>

15 On May 9, 2012, the Commission conducted a prehearing conference before Administrative Law Judge Marguerite E. Friedlander. On May 14, 2012, the Commission entered Order 03/08 consolidating Dockets UE-120436 and UG-120437 with the second phase of Avista's 2011 general rate case in Dockets UE-110876 and UG-110877, in order to address the issue of electric decoupling for the Company in this proceeding.

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<sup>4</sup> Lowry, Exh. No. MNL-1T, at 3:9-11. Dr. Lowry, citing to Staff witness Ken Elgin's testimony in Dockets UE-111048 and UG-111049, describes the purpose of an attrition adjustment as an "[analysis of] actual historical trends in the growth rates of revenues, expenses, and rate base to estimate the erosion in rate of return caused by disparate growth in these categories." Lowry, Exh. No. MNL-1T, at 13:22-24 (citing Elgin, Exh. No. KLE-1T, at 67:6-8, Dockets UE-111048 and UG-111049 (consolidated)).

<sup>5</sup> Thies, Exh. No. MTT-1T, at 26 (Illustration No. 8).

<sup>6</sup> Avera, Exh. No. WEA-1T, at 4:7-10.

<sup>7</sup> Id., at 6:14-16.

- 16 On September 19, 2012, the parties prefiled direct and response testimony and exhibits. In addition to Avista, Staff was the only other party to perform an attrition study; determining that the Company would experience a revenue shortfall due to attrition in the amount of \$19.066 million for electric service and \$2.837 million for natural gas service.<sup>8</sup> In addition, Staff made several adjustments to the Company's initial case resulting in a revenue surplus of \$20.378 million for electric operations and a revenue deficiency of \$1.135 million for natural gas operations.<sup>9</sup> In total, Staff's finding of attrition in the amount of \$19.066 million, combined with its revenue surplus projection of \$20.378 million, results in an attrition-adjusted surplus of \$1.312 million for electric service.<sup>10</sup> Likewise, Staff's attrition adjustment of \$2.837 million plus Avista's revenue deficiency of \$1.135 million amounts to an attrition-adjusted revenue deficiency of \$3.972 million for natural gas service.<sup>11</sup>
- 17 With regard to the Company's capital structure, Staff recommended a 46 percent equity ratio and a 9.0 percent ROE,<sup>12</sup> for an overall rate of return at 7.22 percent.<sup>13</sup>
- 18 Public Counsel did not file a full revenue requirements case nor did it perform an attrition study. Instead, Public Counsel's response testimony focused on several incremental adjustments to Avista's test year results of operations, as well as policy recommendations relating to the Pullman Smart Grid Demonstration and executive compensation.<sup>14</sup> Public Counsel also specifically opposed Avista's proposed electric

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<sup>8</sup> Breda, Exh. No. KHB-1CT, at 26:13, 16.

<sup>9</sup> Id., at 4:7, 11.

<sup>10</sup> Id., at 4:7-8.

<sup>11</sup> Id., at 4:10-12.

<sup>12</sup> Elgin, Exh. No. KLE-2T, at 40:19-21.

<sup>13</sup> Id., 54:19.

<sup>14</sup> Dittmer, Exh. No. JRD-1T, at 3:17-22.

and natural gas attrition adjustments.<sup>15</sup> In total, Public Counsel recommended electric adjustments to Avista's initial filing in the amount of \$32.648 million and \$4.226 million in adjustments to the Company's initial natural gas revenue request.<sup>16</sup> Public Counsel did not propose a capital structure, an ROE, or an overall rate of return.

19 In its response testimony, ICNU urged the Commission to reject the Company's attrition adjustment.<sup>17</sup> ICNU also recommended an ROE of 9.4 percent, a common equity ratio of 47.3 percent, and an overall rate of return of 7.48 percent.<sup>18</sup> ICNU calculated a revenue surplus of \$7.7 million for the Company.<sup>19</sup>

20 The Commission held separate public comment hearings in both Spokane, Washington, and Spokane Valley, Washington, on September 27, 2012, and September 28, 2012, respectively. Collectively, eleven members of the public spoke at the public comment hearings; none of the commenters spoke in favor of Avista's proposed rate increase. In total, the Commission and Public Counsel received 176 written comments about the proposed rate increase from Washington customers, with 145 comments opposing the increase, and 31 commenters undecided.<sup>20</sup>

21 On October 19, 2012, all parties except Public Counsel and NWEC<sup>21</sup> filed a Multi-Party Settlement Stipulation (Settlement), attached to this Order as Appendix A and

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<sup>15</sup> *Id.*, at 4:21-22.

<sup>16</sup> *Id.*, at 5:3-5.

<sup>17</sup> Gorman, Exh. No. MPG-1T, at 4:13-15.

<sup>18</sup> *Id.*, at 2:12-15.

<sup>19</sup> Deen, Exh. No. MCD-5, at 6.

<sup>20</sup> Exh. No. 6.

<sup>21</sup> NWEC does not oppose the Settlement. Instead, at least initially, NWEC wanted to reserve its right to pursue further litigation of the electric decoupling issue. However, on November 9, 2012, NWEC filed a Motion to Withdraw its Decoupling Proposal (Motion). The Commission declines to entertain NWEC's Motion at this time.



incorporated by reference as if set forth in full in the body of this Order, addressing the Company's revenue requirement, cost of capital, the ERM structure, rate spread and rate design, as well as several other issues. The settling parties also filed joint testimony in support of the Settlement at that time. On November 9, 2012, Public Counsel filed testimony in opposition to the Settlement and suggested that the Commission reject the agreement in favor of a full hearing on various contested issues including attrition, ROE, executive compensation, and smart grid issues. Avista, Staff, and ICNU filed rebuttal testimony in support of the Settlement on November 19, 2012.

- 22 An evidentiary hearing was convened in Olympia, Washington, on November 29, 2012. Chairman Jeffrey D. Goltz, Commissioner Patrick J. Oshie, and Commissioner Philip B. Jones were assisted at the bench by Judge Friedlander. On December 7, 2012, Commission Staff, Public Counsel, Avista, ICNU, and NWIGU filed simultaneous post-hearing briefs. Altogether, the record includes more than 250 exhibits entered during the evidentiary hearing. The transcript of this proceeding exceeds 350 pages in length.

## **II. Discussion and Decisions**

### **A. Introduction**

- 23 The Commission's statutory duty, in the context of a general rate case, is to balance the needs of the public to have safe and reliable electric service at reasonable rates with the financial ability of the utility to prospectively provide such service. In fulfilling its statutory duty, the Commission must establish rates that are "fair, just, reasonable and sufficient."<sup>22</sup> The rates must be fair to both customers and the utility, just in that the rates are based solely on the record in this case following the principles of due process of law, reasonable in light of the range of potential outcomes presented

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<sup>22</sup> RCW 80.28.010(1); RCW 80.28.020.

in the record, and sufficient to meet the financial needs of the utility to cover its expenses and attract capital on reasonable terms.<sup>23</sup>

24 Pursuant to WAC 480-07-750(1), the Commission will approve settlements when doing so is lawful, the settlement terms are supported by an appropriate record, and when the result is consistent with the public interest in light of all the information available to the Commission.

