

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND)	
TRANSPORTATION COMMISSION,)	
)	
Complainant,)	DOCKETS UE-160228 and
)	UG-160229 (<i>Consolidated</i>)
)	
v.)	
)	
AVISTA CORPORATION, DBA)	
AVISTA UTILITIES,)	
)	
Respondent.)	
_____)	

**CROSS-ANSWERING TESTIMONY OF ROBERT R. STEPHENS
ON BEHALF OF
THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES**

September 19, 2016

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 **A.** Robert R. Stephens. My business address is 16690 Swingley Ridge Road, Suite 140,
3 Chesterfield, MO 63017.

4 **Q. WHAT IS YOUR OCCUPATION?**

5 **A.** I am a consultant in the field of public utility regulation and a Principal of Brubaker &
6 Associates, Inc., energy, economic and regulatory consultants.

7 **Q. ARE YOU THE SAME ROBERT R. STEPHENS WHO PREVIOUSLY FILED**
8 **TESTIMONY IN THIS PROCEEDING?**

9 **A.** Yes. On August 17, 2016, I filed Response Testimony on behalf of the Industrial
10 Customers of Northwest Utilities (“ICNU”). In that Response Testimony, I addressed
11 issues related to cost of service, revenue allocation (or “rate spread”), and rate design.

12 **Q. HAVE YOU REVIEWED THE TESTIMONIES OF STAFF AND INTERVENOR**
13 **WITNESSES AS THEY RELATE TO THE ISSUES THAT YOU ADDRESSED**
14 **IN YOUR RESPONSE TESTIMONY?**

15 **A.** Yes, I have.

16 **Q. DOES THE RESPONSE TESTIMONY OF STAFF OR INTERVENOR**
17 **WITNESSES CAUSE YOU TO CHANGE ANY OF THE POSITIONS THAT**
18 **YOU TOOK IN YOUR RESPONSE TESTIMONY?**

19 **A.** No, it does not.

20 **Q. WHAT IS THE PURPOSE OF YOUR CROSS-ANSWERING TESTIMONY?**

21 **A.** I will address the testimony of Washington Utilities and Transportation Commission
22 (“WUTC”) Staff witness Jason L. Ball as relates to cost of service and rate spread.

23 The fact that I do not address any particular issue should not be interpreted as
24 tacit approval of any position taken by Avista Corporation (“Avista” or the “Company”)
25 or any other party.

1 **Q. PLEASE SUMMARIZE YOUR CROSS-ANSWERING TESTIMONY.**

2 **A.** My Cross-Answering Testimony can be summarized as follows:

3 1. I agree with Staff's recommendation that the Commission institute a generic
4 proceeding to review cost of service methodologies for all investor-owned utilities
5 in Washington.

6 2. I conditionally agree with Staff's recommendation that the Commission defer all
7 major decisions regarding any specific cost of service methodology in the present
8 case, if the Commission chooses to initiate the generic proceeding recommended by
9 Staff.

10 3. I disagree with Staff's recommendation to maintain the status quo with respect to
11 rate spread, i.e., to spread the proposed rate increase across all customer classes on
12 an equal percentage basis. Such an approach would needlessly continue the large
13 cost disparity between Schedule 1 revenues and cost of service. Schedule 1 has been
14 subsidized for a number of years and, as I explained in my Response Testimony,
15 movement toward cost of service should be made. This is true even if the precise
16 cost of service result from a generic cost of service proceeding is not yet knowable,
17 because under any reasonably anticipated outcome, Schedule 1 is likely to be shown
18 to be well below cost of service.

19 **Q. AT PAGE 4, MR. BALL STATES STAFF'S POSITION REGARDING THE**
20 **INITIATION OF GENERIC COST OF SERVICE PROCEEDINGS, ONE FOR**
21 **ELECTRIC AND ONE FOR GAS. HE GOES ON TO OPINE THAT SUCH A**
22 **PROCEEDING WOULD**

23 **"OFFER THE COMMISSION THE OPPORTUNITY TO**
24 **ARTICULATE A COHERENT AND CONSISTENT COSS**
25 **APPROACH FOR ALL IOUS IN WASHINGTON THROUGH A**
26 **SINGLE POLICY STATEMENT OR ORDER."**

27 **HOW DO YOU RESPOND?**

28 **A.** I generally agree. Presently, the Commission has approved significantly different cost
29 of service approaches for the different Washington utilities. Further, due to a series of
30 case settlements, cost of service has not been critically litigated before the Commission
31 in every case. Thus, both the Commission and the utilities could be aided by a
32 proceeding that establishes guidance to the utilities on determining the cost of serving
33 each customer class.

