Exh. EMA-10T

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-170485

DOCKET NO. UG-170486

REBUTTAL TESTIMONY OF

ELIZABETH M. ANDREWS

REPRESENTING AVISTA CORPORATION

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Exh. EMA-13 Electric Growth Factor Calculation (Used for Rate Years 2 & 3)	(pgs 1 - 4)
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1 **I. INTRODUCTION**

2 **Q. Please state your name, business address, and present position with**
3 **Avista Corporation.**

4 A. My name is Elizabeth M. Andrews. I am employed by Avista Corporation as
5 Senior Manager of Revenue Requirements in the State and Federal Regulation Department.
6 My business address is 1411 East Mission, Spokane, Washington.

7 **Q. Have you previously provided direct testimony in this Case?**

8 A. Yes. My testimony covered the need for rate relief requested in Avista's
9 original filing, and summarized the Company's proposed Three-Year Rate Plan ("Rate
10 Plan") effective May 1, 2018 through April 30, 2021, based on the Company's electric and
11 natural gas 2017 End-of-Period (EOP) Rate Base revenue requirement studies. I also
12 explained three additional studies sponsored by me, the purpose of which were to support
13 our need for rate relief. Lastly, I provided the calculation of the Company's electric and
14 natural gas revenue growth factors used to determine years 2 and 3 revenue increases,
15 referred to by Avista as the electric and natural gas "K-Factor".

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

17 A. My testimony is provided to support the Company's electric and natural gas
18 revenue requirement positions on rebuttal, and to respond to testimonies of Staff and other
19 parties in this proceeding.[1] My rebuttal testimony explains that the Company's request for
20 rate relief for both electric and natural gas have been adjusted <u>downward</u> to reflect updated

[1] I will refer to each of the non-Company parties in these Dockets as follows: the Staff of the Washington Utilities and Transportation Commission (Staff), the Public Counsel Unit of the Washington Office of Attorney General (Public Counsel), the Industrial Customers of Northwest Utilities (ICNU), the Northwest Industrial Gas Users (NWIGU), and The Energy Project.

1 information, certain adjustments as proposed by Staff or other intervening parties, as well as
2 attempting to find "common ground" on revenue requirement with Staff.

3 Next, I discuss the drivers of the Company's need for rate relief to address capital
4 additions, and how the Company has revised its position on the level of capital to include on
5 rebuttal to reflect concerns by the parties. It also speaks to the severe impact on the
6 Company from regulatory lag, if rate year levels are not properly set. This testimony stresses
7 the importance of setting year one (effective May 1, 2018) revenue requirements in the Rate
8 Plan at an appropriate level, as the Company would not have an opportunity to file a new
9 general rate case for the two years following Rate Year 1. Moreover, the revenue growth
10 factor (K-Factor) used for Year 2 (2019) and Year 3 (2020) build on the base established for
11 Year 1 (2018). Accordingly, any shortfall in revenue requirement in year 1 will be
12 compounded in years 2 and 3.

13 I will then explain the Company's revised revenue growth factors (K-Factor) used
14 during the Three-Year Rate Plan to determine Rate Year 2 and 3 revenue increases, which
15 reflects agreement, in part, with the revenue growth factors proposed by Staff.

16 Next, I will provide an explanation of the adjustments included in the electric and
17 natural gas rebuttal revenue requirements per the Company's revised study results, after
18 reflecting corrections and updates that have been identified through the process of this case,
19 as well as discuss the remaining contested adjustments.

20 Lastly, I will provide Avista's response to ICNU and NWIGU witness Mr. Mullins,
21 who makes recommendations regarding his attrition study analyses. My testimony will
22 explain that Mr. Mullins' recommendations do not lead to reasonable results.

Q. Would you please summarize your rebuttal testimony?

A. Yes. Below is a summary of the principal topics discussed in my rebuttal testimony:

- On rebuttal, the Company is requesting electric rate relief over its Three-Year Rate Plan of $54.4 million effective May 1, 2018, $13.5 million effective May 1, 2019, and $13.9 million effective May 1, 2020. Rate Years 2 and 3 revenue increases are based on a revenue growth factor of 3.14% annually.

- On rebuttal, the Company is requesting natural gas rate relief over its Three-Year Rate Plan of $6.6 million effective May 1, 2018, $3.7 million effective May 1, 2019, and $3.8 million effective May 1, 2020. Rate Years 2 and 3 revenue increases are based on a revenue growth factor of 4.14% annually.

- Staff and Avista reach similar conclusions that: 1) additional rate relief is necessary beyond the traditional modified historical approach and 2) it is appropriate to approve a Three-Year Rate Plan based on the use of revenue growth escalators to determine the electric and natural gas revenue increases for Rate Years 2 and 3.

- The main differences between Avista and Staff's proposed electric Rate Year 1 revenue requirement (beyond Cost of Capital of $13.5 million), relate to two issues representing $29.2 million of revenue requirement in Rate Year 1: (1) whether to update power supply net expenses ($16.6 Million); and (2) what level of rate base, including what subset of 2017 capital additions, should be included beyond the end of the 2016 historical test period ($12.6 million).[2] / [3]

- The main difference between Avista and Staff's proposed natural gas Rate Year 1 revenue requirement (beyond Cost of Capital of $2.8 million), relates to what level of rate base, including what subset of 2017 capital additions should be included beyond the end of the 2016 historical test period ($2.5 million). [4] / [5]

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[2] These are also the main differences between Avista and the other intervening parties, i.e., Public Counsel and ICNU.

[3] The remaining $1.7 million difference between Staff and Avista relates to the inclusion by Avista of the Montana Senate Bill #363 Hydro Facilities Fee imposed on the Company in July of 2017 to control aquatic invasive species ($1.0 million annually), and a pro forma property tax calculation error made by Staff when including its updated pro forma property tax adjustment ($694,000).

[4] These are also the main differences between Avista and the other intervening parties, i.e., Public Counsel and NWIGU.

[5] The remaining $214,000 difference between Staff and Avista relates to Staff's calculation of working capital, lowering rate base by $2.2 million.

- Staff's proposed revenue requirements for Rate Year 1 of $10.0 million for electric and $1.1 million for natural gas, as well as other intervening parties' lower recommendations, are far from what is needed and supported by the Company.

- Staff's proposed revenue requirement for electric and natural gas would result in earned equity returns (ROEs) of 8.1% and 8.0%, respectively. For Public Counsel and ICNU/NWIGU, their proposed electric revenue requirements would result in ROE's of 7.8% and 7.2%, respectively, with natural gas results at 8.1% and 7.5%, respectively. These results reflect a reduction of between 140 to 230 basis points below that currently authorized (9.5%), and would not provide the Company with a reasonable opportunity to earn its authorized rate of return.

- Staff's recommended level of rate base for Year 1 would result in a combined electric and natural gas rate base regulatory lag of over $100 million **annually** over Washington's Three-Year Rate Plan, and an **annual** combined revenue loss of between $21 million and $25 million. This goes well beyond merely providing an incentive to better manage costs; it cuts into the very marrow of cost recovery for prudent plant additions. In doing so, it precludes the Company from any reasonable opportunity to earn its authorized rate of return.

- Avista, for its part on rebuttal, has already agreed to essentially incur a combined electric and natural gas rate base regulatory lag of $35 million to $50 million annually over the Rate Plan, and a revenue requirement loss of approximately $7 to $10 million annually. These represent substantial concessions.

- Representing ICNU and NWIGU, Mr. Mullins for Rate Year 1 proposes an electric increase of $197,000 and a natural gas decrease of $530,000.[6] Mr. Mullins opposes a Three-Year Rate Plan; however he suggests if this Commission were to approve a Three-Year Rate Plan, they should use the results of his electric and natural gas Attrition Studies. As discussed below, Mr. Mullins merely dusted off his 2016 prior Avista general rate case (GRC) attrition studies, extending them an additional year. Consistent with my testimony in Docket UE-160228 and UG-160229, these studies used inconsistent trending periods and understated growth factors, significantly understating the revenue requirement need and producing results that are not reasonable or appropriate.

[6] These reduced revenue requirements are mainly the result of a reduced cost of capital, exclusion of any increase in base power supply costs, and use of an arbitrary threshold to include only 1 electric and 1 natural gas capital project Mr. Mullins describes as major additions. Company witnesses Mr. Thies and Mr. McKenzie discuss the issues surrounding cost of capital, Mr. Kalich discusses the appropriate power supply net costs to include in this case, and Ms. Schuh discusses Mr. Mullins' lack of proper quantification of the appropriate capital projects to include in this case.

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

2 A. Yes. I am sponsoring Exh. EMA-11 through Exh. EMA-16, which were
3 prepared by me. Exh. EMA-11 (Electric) and Exh. EMA-12 (Natural Gas) present the
4 results of the Company's Rebuttal Revenue Requirement Studies for the Rate Plan effective
5 May 1, 2018 through April 30, 2021. Exh. EMA-13 (Electric) and Exh. EMA-14 (Natural
6 Gas) present the Growth Factor Calculations used to determine the revenue increases for
7 Rate Years 2 and 3. These two exhibits also provide a comparison of Avista's and Staff's
8 proposed electric and natural gas growth factors. Exh. EMA-15, page 1, provides the listing
9 of Uncontested Adjustments, while page 2 provides the listing of Contested Adjustments.
10 Pages 3 (electric) and 4 (natural gas), provides a reconciliation of revenue requirement
11 positions of the parties, including Avista on rebuttal, compared to the Company's direct filed
12 case. Lastly, Exh. EMA-16, provides additional electric and natural gas support for certain
13 adjustments included in the Company's revenue requirement models on rebuttal.

14

15 # SECTION 1 – RATE PLAN RELIEF REQUESTED

16

17 ## II. SUMMARY OF REBUTTAL ELECTRIC AND NATURAL GAS
18 ## REVENUE REQUIREMENT

19

20 ### A. Summary of Revenue Requirement – As-Filed versus Rebuttal

21 **Q. Have you prepared a summary table that shows the Company's revenue**
22 **requirement need for its electric and natural gas services proposed on rebuttal,**
23 **compared to the Company's originally filed case?**

24 A. Yes. In Avista's rebuttal filing, it has updated its electric and natural gas
25 revenue requirement calculations based on current information, and in response to

1 testimonies of the parties. For this update, Avista started with its filed revenue requirement
2 models and incorporated adjustments for known corrections and updates during the
3 pendency of this case, other adjustments agreed to by the Company, as well as included its
4 revised position on the appropriate level of certain 2017 capital additions to include. The
5 summary of those adjustments results in the level of revenue requirement proposed on
6 rebuttal as shown in Table No. 1 below.[7]

7 **Table No. 1**

Summary of Revenue Requirement - As-Filed versus Rebuttal (000s)						
	Electric			Natural Gas		
	May 1, 2018	May 1, 2019 (1)	May 1, 2020 (1)	May 1, 2018	May 1, 2019 (1)	May 1, 2020 (1)
As-Filed Revenue Requirement	$ 61,356	$ 13,983	$ 14,432	$ 8,269	$ 4,220	$ 4,417
Updates/Agreed-To Adjustments	$ (1,381)			$ (282)		
Reduction in Capital Projects (2)	$ (5,588)			$ (1,357)		
Rebuttal Revenue Requirement	**$ 54,387**	**$ 13,459**	**$ 13,882**	**$ 6,630**	**$ 3,690**	**$ 3,842**
% Increase Base	11.05%	2.46%	2.48%	7.47%	3.87%	3.88%
% Increase Billed	10.63%	2.38%	2.39%	4.36%	2.32%	2.37%
(1) Rate Years 2 and 3 based on Revenue Growth Factor (K-Factor) on prior year proposed revenues.						
(2) "Reduction in Capital Projects" result of Company revising its approach to reflect a "functionalized threshold" method (similar to Staff witness Wright proposed approach in Puget Sound Energy Docket Nos. UE-170033/UG-170034.)						

14 Details regarding the "Updates/Agreed-To Adjustments" and "Reduction in Capital
15 Projects" amounts in Table No. 1 above are discussed further in Section V.

16 **Q. How does the Company's revenue requirement need proposed on direct**
17 **and rebuttal compare to that proposed by Staff and the other intervening parties?**

18 A. Included below in Table No. 2 is a summary of the revenue requirement
19 positons by Staff and other intervening parties, Public Counsel, ICNU and NWIGU. As
20 noted in the table, Public Counsel, ICNU and NWIGU oppose a Rate Plan supported by

[7] The adjusted rates of return (ROR) for Rate Year 1 (May 1, 2018 – April 30, 2019) determined in Exh. EMA-11 and Exh. EMA-12, page 1 on rebuttal is 5.61% for electric and 6.47% for natural gas.

Avista and Staff.