25 Thus, the Commission considers the individual components of the settlement under a three-part inquiry. We ask:

- Whether any aspect of the proposal is contrary to law.
- Whether any aspect of the proposal offends public policy.
- Whether the evidence supports the proposed elements of the settlement as a reasonable resolution of the issues at hand.

26 The Commission then must reach one of three possible results:

- Approve the proposed settlement without condition.
- Approve the proposed settlement subject to one or more conditions.
- Reject the proposed settlement.

## **B. Multi-Party Settlement**

### **1. Summary of Settlement**

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<sup>23</sup> *Federal Power Commission v. Hope Natural Gas*, 320 U.S. 591 (1944); *Bluefield Water Works & Improvement Company v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923). See *People's Organization for Washington Energy Resources v. Washington Utilities & Transportation Comm'n*, 104 Wn.2d 798, 807-13, 711 P.2d 319 (1985) (describing rate setting process in Washington).

27 On October 19, 2012, the Company filed a Settlement on behalf of all parties except Public Counsel and NWECC. While Public Counsel opposes the Settlement, NWECC does not.

28 The agreement itself is a “black box” Settlement. This means that the settling parties agree on some important components in the rate case, such as revenue requirements, cost of capital, capital structure, and rate spread and rate design, but the Settlement does not articulate the “give and take” process that produced these results. Put another way, the settling parties agree to firm end-result numbers without indicating which parties’ adjustments or issues have been included in the final numbers.

29 Some of the contested issues that the Settlement proposes to resolve are:

- Revenue Requirements for 2013 and 2014 (both electric and natural gas);
- Cost of Capital, Capital Structure and Rate of Return;
- Depreciation Rates Based on the Depreciation Study by Avista;
- ERM Rate Adjustment Trigger;
- Power Supply Revenues and Expenses;
- Renewable Energy Credit Revenue Deferral to Customers;
- An agreement not to advocate for electric decoupling prior to January 1, 2015;  
and
- Rate Spread and Rate Design (both electric and natural gas).

30 *Revenue Requirements.* The settling parties agree to a two-step rate increase: the first rate increase would become effective with service on and after January 1, 2013, and the second increase would begin on or after January 1, 2014. This two-year rate increase is projected to produce an additional \$13.650 million (or 3.0 percent on average) in revenue for Avista from electric ratepayers in the first year and \$14.038 million (or 3.0 percent on average) in the second year.<sup>24</sup> The Company’s natural gas customers would pay \$5.300 million in additional rates (or 3.7 percent on average) for

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<sup>24</sup> Exh. No. 5, ¶¶ 4 and 5.

the first year and \$1.400 million in additional rates (or 0.9 percent on average) in the second year.<sup>25</sup>

- 31 Electric customers would see a credit of \$4.4 million during 2013 to mitigate the \$13.650 million rate increase.<sup>26</sup> Likewise, the settling parties agree that electric customers should receive a \$9 million credit to mitigate the 2014 rate increase.<sup>27</sup> Both credits would originate from monies in the ERM deferral balance, and the 2014 credit would be contingent upon the availability of such funds.<sup>28</sup> The settling parties envision these credits would reduce each year's electric rate increase to 2 percent on average.<sup>29</sup>
- 32 *Cost of Capital, Capital Structure and Rate of Return – Electric and Natural Gas.* The settling parties propose a 9.8 percent ROE, with a 47.0 percent common equity ratio, and an overall rate of return of 7.64 percent.<sup>30</sup>
- 33 *Attrition.* While the settling parties state that each of their respective litigation positions have been taken into account in reaching the agreement, the settling parties have explicitly not agreed to a specific attrition allowance.<sup>31</sup>

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<sup>25</sup> Id.

<sup>26</sup> Id., ¶ 4.

<sup>27</sup> Id., ¶ 5.

<sup>28</sup> Id., ¶¶ 4 and 5.

<sup>29</sup> Id.

<sup>30</sup> Id., ¶7.

<sup>31</sup> Id., ¶ 8.

- 34 *Depreciation Rates.* The settling parties agree to accept the Company's updated electric and natural gas depreciation rates, including for transportation equipment, effective January 1, 2013.<sup>32</sup>
- 35 *ERM Structure and Authorized Amounts.* The settling parties propose no modifications to the current ERM deadband or sharing bands but do agree that a new rate adjustment trigger should be set.<sup>33</sup> They recommend that the trigger be changed to a \$30 million threshold, from the current 10 percent of base revenues (approximately \$45 million at current base rates).<sup>34</sup> Once the \$30 million trigger is reached, Avista would either surcharge or rebate the balance to ratepayers.<sup>35</sup> The Retail Revenue Credit would be determined according to the Company's original proposal to base the amount only on the energy classified portion of the fixed and variable production and transmission revenue requirement.<sup>36</sup>
- 36 The settling parties agree to power supply revenues, expenses, retail load, and retail revenue credit, beginning January 1, 2013, and as set forth in Appendix 1 to the Settlement.<sup>37</sup> The settling parties also stipulate that the Palouse Wind Project is a prudent investment, and its costs and benefits have been included in the above-mentioned power supply revenues and expenses in Appendix 1 to the Settlement.<sup>38</sup>
- 37 *Renewable Energy Credit Revenues.* Beginning January 1, 2013, Renewable Energy Credit (REC) revenues would be tracked separately and deferred completely by

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<sup>32</sup> Id., ¶ 9.

<sup>33</sup> Id., ¶ 10.

<sup>34</sup> Id.

<sup>35</sup> Id.

<sup>36</sup> Id.

<sup>37</sup> Id., ¶ 11.

<sup>38</sup> Id.

Avista over that which is included in base rates, and the monies will not be subject to any deadbands or sharing bands.<sup>39</sup> The deferral would be for the benefit of the ratepayers and will accrue interest consistent with other ERM balances.<sup>40</sup>

- 38 *Natural Gas Decoupling Baseline and Application.* The baseline for the natural gas decoupling mechanism is updated with the test year information employed in this proceeding, and the settling parties include the updated baseline in Appendix 2 to the Settlement.<sup>41</sup> Schedule 159 shall continue in effect for Avista's natural gas customers with the updated baseline, and given the new rate design in Schedule 101, which adds a new block making the schedule an inclining two-block rate, the margin rate for determining deferrals will be the weighted average block rate.<sup>42</sup>
- 39 *Electric Decoupling.* The settling parties agree that Avista will not support adoption of an electric decoupling mechanism prior to its next general rate case, nor would any of the settling parties support implementation of electric decoupling for Avista prior to January 1, 2015.<sup>43</sup>
- 40 *"Stay Out" Provision.* Indeed, the Company agrees not to file a general rate case that seeks to implement a rate increase that would become effective before January 1, 2015.<sup>44</sup>
- 41 *Deferred Accounting for Maintenance Costs of Colstrip and Coyote Springs 2.* The deferral mechanism associated with annual maintenance costs of Colstrip Units 3 and

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<sup>39</sup> Id., ¶ 12.

