BEFORE THE WASHINGTON STATE

UTILITIES & TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,

COMPLAINANT,

V.

AVISTA CORPORATION, d/b/a AVISTA UTILTIES

RESPONDENT.

DOCKETS UE-150204 and UG-150205 (*Consolidated*)

CROSS-ANSWERING TESTIMONY OF DONNA M. RAMAS (EXHIBIT NO. DMR-26T)

ON BEHALF OF

PUBLIC COUNSEL

SEPTEMBER 4, 2015

CROSS-ANSWERING TESTIMONY OF DONNA M. RAMAS
(EXHIBIT NO. DMR-26T)
DOCKETS UE-150204 and UG-105205 (*Consolidated*)

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I. INTRODUCTION

Q: Please state your name, occupation and business address.

A: My name is Donna M. Ramas. I am a Certified Public Accountant licensed in the State of Michigan and Principal at Ramas Regulatory Consulting, L.L.C., with offices at 4654 Driftwood Drive, Commerce Township, Michigan 48382.

Q: Are you the same Donna M. Ramas that filed Direct Testimony in this proceeding on July 27, 2015, on behalf of the Public Counsel Unit of the Washington Attorney General's Office (Public Counsel)?

A: Yes, I am.

Q: What is the purpose of your cross-answering testimony?

A: My cross-answering testimony responds to several fundamental policy issues presented in the Testimonies of witnesses Chris R. McGuire, Christopher S. Hancock, and David C. Gomez on behalf of the Staff of the Washington Utilities and Transportation Commission ("Staff"). My cross-answering testimony also responds to one adjustment recommended in the Testimony of Staff witness Jason L. Ball. Specifically, in this cross-answering testimony, I address the following topics:

- <u>Attrition Approach to Setting Rates</u> – Consistent with my Direct Testimony, I continue to oppose setting rates based on attrition studies for Avista's electric and natural gas operations. I recommend that Staff's attrition analysis and attrition studies, presented by Staff witness Chris R. McGuire, not be used in determining the revenue requirements for Avista's electric and natural gas operations.

- Extension of Net Plant in Service to December 31, 2014 – I disagree with Staff's inclusion of all post-test year capital additions that were placed into service between October 1, 2014, and December 31, 2014. The blanket inclusion of three additional months of plant additions without limiting such additions to projects that would be considered Major plant additions results in a mismatch of the test year used in determining rates.
- Use of End of Period Rate Base for Electric Operations – I disagree with Staff's use of end of period rate base, particularly one that extends three months beyond the end of the test period, for Avista's electric operations.
- Major Plant Additions – Definitions/Qualifications – I explain why several projects Staff has identified as Major plant additions do not meet Staff's definition or qualifications to be considered Major plant additions.
- Major Plant Additions - Specific Projects – I recommend that capital projects that consist of numerous separate additions to plant in service or blanket-type projects, instead of distinct individual projects, be excluded from consideration as a Major plant addition.
- Information Technology and Services Expense – While the adjustment to information technology and service expense proposed by Staff witness Jason L. Ball is substantially lower than the adjustment proposed by Avista, I continue to recommend that the adjustment be rejected in its entirety.

Q: If you do not address specific adjustments recommended by Staff or other intervenors in this cross-answering testimony, does that mean that you agree with the adjustment?

A: No. While Public Counsel may elect to support some adjustments made by other parties in this proceeding, silence in this testimony on specific adjustments should not be interpreted as my agreement that the adjustment is appropriate.

II. ATTRITION APPROACH TO SETTING RATES

Q: Did Staff recommend that an attrition adjustment be made in this case?

A: Yes. Staff witness Chris R. McGuire states: "Staff recommends that the Commission exercise its discretion and provide Avista with attrition allowances for electric and natural gas operations that are incremental to the revenue requirements calculated using Staff's modified historical test year analysis."[1]

Q: What attrition allowance or adjustment for attrition is Staff recommending in this case?