Table No. 2

Summary of Proposed Revenue Requirement Positions (000s)						
	Electric			Natural Gas		
	May 1, 2018	May 1, 2019 [1]	May 1, 2020 [1]	May 1, 2018	May 1, 2019 [1]	May 1, 2020 [1]
Avista As-filed	$ 61,356	$ 13,983	$ 14,432	$ 8,269	$ 4,220	$ 4,417
Avista Rebuttal	$ 54,387	$ 13,459	$ 13,882	$ 6,630	$ 3,690	$ 3,842
Staff [2]	$ 10,034	$ 9,520	$ 9,740	$ 1,107	$ 2,698	$ 2,784
Public Counsel	$ 7,486	[3]		$ (530)	[3]	
ICNU	$ 197	[3]		n/a	[3]	
NWIGU	n/a	[3]		$ 1,592	[3]	

[1] Rate Years 2 and 3 based on Revenue Growth Factor on prior year proposed revenues.

[2] Main difference with Staff is cost of capital, removal of power suppy update and level of capital additions.

[3] Public Counsel, ICNU and NWIGU oppose a Three-Year Rate Plan.

As shown in Table No. 3 below, approval of any of the recommended revenue increases proposed by Staff, Public Counsel, or ICNU/NWIGU in Table No. 2 above for Rate Year 1 (2018), would result in a return on equity (ROE) of over 140 to 230 basis points under that currently authorized (9.5%).

Table No. 3

Resulting ROE of Proposed Revenue Positions of Parties		
	ROE Electric	ROE Natural Gas
Staff	**8.10%**	**8.00%**
Public Counsel	**7.80%**	**8.10%**
ICNU/NWIGU	**7.20%**	**7.50%**

B. Similarities Between Avista and Staff

Q. Please explain the similarities between the Avista rebuttal position and Staff's electric and natural gas positions in this case.

A. In general, Avista's understanding is that Staff and Avista agree on the following:

- Avista has supported a revenue requirement need beyond that produced from the "Traditional Historical Pro Forma" method, as shown by the inclusion of the same End-of-Period (EOP) 2016 restating adjustment proposed by Staff.

- A Three-Year-Rate Plan is supported based on evidence in the record. The Year 2 and 3 revenue requirement amounts are produced using a revenue growth factor applied to the prior year's proposed non-ERM and non-gas cost revenues. Staff and Avista also agree on 3 of the 5 revenue growth factor components: 1) O&M; 2) Net Plant after ADFIT; and 3) Annual Growth in Sales Revenues.[8]

- In addition to the numerous uncontested adjustments by all parties, the Company and Staff agree on what Staff has characterized as "Staff Contested"[9] restating and pro forma adjustments: 1) Restate Property Tax; 2) Uncollectible / Conversion Factor; 3) Restate Incentives; 4) Addition of 2016 AMA to EOP 2016 (Rate Base)[10]; 5) Pro Forma Incentives,; 6) Pro Forma Director Fees; and 7) Removal of EOP 2017 Capital Additions. See Exh. EMA-15 page 1-3 which provides a listing of Electric and Natural Gas Uncontested / Contested Adjustments.[11]

C. Differences Between Avista and Staff/Intervening Parties

Q. Before discussing Rate Year 1, what are the primary differences between Avista's proposed Year 2 and 3 revenue requirements and that of the intervening parties, including Staff?

A. As noted within Table No. 2 above, Public Counsel, ICNU and NWIGU oppose a Rate Plan, providing a revenue requirement amount for Rate Year 1 only.

[8] The two revenue growth factor components still at issue, as discussed further in my testimony, are: 1) Depreciation Expense; and 2) Taxes other than Income. Staff used a historical period of 2007 - 2016, whereas, Avista used the historical period 2013 - 2016 to determine the growth rate.

[9] "Contested" labeled adjustments as noted by Staff witness Ms. Huang, Exh JH-2, pgs 5-10 and JH-3 pgs 5-9.

[10] Staff and Avista do disagree on the inclusion of depreciation expense within the 2016 AMA to EOP adjustment. Staff excludes depreciation expense, whereas Avista includes depreciation expense to reflect recovery of (return of) the rate base additions from 2016 AMA to EOP, not just the return on those additions.

[11] Avista believes Staff and Avista agree on the level for pro forma property taxes per updated Staff_DR_160; however, based on review of Staff workpapers, the Company believes that Staff witness Ms. White has a calculation error within her electric pro forma property tax calculation understating the appropriate amount as proposed. This is discussed further in Section V. of my testimony.

1 However, the primary differences between Staff and Avista for Rate Years 2 and 3 of
2 approximately $4.0 million electric and $1.0 million natural gas, are due to: 1) the size of the
3 Year 1 revenue increase, and 2) the revenue growth factor used to determine Years 2 and 3,
4 which is applied to the previous year's proposed revenue. Both of these issues will be
5 discussed further in Sections III. and IV.

6 **Q. Turning to Rate Year 1, please explain the primary differences between**
7 **Avista's proposed Year 1 electric and natural gas revenue requirements and that of**
8 **Staff and the other parties.**

9 A. The primary differences between each of the parties, including Staff, Public
10 Counsel, ICNU and NWIGU, and Avista on rebuttal, relate to 1) a lower cost of capital; 2)
11 removal of any update to base power supply costs; and 3) a significantly lower level of
12 capital additions (or rate base) to be included for Rate Year 1. A reconciliation of these
13 parties' proposals compared to the Avista "as-filed" on direct is provided at Exh. EMA-15,
14 pages 2 (electric) and 3 (natural gas)[12]. A similar adjustment between the parties (and Staff
15 as discussed further below), in addition to removal of base power supply costs, is the
16 removal of the Company's EOP 2017 rate base adjustment. As discussed by Ms. Schuh,
17 ICNU and NWIGU for their part also removed certain pro forma 2017 threshold capital
18 additions otherwise included by the Company, further reducing its revenue requirement
19 below that of Staff. Given these similar positions, which are discussed elsewhere or by other
20 Company witnesses, I will now focus my attention on the differences with Staff.

[12] All adjustments noted above or other miscellaneous adjustments, such as that proposed by either ICNU, NWIGU or Public Counsel related to pro forma non-labor or pro forma property taxes, are discussed in Section V. of my testimony.

1 **Q. Please provide additional information regarding the differences between**
2 **Avista's proposed Year 1 electric and natural gas revenue requirements and that of**
3 **Staff.**

4 A. The primary differences between Avista and Staff's electric and natural gas
5 revenue requirement positions for Year 1 are summarized in Table No. 4 below.

6 <u>**Table No. 4**</u>

Line:	Reconcilation of Avista Rebuttal versus Staff Revenue Requirement - Year 1 (000s)					
				Electric	Natural Gas	
1	**Staff Filed**			**$ 10,034**	**$ 1,107**	
2	Power Supply			$ 16,609	-	See Company witnesses Kalich / Johnson
	Miscellaneous Contested Adjustments:	Electric	Nat. Gas	$ 1,690	$ 234	See Andrews (Section V. below)
3	Working Capital	$ (75)	$ 234			
4	Pro Forma Property Tax [(1)]	$ 694	-			
5	MT SB #363 Hydro Fee	$ 1,071	-			
6	Net Capital Adjustments			$ 12,632	$ 2,547	See Company witness Schuh & Andrews (Section III. below)
7	Cost of Capital			$ 13,422	$ 2,742	See Company witnesses Thies / McKenzie
8	**Avista Rebuttal**			**$ 54,387**	**$ 6,630**	

(1) Avista believes Staff errorred in its calculation of its electric pro forma property tax adjustment. Once corrected, Avista and Staff would agree.

14 As can be seen in Table No. 4 above, the <u>primary differences</u> between Staff and
15 Avista are shown on lines (2) <u>Power Supply</u> ($16.6 million electric); (6) <u>Net Capital</u>
16 <u>Adjustments</u> ($12.6 million electric / $2.5 million natural gas); and (7) <u>Cost of Capital</u>
17 ($13.4 million electric / $2.7 million natural gas). Each of the adjustments included in lines
18 2 through 7 in Table No. 4 are discussed further below in Section V. "Identified Adjustments
19 to Company Filed Case."[13 / 14]

[13] Additional testimony regarding line (2) Power Supply can be found in the rebuttal testimonies of Company witnesses Mr. Kalich and Mr. Johnson, and line (7) Cost of Capital can be found in the rebuttal testimonies of Company witnesses Mr. Thies and Mr. McKenzie. In addition to my testimony, Company witness Ms. Schuh discusses the adjustments impacting line (6) Net Capital Adjustments.
[14] These areas are also the primary differences with ICNU, NWIGU, and Public Counsel. See Exh. EMA-15 for a reconciliation of each party, including Avista on rebuttal, compared to the Company's filed case.

1 Beyond the Miscellaneous Contested Adjustments (lines 3-5) discussed further in
2 Section V., the testimony that follows will focus on line (6) Net Capital Adjustments.

3

4 III. CAPITAL ADDITIONS & APPROPRIATE LEVEL OF RATE BASE ARE 5 MAIN DRIVERS OF AVISTA'S NEED FOR RATE RELIEF

6 **Q. As noted within the Company's direct filed case, capital additions are a**
7 **main driver for the need for rate relief in this case, and therefore a main topic of**
8 **consideration by the parties. Please explain.**

9 A. Capital additions have been and will continue to be the main driver of the
10 need for rate relief over the Company's Three Year Rate Plan. The overall level of rate base
11 to be included during the subject rate period, therefore, is a major topic of discussion and
12 consideration by Staff and other intervening parties. Specifically, although no party has
13 proposed to disallow, as imprudent, any project proposed by the Company to be included in
14 its requested rate relief, Staff discusses some possible benefits of regulatory lag[15] and
15 contests the level of rate base included by the Company.[16] They also contend that the
16 methods by which the Company determines its level of rate base is a request of
17 "extraordinary" rate relief.[17]

18 **Q. In Avista's filed case, did the Company provide ample support for its**
19 **requested capital additions?**

20 A. In the Company's direct filed case, Company witnesses, including Mr.
21 Kinney, Ms. Rosentrater and Mr. Kensok, attest to the numerous projects that move into-

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[15] "Regulatory lag is the period of time that occurs between the time in which a cost to a utility changes, and the time when that change is reflected in customer rates." Exh. CSH-1T, pp. 6:20 – 7:1; pp. 9:8 – 10:17.
[16] Hancock, CSH-1T, p. 25, ll. 2-9.
[17] Hancock, CSH-1T, p. 6, ll. 1-8 and Mullins, Exh. BGM-1T, pp. 5-6.

1 service before the start of the Rate Plan and that are necessary to deliver safe and reliable
2 service to customers.[18] Each of the Company witnesses, for their respective areas, provided
3 details of capital projects in progress, as well as planned projects, and address why they need
4 to be done in the planned time frame, and what the risks and consequences are of not
5 completing the projects in that time frame.

6 **Q. Before discussing in detail your concerns with Staff and other parties**
7 **positions in this case, what summary comments do you have?**

8 A. The testimony that follows is in direct response to Staff and intervening
9 parties' criticism of Avista's approach within its direct filed case. I first briefly discuss
10 Avista's as-filed approach, the approach proposed by Staff, and then, in the alternative,
11 Avista's revised approach for setting the appropriate level of rate base it is recommending on
12 rebuttal. In summary, the testimony that follows will explain that:

13 • The Company did not seek "extraordinary" rate relief, but simply provided
14 alternative methods, "or tools," available to this Commission for setting rates that are
15 appropriate during the rate-effective period.

16 • Furthermore, the Company had proposed a level of rate base within its direct filed
17 case <u>that will be transferred to plant in-service, serving customers and "used and</u>
18 <u>useful" 4 months prior to rates going into effect May 1, 2018</u> – and for some projects,
19 several months to one year in advance.

[18] Exh. HLR-1T, Exh. JMK-1T, and SJK-1T. Company witness Mr. Morris at Exh. SLM-3 also provides the Company's Infrastructure Investment Plan, which provides an explanation of Avista's six major capital investment drivers, and how the Company's capital investments are identified and prioritized across the Company.

1 • The rate base level proposed by Staff and other intervening parties would impose a
2 regulatory lag of over 2 1/3 years relative to plant that will be in service serving
3 customers well in advance of the Rate Year 1 effective date (May 1, 2018). This level
4 of "regulatory lag" will be detrimental to the Company's financial position,
5 preventing it from realizing the opportunity to earn the authorized rate of return
6 approved by this Commission.

7 • The Company, for its part, has revised its approach on rebuttal, lowering the level of
8 rate base included in its request for rate relief, striking a balance between its original
9 filed request and that proposed by Staff. The level of rate base that will be in-service
10 serving customers prior to Rate Year 1, as reflected in its rebuttal, <u>will still far</u>
11 <u>exceed that included in the actual rate year</u>.