<sup>40</sup> Id.

<sup>41</sup> Id., ¶ 13.

<sup>42</sup> Id.

<sup>43</sup> Id., ¶ 14.

<sup>44</sup> Id., ¶ 23.

4 and Coyote Springs 2 will terminate on December 31, 2012, while the 2011 and 2012 deferred amounts will be amortized over a four year period.<sup>45</sup>

42 *Aldyl-A Accounting.* Avista will begin tracking separately, on January 1, 2013, all projects associated with the Aldyl-A natural gas pipeline replacement program so the data will be available for future review by the Commission.<sup>46</sup>

43 *Allocation Methods.* Avista will provide justification for the service and jurisdictional cost allocation methodologies it employs in its next general rate case filing.<sup>47</sup>

44 *Rate Spread and Rate Design.* The settling parties propose to apply an equal percentage increase to all electric and natural gas service schedules for purposes of recovering the Company's revenue requirement effective January 1, 2013, and January 1, 2014.<sup>48</sup> The Residential Basic Charge for both electric (Schedule 1) and natural gas (Schedule 101) customers would increase from \$6.00 per month to \$8.00 per month on January 1, 2013, but there will be no additional increase on January 1, 2014.<sup>49</sup>

45 *Low Income Rate Assistance Program Funding.* The settling parties propose an increase in Low Income Rate Assistance Program (LIRAP) funding in the amount of \$176,000 for 2013, and for 2014, LIRAP funding will increase an additional \$131,000.<sup>50</sup>

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<sup>45</sup> Id., ¶ 15.

<sup>46</sup> Id., ¶ 16.

<sup>47</sup> Id., ¶ 17.

<sup>48</sup> Id., ¶¶ 18(a) and 19(a).

<sup>49</sup> Id., ¶¶ 18(b) and 19(b).

<sup>50</sup> Id., ¶ 21.

46 *Effective Date.* The settling parties propose effective dates of January 1, 2013, and January 1, 2014, respectively, for the two-step rate increases.<sup>51</sup> They indicate that this provision is an integral part of the Settlement.<sup>52</sup>

## 2. Public Counsel's Objection to Settlement

47 Public Counsel contests the Settlement. For a number of reasons, it attacks the magnitude of the proposed rate increases, both for 2013 and 2014. Public Counsel also objects to use of the ERM to offset any portion of those rate increases.

48 *Arguments of the Settling Parties.* The settling parties propose a two-step rate increase for Avista which would allow the Company to collect additional revenue during the 2013 and 2014 rate years. Beginning on or after January 1, 2013, the Settlement would allow Avista to collect \$13.650 million (or 3.0 percent on average) in additional electric revenues and \$5.300 million (or 3.7 percent on average) in additional natural gas revenues.<sup>53</sup> On or after January 1, 2014, the Company would be authorized to collect \$14.038 million in additional revenue from electric customers (or 3.0 percent on average) and \$1.400 million from natural gas customers (or 0.9 percent on average).<sup>54</sup> To mitigate the effect of the rate increases on electric customers, the Settlement provides for a credit in 2013 of \$4.400 million from the existing ERM deferral balance, thereby reducing the electric rate increase to 2.0 percent on average in 2013.<sup>55</sup> Likewise, the settling parties pledge \$9 million from

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<sup>51</sup> Id., ¶ 22.

<sup>52</sup> Id.

<sup>53</sup> Id., ¶ 4.

<sup>54</sup> Id., ¶ 5.

<sup>55</sup> Id., ¶ 4.



the ERM deferral balance in 2014 to reduce the overall impact of the 2014 rate increase on electric customers, if such funds are available.<sup>56</sup>

- 49 Avista claims that the two-step rate increases outlined in the Settlement will provide its “customers more certainty in their energy rates for the next two years ....”<sup>57</sup> The proposed increases, if combined, would be lower than the rate increase the Company initially requested for one year, 2013, and “will provide a sufficient earnings opportunity for Avista only with the implementation of additional, aggressive cost management measures....”<sup>58</sup> Indeed, the settling parties state that the Company’s revised initial electric rate request of \$41.9 million for 2013 “is well above the combined revenue increases for 2013 [\$13.650 million] and 2014 [\$14.038 million] in the Settlement....”<sup>59</sup>
- 50 Avista filed an attrition study prepared by its witness, Dr. Mark N. Lowry, with its initial case that revealed attrition on a continuing basis resulting in 2013 revenue shortfalls for the Company of \$41 million for electric operations and \$10.4 million for natural gas operations.<sup>60</sup> After reducing Dr. Lowry’s attrition analyses results for 2013 to reflect the Settlement ROE of 9.8 percent and equity ratio of 47 percent, the Company’s requested revenue increase would drop from \$41 million to \$29 million for electric operations, and from \$10.4 million to \$8.3 million for natural gas operations.<sup>61</sup> When combined, the Company’s adjusted total of \$37.3 million is well

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<sup>56</sup> Id., ¶ 5. The parties expect the Company to recover the \$9.9 million transferred from the ERM account into general rates through a tariff filing made late in 2014. If approved, general rates will increase by approximately 2.0 percent on January 1, 2015.

<sup>57</sup> Exh. No. JT-1T, at 21:5-6.

<sup>58</sup> Id., at 21:13-15.

<sup>59</sup> Id., at 22:18-22.

<sup>60</sup> Norwood, Exh. No. KON-7T, at 9:14-20.

<sup>61</sup> Id., at 10:2-5.

above the \$18.95 million combined electric and natural gas increase in the Settlement for 2013.<sup>62</sup>

51 With regard to the Settlement's proposed 2014 rate increases, Avista argues that, while the increases themselves were not discussed in the Company's original filing, Mr. Norwood's direct testimony demonstrated the need for additional rate relief in the years following 2013.<sup>63</sup> In his testimony, Mr. Norwood included a graph projecting that net plant investment and non-fuel operations and maintenance expenses will continue increasing at a faster pace than kilowatt-hour sales and therm sales for 2014 and 2015.<sup>64</sup> This disparity, Mr. Norwood contends, will require additional rate increases for 2014 and in the future.<sup>65</sup> Mr. Norwood asserts that the Company's Response to Staff Data Request No. 137 also provides a financial forecast for the years 2012 through 2015, and further demonstrates Avista's need for revenue increases during this period that are greater than have been agreed to in the Settlement.<sup>66</sup>

52 Avista also contends that the two-step rate increases, combined with the "stay out" provision preventing the Company from filing for new rates that would become effective prior to January 1, 2015, will "break the yearly cycle of general rate case filings" and will benefit customers, the Commission, Staff, intervenors, and Avista.<sup>67</sup> In acknowledging that the revenue increases reached among the parties are part of a "black box" revenue requirement, the Company asserts that Public Counsel's concerns regarding administrative and general costs, executive compensation, revenue

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<sup>62</sup> Id., at 10:5-7.

<sup>63</sup> Exh. No. JT-1T, at 22:32-33.

<sup>64</sup> Id., at 23:1-5.

<sup>65</sup> Id., at 23:6.