A: In determining the amount of attrition adjustment, Staff takes the difference between the results of the attrition studies prepared by Staff witness Chris R. McGuire and the results of Staff's modified historic test year analysis. This comparison results in a $14.7 million attrition adjustment for Avista's electric operations and a $5.4 million attrition adjustment for the natural gas operations.[2] These are fairly substantial adjustments to the calculated revenue requirements. Under this approach, rates would be set based on the results of Staff's attrition studies.

Q: If revisions are made to Staff's modified historic test year analysis, would this impact the amount of revenue requirement recommended by Staff?

[1] Testimony of Chris R. McGuire, Exhibit No. CRM-1T at 5:17-20.
[2] McGuire, Exhibit No. CRM-1T at 27:13 - 28:14.

A: Apparently not. For example, if the Commission did not agree with some of Staff's adjustments under its modified historic test year analysis, or if the Commission were to adopt adjustments recommended by Public Counsel or other parties in this case, the individual adjustments would essentially be irrelevant if the attrition study approach is adopted. This is because the revenue requirement would be set based on the results of the attrition studies, and the attrition adjustment would change to reflect the difference between the attrition study results and the revenue requirement, as calculated using the modified test year approach. If that difference is larger (or smaller) as a result of the Commission's adoption or rejection of specific adjustments, the attrition adjustment would be larger (or smaller). In other words, the amount of attrition adjustment for Avista's electric and gas operations under Staff's approach is calculated to result in the revenue requirements determined using the attrition studies.

Q: In your Direct Testimony filed on July 27, 2015, you recommended that Avista's attrition studies be rejected and that the revenue requirements be determined based on the well-established modified test year approach. Has Staff's recommendation that rates be determined based on its attrition studies caused you to change your recommendation?

A: No. For the reasons set out in my Direct Testimony, I continue to recommend that an attrition adjustment not be made for the electric or the natural gas operations and that revenue requirements not be established based on an attrition study approach. I continue to believe that a modified test year approach will result in fair and reasonable rates for Avista. While there are some differences between the attrition studies prepared by Staff witness Mr. McGuire and the attrition studies prepared by Avista, the revisions made by Mr. McGuire would not result in rates that are based on a historic test period with known and measurable post-test year adjustments made thereto. The attrition adjustments proposed by Staff are not known and measurable amounts, but rather projections or estimations of what may, or may not, transpire between the end of the test year and the end of 2016.

Q: In your Direct Testimony, you stated that "…the approach taken in determining what escalation factors to apply, as well as what historic years are used in determining the escalation factors, has a large and significant impact on the results of the attrition studies."[3] Since Staff has made several modifications to Avista's attrition studies, is this still a concern?

A: Absolutely. As demonstrated in my Direct Testimony, changing the approach in determining the escalation factors as well as changing the historic years used in determining the escalation rates has a substantial impact on the attrition study results. An attrition adjustment cannot be a known and measurable change when slight changes in time periods or methodologies used to derive the escalation trends have such a significant impact on the results. While Staff's attrition approach incorporates more historical trends than the attrition approach proposed by Avista, it is still essentially an estimate of what will happen in the future based on a combination of historic trends and projected escalations.

Q: Are any of the escalation rates incorporated in Staff's attrition studies based on projections or forecasts as opposed to historic trends?

[3] Direct Testimony of Donna M. Ramas, Exhibit No. DMR-1CT at 21:17-20.

A: Yes. For example, Mr. McGuire indicates that, with one exception, he used Avista's methodology to estimate retail revenues for 2016, which was derived from Avista's 2016 load forecast. He states further that, "The revenue escalation factor was calculated using Avista's expected growth rate of individual billing determinants between September 2014 and December 2016."[4] Thus, the retail revenues in Staff's attrition studies are based on projected billing determinates.