12 **<u>A. Traditional Pro Forma vs EOP Rate Base</u>**

13 **Q. Each of the parties in this case expressed concerns with the level of rate**
14 **base included in the Company's initial filing. Specifically, they criticized the Company**
15 **for its use of EOP 2017 rate base and the number of capital additions included through**
16 **2017.[19] Before specifically discussing party concerns, and the Company's approach on**
17 **rebuttal to address those concerns, please summarize the approach taken by the**
18 **Company within its direct filed case.**

19 A. As discussed by Ms. Schuh, within the Company's direct filed case it had
20 included net plant after ADFIT (plant rate base) balances as of EOP 2017.[20] To produce this

[19] Hancock, CSH-1T, p. 25; Scanlan, Exh. KBS-1T, p. 26 – 27; Mullin, Exh. BGM-1T, p. 23; Garrett. Exh. MEG-1T, p. 10.
[20] Schuh direct, Exh. KKS-1T.

1 level of rate base, related to plant only, the Company started with its 2016 historical rate
2 base on an AMA basis. Next, to first demonstrate that, based on the "Traditional Pro Forma
3 Study" approach, the level of plant in rate base included in Year 1 would not sufficiently
4 recognize the rate base level expected during the Rate Year 1 (effective May 1, 2018), the
5 Company applied a 0.5% of rate base[21] "threshold" consistent with a prior Commission
6 Order.[22] This first adjustment was included in the Company's direct filed case as
7 Adjustment 3.10 and labeled "Pro Forma 2017 Threshold Capital Adds," adding $34.9
8 million of rate base for electric[23], and $17.8 million of rate base for natural gas.[24]

9 **Q. What did this first rate base adjustment beyond the historical test year**
10 **show regarding the level of overall rate base?**

11 A. The results of the Traditional Pro Forma adjustment produced net rate base
12 balances of $1.411 billion and $280.8 million, for electric and natural gas respectively.[25]

13 **Q. Why did the Company believe this level of plant rate base was**
14 **insufficient?**

15 A. First, to support its level of rate relief necessary in Rate Year 1 (effective May

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[21] "Rate Base" is defined as gross plant adjusted for accumulated depreciation (AD) and accumulated deferred federal income taxes (ADFIT). "Net Plant" is defined as Gross plant adjusted for AD (prior to any offsetting ADFIT). The revenue requirement established for utility rate making is based on a utility's rate base for the rate effective period, at its authorized rate of return, to determine the net operating income requirement during the rate period. This operating income requirement is compared to the net operating income during the rate period to determine if there is a deficiency or sufficiency.

[22] Per Commission Order 05, ¶ 40, Docket UE-150204 and UG-150205: "Staff's proposed threshold for major plant additions relies on an established rule, albeit one established in a somewhat different setting. It has, however, the advantage of being proportional to the size of the Company's rate base and therefore relevant to the issue of the financial impact on the Company in the setting of rates. We find it reasonable to set the threshold in proportion to a company's rate base. In the instant case, we find it reasonable to use the one-half of one percent threshold."

[23] Andrews, Exh. EMA-3, page 9.

[24] Andrews, Exh. EMA-7, page 8.

[25] Andrews, Exh. EMA-3, page 9 (electric) and Exh. EMA-7, page 8 (natural gas).

1 1, 2018), the Company reviewed what level of rate base was expected by year-end 2017 (4
2 months prior to the rate effective date of May 1, 2018). Second, to support its level of rate
3 relief requested over the Three-Year Rate Plan, the Company prepared what it called its
4 electric and natural gas "Rate Year Studies,"[26] prepared based on expected transfers-to-plant,
5 expenses and revenues over the three-year rate period from May 1, 2018 through April 30,
6 2021. Although those studies were akin to the Company's forecast (or a forecasted test
7 period) and therefore not used for setting rates, it provided some indication to the Company
8 of what the expected plant-related rate base would be effective December 31, 2017. More
9 importantly, it provided what the expected plant-related rate base would be effective May 1,
10 2018 through April 30, 2021. These studies were filed as Exh. EMA-5 and Exh, EMA-9 for
11 informational purposes only.
12 Table No. 5 below compares the Net Plant after ADFIT (rate base) balances
13 produced by the Pro Forma Study, with that at December 31, 2017 and for each of the rate
14 years effective May 1, 2018, May 1, 2019 and May 1, 2020:
15 **Table No. 5**
16
17
18

Net Plant After ADFIT (Rate Base) (000s)					
	Pro Forma Study	At	May 2018 - Apr 2019	May 2019 - Apr 2020	May 2020 - Apr 2021
		12.31.2017	Rate Year 1	Rate Year 2	Rate Year 3
Electric	$ 1,410,595	$ 1,530,469	$ 1,539,337	$ 1,574,348	$ 1,634,379
Natural Gas	$ 280,772	$ 294,398	$ 300,122	$ 315,188	$ 331,011
Reference: Exhs.	EMA-2 & 6	EMA-3 & 7	EMA-5 & 9	EMA-5 & 9	EMA-5 & 9

19 As can be seen from Table No. 5, at December 31, 2017 the rate base balances are
20 expected to be approximately $1.53 billion for electric and $294.4 million for natural gas,
21 and even higher for Rate Year 1 effective May 1, 2018. The Pro Forma Study, however, as

[26] Andrews, Exhs. EMA-5 and EMA-9.

1 compared to December 31, 2017 is lower by approximately $120 million for electric and
2 $13.6 million for natural gas.[27 / 28] This difference is far more significant and impactful on a
3 utility of Avista's size to just be dismissed as inevitable "regulatory lag." That significant
4 difference shows that the "Traditional Pro Forma Study" was not going to produce results
5 reflective of the Rate Year. These results would therefore, also not set rates which are "fair,
6 just, reasonable and sufficient," in accordance with RCW.80.28.010 during the rate effective
7 period, depriving the Company of a reasonable opportunity to recover its costs and earn a
8 fair rate of return.

9 **Q. Since forecasted test periods have not been embraced by Washington**
10 **regulation, what then did the Company do to support a higher level of plant rate base**
11 **within its filed case?**

12 A. In particular, the Company reviewed past Commission orders, in which this
13 Commission noted:[29]

14 While the Commission traditionally has described its ratemaking practice as being
15 based on the historical test year, a key operative part of this description is "based on."
16 In point of fact, our practice is quite forward looking and in actuality a process
17 sometimes referred to as a "hybrid test year."
18
19 The Commission cited examples of "tools" it may use for ratemaking purposes to

[27] Electric ($1.53 billion - $1.41 billion) and natural gas ($294.4 million - $280.8 million). The revenue requirement impact of this variance between the Pro Forma Study and 12.31.2017 rate base balances including depreciation expense at the Company's proposed rate of return is $21.5 million for electric and $3.3 million for natural gas. See Andrew's Exh. EMA-3, page 10 and EMA-7, pge 8.
[28] Comparing the Pro Forma Study results of $1.41 billion and $280.8 million, for electric and natural gas respectively, to the May 1, 2018 Rate Year 1, that is a difference of $128.8 million electric and $19.3 million for natural gas of expected plant rate base excluded from the electric and natural gas Pro Forma Studies.
[29] Docket Nos. UE-160228 and UG-160229, Order 06, p. 48, paragraph 82.

1 produce its "hybrid test year," such as significant discretion around the determination of *pro*
2 *forma* adjustments, noting that it has not established "bright-line standards."[30] The
3 Commission also gave examples of what they might allow: new generation plant or other
4 infrastructure in rate base even when the new facilities are placed in service subsequent to
5 the end of the test period; end-of-period rate base when this is shown to be appropriate; and
6 hypothetical capital structures to improve a utility's financial condition.[31 / 32]

7 Lastly, the Company took into consideration the criticism by the Commission and
8 intervening parties in its 2016 case, by only including plant additions at the time new rates
9 go into effect, that are "used and useful" and in-service serving customers. It also provided
10 more than sufficient time to audit the proposed rate base.[33]

11 **Q. How did the Company develop its requested level of rate base?**

12 A. The Company limited its requested level of rate base and adjusted its "Pro
13 Forma Studies" to reflect only projects in service as of December 31, 2017.[34] Although the
14 Company's initial filing on May 25, 2017, would therefore need to include certain estimated
15 costs from May through December 2017, those costs would become "known and
16 measureable" during the pendency of the case.[35] The Company believed this to be

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[30] *Ibid.*
[31] As discussed by Mr. Thies (Exh. MTT-6T, p. 12), consistent with Avista's direct filed case, the Company is requesting a capital structure of 50% equity / 50% debt, reflecting long-term debt and equity excluding the impact of short term debt. This method is consistent with that approved in Avista's Idaho and Oregon jurisdictions.
[32] Docket Nos. UE-160228 and UG-160229, Order 06, p. 48, paragraph 82.
[33] Docket Nos. UE-160228 and UG-160229, Order 06, p. 43, paragraph 72 and 80.
[34] The Company labeled these studies "EOP Rate Base Studies," and filed them as Exh. EMA-3 and EMA-7.
[35] The Company did in fact provide updated information and actual transfers-to-plant through August in response to discovery, well in advance of Staff and other party's responsive testimony. September actual data was also provided by a supplemental response to Staff_DR_265 on October 23, 2017, prior to Staff's responsive testimony.

1 appropriate, as the level of rate base reflected within these studies would be used and useful
2 4 months prior to the beginning of Rate Year 1. This would provide ample time for review
3 during the rate case process. Furthermore, this level of rate base would be more reflective of
4 the projects in service serving customers throughout Rate Year 1 (2018). The Company
5 believed this would otherwise be a better option than an arbitrary cut-off which would
6 exclude significant rate base levels or projects from recovery over the Rate Plan.[36]

7 **B. Staff Rate Base Adjustments**

8 **Q. Since Staff rejected Avista's EOP 2017 approach, what alternative**
9 **adjustment did Staff propose to help reduce regulatory lag?**

10 A. As discussed by Staff witness Mr. Hancock, Staff excluded the Company's
11 EOP 2017 Adjustments 3.15 (electric) and 3.14 (natural gas).[37] However, in order to reduce
12 regulatory lag, Mr. Hancock restated the Company's 2016 historical (test period) average-of-
13 monthly-average (AMA) rate base balances to a 2016 EOP basis.[38 / 39]

14 Staff's "Restating 2016 AMA to EOP" adjustments included rate base additions of
15 $69.7 million for electric and $14.2 million for natural gas. This results in increased electric

[36] Furthermore, as discussed by Ms. Schuh (Exh. KKS-1T, p. 20), to support its proposed level of rate base over the Rate Plan, the Company had proposed to file capital reports annually by February 15th, prior to the May 1 effective date of Rate Years 2 and 3 in 2019 and 2020. These reports will allow Staff and other parties an opportunity to review and ensure the levels approved in Rate Years 2 and 3 are based on plant that is used and useful, and serving customers prior to the effective date. The Company plans to file a similar report by February 15, 2018 showing the level of rate base at December 31, 2017, to prove the level of proposed rate base included on rebuttal is, in fact, in-service and serving customers, well in advance of the May 1, 2018 effective date.
[37] Hancock, Exh. CSH-1T p. 25:4 – 26:17.
[38] *Id.* p. 27:17 – 28:17.
[39] In support of Staff's adjustment Mr. Hancock states: "EOP has been found to be appropriate to counter the effects of regulatory lag. Staff recognizes that an AMA accounting, with limited pro forma adjustments, will likely understate the level of rate base in service during the first year of the rate plan." Exh. CSH-1T at p. 28, ll. 2-5.

1 and natural gas revenue requirement amounts of $7.0 million and $1.4 million, respectively,
2 after isolating the effect of only their rate base adjustment.[40]

3 **Q. Staff excluded depreciation expense when it adjusted its 2016 AMA**
4 **balances to an EOP basis, arguing it would distort test year relationships.[41] Do you**
5 **agree with this?**

6 A. No, I do not. Although the Company is supportive of adjusting 2016 AMA
7 balances to an EOP basis, the Company believes it is equally important to adjust the
8 associated depreciation expense <u>to match</u> the rate base balances being adjusted. That
9 "matching" is a fundamental rate-making principle.