<sup>66</sup> Id., at 23:17-21.

<sup>67</sup> Id., at 24:6-12.

normalization, and other issues, were all taken into account in the formulation of the Settlement terms.<sup>68</sup>

53 Another settling party, ICNU, bases its support of the Settlement on the rate stability provided in the two-step increase.<sup>69</sup> While ICNU does not believe that the rate increases contained within the Settlement are the result of any finding of attrition,<sup>70</sup> Staff, on the other hand, relies heavily on the existence of attrition to justify the 2013 and 2014 rate increases.<sup>71</sup> Staff explains that the Company's capital expenditures for the replacement of facilities combined with little if any load growth through 2014, are significant indicators of attrition for Avista.<sup>72</sup> With regard to the natural gas rate increases, Staff contends that a major cause of attrition is the Company's twenty-year Aldyl-A pipe replacement program.<sup>73</sup>

54 *Argument of Public Counsel.* Public Counsel raises several issues with the Settlement's two-step increase. First, as discussed by its witness, James R. Dittmer, Public Counsel is concerned about any reliance on attrition to justify both the 2013 and 2014 rate increases. He spends considerable effort demonstrating that in fact the

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<sup>68</sup> Id., at 25:1-7.

<sup>69</sup> Id., at 32:14-17.

<sup>70</sup> Id., at 33:7-10. ICNU even indicated that it would not have been a party to the Settlement if such a finding were included.

<sup>71</sup> Id., at 26:12-16.

**Q. Please explain why Staff believes the rate increases in 2013 and 2014 are reasonable.**

A. First, Staff's attrition analysis shows Avista is experiencing significant attrition in its utility operations. This is not a one-time phenomenon, because the historical trends demonstrate attrition is present and ongoing.

<sup>72</sup> Id., at 26:16-19.

<sup>73</sup> Id., at 26:20-21.

2013 and 2014 rate increases include a substantial implicit attrition adjustment.<sup>74</sup> Mr. Dittmer comes to this conclusion by taking Avista's original non-attrition base rate increase of \$20.469 million and adjusting for items specifically agreed-to by the settling parties, such as updated power supply costs and capital structure.<sup>75</sup> The base rate increase for electric operations then totals just \$709,000 without adding any attrition back into the increase.<sup>76</sup> This is \$13 million less than the 2013 electric increase contained within the Settlement.<sup>77</sup>

55 Mr. Dittmer notes that the \$13 million in additional 2013 electric revenue and the entire 2014 rate increase, \$14.038 million, cannot be justified without adding a significant portion of the \$28.714 million attrition allowance claimed by Avista into the equation.<sup>78</sup> He raises both process and substantive issues relating to attrition.

56 Procedurally, he suggests the Commission reject the Settlement to develop a record on which to base a reasoned decision on how attrition adjustments should be made.<sup>79</sup> This, Mr. Dittmer states, would allow the Commission to provide guidance and precedent in an order.<sup>80</sup>

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<sup>74</sup> Dittmer, Exh. No. JRD-12CT, at 8:8-9:1.

<sup>75</sup> Id., at 6:16-7:2.

<sup>76</sup> Id., at 7:8-9.

<sup>77</sup> See Id., at 8 (Table 1).

<sup>78</sup> Id., at 9:9-13. Avista updated its original attrition request of \$20.514 million in its Joint Testimony in Support of the Settlement to include \$8.2 million additional attrition reflecting the revised retail load forecast. Exh. No. JT-1T, at 22:9-14.

<sup>79</sup> Id., at 10:5-10.

<sup>80</sup> Id., at 10:5-10.

- 57 On the substance, Mr. Dittmer takes issue with the use of attrition in contexts other than when the Commission has concerns with a utility's financial integrity.<sup>81</sup> Mr. Dittmer contends that a rate order for Puget Sound Energy, Inc., entered in 1982 resulted in the Commission adopting a financial attrition adjustment due to increasing debt costs and higher than normal long-term interest rates.<sup>82</sup> He argues that our existing historically low long-term debt interest rates do not lend themselves to such an attrition determination.<sup>83</sup>
- 58 Second, Public Counsel criticizes the magnitude of the increase for 2013 resulting from the "black box" Settlement. Mr. Dittmer points out that Commission Staff originally recommended a revenue requirement reduction for the Company totaling \$1.315 million after it had already included an attrition allowance.<sup>84</sup> And, with the stipulated ROE increasing Staff's revenue requirement total for the Company by \$7.924 million, he calculates that Staff's recommendation would then change from a revenue reduction for Avista to a revenue increase of \$6.609 million for 2013.<sup>85</sup> Because this is less than half of the \$13.650 million the Settlement provides for in 2013. Mr. Dittmer questions whether, given Staff's original position, these rates can be fair, just, and reasonable.<sup>86</sup> Likewise, Mr. Dittmer asserts that ICNU originally recommended a rate reduction for Avista in the amount of \$7.728 million, and the intervenor has not provided any support for the change in position now supporting a

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<sup>81</sup> See Dittmer, Exh. No. JRD-10T, at 8:16-19. Mr. Dittmer provides: "...the UTC was specifically concerned about WWP's financial integrity and ability to raise capital at reasonable rates when it broke from its prior precedent, which consisted of routinely limiting utility rate development to use of historic test years with traditional restating and proforma adjustments."

<sup>82</sup> *Id.*, at 9:9-11, and 9:19-20.

<sup>83</sup> *Id.*, at 10:3-6.

<sup>84</sup> Dittmer, Exh. No. JRD-12CT, at 11:9-12.

<sup>85</sup> *Id.*, at 12:6-9.

<sup>86</sup> *Id.*, at 13:1-6.

two-year step increase of \$27.688 million, other than the rate stability it will provide industrial customers.<sup>87</sup>

59 Third, Public Counsel is even more critical of the proposed 2014 rate increase. Mr. Dittmer notes that while the 2013 numbers were based on the initial Company filing employing a 2011 test year to establish reasonable rates for the 2013 rate year,<sup>88</sup> the 2014 stipulated rate increase is based purely on “unaudited forecasted operating results estimated for three years beyond the test year.”<sup>89</sup> He asserts that Avista’s graph addressing recent actual historic and projected percentage changes for 2012 to 2015 in total net plant investment, non-fuel operations and maintenance, retail kilowatt-hour sales, and retail therm sales only provides the percentage changes for the total Company instead of Washington-specific dollar amounts.<sup>90</sup> In addition, there is a lack of original workpapers or exhibits to support any of the projected amounts.<sup>91</sup> Finally, the 2012 through 2015 financial forecast contained within Avista’s Response to Staff’s Data Request 137 is also calculated on a system-wide basis and not a Washington jurisdictional one.<sup>92</sup>

60 Fourth, Public Counsel is critical of a post-settlement announcement by Avista that it will seek to reduce staffing levels by initiating a voluntary employee severance plan.<sup>93</sup> The severance plan is expected to cut \$14 million from the Company’s 2013 operating costs.<sup>94</sup> Staff, ICNU, and NWIGU each acknowledged during the

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<sup>87</sup> Id., at 13:15-14:3.

