BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-991255
APPLICATION TO SELL THE CENTRALIA POWER PLANT

REBUTTAL TESTIMONY OF WILLIAM G. JOHNSON

REPRESENTING AVISTA CORPORATION

Exhibit T-314

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-991255
APPLICATION TO SELL THE CENTRALIA POWER PLANT

EXHIBIT NO. 315

WITNESS: WILLIAM G. JOHNSON AVISTA CORPORATION

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-991255
APPLICATION TO SELL THE CENTRALIA POWER PLANT

EXHIBIT NO. 316

WITNESS: WILLIAM G. JOHNSON AVISTA CORPORATION

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-991255
APPLICATION TO SELL THE CENTRALIA POWER PLANT

EXHIBIT NO. 317

WITNESS: WILLIAM G. JOHNSON AVISTA CORPORATION

Q Please state your name, business address, and present position with Avista Corporation ("Avista").

A My name is William G. Johnson. My business address is East 1411 Mission Avenue, Spokane, Washington. I am employed as a Power Contracts Analyst in the Resource Optimization Department.

Q Have you previously provided direct testimony in this proceeding?

A Yes.

Q What is the scope of your rebuttal testimony in this proceeding?

A My testimony will respond to issues raised by Mr. Lazar's direct testimony on behalf of Public Counsel.

Q. Are you sponsoring any exhibits to be introduced in this proceeding?

A. Yes. I am sponsoring Exhibit No(s). 315 through 317, as previously marked for identification, which were prepared under my supervision and direction.

Q. On page 9, line 21 of his direct testimony, Mr. Lazar asks if long-term forecasts of market prices are speculative. Do you agree with his response?

A. I agree with Mr. Lazar that forecasts of market prices are dependent on many factors including fuel costs, power plant construction costs and the power demand and supply balance. The uncertainty of these factors makes any long-term forecast speculative. I do not agree that the power prices forecast by the Northwest Power Planning Council which Mr. Lazar uses in his analysis are any better or any more appropriate for the analysis of the Centralia plant than are the market prices included in the sellers' analyses. Market price projections are very uncertain and models that predict market prices are based on assumptions that are also very uncertain.

Q. Does Mr. Lazar acknowledge the uncertainty of long-term power price forecasts?

A. Yes he does. In his Exhibit 502 "Economic Evaluation of Centralia Target Solution" he repeatably addresses the uncertainty of long-term power price forecasts. In the second paragraph on page 4 of Exhibit 502 he states, "The studies prepared by Pacificorp are based on specific assumptions, many of which are best guesses due to the uncertainties of long-run cost and market conditions." Again in the last paragraph on page 5 he states, "The value of power over a time far into the future is extremely uncertain." Finally in the third paragraph of page 11 he states, "Most important of these risks is that the value of power is extremely uncertain."

Q. On page 2, line 22 of his direct testimony, Mr. Lazar states that "At the time the proposed sale was conceived, expected future power prices were much lower than are forecast today." Do you agree with that statement?

A. Market energy prices have been moving up from the very low levels in 1995, 1996 and 1997 when prices were less than $14/MWh for an annual

average. Prices have moved to around $21 to $22/MWh in 1998 and 1999. Year 2000 power is trading around $26/MWh currently whereas earlier in the year it was trading under $23/MWh. What this upward movement in near-term prices has done is to increase the starting point for long-term price forecasts. When similar long-term escalations are applied to the new higher starting points, the effect is to produce a much higher long-term forecast. Every price forecast used in the Centralia analysis starts from roughly today's prices and escalates upward. Except for a pause in escalation in around 2010 in the Northwest Power Planning Forecast and Puget Sound Energy's Forecast (both use the Aurora model) the prices continuously increase. This is generally what happens in energy price forecasts because the forecasters do not attempt to model, do not understand how to model, or can't foresee future technologies, events or structural changes that may effect the future escalation of prices. Essentially, every forecast starts from were we are now (a known) and escalates upward continuously from that point.

In the past, energy price forecasts, showing escalating real prices, have been subject to extreme errors. For example, in 1990 BPA forecast the New Resource/Surplus Firm power rate, representing a proxy for the market price and new resources, to be $57.10/MWh in 2000 rising to $115.90/MWh in 2011. Exhibit 315 shows the BPA 1990 forecast. Actual market/new resource rates are less than one-half that in the year 2000. In fact, market prices were higher in 1985 than they were in 1998. Looking back, there may be plausible explanations for why this occurred but it is very unlikely that anyone in 1985 would have predicted prices to be lower in 1998.

Q. Has Avista seen market prices for the near-term, 2000 – 2006 that support the values for power that Mr. Lazar uses in his analysis?

A We have not. Based on market price quotes for longer-term (through 2010) power purchases, Avista believes that replacement power will be less costly than projected plant costs over the next 10 years. Beyond 10 years the market is essentially non-existent and price assumptions are speculative.

Q. Is there precedent for focusing on the next 10 years with regard to resource planning.

A. Yes there is. In Avista's last Integrated Resource Plan (IRP) in 1997, The Washington Utilities and Transportation Committee (WUTC) agreed to allow the company to conduct a 10-year plan. The company proposed this change primarily because there is so much uncertainty beyond 10 years. Beyond 10 years there is a lot of uncertainty regarding the structure of the industry, what our load obligations might be, future generation technologies, fuel costs and environmental regulation. While it may not be appropriate to limit the evaluation of Centralia to 10 years, it may be appropriate to put a greater emphasis on the first 10 years when some of the unknowns are more predictable.