10 To adjust rate base AMA levels to EOP levels, only allows the Company to recover
11 "<u>the return on</u>" that investment. However, without also including the annualized level of
12 depreciation expense on that same level of rate base, prevents the Company from recovering
13 its investment or "<u>return of</u>" that same investment. <u>This mismatch distorts "rate year</u>
14 <u>relationships</u>."[42] In fact, this mismatch distorts the relationship <u>over the full Three-Year</u>
15 <u>Rate Plan.</u> Because this depreciation expense is excluded in Year 1, there is no opportunity
16 to recover it in Years 2 and 3. The resulting impact of Staff excluding the annualized

[40] Huang, Exh. JH-2 and JH-3, p. 7.
[41] Scanlan, Exh. KBS-1T, p. 17, ll. 1-5.
[42] This can be also be explained using a simple example: a capital project that actually went into service in December of the test year (2016), under generally accepted accounting principles (GAAP) would require that depreciation expense be recorded at ½ of one month for the month it moves into service. For this project ½ of one month would be recorded as expense in the test year (4% of the expense), resulting in 11 ½ months of depreciation expense being <u>excluded</u> during the test year (<u>96%</u> of the expense), although the full project amount is included in rate base. Under Staff's proposal 96% of the depreciation expense would be excluded annually Year 1 through Year 3, understating depreciation expense <u>during the entirety</u> of the Three-Year Rate Plan through May of 2021.

1 depreciation expense within its 2016 AMA to EOP adjustment is approximately $4.0 million
2 for electric and $767,000 for natural gas, annually.[43]

3 **Q. Beyond Staff's "Restating 2016 AMA to EOP" adjustment, what**
4 **additional capital adjustment does Staff make?**

5 A. Ms. Scanlan explains Staff proposes "*limited* pro forma rate base additions
6 for those projects or programs" that are above 0.5% of the Company's net utility plant and in
7 service as of August 31, 2017.[44]

8 **Q. What level of rate base additions does Staff's "Threshold 2017 Capital**
9 **Additions" adjustment support?**

10 A. Ms. Scanlan's electric and natural gas "Threshold 2017 Capital Additions"
11 adjustments includes only <u>three</u> electric projects and only <u>five</u> natural gas projects (7 actual
12 projects, as one project is common to both). Using August as Staff's cutoff for determining
13 the balances of these projects results in electric and natural gas <u>rate base adjustments</u> of only
14 $8.7 million for electric and $7.9 million for natural gas. This results in increasing Staff's
15 revenue requirement by only $1.8 million for electric and $1.3 million for natural gas. [45] / [46]

16 **Q. Does Staff propose any additional capital adjustments beyond that**
17 **included by its "Restate 2016 AMA to EOP" and "Pro Forma Threshold 2017 Capital**
18 **Additions"?**

19

[43] Andrews Exh. EMA-15, p. 2 and 3, row 8, revenue requirement column, Staff proposed vs Avista proposed.
[44] Scanlan, Exh. KBS-1T, p. 18, ll. 3-8.
[45] Huang, Exh. JH-2 p. 9 (electric) and JH-3, p. 8 (natural gas).
[46] It is important to note that when Ms. Scanlan argues at Exh. KBS-1T, p. 19, ll. 1-3, that she does not support the Company's use of rate base for its threshold calculation, she alludes to the fact that rate base includes elements such as working capital. The Company does not include any balances beyond plant-related balances when determining its proper threshold.

1 A. No, it does not.

2 **Q. Are Staff's proposed adjustments reasonable?**

3 A. Only in part. Staff witness Mr. Hancock provides testimony in his case
4 regarding the use of EOP 2016 rate base and how it helps with "regulatory lag."[47] Ms.
5 Scanlan, for her part, notes that "EOP plant balances are closer in time to the rate year than
6 AMA balances. In that way, the EOP balances can be a more accurate estimate of the
7 utility's plant balances in the rate year."[48]

8 While the Company appreciate Staff's efforts to reach forward to EOP 2016 to
9 reduce the "regulatory lag," Staff's perception that 2016 EOP balances, standing alone, will
10 provide a "more accurate estimate" of the rate year, is simply not true. While adjusting to
11 EOP 2016 "advances the ball," it does not ultimately take the Company anywhere near the
12 finish line. In fact, as seen in Table No. 6 below, the Company's December 31, 2017
13 balances are far more reflective of that expected during the rate effective period than at
14 December 31, 2016:

15 **Table No. 6**

Net Plant after ADFIT (Rate Base) (000s)			
	12.31.2016 EOP	12.31.2017 EOP	Rate Year 1 05.01.2018 - 04.30.2019 AMA
Electric	$ 1,445,375	$ 1,530,469	$ 1,539,337
Natural Gas	$ 277,091	$ 294,398	$ 300,122

16 17 18 19 20 21

[47] Hancock, Exh. CSH-1T, p. 28, ll. 1-17.
[48] Scanlan, Exh. KBS-1T p. 9 ll. 1-4.

1 Nevertheless, as discussed further below, in order to recognize the concerns raised by
2 Staff (and other parties) of the Company's use of EOP 2017 rate base, Avista has on rebuttal
3 modified its rate base methodology to find common ground with what was proposed by Staff
4 in other dockets.

5 For its part, the Company agrees with Staff to eliminate its "2017 EOP Capital Net
6 Plant Adjustment" (3.15 electric and 3.14 natural gas) and include Staff's proposed "Restate
7 2016 Plant from AMA to EOP" adjustments (new adjustments 2.19 electric and 2.16 natural
8 gas). However, with regards to the AMA to EOP 2016 adjustment, Avista strongly believes
9 it is appropriate to include an increased level of depreciation expense in order to match the
10 rate base included with its associated depreciation expense.[49]

11 The Company also does not agree with Staff witness Ms. Scanlan's method to
12 determine the "Pro Forma Threshold 2017 Capital Additions." As discussed by Ms. Schuh
13 and summarized by me below, on rebuttal, the Company proposes to use a different
14 methodology than that proposed by Staff in this case. The Company uses the same threshold
15 of 0.5% of net plant as used by Staff, but applied on a "functionalized" basis, rather than all
16 plant in the aggregate.[50] The Company's approach is what Staff recommended in the
17 pending Puget case.[51]

18 **Q. What concerns does Avista have with Ms. Scanlan's threshold**
19 **methodology?**

---

[49] This would increase depreciation expense by $3.8 million electric and $731,000 natural gas, and revenue requirement by $4 million electric and $767,000 natural gas. Andrews, Exh. EMA-11, pg 7 and EMA-12, pg 6.
[50] The Company's functional categories include functional plant accounting groups listed in the FERC form 1, including: Generation (thermal, hydro, and other), Transmission, Distribution, General Plant, Underground Storage and Gas Distribution. Schuh, Exh. KKS-3T, p. 16, ll. 1-13.
[51] Puget Docket No. UE-170033 and UG-170034, see Wright, Exh. ECW-1T, p. 6:18 – 7:6,

1 A. Ms. Scanlan states the "Commission historically has limited pro forma plant
2 adjustments to major projects that are used and useful to rate payers."[52] (emphasis added)
3 She also notes that Pro Forma adjustments should be limited in number and scale because it
4 is simply not feasible for a company to demonstrate, or for the intervening parties to verify
5 "every single capital transfer to plant."[53]

6 The Company can appreciate this concern, and has included convenient Business
7 Case summaries to assist the parties, along with supporting testimony and exhibits for the
8 121 total projects (sum of projects for electric, natural gas and common to both services) in
9 its direct filed case.[54] This information was sufficient to allow Staff to determine where it
10 wanted to concentrate its audit efforts.

11 However, based on the evidence in this record, the Company does not believe the
12 "limited pro forma adjustments" as proposed by Staff, resulting in only 7 total projects out of
13 121 (or 5.8%), which reflects 3 electric projects and 5 natural gas projects[55], represent a
14 reasonable application of a "threshold".[56] The Commission itself stated:

15 The Commission retains significant discretion to apply flexibly the
16 requirements that *pro forma* adjustments be known and measurable, used

[52] Scanlan, Exh. KBS-1T, p. 12, ll. 3-13.
[53] *Ibid.*
[54] The Company would expect, however, an audit sampling of its projects to typically occur in order to review for prudency, not a review of "every single capital transfer to plant." This is the approach used by the Commission Staff of Avista's Idaho and Oregon jurisdictions. Both Idaho and Oregon in Avista's last several general rate case proceedings have allowed rate base balances in effect just before the rate effective date, i.e. the Idaho Commission in Avista's 2016 GRC (Docket AVU-E-16-03) approved December 31, 2016 EOP balances effective January 1, 2017.
[55] 7 actual projects, as one project was common to both.
[56] While the use of some type of "threshold" may be useful for providing a starting point for audit work performed by Staff and intervenors, it has become much more than that and is now being used as an absolute "cut-off" point for ratemaking. Surely audit work can be done on more than nine projects over a five month period leading up to the Staff and intervenor testimony. No matter what the project or how necessary, and used and useful it is, if it does not make the $6.8 million threshold for electric plant, it is automatically excluded from even basic audit work, as well as any consideration for ratemaking. I do not believe that represents sound ratemaking practice during times described by the Commission as the "new normal."

1 and useful, and matched to offsetting factors. The Commission **has not**
2 **established bright-line standards** governing the timing or the number of
3 adjustments that can be accepted in a given case, and **has not established**
4 **a minimum size** for *pro forma* adjustments to be recognized.[57] (emphasis
5 added)
6
7 Simply put, Staff's method does not at all reflect what will be in service serving
8 customers during the Rate Year. Furthermore, although the use of this "threshold" was
9 employed by the Staff in the Company's prior rate cases (over its objection), it only served
10 as the starting point for Staff's analysis in those prior cases - not the ending point as is the
11 case here. In the prior cases, after using this "threshold", Staff determined that it did not
12 produce reasonable results and added an attrition adjustment to the pro formed historic test
13 period. That was not done here.
14 The result of Staff's method, therefore, leaves far too many projects (114 projects) on
15 the "cutting room floor". Many of the Staff excluded projects, are projects that Mr. Kinney,
16 Ms. Rosentrater, and Mr. Kensok would argue are regular "bread and butter" type projects,
17 necessary in the day-to-day operation of the utility, undertaken in the ordinary course of
18 business, and will certainly benefit customers.[58]

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[57] Dockets UE-160228/UG-160229, Order 06, p. 48, paragraph 82.

[58] Ms. Scanlan, at SKB-1T, pg 30:18-21, also criticized Avista's estimated transfers-to-plant over time. Specifically, she states: "Staff has identified chronic over-forecasting of transfers to plant in Avista's 2016 and 2015 general rate case proceedings." This is paradoxical, given that Mr. Hancock at CSH-1T, pg 48:10-49:1, contradicts Ms. Scanlan by explaining that "Avista's electric attrition ("AVA Attr RB") study most closely estimated the rate base figures reported in the 2016 Commission Basis Report," and showed a table with Avista's 2016 estimated levels reflecting 101.5% of actuals, as compared with 95.66% and 90.2% for Staff and Public Counsel, respectively. For natural gas, Avista reflected 99.82%, while Staff and Public Counsel's estimates reflected 104.33% and 88.06%, respectively. It is also noteworthy, Ms. Scanlan is pointing to Mr. Hancock's testimony in Dockets UE-150204/UG-150205 in her attempt to reflect history. Avista, for its part, at KON-1T, p. 10 of Mr. Norwood's rebuttal testimony in that docket demonstrated that, although individual project timing and dollar amounts will vary within a year, the Company's overall actual spend compared to that planned over the nine year average 2006-2014 was 101%. This is consistent with that noted above by Mr. Hancock, when he observed the Company's 2016 estimates versus actual levels were slightly over by 101.5% electric and under at 99.82% for natural gas.

1 **Q. What does Avista believe Staff should have done?**

2 A. The Company therefore believes, given the level or rate base expected and
3 supported by the Company even as of December 31, 2017[59] – a level that will be in-service,
4 serving customers several months prior to the 2018 Rate Year effective May 1, 2018 – that
5 Staff should have revised its threshold methodology. Stated another way, Staff should have
6 recognized the limitation in this instant case, and reviewed whether its "*limited* pro forma"
7 projects, standing alone, were otherwise reasonable and appropriate under the circumstances,
8 as did Staff witness Mr. Cooper in the pending Puget Sound Energy (Puget) rate case
9 (Docket No. UE-170033/UG-170034).

10 **Q. Are you referring to a recent example of where the UTC Staff supported**
11 **a change in the application of its "0.5% threshold" methodology?**

12 A. Yes. In fact, in the pending Puget rate case, Staff witness Mr. Wright did just
13 that. In his testimony, Mr. Wright explains, similar to Ms. Scanlan, the standards for
14 evaluating pro forma plant adjustments, i.e., are the proposed plant additions "major,"
15 "known and measureable," "used and useful," and "prudently incurred."[60] However, when
16 responding to whether he was adhering to the Commission guidance on how to analyze these
17 initial questions, he stated:

18 Yes. Although Staff has tailored its review to the specific facts and
19 circumstances in the current rate case, recent Commission orders and guidance
20 strongly inform Staff's analysis.
21
22 First, the Commission recently found it reasonable to define a major plant
23 addition as at least 0.5 percent of the utility's rate base. However, Staff found
24 smaller adjustments that would otherwise be reasonable, such as Distribution

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[59] The Company did not include the otherwise additional planned projects that will go into service in 2018, and certainly during the rate effective period, thus excluding plant from January 1, 2018 through April 30, 2019.
[60] Wright, Exh. ECW-1T, p. 6, ll. 8-12, Puget Docket No. UE-170033 and UG-170034.