<sup>88</sup> Id., at 17:13-15.

<sup>89</sup> Id., at 17:15-17.

<sup>90</sup> Id., at 18:10-13.

<sup>91</sup> Id., at 18:13-15.

<sup>92</sup> Id., at 19:2-4, 19:6-9.

<sup>93</sup> Id., at 20:19-20.

<sup>94</sup> Id., at 21:1-2

evidentiary hearing that the severance plan and its potential savings were not known to them at the time they executed the Settlement.<sup>95</sup> Further, Avista's financial forecast for 2014, as limited as the information was, did not contain any reference to the severance plan cuts.<sup>96</sup>

61 Finally, Public Counsel notes the impact on consumers. Public Counsel witness Lea Daeschel, argues that implementation of the 2013 rate increases on January 1, 2013, would allow the Company to collect over \$2 million in additional revenue than had rates become effective by the March 2013 suspension date.<sup>97</sup> The two-step rate increases, scheduled by the settling parties to take effect on January 1, 2013, and January 1, 2014, will also hit customers with "energy bill increases in the midst of the winter heating season for two consecutive years."<sup>98</sup>

62 *Response of the Settling Parties to Public Counsel.* Avista counters that the Settlement was the result of the give-and-take of negotiations, that voluminous discovery occurred over six months,<sup>99</sup> that the Company responded to 897 discovery requests, and Commission Staff conducted two on-site audits.<sup>100</sup> Mr. Norwood reiterates that the total Settlement rate increase for electric and natural gas customers over the two-year period, which amounts to over \$34 million, is only 64 percent of the Company's \$53.3 million rate request for electric and natural gas customers for one year, 2013.<sup>101</sup>

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<sup>95</sup> Elgin, TR 190:4-18 and Deen, TR 199:18-200:3.

<sup>96</sup> Dittmer, Exh. No. JRD-12CT, at 21:15-18.

<sup>97</sup> Daeschel, Exh. No. LD-1CT, at 6:21-7:2.

<sup>98</sup> *Id.*, at 7:3-5.

<sup>99</sup> Norwood, Exh. No. KON-7T, at 2:6-11.

<sup>100</sup> Exh. No. JT-1T, at 21:17-19.

<sup>101</sup> Norwood, Exh. No. KON-7T, at 7:12-17.

- 63 In addition, Avista argues that its financial forecast from 2011 to 2013 clearly shows that utility operating expenses will increase approximately \$14 million in 2013 due to higher pension expenses, post-retirement medical costs, and power plant operations and maintenance costs.<sup>102</sup> The Company's revised load forecast for 2013 also demonstrates an \$8 million retail revenue decrease due "to an expectation that the recovery in the economy will not occur as quickly as [the Company] had previously expected."<sup>103</sup>
- 64 Mr. Norwood acknowledges that the settling parties were not aware that the Company was considering a voluntary severance plan to reduce costs for 2013.<sup>104</sup> He goes on to say that Avista initiated such a program knowing that the agreed-to revenue increases for 2013 would not be sufficient to allow the Company to earn a rate of return close to the 7.64 percent without additional savings efforts on the part of Avista.<sup>105</sup>
- 65 As for 2014, Avista argues that its attrition study shows a continued revenue shortfall if the disparity of growth in costs and limited revenues is not addressed in the ratemaking process.<sup>106</sup> A simple extension of the trend analysis in Dr. Lowry's attrition study to 2014 would show, according to Mr. Norwood, the need for an incremental electric revenue increase of \$14.5 million for 2014.<sup>107</sup> Mr. Norwood states that, even factoring in the Settlement cost of capital, the combined electric and natural gas revenue requirement for 2013 and 2014 would total \$56.0 million.<sup>108</sup>

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<sup>102</sup> Id., at 18:12-14.

<sup>103</sup> Id., at 18:19-22.

<sup>104</sup> Id., at 17:4-5.

<sup>105</sup> Id., 17:5-9.

<sup>106</sup> Id., at 9:20-22.

<sup>107</sup> Id., at 10:8-10.

<sup>108</sup> Id., at 10:17-19 (citation to footnote omitted).



- 66 Mr. Norwood also asserts that the Commission does not need to address a specific attrition allowance in order to approve the Settlement “because there are multiple approaches or methods to address the same issue.”<sup>109</sup> For example, Mr. Norwood points to the shortfall Avista is experiencing in its earned ROE of at least 200 basis points.<sup>110</sup> Avista calculates this revenue shortfall for its Washington utility operations at approximately \$21 million.<sup>111</sup>
- 67 Avista asserts, in its post-hearing brief, that the updated information in response to Bench Request No. 8C demonstrates, “... an even greater erosion in margin recovery for both 2013 and 2014 than the earlier February 29, 2012 forecast.”<sup>112</sup> In fact, the Company contends that the August 2012 forecasts show trends in net plant investment, non-fuel operations and maintenance, and sales through 2015 have worsened as far as cost recovery.<sup>113</sup> Utility operating expenses increased by \$14 million in 2013 and \$12 million in 2014 from the earlier February 29, 2012, forecast, at least in part attributable to pension expense, post-retirement medical costs, and power plant operations and maintenance costs.<sup>114</sup> Staff agrees and argues that Avista’s Response to Bench Request No. 8C shows that 2014 non-fuel expenses and continued annual facility investments are consistent with Staff’s attrition study trending estimates of rate base, expenses, and revenue.<sup>115</sup>

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<sup>109</sup> Id., at 13:3-5.

<sup>110</sup> Id., at 14:5-6.

<sup>111</sup> Id., at 14:6-7.

<sup>112</sup> Avista’s Post-Hearing Brief, ¶ 7.

<sup>113</sup> Id., n. 7.

<sup>114</sup> Id., ¶ 8.

<sup>115</sup> Staff’s Post-Hearing Brief, ¶10.

68 Indeed, Staff's attrition study showed that the Company will likely experience \$19.1 million and \$2.8 million, respectively, in electric and natural gas attrition in 2013.<sup>116</sup> Mr. Elgin asserts that Public Counsel neither prepared its own attrition study nor testified that the Company was not experiencing attrition at all.<sup>117</sup>

69 Staff points to Avista's nearly annual general rate case filings over the last decade, and states that, for the most recent three-year period, the average rate increase has been 4.9 percent.<sup>118</sup> This pattern has been, according to Mr. Elgin, the result of capital expenditures twice as great as depreciation expense, increasing non-fuel operating expenses, and low revenue growth.<sup>119</sup> With regard to the 2014 rate increase contemplated by the Settlement, Mr. Elgin asserts that Staff considered the Company's financial forecasts which show Avista intends approximately \$250 million in additional investments, slow economic growth continues to hamper revenues, and Avista will continue to face upward pressure in non-fuel operating costs.<sup>120</sup>

70 *Discussion and Decision.* Historically, the Commission has approved attrition adjustments in the context of litigated rate cases, although the Commission has not ruled on such an adjustment in recent years. Such a context permits a thorough review of the evidence necessary for an appropriate adjustment. In the context of this Settlement, however, we have not had the opportunity either to articulate the appropriate standards by which to assess a proposed attrition adjustment nor evaluate thoroughly the evidence in support of such an adjustment. Here, both the Company

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<sup>116</sup> Elgin, Exh. No. KLE-7T, at 3:1-3. Staff's witness, Mr. Kenneth L. Elgin, says attrition was considered in Staff's determination that the Settlement is reasonable. Elgin, Exh. No. KLE-7T, at 2:14-15. See Elgin, TR 178:9-12 and TR 179:11-14.