Staff modified the load growth rate in its natural gas revenue analysis for weather-sensitive rate schedules. This was accomplished by averaging the projected natural gas load growth for Schedules 101, 111/112 and 121/122 presented in Avista's 2014 rate case and the current rate case. Accordingly, the projected natural gas revenues for certain rate schedules are based on an average of two separate natural gas load growth projections.[5] The table below, which is a replica of the table presented on page 36 of Mr. McGuire's testimony, demonstrates how much the natural gas load growth projections changed between the 2014 rate case and the present rate case, as well as the projection used in Staff's attrition analysis:

Projected Natural Gas Load Growth

	2014 GRC (annual)	**2015 GRC (annual)**	**Staff Used (annual)**
Schedule 101	0.78%	-0.46%	0.39%
Schedule 111/112	0.83%	0.08%	0.46%
Schedule 121/122	1.88%	1.59%	1.74%

[4] McGuire, Exhibit No. CRM-1T at 35:21 – 36:3.
[5] *Id.* at 35:19-37:5.

For Schedule 101, Staff took the average of load growth projection from the 2014 rate case and zero percent for 2015. For the remaining schedules in the table, Staff used the average of the projections incorporated in Avista's 2014 rate case and the current rate case. Therefore, Staff's approach for the retail revenues in its Attrition Studies is based on various load growth projections as opposed to historical trends.

Q: Are there other examples of escalations incorporated in Staff's Attrition Studies that are not based on historic trends?

A: Yes. As pointed out in my Direct Testimony, Avista used a three percent annual growth rate for operating expenses instead of the rate calculated based on a historic trend.[6] Avista explained that it did not use the historical growth rate as it would not pick up the impacts of significant cost-cutting measures instituted after 2012. Instead, Avista arbitrarily selected to use an annual expense growth rate of three percent. Staff witness Mr. McGuire indicates that Avista did not provide any workpapers supporting the proposed three percent annual expense growth rate and that Staff "…could not determine whether the proposed 3.0 percent growth rate was reasonable or unreasonable."[7] Staff used the average of the actual expense growth rate between 2013 and 2014 and the three percent rate used by Avista that Staff indicated it could not determine as reasonable. This resulted in a 2.42 percent annual growth rate for electric expenses and a 2.17 percent annual growth rate for natural gas operations.[8] Thus, Staff's expense growth rate is

[6] Ramas, Exhibit No. DMR-1CT at16:22 – 17:8.
[7] McGuire, Exhibit No. CRM-1T at 40:8-12.
[8] *Id.* at 40:12-17.

based on an average of one-year of change in expenses and the arbitrary three percent used by Avista in its analysis.

Q: If Staff's attrition studies are adopted, would rates be set based on a historic test year with known and measurable pro forma adjustment made thereto?

A: No. Rather, rates would be set based on estimates or projections of what could happen between 2014 and the end of 2016. The assumption is that a historical trending of the relationship between the various components of the revenue requirement equation will continue. Each of the separate components is then forecasted into a future period. The result is essentially a future test year based on various escalations and projections, not a historic test year with known and measurable pro forma adjustments made thereto.

III. RATE BASE APPROACH

Q: In addition to its attrition studies, Staff also provided revenue requirement calculations using a modified historical test period approach with limited pro forma adjustments. What approach did Staff take in its modified historical test period for determining the amount of plant in service to include in rate base?

A: While the historic test period is the 12 months ended September 30, 2014, Staff made pro forma adjustments to include plant in service based on the actual December 31, 2014, plant balances.[9] Thus, Staff's approach not only extends certain rate base items three-months beyond the end of the historic test period, but it also uses an end of period approach based on the same three-months post-test

[9] Staff's approach also included the associated impact from the plant additions on accumulated depreciation, accumulated deferred income taxes and depreciation expense.

year period. Thus, all projects placed into service by Avista between the end of the historic test period (i.e., September 30, 2014) and December 31, 2014, are included in Staff's adjusted rate base. Staff then increased the actual December 31, 2014, plant in service amounts to include projects placed into service during 2015 that it considered major plant additions, which will be discussed in the next section of this testimony.

Q: Did Staff discuss the matching principle in its testimony?