1 plant adjustments, would not be captured if the threshold were only applied to
2 gross rate base. Therefore, Staff refined the standard in this case, applying the
3 one-half of one percent threshold to net utility plant in service by category
4 instead of rate base. Staff believes the refinement will allow a better review of
5 plant adjustments in this, and future, rate cases. (emphasis added) [61 / 62]
6

7 Essentially, Staff witness Cooper, applied the 0.5% of net plant "threshold" on what I
8 would call a "functionalized" basis to each major functional category – i.e., production,
9 transmission, distribution and general plant. This is far different than applying the 0.5% of
10 net plant threshold to the aggregate of all plant and leads to dramatically different results.[63]

11 **Q. What evidence does the Company have that the level of rate base**
12 **proposed by Staff is insufficient, and will not reflect levels appropriately representative**
13 **of the Rate Year, warranting a revision to Staff's methodology?**

14 A. One may simply look at the level of rate base Staff is proposing of $1.454
15 billion for electric and $285.0 million for natural gas, effective for Rate Year 1 (May 1, 2018
16 – April 30, 2019), and compare that to the level of rate base expected by Avista as of
17 December 31, 2017, a mere one month after the filing of this testimony.[64]

---

[61] *Id.* pp. 6:18 – 7:6.

[62] Mr. Wright further explains his threshold by "category" included a separate electric and natural gas threshold for each of the following categories as reported in Puget's 2015 FERC Form 1 and 2 reports: 1) Production; 2) Transmission; 3) Distribution; and 4) General plant. *Id.* p. 7, footnote 12.

[63] Mr. Wright filed his testimony in the Puget docket on June 30, 2017, approximately one month after Avista filed its direct testimony, and well in advance of Ms. Scanlan's review of the Company's projects.

[64] The fact that the Company is comparing Staff's level of rate base to levels expected as of December 31, 2017, one month after the filing of its testimony, should allay the concerns raised by Ms. Scanlan that "forecasts will by nature be inaccurate because of uncertainty increases with longer time horizons, ..." (KBS-1T, pg 30:14-15). Furthermore, the Company provided actuals through September 31, 2017 prior to Staff filing its responsive testimony. In addition, Avista has October balances as of the filing of its rebuttal, leaving November and December balances only as estimates prior to the end of the year 12.31.2017.

1 Summary Table No. 7 below shows that proposed by Staff over the Rate Plan (based
2 on Staff's proposed Year 1 rate base balances per Huang, Exh. JH-2 and JH-3), and that
3 expected at December 31, 2017 per Avista:

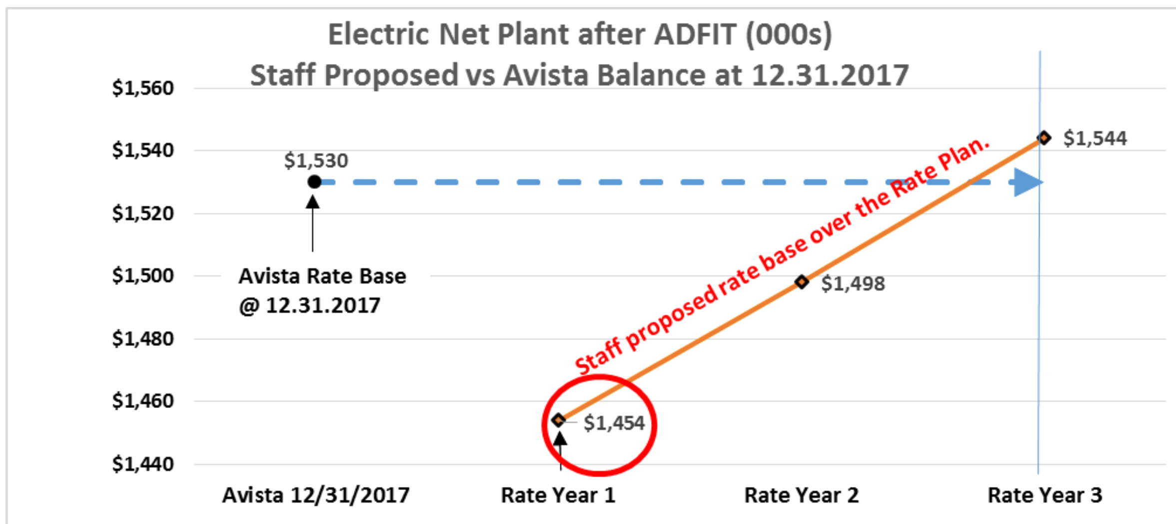
4 **Table No. 7**

	Net plant after ADFIT (Rate Base) (000s)			
	Avista	Staff Proposed		
		Rate Year 1	Rate Year 2	Rate Year 3
	12/31/2017	5/1/2018	5/1/2019 (1)	5/1/2020 (1)
Electric	1,530,469	1,454,074	1,498,278	1,543,825
Natural Gas	294,398	284,963	299,268	314,291

(1) Rate Years 2 and 3 determined by adjusting Rate Year 1 rate base balances by Staff's Net Plant after ADFIT growth rate of 3.04% (electric) and 5.02% (natural gas).

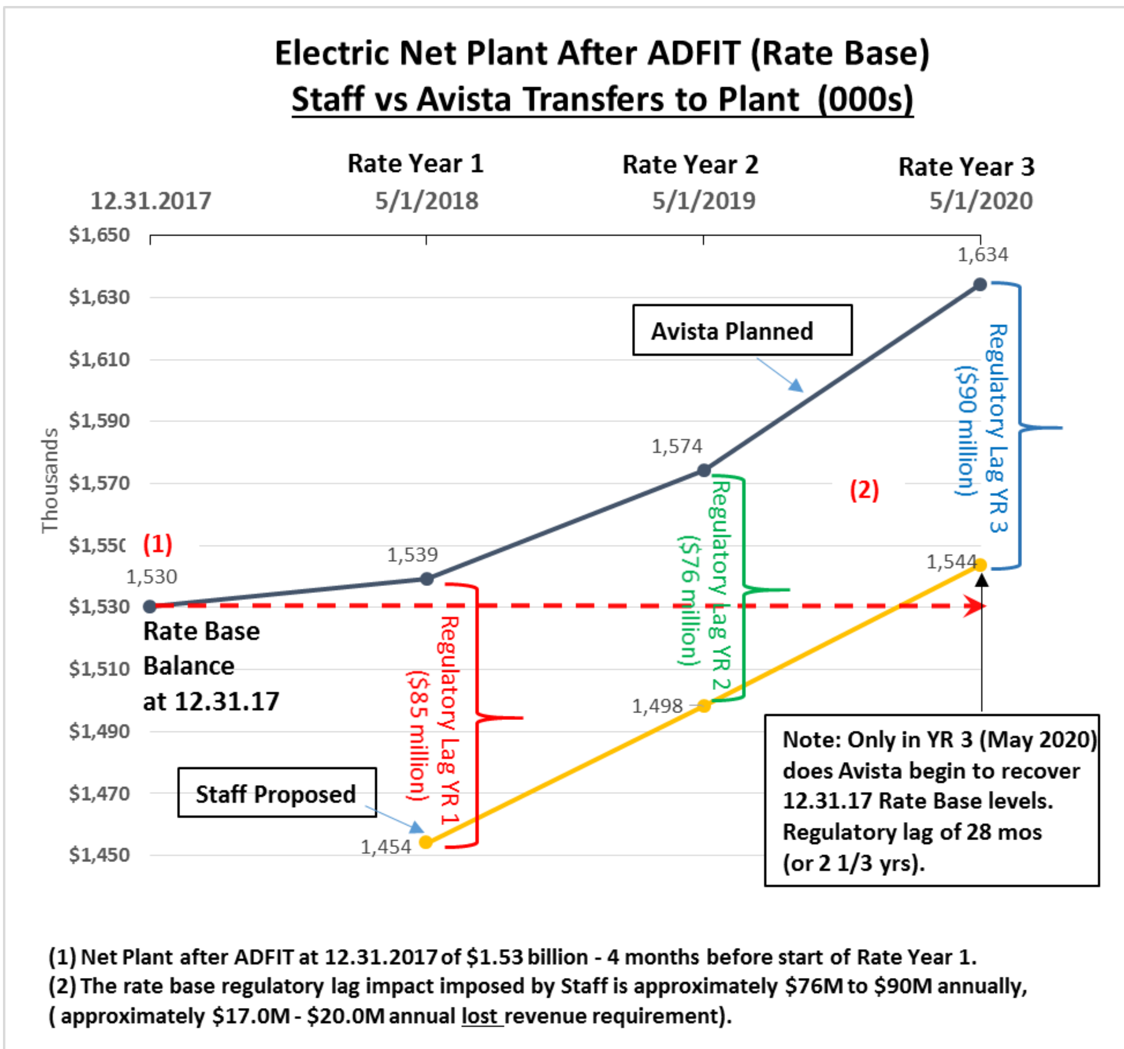
10 Illustration No. 1 below, depicts this level of electric rate base expected by Avista at
11 December 31, 2017, compared with that proposed by Staff in each of the Rate Years 1 – 3.

12 **Illustration No. 1**



20 As can be seen in Illustration No. 1 above, if the Commission were to approve Staff's
21 Rate Year 1 level of rate base of $1.45 billion (electric), this level would be significantly less
22 than Avista will have serving customers as of December 31, 2017. And, when Staff escalates

1 this $1.45 billion over the Three Year Rate Plan, it does not capture the level of rate base
2 actually in service on December 31, 2017 until Year 3, as shown above.
3 Including Staff's proposed natural gas rate base balance of $285.0 million compared
4 with Avista's balance at December 31, 2017 of $294 million, as noted in Table No. 7 above,
5 would result in over $85 million of combined electric and natural gas rate base less than
6 levels expected at December 31, 2017 by Avista. Chart No. 1 below shows just how
7 unrepresentative Staff's proposed level of rate base will be during the Rate Plan:
8 **Chart No. 1**



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1 Chart No. 1 above, representing electric only, highlights some very important
2 problems with Staff's rate base proposals:

3-6 1) Avista would not begin to recover December 31, 2017 rate base levels that will be used and useful, and benefiting customers prior to Rate Year 3 (beginning May 1, 2020); an imposed "regulatory lag" of 28 months or 2 1/3 years.
7-11 2) Under the Three-Year Rate Plan, supported by both Avista and Staff, the Company will not be able to file a new general rate case to reset to more current rate base balances until 2020 for rates effective May 2021, underscoring on the importance of establishing the appropriate balance in Year 1, as a starting point.
12-14 3) The electric "regulatory lag" exposure to the Company alone would be approximately $85 million in Rate Year 1 and grow to $90 million during Rate Year 3.
15-16 4) The revenue requirement impact of that "regulatory lag" exposes the Company to between $17.0 and $20.0 million of annual lost revenue.

17
18 **Q. Have you performed a similar analysis that also includes natural gas rate**
19 **base?**
20 A. Yes. Including Staff's natural gas proposed rate base, the combined
21 "regulatory lag" for the Washington jurisdiction would be $100 - $107 million annually, and
22 result in annual lost revenues between $21.0 - $24.0 million. This roughly translates into a
23 140 to 160 basis point shortfall compared to the Company's current authorized 9.5% ROE.
24 **Q. Do the other parties to the case recommend even lower levels of rate base**
25 **than that proposed by Staff?**
26 A. Yes. Both Public Counsel and ICNU/NWIGU propose even lower rate base
27 balances than those proposed by Staff.[65] These parties, consistent with Staff, remove the
28 Company's 2017 EOP adjustment. However, unlike Staff, they do not restate 2016 AMA
29 plant related balances to EOP, and they each include different "2017 Threshold Capital

1 Additions" adjustments. For its part, Public Counsel leaves the Company's original 2017
2 threshold adjustment as-filed. However, Mr. Mullins, on behalf of ICNU/NWIGU, uses an
3 arbitrary cut-off to further reduce his proposed rate base balances. Ms. Schuh discusses
4 Avista's concern with Mr. Mullin's method in her responsive testimony.[66]

5 **Q. Do other parties comment on the use of "regulatory lag" or the**
6 **Company's need to be efficient?**

7 A. Yes. On behalf of Public Counsel, Mr. Garrett suggests that the Company
8 need only be more efficient, and when the "…regulated utility can no longer manage its
9 company in a manner that achieves a reasonable return" it can remedy the situation by filing
10 a new rate case.[67] However, what Public Counsel fails to point out, is that if this
11 Commission approves a Three-Year Rate Plan (as proposed by Staff and Avista) based on
12 Public Counsel's recommended rate base levels, the Company would not be able to remedy
13 the situation with a new rate case. The Company would be left with the level as proposed by
14 Public Counsel, or by Staff for that matter, which far understate the necessary level of rate
15 base and rate relief in Year 1. This "under-earning opportunity" imposed on the Company
16 would then be compounded in Years 2 and 3 of the Rate Plan, causing the Company to
17 continue to under-earn at a significant level, year-after-year, during the Rate Plan.