<sup>117</sup> Id., at 3:5-6.

<sup>118</sup> Id., at 6:14-15.

<sup>119</sup> Id., at 6:17-19.

<sup>120</sup> Id., at 7:1:4.

and Staff performed attrition studies to project 2013 rates. We agree with the Company and Staff that the proposed 2013 rate increase is based significantly on attrition. Even adjusting Commission Staff's original recommended revenue decrease for Avista of \$1.3 million for the modified 9.8 percent ROE, at least half of the Settlement's 2013 rate increase must be associated with some aspect of attrition. We find sufficient evidence in both Staff and the Company's attrition analyses to demonstrate that, based on the 2011 test year data, Avista will experience some level of attrition in 2013. Public Counsel, not having conducted an analysis of its own, fails to rebut the numbers arrived at by both Staff and Avista for 2013.

71 Much of the attrition is based on continued capital investment by Avista. The Company has put forth its 2013 capital construction plan, and its representation that it will continue to make such needed investments in upcoming years. However, we deem it desirable to monitor the Company's progress in achieving its plan for capital expenditures so that the ratepayers can be assured that the rate increase designed to assist the Company in making those investments can continue to be justified.

72 While the Company and Staff have each submitted attrition studies that justify the 2013 increase, they did not submit such studies for the 2014 increase, which also is justified substantially on anticipated continued attrition.<sup>121</sup> Rather, they argue that the trends of attrition from 2013 will continue through 2014, thereby justifying a further rate increase. For the purposes of this Settlement, we accept the trending analysis from both Staff and Avista. However, we make clear that the testimony and trending data offered in support of the proposed rate increase for 2014 are substantially less precise than we would require in a fully-litigated rate case. For this reason, we find that the 2014 rate increase should be instituted on a temporary basis such that, on January 1, 2015, Avista's rates would revert back to their 2013 levels, absent intervening Commission action.

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<sup>121</sup> Elgin, TR 248:5-14.

- 73 The trending data supplied by Avista, wherein the Company pledged to continue its multi-year capital expenditure program for both 2013 and 2014, forms a cornerstone of our approval of the two-step rate increases.<sup>122</sup> As Public Counsel rightly points out, we do not have a detailed capital expenditure plan for 2014 before us. Given that a detailed capital expenditure plan for 2014 may not be available until well into the third quarter of 2013, we require Avista to file such an updated capital expenditure plan on or before September 30, 2013. This filing should also describe the Company's actual expenditures in 2013 compared to the projected amounts. In addition, we require that the Company provide updates on changes in meeting the calendar year 2014 capital expenditure plan and the Company's progress in making such improvements on June 1, September 1, and December 1, 2014, respectively, for the previous quarters. Should Avista's representations in this proceeding regarding the necessity of such expenditures prove unsupported as compared to the Company's actual expenditures, the Commission may exercise our statutory authority and reopen this proceeding.
- 74 The Settlement also stipulates a 9.8 percent ROE. Though that is consistent with what we have approved in recent cases involving other utilities,<sup>123</sup> we note that equity returns continue to trend downward.<sup>124</sup> If this case had been litigated, we may very well have decided that an ROE of less than 9.8 would be warranted. However, we are convinced that, at the very least, 9.8 percent is within a zone of reasonableness, and we defer to the judgment of those parties that put on cost of capital evidence, both of which joined in the Settlement. Part of our motivation for setting the 2014 rate

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<sup>122</sup> As Mr. Elgin explained at hearing, natural gas attrition related to Avista's pipeline replacement plan is addressed in the Settlement, and any costs over and above the plan will be recovered using the cost recovery mechanism. Elgin, TR at 253:6-254:8.

<sup>123</sup> For example, *WUTC v. Puget Sound Energy, Inc.*, Dockets UE-111048 and UG-111049 (consolidated), Order 08, ¶ 89 (May 7, 2012).

<sup>124</sup> See Edison Electric Institute, Rate Case Summary, Q3 2012 Financial Update, at 1. Phillip S. Cross, *How Much Is Enough? Utilities Face Rate Pressure As Financing Costs Hit Rock Bottom*, 150 Public Utilities Fortnightly 22 (November 2012).

increase as temporary is our anticipation of revisiting the appropriate level of ROE, if the Company files a new general rate case in the early part of 2014.

75 In the course of consideration of the Settlement, Avista proposed a cap on its earnings at the 9.8 percent ROE level. We decline to accept that offer. It would send the wrong signal to the Company. Under ratemaking theory applied by this and other state commissions for decades, companies should have every incentive to manage the company efficiently in order to earn more for the company shareholders. We should not set an artificial cap on earnings that could diminish that incentive for efficient management. Further, if Avista were to “overearn” through savings efforts, those savings would become the new norm in the next rate case which would serve to benefit ratepayers in the future. Indeed, the Company’s efforts to save money through efficiency are a key element to earning its allowed rate of return. Avista states that, to earn its authorized rate of return, it intends to aggressively cut costs.<sup>125</sup> We consider such aggressive measures long overdue. In setting temporary rates for 2014, the Commission will be afforded the opportunity to compare the effect of cost cutting measures during the 2013 and 2014 period to previous periods in which the Company has claimed it under-earned should the Company file a rate case. The Company, as it has done with the voluntary severance program, should continue to develop and implement cost-cutting measures that balance efficient management with safe and reliable operations of its electric and natural gas systems.

76 While the attrition trending analysis supports the Settlement, there are other factors that support the “end result” as well.<sup>126</sup> The Settlement provides rate stability for customers for two years and represents an innovative approach that will provide incentives to Avista to cut costs in order to earn a fair rate of return. Moreover, the lack of annual rate filings will provide the Company, Commission Staff, and all parties with a respite from the burdens and costs of litigation.

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<sup>125</sup> Norwood, TR 236:9-15 and 17-20.

<sup>126</sup> Ultimately, it is the “end result” that is the test of whether proposed rates are fair, just, reasonable, and sufficient. See *POWER*, 104 Wn.2d at 111, citing [Federal Power Comm'n v. Hope Natural Gas Co.](#), 320 U.S. 591, 603, 64 S.Ct. 281, 88 L.Ed. 333 (1944).