Q. Do you agree with Mr. Lazar's analysis in Exhibit 501 that estimates that the present value of future plant costs is around $1.1 billion less than the cost of replacement power?

A. No I do not. First, based on conversations in the last two weeks with staff at the Northwest Power Planning Council (NWPPC), it appears as

though the market price forecast used in Exhibit 501 is not appropriate for valuing the replacement cost of Centralia power. The NWPPC forecast presented to its Regional Technical Forum included certain assumptions that created unrealistically high prices.

More importantly, the NWPPC market price forecast is not necessarily intended to project the market price of longer-term fixed purchase arrangement. The model is intended to project spot market wholesale prices in a deregulated environment. Avista is not planning to replace Centralia with spot market purchases.

Do you agree with Mr. Lazar's assertion that ratepayer's have overpaid for Centralia power by $512 million?

A. I do not. Mr. Lazar's analysis as shown on Exhibit 504 compared the total cost of Centralia to short-term market prices. This is not a valid comparison. Centralia is a long-term firm energy resource. During the 1980's and until the later 1990's firm power, such as Centralia, was priced with both an energy and capacity component. The firm power replacement for Centralia during the period in Mr. Lazar's analysis, 1986 through 1998, needs to be calculated with both an energy and capacity value. Including the value of capacity with the short-term energy value Mr. Lazar uses in Exhibit 504 would produce a long-term firm power value that is more comparable with the total cost of Centralia. I calculated that the minimum average capacity value to eliminate Mr. Lazar's claimed $512 million "Ratepayer's Loss" would have had to be $2.45/kW/month over the period 1986 to 1998. During that period 1989 through 1997, Avista made a long-term firm power sale to Pacificorp with capacity rates ranging from $3.50/kW/month to $6.00/kW/month. In 1998, Avista sold firm-energy to Clark PUD with a capacity charge of $2.65/kW/month. Including an average capacity charge of $3.50/kW/month in Mr. Lazar's Exhibit 504 changes the claimed "Ratepayer's Loss" of $512 million to a gain of $219 million. These calculations are shown in Exhibit 316. The value of the Centralia plant as a firm power resource was much greater than just the value of shot-term energy as proposed in Mr. Lazar's Exhibit 504. Including the value of capacity in Mr. Lazar's analysis shows that the cost of the Centralia plant was less than the value of long-term firm power over the period 1986 to 1998.

Q. Do you have any comments on Mr. Lazar's testimony suggesting that a sale price for Centralia of $1.361 billion would be required for ratepayers to breakeven?

A. Yes. Mr. Lazar's sale price does not pass the test of reasonableness. Mr. Lazar's suggested sales price would be 10.8 times book value, as shown in the calculations below. The actual ratio of sales price to book value under the sale to TECWA is 3.4 times book value.

Mr. Lazar's suggested sale price for breakeven	$1,361,300,000
Less: Book value for mine per Exh. 501, Page 7	$107,200,000
Suggested sale price for plant	$1,254,100,000
Avista's ownership percentage	15%
Avista's share of Mr. Lazar's sale price	$188,115,000
Avista's estimated book value at 12/31/99	17,477,000

Ratio of sale price to book value	10.8 times
Sale proceeds from sale to TECWA	$59,298,000
Avista's estimated book value at 12/31/99	17,477,000
Ratio of TECWA sale price to book value	3.4 times

A November 1, 1999 article entitled "Did Power Plant Buyers Pay Too Much?" by Art Holland (Public Utilities Fortnightly, pp. 26-36), contains a table of eighteen recent power plant sales. The table shows a range of sale prices to net book value of 0.17 times to 5.85 times with an average of 2.18 times. This table is shown in Exhibit 317. It is understood that there are many factors that will cause one plant to receive a sale price multiple different that another, such as the age of the plant, the condition of the plant, environmental compliance, availability and quality of fuel, recent operating performance, etc. This data, however, suggests that Mr. Lazar's sale price of 10.8 times book value for the Centralia Plant is outside the bounds of reasonableness.

Q. Would you please summarize your testimony?

A. Yes. The analysis of the value of the Centralia plant depends, along with other factors, on the projection of replacement power costs. Projections of long-term power costs are highly uncertain. Mr. Lazar has used a long-term price forecast that is higher than the price forecast used by Avista or the other sellers. Price forecasts beyond 10 years are truly speculative and dependent on assumptions made in the forecasting process. The recent uptick in near-term prices has resulted in long-term forecasts increasing because of the higher starting point. While all forecasts tend to show prices continuously increasing, history has shown that energy prices can decrease as witnessed by 1998 market prices being lower than 1985 prices.

Mr. Lazar’s analysis showing that the cost of power from Centralia exceeding the market price of power by $512 over the period 1986 through 1998 is flawed because it compares a long-term firm power resource, Centralia, with short-term energy prices. Including value for capacity for the period shows that the value of the power from Centralia exceeded the cost of the plant by $219 million.

Q. Does that conclude your rebuttal testimony?

A. Yes.