18 Illustration No. 2 below depicts the ROE impact on Avista of the positions of the
19 parties (as noted in Table No. 3 above.)
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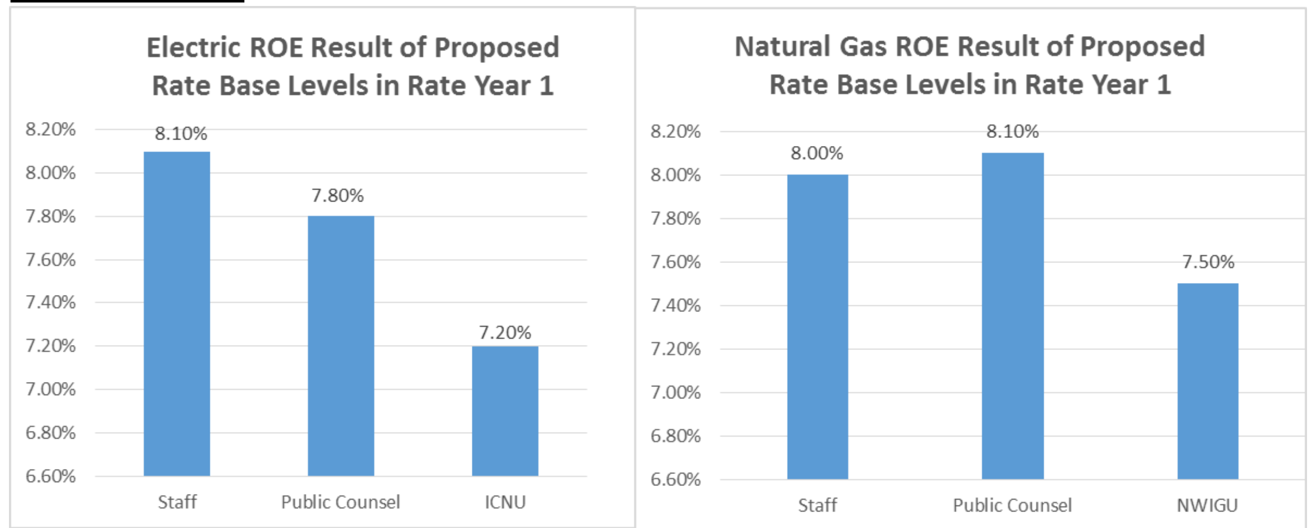
[65] See Exh. EMA-15, pp. 2-3.
[66] Schuh rebuttal, Exh. KKS-3T, pp. 24:15 – 27:6.
[67] M. Garrett, MEG-1T, pg 11:17 – 12:4.

1 **<u>Illustration No. 2</u>**



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9 As far as efficient operations go, or the need to cut costs to reflect better earnings
10 during the three-year rate effective period (May 1, 2018 – April 30, 2021), what each of the
11 parties fail to recognize, is that the level of rate base proposed by parties is <u>already</u>
12 <u>significantly lower</u> than that expected by Avista by the end of 2017. Therefore, this is not
13 about Avista simply cutting future capital projects it has planned in 2018, 2019 or 2020 to
14 have the opportunity to earn its authorized rate of return. Avista can't "cut" already
15 completed projects, capital expenditures that are already spent, and rate base serving
16 customers today.

17 **<u>C. Avista Rebuttal – "Functionalized Threshold" Method</u>**

18 **Q. What then does Avista propose on rebuttal in order to reflect the proper**
19 **rate base in Year 1 and over the Three-Year Rate Plan?**

20 A. As noted above, first to address the concerns of the parties over its use of
21 2017 EOP plant-related rate base, Avista has <u>eliminated</u> its "2017 EOP Capital Net Rate
22 Base" adjustments (3.15 electric and 3.14 natural gas). It begins by accepting Staff's

1 "Restate 2016 AMA Rate Base to EOP" adjustment (2.19 electric and 2.16 natural gas), with
2 the exception that the Company also includes matching depreciation expense on that same
3 plant.

4 Beyond EOP 2016 rate base, however, as discussed further by Ms. Schuh (Exh.
5 KKS-3T), the Company has revised its "Pro Forma 2017 Threshold Capital Additions"
6 adjustments (3.10 for electric and natural gas) to include only 2017 capital additions based
7 on its revised "functionalized threshold." As described by Ms. Schuh, it has revised its
8 threshold to include projects which meet a threshold of 0.5% of net plant (prior to ADFIT)
9 by FERC "functional" group,[68] as did Staff witness Wright in the pending Puget case. This
10 includes setting a threshold by functional rate base category rather than as an aggregated
11 total rate base, as Staff witness Scanlan did here.[69] Using this revised threshold, allows some
12 (but not all) smaller projects that are reasonable to include. This revised "threshold" was
13 applied to projects planned to be completed during 2017, yielding 36 total discrete projects
14 (including 31 electric and 17 natural gas, 12 of which are common to both). To put this in
15 context, this would still only capture 36 out of 121 projects that will be in-service, but far
16 more than the 7 examined by Ms. Scanlan. Furthermore, to reflect concerns by the parties
17 that projects included meet the "used and useful," and "known and measureable" tests, the
18 Company only included those actual project costs that actually transferred into service as of

[68] This includes "functional" groups for generation (thermal, hydro, other), transmission, distribution, underground storage, and general plant. Schuh rebuttal, Exh. KKS-3T, starting at p. 16, ll. 12.

[69] Although the Company believes it is appropriate to use net plant after ADFIT (plant rate base) to determine the threshold, in order to minimize the issues in this case, the Company used net plant (prior to ADFIT) to determine its "functionalized threshold" capital additions, consistent with Staff witness Wright in the Puget case. If the Company had used net plant after ADFIT, this would have increased the projects captured in the "functionalized threshold" and increased the Company's requested revenue requirement in this case.

1 October 31, 2017. Comparing the 36 threshold projects selected by the Company out of the
2 total 121 projects originally included in Avista's direct filed case, still results in less than
3 30% of the projects being selected (or 70% excluded) and still excludes between $20 to $33
4 million annually. This concession, in and of itself, will create significant regulatory lag.

5 In addition, as explained later in my testimony, the Company has also included a
6 reduction to expense by way of a "Pro Forma O&M Offsets" adjustment (3.11). These
7 offsets are related to any 2017 capital projects included in the Company's rebuttal filing.
8 The overall reduction to expense included by the Company is $1.1 million for electric and
9 $5,000 for natural gas. As discussed by Ms. Schuh, many projects undertaken by Avista do
10 not have, and have not been justified by, O&M offsets.[70] Many projects are justified based
11 solely on other investment drivers, as discussed by Mr. Morris.[71] However, to provide a
12 meaningful benefit to customers for real savings expected during the 2018 Rate Year,
13 included in the electric O&M offset adjustment is a reduction to expense of $800,000 related
14 to the project "Street Light Conversion to LED Fixtures" (ER 2584), even though this
15 project is not included as one of the threshold selected projects (i.e. this project was left on
16 the "cutting room floor"). This adjustment provides a 10% reduction in the electric revenue
17 requirement amount included related to the 2017 capital additions.[72]

18 Chart No. 2 below, reflecting electric net plant after ADFIT, shows the level of rate
19 base (and regulatory lag) proposed by Avista on rebuttal for each of the three Rate Years,

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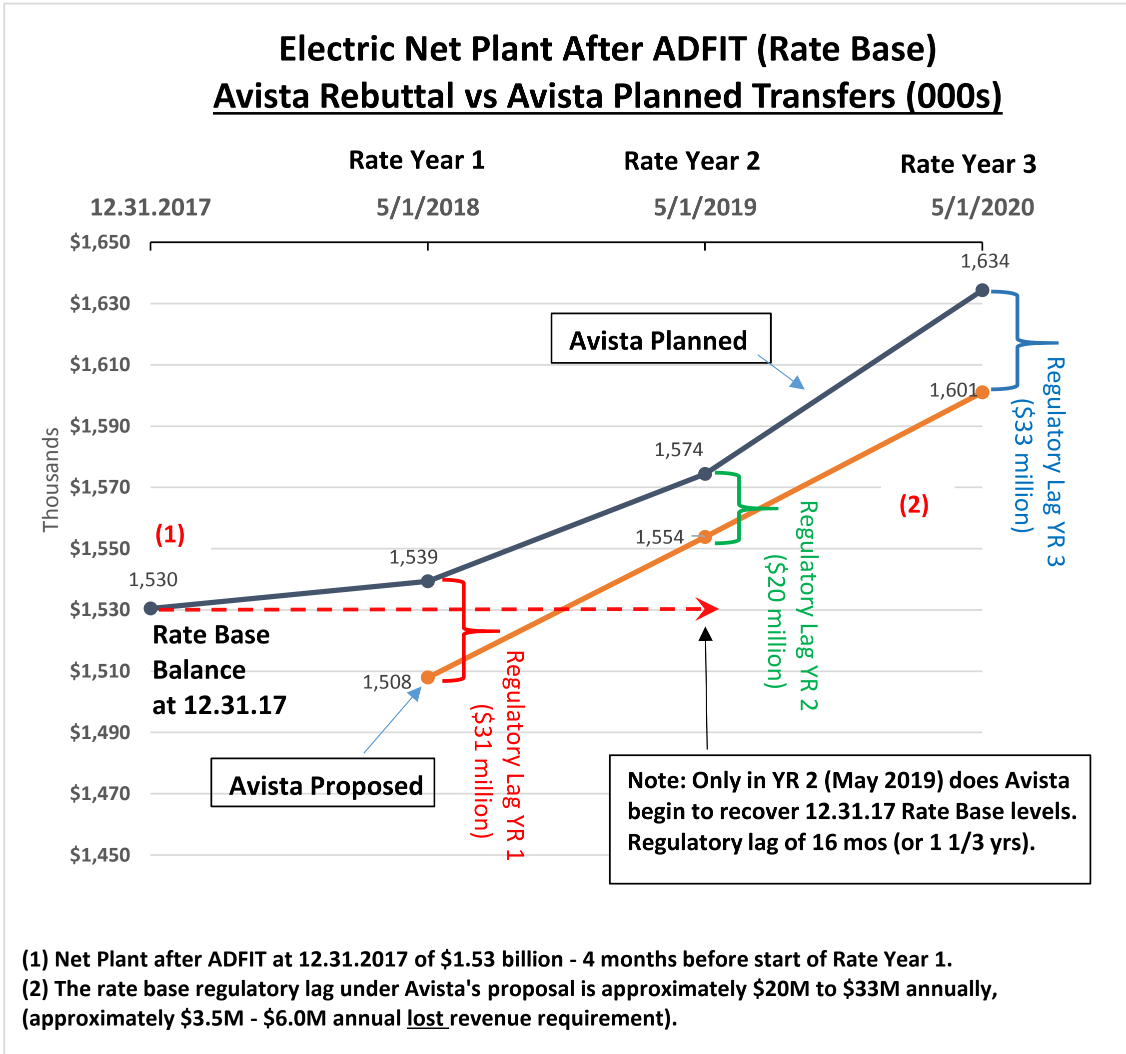
[70] Schuh rebuttal, Exh. KKS-3T, p. 23, ll. 1-5.
[71] Morris direct, Exh. SLM-1T, p. 32, ll. 7-18.
[72] Electric Pro Forma threshold adjustment revenue requirement total ($11.6 million) versus electric O&M adjustment (-$1.2 million).

1 effective May 1, 2018, 2019 and 2020, compared to the levels of expected plant-in-service in
2 those same years.