- 77 In conditionally approving the Settlement, we are not endorsing the specific attrition methodologies, assumptions, or inputs used in this case. Indeed, Commission Staff witness Kathryn Breda cautioned us about using her analysis as the model for future attrition decisions. Though we agree with Commission Staff that an attrition adjustment should not be limited to circumstances where the utility can demonstrate extreme financial distress, as advocated by Public Counsel,<sup>127</sup> we intend to clarify the conditions wherein attrition should be considered when setting rates. As noted above, the Settlement has limited our opportunity to do so here. Accordingly, we will in the near future initiate an inquiry into the appropriate use of attrition analysis in setting rates, including the appropriate methodology to use in preparing attrition studies.
- 78 One other issue that is unresolved by this Settlement is the appropriate level of executive compensation and the appropriate methodology for determining that level. We broached this issue in the last Avista general rate case by asking for reports from the Company and inviting the parties to address the issue in this case.<sup>128</sup> Both Public Counsel and Commission Staff accepted our invitation with some thorough studies of compensation levels and recommendations on adjustments to reflect the appropriate level of such compensation. While disappointed that the Settlement did not address this topic specifically, we are convinced that the Commission will have another opportunity to examine executive compensation in Avista's next general rate case, in light of Avista's stated intent to look aggressively at cost cutting measures.

### 3. Proceeds From Sales of Renewable Energy Credits

- 79 Under the Settlement, \$3,410,297 in projected REC sale proceeds is included in base retail rates via the ERM.<sup>129</sup> The Settlement proposes that any deviation, above or

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<sup>127</sup> Dittmer, Exh. No. JRD-10T, at 11:19-12:19.

<sup>128</sup> *WUTC v. Avista Corporation d/b/a Avista Utilities*, Dockets UE-110876 and UG-110877, Order 06, ¶¶ 42 and 43, December 16, 2011.

<sup>129</sup> Norwood, Exh. No. KON-7T, at 25:7-8.

below the level of projected REC sale proceeds be deferred within the ERM but not subject to the deadband or sharing bands.<sup>130</sup> The separately tracked REC deferrals would presumably remain a component within the ERM deferral for an unspecified duration or perhaps could be credited to customer's rates, if and when, the ERM deferral trigger was met. The Settlement does not specify a firm trigger for the crediting of REC sale proceeds to customer rates.

80 Public Counsel proposes that 100 percent of all 2013 REC sale proceeds be removed from 2013 base rates, deferred in a separate account, and returned via a bill credit.<sup>131</sup> Ms. Daeschel, on behalf of Public Counsel, recommends the Commission order Avista to work with parties to develop the details of a separate tracker and bill credit.<sup>132</sup> She also recommends that the 2012 REC sale proceeds above the \$4,077,485 REC sale proceeds included in base rates in the last general rate case be returned to ratepayers.<sup>133</sup>

81 The Commission considers REC sale proceeds akin to revenues from property sales that belong to ratepayers and should be returned to them in full.<sup>134</sup> While cumbersome, the Settlement's treatment of REC sale proceeds accomplishes this goal, with one exception.

82 By setting a projected amount of REC sale proceeds in rates not subject to any deadband or sharing band, the Settlement returns that specified amount of REC revenue to ratepayers via Schedule 93.<sup>135</sup> We see value in the Company providing its

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<sup>130</sup> Id., at 25:16-18; 26:1-2.

<sup>131</sup> Daeschel, Exh. No. LD-1CT at 14:4-9.

<sup>132</sup> Id., at 14:7-9.

<sup>133</sup> Id., at 14:2-4.

<sup>134</sup> *WUTC v. PacifiCorp*, Docket UE-100749, Order 10, ¶ 24.

<sup>135</sup> Schedule 93 is the Power Cost Surcharge added to base electricity rates to recover deferral balances generated by the ERM approved by the Commission in Docket UE-011595.

customers with rate relief when it can. However, the Settlement does not provide a mechanism for the return of the difference between the REC sale proceeds in base rates and actual REC sale proceeds.

83 The Commission orders Avista to defer the difference between the REC sale proceeds in base rates and actual REC sale proceeds to a separate tracking account not subject to the trigger mechanism of the ERM. At the time of its next filed rate case, Avista will propose a mechanism for returning any such accumulated difference of REC sale proceeds in a true-up. The Commission recognizes that the balance in this account at the time of the next general rate case may be a credit or debt to customers.

84 To simplify the treatment of REC sale proceeds in the next general rate case, the Commission orders Avista to remove REC sale proceeds from the ERM account and base rates, to project the revenues expected in the rate year, and to defer such revenues to a tracking account established by the Company. The REC sale proceeds will be returned to ratepayers via a mechanism consistent with those used by Puget Sound Energy and PacifiCorp and presented for approval in the next general rate case.

85 For the 2012 REC sale proceeds currently accounted for in the ERM, the Commission orders that all such revenues in excess of the \$4,077,485 million now credited to customers be deferred into the tracking account established by this Order without being subject to the ERM deadbands or sharing bands.

#### **4. Energy Recovery Mechanism**

86 The Settlement also alters the retail revenue credit in the ERM. The Commission accepts the Settlement as a non-precedent setting agreement. To extend this modification to the ERM, the Company must seek approval in the next general rate case and provide more extensive testimony in support of its request. We expect the parties to contribute to our determination as to whether extending the change to the retail revenue credit is in the public interest.



## 5. Other Issues

- 87 *Prudence of Palouse Wind Project.* The settling parties have agreed that the costs and benefits associated with the Palouse Wind Project render it prudent. Public Counsel, the only party opposing the Settlement, did not dispute this claim. On the record we have before us, the Commission finds the Palouse Wind Project prudent.
- 88 *Decoupling.* Paragraph 14 of the Settlement provides that “[e]ach of the Settling Parties agrees not to support the implementation of electric decoupling for Avista prior to January 1, 2015.” We believe that it is not appropriate to bind any future commission, or the settling parties, by placing limitations on their views on electric decoupling in future proceedings. Therefore, we do not recognize such limitations provided in this part of the Settlement. Based on this provision within the Settlement, NWECA has also requested authority to withdraw its decoupling proposal for Avista. We decline to rule on NWECA’s request at this time.
- 89 *Aldyl-A.* Regarding Aldyl-A accounting in paragraph 16 of the Settlement, we agree that it is appropriate to establish separate accounting for this particular type of capital investment. We also recognize that certain capital costs of the Company’s ongoing natural gas pipeline replacement program are embedded in the rates we are approving in this case. We note that the Commission will soon issue a policy statement on natural gas pipeline safety, including a cost recovery mechanism allowing for earlier cost recovery on enhanced pipeline replacement programs. Accordingly, if the Company were to file for such a mechanism in a future proceeding, we will exercise great diligence in ensuring that it will not be able to over-earn on such investments in this particular time period.