A: Yes. At page 14 of his testimony, Staff witness Christopher S. Hancock correctly states that, "The Commission has asserted its preference for the average-of-monthly-average (AMA) methodology" and that the AMA methodology "best maintains the matching principle." He explains that, "The average-of-monthly-averages rate base accounting method best maintains the matching principle, because the accompanying revenue items in the test year are also reported as averages throughout the test year."[10]

Q: Given Staff's acknowledgement that the AMA methodology best maintains the matching principle, did Staff explain why it is using an EOP approach in this case?

A: Yes. Staff witness Mr. Hancock explains that the Commission has occasionally used the EOP approach in certain circumstance.[11] Mr. Hancock indicates that using an EOP approach is a tool that has been identified for addressing regulatory lag and attrition, and that Staff witness Mr. McGuire "concludes that attrition may have an impact on the Company's electric if the Commission adopts rates based

[10] Testimony of Christopher S. Hancock, Exhibit No. CSH-1T at 14:9 – 20.
[11] *Id.* at 15:1-19.

on Staff's *pro forma* revenue requirement."[12] Mr. Hancock then explains that, "Exhausting a long-accepted tool, such as EOP, is appropriate prior to entertaining an even more extraordinary tool, such as an attrition allowance."[13] Apparently, Staff is proposing to use an EOP approach extending three additional months beyond the end of the historic test period as a tool that should be used before accepting an attrition allowance. However, since Staff's primary recommendation appears to be that Avista's revenue requirements be set based on its modified attrition study, Staff's adjustment to use an EOP method extending three-months after the test year merely serves to reduce the size of the resulting attrition adjustment.

Q: Do you agree that all plant additions for the three months post-test year should be included in rate base?

A: No. As addressed in my Direct Testimony, the Commission has acknowledged concerns with using the EOP approach with respect to the matching principle, and extending the plant additions three additional months beyond the end of the test period would exacerbate the mismatch. While I agree that it may be appropriate to include certain known and measurable major post-test year plant additions on a project-by-project basis, such that all impacts of those major projects can be considered and matched, I do not agree that haphazardly extending limited portions of the revenue requirement equation beyond the end of the test year is appropriate. Under Staff's proposed approach, one would use a test period for plant in service, accumulated depreciation, and depreciation expense that differs

[12] *Id.* at 16:12-17.
[13] *Id.* at 16:17-18.

from the test period being used for other components of the revenue requirement equation, such as revenues and non-depreciation expenses. Two separate test periods would essentially be meshed together without matching the various components of the revenue requirement equation.

Q: Setting aside the fact that Staff's approach extends the test period for plant in service three additional months, do you agree with Staff's position that the use of the EOP method is needed in this case as a tool to address regulatory lag or attrition?

A: For the reasons presented in my Direct Testimony, I do not agree that an EOP approach is needed for determining the revenue requirement for Avista's electric operations. Additionally, while I did not oppose the use of the EOP approach to determine rate base for the natural gas operations for the reasons presented in my Direct Testimony, I continue to disagree with the extension of the natural gas rate base to a period three months beyond the end of the test year.

IV. MAJOR PRO FORMA PLANT ADDITIONS

Q: How many post-test year projects did Staff recommend be included as major pro forma plant additions in its modified historic test year approach?

A: As mentioned previously, Staff has included all post-test year additions placed into service between October 1, 2014, and December 31, 2014, in its modified historic test year approach. Staff also included certain projects that it considered to be major plant additions that were transferred to plant in service on Avista's books between January 1, 2015, and June 30, 2015. This included a total of ten projects: five projects specific to the electric operations, three projects specific to the natural gas operations and two projects that impacted both the electric and natural gas operations. As addressed in my Direct Testimony, I recommended that: 1) one electric project be included as a post-test year plant addition (i.e., Clark Fork Project); 2) one natural gas project be included as a post-test year plant addition (Aldyl-A Replacement); and 3) Project Compass be included as a post-test year plant addition for both the electric and natural gas operations. Thus, the projects considered by Staff to be major plant additions go far beyond the projects recommended for consideration as major projects in my Direct Testimony.