3 **Chart No. 2**



18 Chart No. 2 above, representing electric only as proposed by Avista, highlights that:

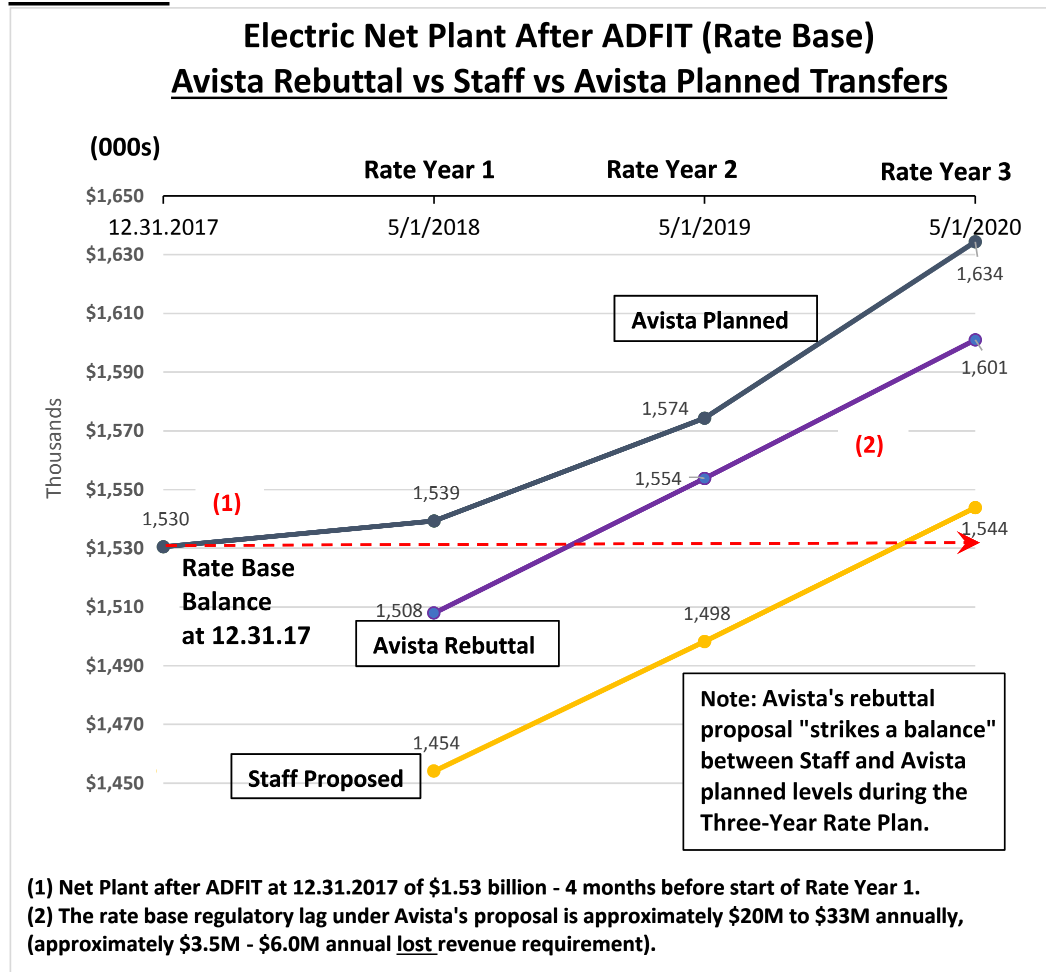
19–22 1) Avista would not begin to recover its December 31, 2017 rate base levels that will be used and useful, and benefiting customers prior to Rate Year 2 (beginning May 1, 2019); an imposed "regulatory lag" of 16 months or 1 1/3 years.

23–25 2) Even under Avista's "functionalized threshold," Avista would experience a "regulatory lag" of approximately $31 million in Year 1, which would grow to $33 million by Year 3.

3) The revenue requirement impact of that "regulatory lag" exposes the Company to between $3.5 million and $6.0 million of annual lost revenue.[73]

Chart No. 3 below, combines the earlier Chart Nos. 1 and 2, and compares Avista's level of rate base using its functionalized threshold on rebuttal, Staff's proposed level of rate base, and Avista's planned level of rate base transferring to plant over the Three-Year Rate Plan.

Chart No. 3



[73] For natural gas, the result is a regulatory lag of $6 million to $7 million annually, and lost revenue of $1.3 million to $1.5 million annually. Combined, this results in a Washington jurisdiction regulatory lag of $37 million to $40 million annually, and lost revenue between $4.8 million and $7.5 million annually.

1 The conclusion to be drawn from this last comparison Chart No. 3, is that Avista's
2 rebuttal position attempts to strikes a balance with what was proposed by Staff and employs
3 the same approach by Staff in the pending Puget GRC. Even Avista's rebuttal position
4 would impose more "regulatory lag" than would be necessary (some would argue) for Avista
5 to manage its costs and operate its utility business efficiently in order to have the opportunity
6 to earn its authorized rate of return. In fact, if the Company were to assume the currently
7 authorized cost of capital, Avista's rebuttal position would only allow it to earn 9.2%
8 compared to the Company's currently authorized ROE of 9.5%.

9 **Q. What is the impact on the Company's revenue requirement of including**
10 **the Company's revised adjustments reflecting its "functionalized threshold"?**

11 A. On rebuttal the Company has included revised electric and natural gas "Pro
12 Forma 2017 Threshold Capital Additions" adjustments (3.10). These adjustments reflect a
13 rate base increase of $62.5 million for electric and $16.5 million for natural gas, increasing
14 the requested revenue requirement by $11.61 million for electric and $3.17 million for
15 natural gas.[74]

16 Table No. 8 below, summarizes the rate base and revenue requirement values for the
17 electric and natural gas 2016 AMA to EOP restating adjustments and 2017 Pro Forma
18 Threshold adjustments using actual October balances, as proposed by the Company. Also
19 included in Table No. 8, <u>for informational purposes</u> as Ms. Schuh explains, <u>are August and</u>

[74] Ms. Schuh discusses these adjustments in her rebuttal testimony at Exh. KKS-3T. Supporting workpapers for Ms. Schuh are also provided along with the Company's rebuttal testimony.

1 September actual balances using the Company's "functional threshold," should the
2 Commission utilize a different ending point for capital additions.[75]

3 **Table No. 8**

Company Proposed Adjustments on Rebuttal			For Information Only	
(000s)	12/31/2016 to EOP Adjustment (Adj. 2.19 E / 2.16 G)	2017 Pro Forma Additions (Through October) (Adj. 3.10 E & G)	2017 Pro Forma Additions (Through September)	2017 Pro Forma Additions (Through August)
Electric			Electric	
Net Rate Base	$ 69,691	$ 62,544	$ 53,029	$ 45,841
Revenue Requirement	$ 11,639	$ 11,610	$ 10,055	$ 8,671
Natural Gas			Natural Gas	
Net Rate Base	$ 14,160	$ 16,488	$ 14,189	$ 12,453
Revenue Requirement	$ 2,315	$ 3,170	$ 2,787	$ 2,441

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10 **IV. REVENUE GROWTH FACTORS FOR RATE YEARS 2 AND 3**

11 **Q. Please briefly describe the Three-Year Rate Plan as proposed by the**
12 **Company.**

13 A. As described in the Company's direct filed case, the Company is proposing a
14 Three-Year Rate Plan with rate changes effective May 1, 2018 (Year 1), May 1, 2019 (Year
15 2), and May 1, 2020 (Year 3). As noted previously, on rebuttal the Company's electric and
16 natural gas Rate Year 1 revenue requirements are based on its originally-filed revenue
17 requirement models, adjusted for known corrections and updates during the pendency of this
18 case, other adjustments agreed to by the Company, as well as its revised functionalized
19 threshold position to reflect an appropriate level of 2017 capital additions. For Rate Years 2

[75] Schuh rebuttal, Exh. KKS-3T, p. 21, Table No. 7.

1 and 3, the electric and natural gas revenue increases are based on revenue growth factors[76]
2 (or an escalation rate) applied to prior year non-ERM and non-gas cost revenues.

3 **A. Revenue Growth Factors – Similarities and Staff/Avista Agreement**

4 **Q. Does Staff witness Mr. Hancock use a similar approach to determine**
5 **Rate Years 2 and 3?**

6 A. Yes. Similar to Avista, Mr. Hancock applies a revenue growth factor
7 (escalation rate) to his base Year 1 revenue to determine Year 2. Year 2 revenues then
8 become the base for determining Year 3.[77]

9 **Q. Are there similarities between Avista and Staff's revenue growth**
10 **factors?**

11 A. Yes. Both Avista and Staff calculate separate electric and natural gas revenue
12 growth factor percentages, consolidated from the weighted average revenue escalation
13 factors of the following components: (1) depreciation; (2) O&M expense; (3) Taxes Other
14 Than Income; and (4) Net Plant After ADFIT). The result of these components are offset by
15 a fifth component (5) Annual Growth in Sales Revenue.[78]

16 **Q. How does Mr. Hancock's electric and natural gas revenue growth factors**
17 **compare to that proposed by the Company on rebuttal?**

[76] The Company labeled this revenue growth factor within its direct filed case a "K-Factor," similar to that used by Puget Sound Energy in 2013 within their multi-year rate plan (Docket Nos. UE-121697 and UG-121705). Nonetheless, based on Mr. Hancock's apparent criticism of the use of this term, the Company is using the term "revenue growth factor."
[77] Hancock, Exh. CSH-1T, p. 34, ll. 21-23.
[78] A complete description of Avista's calculation of its revenue growth factor can be found at Exh. EMA-1T, starting at page 31, line 15. Staff's descriptions of its calculations can be found at Hancock Exh. CSH-1T, starting at p. 34, ll. 16.

1 A. The Company has revised its revenue growth factors for Rate Years 2 and 3
2 to 3.14% for electric and 4.14% for natural gas.[79] This varies from Mr. Hancock's revenue
3 growth factors for Rate Years 2 and 3 of 2.32% for electric and 3.2% for natural gas.[80]
4 Table No. 9 below compares the calculation of the electric revenue growth factor
5 proposed by Avista on rebuttal with that proposed by Staff:[81] (The shaded lines 1, 4 and 5
6 reflect areas of agreement)
7 **Table No. 9 - Electric**
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Line	Avista Revised Revenue Growth Factor Category	(a) Growth Rate	(b) Revenue Portion of Category	(c) Weighted Avg Escalation (a) x (b)
1	Operating Expenses (1)	2.36%	35.74%	0.84%
2	Depreciation/Amortization	9.13%	20.05%	1.83%
3	Taxes Other than Income	4.53%	9.82%	0.44%
4	Net Plant After ADFIT (2)	3.04%	34.40%	1.05%
5	Annual Growth In Sales Revenue (2)		*100.00%*	-1.02%
	Total Escalator %			**3.14%**

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Line	Staff Revenue Escalator Calculation Category	(a) Growth Rate	(b) Revenue Portion of Category	(c) Weighted Avg Escalation (a) x (b)
1	Operating Expenses - (UTC Indices)	2.36%	35.74%	0.84%
2	Depreciation/Amortization	4.70%	20.05%	0.94%
3	Taxes Other than Income	5.13%	9.82%	0.50%
4	Net Plant After ADFIT (2)	3.04%	34.40%	1.05%
5	Annual Growth In Sales Revenue (2)		*100.00%*	-1.02%
	Total Escalator %			**2.32%**

16 Table No. 10 compares the calculation of the natural gas revenue growth factor
17 proposed by Avista on rebuttal with that proposed by Staff: [82] (The shaded lines 1, 4 and 5
18 reflect areas of agreement)
19

[79] Andrews, Exh. EMA-11, p. 1 (electric) and Exh. EMA-12, p. 1 (natural gas).
[80] Hancock, Exh. CSH-4. p. 1 for both electric and natural gas.
[81] Andrews, Exh. EMA-11, p. 1 and Hancock, Exh. CSH-4. p. 1.
[82] Andrews, Exh. EMA-12, p. 1 and Hancock, Exh. CSH-4. P. 1.

1 **<u>Table No. 10 – Natural Gas</u>**

Line	Avista Revised Revenue Growth Factor Category	(a) Growth Rate	(b) Revenue Portion of Category	(c) Weighted Avg Escalation (a) x (b)
1	Operating Expenses (1)	2.03%	41.40%	0.84%
2	Depreciation/Amortization	10.93%	20.13%	2.20%
3	Taxes Other than Income	5.21%	7.33%	0.38%
4	Net Plant After ADFIT (2)	5.02%	31.15%	1.56%
5	Annual Growth In Sales Revenue (2)		*100.00%*	-0.84%
	Total Escalator %			**4.14%**

Line	Staff Revenue Escalator Calculation Category	(a) Growth Rate	(b) Revenue Portion of Category	(c) Weighted Avg Escalation (a) x (b)
1	Operating Expenses - (UTC Indices)	2.03%	41.40%	0.84%
2	Depreciation/Amortization	6.17%	20.13%	1.24%
3	Taxes Other than Income	5.41%	7.33%	0.40%
4	Net Plant After ADFIT (2)	5.02%	31.15%	1.56%
5	Annual Growth In Sales Revenue (2)		*100.00%*	-0.84%
	Total Escalator %			**3.20%**

(1) On rebuttal Avista agrees with Staff's operating expenses growth component.
(2) Staff witness Mr. Hancock supports Avista's Net Plant after ADFIT and Annual Growth in Sales Revenue components.