## **FINDINGS OF FACT**

- 90 Having discussed above in detail the evidence received in this proceeding concerning all material matters, and having stated findings and conclusions upon issues in dispute among the parties and the reasons therefore, the Commission now makes and enters

the following summary of those facts, incorporating by reference pertinent portions of the preceding detailed findings:

- 91 (1) The Washington Utilities and Transportation Commission is an agency of the State of Washington, vested by statute with authority to regulate the rates, rules, regulations, practices, and accounts of public service companies, including electrical and gas companies.
- 92 (2) Avista Corporation d/b/a Avista Utilities (Avista or the Company) is a “public service company,” an “electrical company,” and a “gas company” as those terms are defined in RCW 80.04.010 and used in Title 80 RCW. Avista is engaged in Washington in the business of supplying utility services and commodities to the public for compensation.
- 93 (3) Avista filed on April 2, 2012, certain revisions to its currently effective tariffs, including rate increases for customers of its electric and natural gas services in Washington. The revised tariff sheets bore an effective date of May 3, 2012.
- 94 (4) The Commission suspended the operation of the proposed tariff revisions on April 26, 2012, pending an investigation and hearing in Dockets UE-120436 and UG-120437.
- 95 (5) On May 14, 2012, the Commission entered Order 03/08, Prehearing Conference Order, consolidating Dockets UE-120436 and UG-120437 with the second phase of Dockets UE-110876 and UG-110877.
- 96 (6) On October 19, 2012, Avista, the Commission’s regulatory staff (Staff), the Industrial Customers of Northwest Utilities (ICNU), the Northwest Industrial Gas Users (NWIGU), and The Energy Project filed a Multi-Party Settlement Stipulation (Settlement) that, if approved, would resolve all issues concerning cost of capital, power costs, rate spread and rate design, and other matters.

The Settlement is attached to this Order as Appendix A and incorporated by reference as if set forth in full in the body of this Order.

- 97 (7) The Settlement provides for a revenue increase for Avista of \$13.650 million from electric customers and \$5.3 million from natural gas customers effective January 1, 2013. A credit of \$4.4 million would be returned to electric customers to mitigate the 2013 rate increase from the existing Energy Recovery Mechanism (ERM) deferral balance. The Settlement also provides for a revenue increase for Avista of \$14.038 million from electric customers and \$1.4 million from natural gas customers effective January 1, 2014. The settling parties propose a credit of \$9 million be returned to electric customers to mitigate the 2014 rate increase from the then-existing ERM deferral balance, if such funds are available.
- 98 (8) The Company has requested that we find that its acquisition of renewable energy from the Palouse Wind Project in a power purchase agreement with First Wind is prudent, and that its costs should be included in the overall calculation of ERM-authorized power costs and expenses in Appendix 1 to the Settlement. We find that this contract is prudent, and that it is consistent with the Company's obligations to meet the renewable energy targets established in I-937.
- 99 (9) While Avista provided 2011 test year documentation to support its proposed 2013 rate increase, the Company has failed to file any capital expenditure plan for 2014.
- 100 (10) The rates, terms, and conditions of service that result from adoption of the Settlement, coupled with the additional conditions placed on the Settlement by the Commission, result in rates for Avista's electric and natural gas services that are fair, just, reasonable and sufficient.
- 101 (11) The rates, terms, and conditions of service that result from the Commission's determinations in this Order are neither unduly preferential nor discriminatory.

**CONCLUSIONS OF LAW**

- 102 Having discussed above all matters material to this decision, and having stated detailed findings, conclusions, and the reasons therefore, the Commission now makes the following summary conclusions of law, incorporating by reference pertinent portions of the preceding detailed conclusions:
- 103 (1) The Washington Utilities and Transportation Commission has jurisdiction over the subject matter of, and parties to, these proceedings.
- 104 (2) The rates proposed by tariff revisions filed by Avista on April 2, 2012, and suspended by prior Commission order, were not shown to be fair, just or reasonable and should be rejected.
- 105 (3) The existing rates for electric and natural gas services that Avista provides in Washington are insufficient to yield reasonable compensation for the services rendered.
- 106 (4) Avista requires relief with respect to the rates it charges for electric service and gas service provided in Washington.
- 107 (5) The Settlement filed by Avista, Staff, ICNU, NWIGU, and The Energy Project on October 19, 2012, if approved subject to the conditions stated in this Order requiring additional reporting of Avista's plan for capital expenditures during 2013 and 2014 as well as requiring the 2014 rates to expire on January 1, 2015, would result in rates for Avista that are fair, just, reasonable and sufficient, and are neither unduly preferential nor discriminatory. The Settlement is attached to this Order as Appendix A, and incorporated by reference as if set forth in full in the body of this Order.
- 108 (6) The Settlement should be approved by the Commission, subject to the conditions stated in this Order, as a reasonable resolution of the issues

presented. Approval and adoption of the Settlement, as conditioned, is in the public interest.

- 109 (7) Avista should be required to make such compliance and subsequent filings as are necessary to effectuate the terms of this Order.
- 110 (8) The Commission should retain jurisdiction to effectuate the terms of this Order.

### **ORDER**

#### THE COMMISSION ORDERS:

- 111 (1) The tariff revisions Avista Corporation d/b/a Avista Utilities, filed on April 2, 2012, and suspended by prior Commission order, are rejected.
- 112 (2) The Settlement filed by Avista, Staff, ICNU, NWIGU, and The Energy Project on October 19, 2012, is approved and adopted as being in the public interest, subject to the additional capital expenditure reporting requirements, the temporary implementation of the 2014 rate increases, and other conditions spelled out in the body of the Order.
- 113 (3) Avista is authorized and required to file tariff sheets that are necessary and sufficient to effectuate the 2013 rate increases of this Order. The required tariff sheets must be filed no later than 4:00 p.m. on Thursday, December 27, 2012, to give the Commission an opportunity to review the Company's compliance filing, and shall bear an effective date of January 1, 2013. The Commission has placed conditions on the Company in this Order that, collectively, result in fair, just, reasonable, and sufficient rates. By its compliance tariff sheets effective January 1, 2013, Avista will be deemed to have consented to all of the Commission's conditions within this Order.

- 114 (4) With regard to its planned capital expenditures for calendar year 2013, Avista must file: (1) a progress report on its 2013 capital expenditures on or before September 30, 2013; and (2) a comprehensive report on the final totals for 2013 capital expenditures on or before March 1, 2014.
- 115 (5) As to the capital expenditures Avista plans to make in calendar year 2014, the Company must file: (1) its capital expenditure plan for 2014 on or before September 30, 2013; and (2) updates on changes in meeting its capital expenditure plan for 2014 and reports on progress in making such capital improvements on June 1, September 1, and December 1, 2014, respectively, for the previous quarters.
- 116 (6) The Commission Secretary is authorized to accept by letter, with copies to all parties to this proceeding, such filings as Avista makes to comply with the terms of this Order.
- 117 (7) The Commission retains jurisdiction to effectuate the terms of this Order.

Dated at Olympia, Washington, and effective December 26, 2012.

**WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**JEFFREY D. GOLTZ, Chairman**

**PATRICK J. OSHIE, Commissioner**

**PHILIP B. JONES, Commissioner**

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**NOTICE TO PARTIES: This is a Commission Final Order. In addition to judicial review, administrative relief may be available through a petition for reconsideration, filed within 10 days of the service of this order pursuant to RCW 34.05.470 and WAC 480-07-850, or a petition for rehearing pursuant to RCW 80.04.200 and WAC 480-07-870.**

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**APPENDIX A**

**MULTI-PARTY SETTLEMENT STIPULATION**  
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**(consolidated)**