Q: Did Staff identify what factors it used in determining whether or not a known and measurable post-test year plant addition qualifies as a major plant addition?

A: Yes. Mr. Hancock explains that WAC 480-140-040, Commission general – Budgets, guided Staff's definition of a major rate base addition in this case. Mr. Hancock quoted the following from WAC 480-140-040 at page 12 of his Direct Testimony:

> Major construction projects will be determined for water, gas, and electrical companies, as all projects where the Washington-allocated share of the total project is greater than five-tenths of one percent of the company's latest year-end Washington-allocated net utility plant in service, but does not include any project of less than three million dollars on a total project basis. This determination for companies providing combined industry services will be done on an industry-specific basis.

Based on the above quoted language, Staff arrived at the figure of $6,365,785 as being considered a major project for the electric operations and $1,251,285 as being considered major for the gas operations. Staff treated the pro forma plant adjustments in excess of these amounts as "major." While the portion of

WAC 480-140-040 quoted in Mr. Hancock's testimony specifically indicates that major construction projects do not include "…any project of less than three million dollars on a total project basis," the threshold identified by Staff for gas operations is considerably lower than the $3 million amount. At page 13 of his testimony, Mr. Hancock also indicates that in order to be considered a major rate base addition, "a 'project' must be a discrete unit of utility plant-in-service."

Q: Do any of the pro forma major plant additions that Staff recommended for inclusion in rate base seem to fall outside of its definition of a major plant addition?

A: Yes. Staff has included amounts for many projects that fall below the amounts it identified as being considered a major project. Many of the projects included by Staff are ongoing projects for which only a portion of the total project costs had been completed and placed into service on Avista's books by June 30, 2015. Thus, Staff considered the total projected or forecasted costs for a project, rather than the amounts that have already been completed and placed into service, in determining whether or not a project should be incorporated as a post-test year plant addition. For example, for electric operations, Staff has included $3.09 million for the Nine Mile Rehab project, $2.35 million for the Little Falls Plant Upgrade project and $1.6 million for the Distribution Grid Modernization, which all fall short of the Staff's threshold of $6.4 million. In fact, for the electric operations, only one project – Project Compass – had amounts placed into service as of June 30, 2015, that exceeded Staff's identified $6.4 million threshold.

Additionally, several of the projects included by Staff consist of projects that would be considered more typical blanket-type work orders, as opposed to individual projects. As an example, Staff has included costs associated with the Technology Refresh to Sustain Business Process, which Avista witness James M. Kensok has described as a program comprising over one-hundred separate projects. Similarly, the Gas Non-Revenue program, Distribution Grid Modernization, and Distribution Wood Pole Management Program consist of numerous individual assets and units that are placed into service over an extended timeframe, as opposed to discreet units of utility plant-in-service. With the exception of the Aldyl-A Pipe Replacement capital costs addressed in my Direct Testimony,[14] I do not agree that blanket-type projects should be considered to be major pro forma plant additions to be added to the historic test period. An exception was made in my direct testimony for Aldyl-A Pipe replacement capital costs as a measure to address the consistent under-earnings for Avista's natural gas operations.

Q: Could you explain why you believe that blanket-type projects should not be considered major pro forma plant additions and, thus, not added to the historic test period?

A: While it may be appropriate to consider inclusion of actual known and measurable major pro forma plant additions to a historic test period in certain circumstances, inclusion should be limited to larger capital additions that can be evaluated to determine all impacts of the major capital projects under consideration on the other components of the revenue requirement equation.