1 This is not to say that the cost of service approach must be identical for each
2 Washington utility. Differential circumstances, data availability, etc., may warrant the
3 use of somewhat different approaches. However, the generic proceeding should afford
4 the Commission the opportunity to give overarching guidance to the study methods.

5 **Q. WHAT IS TYPICALLY THE LARGEST COST ITEM IN AN ELECTRIC COST**
6 **OF SERVICE STUDY THAT THE COMMISSION COULD PROVIDE**
7 **OVERARCHING GUIDANCE ON?**

8 **A.** Classification and allocation of production fixed costs. Presently, different utilities use
9 different classification methods to establish how much production plant investment
10 should be allocated on energy or demand bases. Greater uniformity in the classification
11 approach, and consistency with industry norms, would be a desirable potential outcome
12 of the generic cost of service proceeding.

13 Allocation methods for fixed production costs are also important factors in
14 determining the cost of service. For example, what measure of classes' demands should
15 be used to develop the demand allocators? Similarly, what is the best approach for
16 developing allocators of energy costs? These questions could be addressed in the
17 generic proceeding.

18 **Q. AT PAGE 5, MR. BALL EXPLAINS WHY STAFF DID NOT PRESENT A COST**
19 **OF SERVICE METHODOLOGY IN THE CURRENT CASE, INSTEAD**
20 **FAVORING ESTABLISHMENT OF THE GENERIC PROCEEDING. HOW**
21 **DO YOU RESPOND?**

22 **A.** Absent a cost of service result by Staff, in the event the Commission declines to initiate
23 a generic cost of service proceeding, or if such proceeding is delayed for a significant
24 amount of time, the Commission will have to rely on Avista's and ICNU's studies to
25 gauge the level of subsidies present in current rates. It will not have the benefit of Staff's
26 input on specific classification or allocation recommendations. Similarly, the

1 Commission will not have the benefit of Staff's calculated parity ratios, which Mr. Ball
2 claims is the principal output of the COSS.^{1/} As Mr. Ball explains at page 7, a rate
3 schedule with a parity ratio well below 1.00 means that the schedule is essentially being
4 subsidized by other schedules.^{2/} For example, the rate schedule the furthest below unity
5 (1.00) is Schedule 1, with a parity ratio of 0.55 under Avista's measure of class cost and
6 0.46 under my measure of class cost.^{3/} Parity ratios in this range indicate that Schedule
7 1 is providing only about half the return that Avista receives on average from all the
8 classes. Thus, it is heavily subsidized and has been for some time.

9 **Q. WHY DO YOU BELIEVE THAT SCHEDULE 1 HAS BEEN HEAVILY**
10 **SUBSIDIZED FOR SOME TIME PERIOD?**

11 **A.** I have reviewed the parity ratios of the Schedule 1 class going back to 2009, according
12 to the Company's prior cost of service determinations.^{4/} These are shown in Table 1,
13 below.

^{1/} Exh. No. JLB-1T at 6.

^{2/} Id. at 7.

^{3/} I show this in Table 4 of my Response Testimony.

^{4/} WUTC v. Avista, Dockets UE-160228 *et al.*, TLK-1T at 13 (Feb. 19, 2016); WUTC v. Avista,
Dockets UE-150204 *et al.*, TLK-1T at 14 (Feb. 9, 2015); WUTC v. Avista, Dockets UE-
140188 *et al.*, TLK-1T at 16 (Feb. 5, 2014); WUTC v. Avista, Dockets UE-120436 *et al.*,
TLK-1T at 18 (Apr. 2, 2012); WUTC v. Avista, Dockets UE-110876 *et al.*, TLK-1T at 16
(May 16, 2011); WUTC v. Avista, Dockets UE-100467 *et al.*, TLK-1T at 15 (Mar. 23, 2010);
WUTC v. Avista, Dockets UE-090134 *et al.*, TLK-1T at 13 (Jan. 23, 2009).

TABLE 1

**History of Schedule 1 Parity Ratios
Under Avista Cost of Service
Determinations**

<u>Rate Case</u> <u>Year</u>	<u>Schedule 1 Parity Ratio</u>
2016	0.55
2015	0.58
2014	0.65
2012	0.58
2011	0.63
2010	0.55
2009	0.66

1 Thus, as shown in Table 1, Schedule 1 has enjoyed a large and sustained subsidy for
2 several years.^{5/}

3 **Q. AT PAGES 8 THROUGH 9 OF HIS TESTIMONY, MR. BALL IDENTIFIES**
4 **SEVERAL TOPICS THAT POTENTIALLY WOULD BE EXPLORED IN THE**
5 **CONTEXT OF A GENERIC PROCEEDING. DO YOU AGREE WITH MR.**
6 **BALL’S LIST?**

7 **A.** Although I would not necessarily have worded each of the points the way that Mr. Ball
8 does, I think he has captured the major points of impact in a cost of service study. I
9 would also note that some of these points are the same as the ones I addressed in my
10 Response Testimony. For example, I addressed the classification and allocation of
11 production costs (his first bullet), the treatment of transmission-related costs (his third

^{5/} Although I acknowledge that the Commission has not necessarily approved Avista’s measure of cost results in all of the years shown in Table 1, Avista is the only party to have computed these numbers in each of the years shown. Furthermore, given that Avista’s production cost classification and allocation methods are highly favorable to low load factor classes, the true cost of serving Schedule 1 would likely result in even lower parity ratios than calculated by Avista.

1 bullet), and the need for potential changes in measuring cost of service due to items such
2 as smart grid (his fifth bullet).

3 **Q. DOES MR. BALL LEVY SPECIFIC CRITICISMS AT AVISTA’S COST OF**
4 **SERVICE RESULT?**

5 **A.** No. In fact, Mr. Ball believes that Avista’s cost of service study “should be considered
6 *directionally* accurate for the purpose of setting rates.”^{6/} As indicated in Table 4 of my
7 Response Testimony, Avista’s and my recommended ECOS studies are directionally
8 identical in the results. That is to say, my results and Avista’s results show the parity
9 ratios of each rate schedule to be above or below unity, on a consistent basis. Our
10 differences are in how far above or below unity the results are for any particular rate
11 schedule.

12 **Q. IS IT POSSIBLE THAT THE COMMISSION’S DETERMINATION IN A**
13 **GENERIC COST OF SERVICE PROCEEDING ULTIMATELY WOULD**
14 **SHOW THAT SCHEDULE 1 IS NOT BEING SUBSIDIZED, I.E., THAT ITS**
15 **PARITY RATIO IS ACTUALLY GREATER THAN 1.00?**

16 **A.** This is an unrealistic outcome. The reason is because the classification and allocation
17 methods used by Avista on the major cost drivers, namely production fixed costs and
18 transmission costs, are already skewed heavily in favor of low load factor classes, such
19 as Schedule 1. I explain this in depth in my Response Testimony. In my experience in
20 reviewing cost of service methodologies in many jurisdictions in the United States, I
21 can think of few, if any, approaches that would be more favorable to low load factor
22 classes such as Schedule 1 than Avista’s. If such methods exist, they would be outside
23 of industry norms and would be highly questionable. Thus, it is fair to say that under
24 any reasonably anticipated outcome of the generic cost of service proceeding, should

^{6/} Exh. No. JLB-1T at 9 (emphasis in original).

1 the Commission initiate one, the likelihood of Schedule 1 being found to have a parity
2 ratio above 1.00 is virtually nil. In fact, even in the extreme, but unrealistic, “best case”
3 scenario for Schedule 1, where all production and transmission costs are classified as
4 100% energy-related (rather than the 62% used in the Avista study), the parity ratio for
5 Schedule 1 would only be .68, still well below 1.00.