Blanket-type work orders and project expenditure requests may cover numerous separate individual plant items of smaller dollar value as compared to a

[14] Ramas, Exhibit No. DMR-1CT at 60:13 – 61:3.

major plant addition. For example, as mentioned above, the Technology Refresh to Sustain Business Process is comprised of over one hundred separate projects across numerous technology types and would include assets that are replaced regularly, such as personal computers and communications equipment. At page 15 of this testimony, Avista witness James M. Kensok states: "A sample of the 2015 project scope is as follows: Enterprise Voice Portal (IVR), Office Communicatory & Voicemail, Communication Management System, Metropolitan Area Network Transport, Avista Intranet, Financial Forecast Model, Claims System, Java 1.7x, Nucleus, Oracle Database 12c, Internet Explorer 11, Citrix Platform, HP CAE/Radia, MS Office 2013, Rugged Computers, and TWACS telemetry."[15] By opening the door to include blanket-type projects that consist of a multitude of smaller capital assets, such as distribution pole replacements, printer and computer replacements, etc., it would allow for utilities to attempt to bundle numerous smaller capital projects into a single expense requisition request in order to meet a "major" plant threshold, and would make it increasingly difficult to ensure that all impacts of such smaller plant additions are matched within the adjusted test year.

Additionally, many of the blanket-type projects, such as the replacement of wood distribution poles, maintenance of pipeline segments, and individual personal computers, are replacing existing assets. While the plant in service, accumulated depreciation and depreciation expense are adjusted for these individually minor plant additions, there are numerous assets replaced under these projects for which the depreciation expense is not removed. This results in an

[15] Direct Testimony of James M. Kensok, Exhibit No. JMK-1T at 15:23-28.

adjusted test year that includes costs associated with the new pro forma plant additions, as well as the costs of plant (accounted for in the historic test year) that is being replaced.

The consideration of special pro forma adjustments to consider major plant additions should be limited to individual sizable projects and not expanded to include blanket projects that consist of up to hundreds of separate individual plant additions. Limiting the consideration to individual projects that truly are more sizable or major in nature would result in greater ability to ensure that all impacts are being matched within the adjusted test year.

Q: Based on Staff's testimony and adjustments for major pro forma plant additions, are you revising your recommended adjustments for major pro forma plant additions at this time?

A: No. At this time, I continue to recommend that only the following projects be considered as major pro forma plant additions, consistent with the recommendations contained in my Direct Testimony: 1) capital costs closed to plant in service associated with the Clark Fork Protection, Mitigation and Enhancement ("PM&E") measures under the Clark Fork Settlement Agreement (electric operations); 2) Project Compass plant additions closed to plant in service (electric and natural gas operations); and 3) Aldyl-A Pipe Replacement capital additions (natural gas operations).

V. INFORMATION TECHNOLOGY AND SERVICES EXPENSE

Q: In your Direct Testimony, you recommended that Avista's Information Services/Information Technology ("IS/IT") expense adjustment, which increased the historic test year expenses by $3.15M on a total Company basis,

be rejected in its entirety. Did Staff address Avista's IS/IT expense adjustment?

A: Yes. While rejecting most of Avista's proposed pro forma IS/IT expense adjustment, Staff did allow for much smaller increases to include expenses for which Avista provided signed agreements or contracts.[16]

Q: Do you agree that the smaller IS/IT expense adjustment recommended by Staff based on actual signed agreements or contracts should be adopted by the Commission?

A: No, I do not. As indicated in my Direct Testimony, there are certain cost reductions that would result from the implementation of Project Compass. At page 7 of his Direct Testimony, Avista witness James M. Kensok indicates that there is a corresponding offset to the Project Compass support costs for "the annual expense reduction in contract services and mainframe computer costs associated with the retirement of Avista's Legacy Customer Service and Work Management System." Avista's workpapers identify $2,357,670 of cost reductions associated with Project Compass, $988,800 of which is associated with the reduction in mainframe costs. The reduction of mainframe costs are known and measurable cost reductions, as these costs will discontinue now that Project Compass has been placed into service. These known and measurable cost reductions exceed the amounts being added by Staff for the signed agreements or contracts and have not been factored into Staff's adjustment. Thus, I continue to recommend that Avista's pro forma IS/IT expense adjustment be rejected in its entirety.

[16] Testimony of Jason L. Ball, Exhibit No. JLB-1T at 25:1-19.

Q: Does this conclude your cross-answering testimony?

A: Yes, it does.