6 **Q. HAVE YOU REVIEWED STAFF’S PROPOSED RATE SPREAD FOR**
7 **ELECTRIC SERVICE?**

8 **A.** Yes, I have. Mr. Ball addresses this at pages 14 through 16 of his testimony.

9 **Q. WHAT IS STAFF’S POSITION ON RATE SPREAD?**

10 **A.** As explained at page 16 of his testimony, Mr. Ball indicates that the Company’s
11 proposed rate spread is consistent with the Company’s cost of service study, but that the
12 precision of the Company’s cost of service study is concerning. Mr. Ball goes on to
13 state that: “Without a completely accurate COSS, however, it is impossible to tell if
14 cross-class subsidization exists or, accordingly, whether a specific customer class
15 should be assigned a higher- or lower-than-average increase.”^{7/} Accordingly, “Staff
16 proposes spreading any increases to rates amongst the customer classes uniformly.”^{8/}

17 **Q. DO YOU AGREE THAT THE PRECISION OF THE COMPANY’S COST OF**
18 **SERVICE STUDIES IS CONCERNING?**

19 **A.** Yes, but only to a limited degree. My concerns are that the Company’s study does not
20 show the full extent of the inequity present in current rates. Said another way, I believe
21 that proper cost of service study techniques would reveal that Schedule 1 is being even
22 more heavily subsidized than Avista’s cost of service study suggests.

^{7/} Id. at 16.

^{8/} Id. at 14.

1 **Q. DO YOU AGREE THAT “WITHOUT A COMPLETELY ACCURATE COSS,**
2 **IT IS IMPOSSIBLE TO TELL IF CROSS-CLASS SUBSIDIZATION EXISTS”?**

3 **A.** No. If there is a clear indication of cross-class subsidization in reasonably accurate cost
4 of service studies, such as those present in this case, it is most reasonable to conclude
5 that a significant cross-class subsidy exists. Again, for the Schedule 1 class, refinement
6 to the cost of service study may determine that the class parity ratio is something
7 different from 0.55 or 0.46, but it is unrealistic to think that a refinement would cause
8 the ratio to be found anywhere near parity, never mind to be found greater than one.
9 This is especially true when the likely refinements, if any, would tend to lower, rather
10 than increase, the parity ratio from Avista’s calculated 0.55, as previously discussed.
11 Thus, the cost of service information in this record makes it quite clear that very
12 significant cross-class subsidization continues to exist, at least as relates to Schedule 1.

13 Further, I must take some issue with Mr. Ball’s quest for a “completely accurate
14 COSS.” While the “holy grail” of a perfect cost of service study is certainly desirable,
15 it is unlikely to be achieved. And, if it was achieved, we would have no way to know
16 for sure that it has been. Rather, rate setting routinely and properly relies on reasonable
17 estimations of class cost of service, based on sound and supportable measurement
18 techniques.

19 **Q. AT PAGE 14, MR. BALL CLAIMS THAT INCREASING RATES AMONG THE**
20 **CUSTOMER CLASSES UNIFORMLY PROVIDES AN “APPEARANCE OF**
21 **FAIRNESS.” HOW DO YOU RESPOND?**

22 **A.** As I indicated in my Response Testimony, Schedule 1 would need a 25% to 30% rate
23 increase to provide the average return. It does not appear fair for this class to receive
24 the approved system average increase, which likely will be something below the 7.8%

1 increase requested by Avista. Rather than exhibiting fairness, an across-the-board
2 increase would only prolong unnecessarily the existing unfairness in current rates.

3 All in all, the rate spread proposed by Avista in its direct testimony is reasonable,
4 at the Company's full requested increase. It is based on Avista's cost of service results
5 and employs a level of moderation, as relates to rate Schedule 1 particularly, and allows
6 for some movement toward cost of service. I recommend it be adopted, with the caveats
7 contained in my Response Testimony.^{2/}

8 **Q. DOES THIS CONCLUDE YOUR CROSS-ANSWERING TESTIMONY?**

9 **A.** Yes, it does.

^{2/} Exh. No. RRS-1TC at 36-38.