10 **Q. Did Staff agree with any growth factor components as proposed by**
11 **Avista?**

12 A. Yes. As can be seen in the <u>shaded</u> portions of Table Nos. 9 and 10 above,
13 Mr. Hancock supports the Company's electric "Net Plant after ADFIT" component of 3.04%
14 for electric and 5.02% for natural gas (line 4). Mr. Hancock also supports the Company's
15 "Annual Growth In Sales Revenue" offset of -1.02% for electric and -0.84% for natural gas
16 (line 5).

17 **Q. Does the Company propose to revise any of its components on rebuttal**
18 **based on the recommendations of Mr. Hancock?**

19 A. Yes. As can be seen in the shaded portions of Table Nos. 9 and 10 above (line
20 1), Mr. Hancock proposes to use an individual growth factor for O&M of 2.36% for electric
21 and 2.03% for natural gas. This compares to Avista's as-filed O&M growth factor of 2.55%

1 for electric and 3.26% for natural gas for Rate Years 2 and 3. On rebuttal Avista has revised
2 its O&M growth factor component to agree with Staff's.

3 **Q. Why has the Company revised its O&M growth factor component to**
4 **agree with Staff's?**

5 A. The Company has revised its O&M growth factor component to agree to that
6 proposed by Staff to further try to reach a compromise of positions, and to further minimize
7 the issues in this case. For this case, the level of O&M growth proposed by Staff appears
8 reasonable and provides a sufficient level of incentive for Avista to manage its O&M costs
9 during Rate Years 2 and 3.

10 **B. Revenue Growth Factors– Differences Between Avista & Staff**

11 **Q. Please explain where Avista and Staff do not agree with regards to the**
12 **growth factor components.**

13 A. Mr. Hancock takes exception with the two components "Depreciation" and
14 "Taxes Other Than Income" where Avista has used the historical growth in these
15 components for the period 2013 – 2016. Mr. Hancock, per Exh. CSH-5 uses 2007 – 2016 to
16 determine his historical growth rates for both these components.

17 **Q. Does Mr. Hancock explain his use of the period 2007-2016?**

18 A. No, he does not. He states at page 33, line 10-12 of Exh. CSH-1T, "Staff, as
19 we will explore later, finds it more appropriate to use a longer period of time to evaluate the
20 historical growth in these particular expenses," yet he does not actually do that "later" in his
21 testimony. The Company opposes the change in these growth rates by Mr. Hancock. As
22 shown in Table Nos. 9 and 10 above, Mr. Hancock's depreciation growth factor in

1 particular, is almost half that of Avista's, having the effect of significantly understating
2 depreciation expense in Rate Years 2 and 3. Mr. Hancock's growth rate for Taxes other
3 Than Income, however, is higher than that proposed by the Company.

4 **Q. Why did Avista use the historical period 2013-2016?**

5 A. As noted in the Company's direct testimony,[83] the Washington Commission
6 Basis reports from 2013-2016 provide more current results and are more reflective of the
7 increasing trend in capital investment and related costs. As Avista has discussed in its past
8 few general rate cases, Avista's need for increased capital investment has increased in recent
9 years.

10 **Illustration No. 3[84]**

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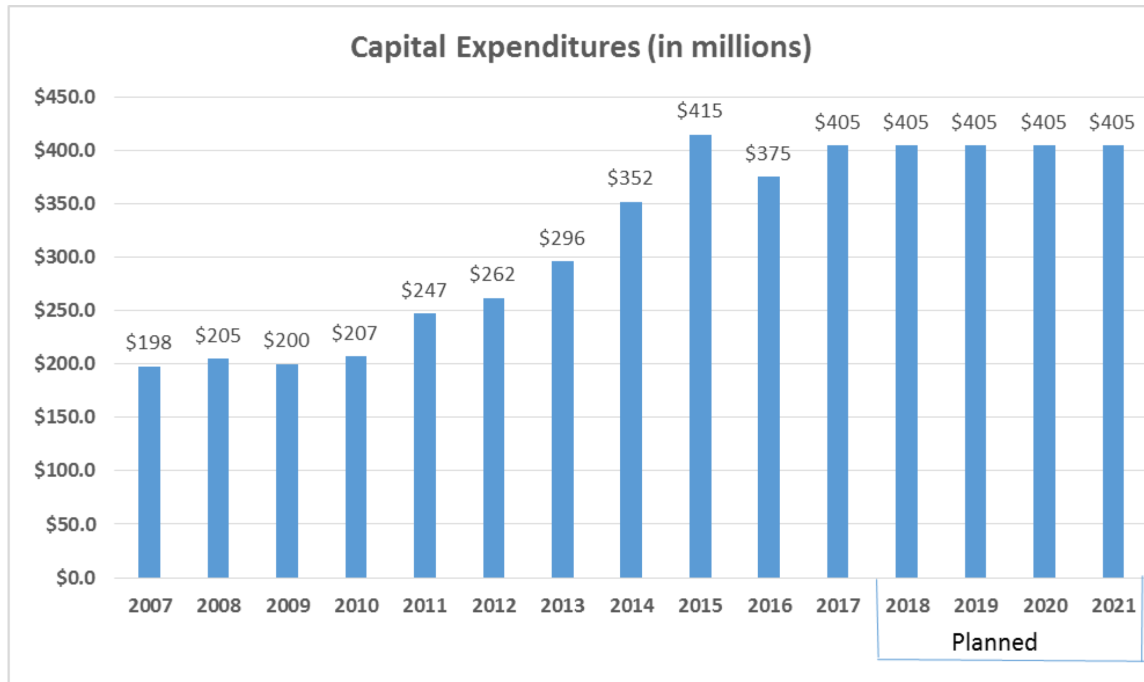

[83] Andrews direct, Exh. EMA-1T, starting at p. 31-37.
[84] Thies direct, Exh. MTT-1T, p. 9, provides a similar illustration for the period 2012-2021. Illustration No. 3 above has been re-produced to include 2007 forward to show the lower level of capital expenditures prior to 2013.

1 As can be seen in Illustration No. 3 above, starting in 2013, the Company began
2 increasing its annual capital investment more significantly than in prior years, until in 2017
3 when it stabilized at $405 million through 2021. The relevance with capital expenditures
4 and growth in rate base for depreciation should be clear – the more recent growth in
5 depreciation is driven by the corresponding growth in capital investment in recent years.
6 This is especially true when there has been a disproportionate growth in shorter-lived assets
7 due to the increased investment in information and technology assets over these same years.
8 (Mr. Kensok discusses the growth in information technology assets within his direct
9 testimony.[85])

10 Taxes Other Than Income also has a direct correlation to the growth in capital
11 investment, as this component is mainly related to growth in property taxes on plant. As
12 growth in plant has consistently increased over recent years, so have the property taxes
13 associated with that plant investment.

14 Based on this information, the Company concluded that the 2013-2016 Commission
15 Basis reports reflect a more current growth level of capital and expenses than prior years,
16 such as the 2007-2016 timeframe proposed by Staff. Furthermore, the growth rates
17 produced from the 2013-2016 historical period more closely represents that expected in Rate
18 Years 2 and 3.
19

[85] Kensok direct, Exh. JMK-1T.

1 **SECTION 2 – CONTESTED ADJUSTMENTS / OTHER DISCUSSION**

2 **V. OTHER IDENTIFIED ADJUSTMENTS TO COMPANY FILED CASE**

3 **Q. Before discussing the other contested adjustments by the parties in this**
4 **case, are there some adjustments that are uncontested by all parties?**

5 A. Yes. Provided as page 1 of Exh. EMA-15, is a listing of 25 electric and 21
6 natural gas adjustments filed by the Company and uncontested by all parties.

7 **A. Contested Adjustments Agreed-to By Avista**

8 **Q. Please explain the contested adjustments the Company accepts on**
9 **rebuttal and has included in its revised revenue requirement.**

10 A. Table No. 11 below provides a listing of adjustments proposed by the
11 identified party that Avista accepts on rebuttal and has included in its revised revenue
12 requirement.

13 **Table No. 11**

14–18

	Electric and Natural Gas Contested Adjustments Accepted by Avista			
Item:	**Adjustment Electric**	**Adjustment Natural Gas**	**Adjustment Name**	**Party Contesting**
a)	2.02	2.02	Restate Property Tax	Staff
		3.06	Pro Forma Property Tax (Nat. Gas)	Staff (contest Public Counsel's adjustment)
b)	2.03	2.03	Uncollectible Expense	Staff
	-	-	Conversion Factor	Staff
c)	2.15	2.14	Restating Incentives	Staff
	3.05	3.05	Pro Forma Incentive Expenses	Staff
d)	3.12	3.12	Pro Forma Director Fees Expense	Staff / ICNU / NWIGU / Public Counsel
e)	3.15	3.14	EOP 2017 Capital Net Rate Base	Staff / ICNU / NWIGU / Public Counsel

19 **Q. Please provide a description of each adjustment shown in Table No. 11.**

20 A. The descriptions that follow explain the adjustments and Avista's acceptance
21 of each adjustment. Exh. EMA-15, page 3 (electric) and page 4 (natural gas) includes each

1 adjustment as part of Avista's as-filed revenue requirement and rate base, as well as that
2 proposed by each party.

3 a) **<u>Restate Property Tax (2.02 – electric and natural gas) / Pro Forma Property Tax</u>**
4 **<u>(3.06 natural gas)</u>**
5
6 Staff witness Ms. White sponsors adjustments to both electric and natural gas
7 restated and pro forma property tax expense based on updated information provided by the
8 Company.[86] Ms. White provided these adjustments in Exh. AIW-2. The Company agrees
9 that restated taxes should be updated to reflect the April 2017 true-up for final 2016 property
10 tax expense and the now available 2017 historical cost assessed values provided by each
11 State (based on 2016 information). It is also appropriate to use this information as the basis
12 for the pro forma property tax expense during the rate-effective period. The Company,
13 consistent with Ms. White has updated Restated Property Tax adjustments (2.02 electric and
14 natural gas) and Pro Forma Property Tax adjustments (3.06 <u>natural gas</u>). However, the
15 Company does not agree with Staff regarding its <u>electric</u> Pro Forma Property Tax adjustment
16 (3.06). As explained below the Company believes Ms. White included a calculation error,
17 that once corrected, would agree with Avista's electric property tax adjustment.[87]
18 The impact of revising Restating Property Tax adjustments (2.02) electric and gas,
19 reduces the Company's as-filed revenue requirement by $664,000 for electric and $122,000
20 for natural gas. The impact of revising Pro Forma Property Tax adjustment (3.06) natural
21 gas, reduces the Company's as-filed revenue requirement by $49,000 for natural gas.[88]

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[86] White, Exh. AIW-1T, pp. 3-5.
[87] Also discussed below is Avista's opposition to the Pro Forma Property Tax adjustment proposed by Mr. Mark Garrett on behalf of Public Counsel.
[88] Avista's proposed electric Pro Forma Property Tax adjustment (3.06) on rebuttal reduces the Company's as-filed revenue requirement by $539,000.

1 **b) Uncollectible Expense (2.03 – electric and natural gas) / (Conversion Factor)**

2 Avista agrees with Staff witness Ms. White's electric and natural gas Uncollectible
3 Expense adjustments reflecting a correction provided by the Company, impacting both
4 Washington electric and natural gas services.[89] The impact of correcting this adjustment,
5 reduces the electric revenue requirement by $205,000, while increasing natural gas revenue
6 requirement by $205,000.[90]

7 As noted by Staff witness Ms. Huang, as result of the Company correcting the
8 uncollectible rate, the Company updated its electric and natural gas conversion factors. The
9 impact of this correction updates the electric conversion factor to 0.619660, and reduces the
10 Company's as-filed revenue requirement by $24,000. In addition, this correction updates the
11 natural gas conversion factor to 0.619798, and reduces the Company's as-filed revenue
12 requirement by $65,000.

13 **c) Restating Incentives (2.15 electric / 2.14 natural gas) and Pro Forma Incentives**
14 **(3.05 electric and natural gas)**
15
16 As noted by Ms. Huang, Staff adjusts Resting Incentives adjustment (2.15 electric /
17 2.14 natural gas) and Pro Forma Incentives adjustment (3.05 electric and natural gas). As
18 described by Ms. Huang, Staff proposes to use a six-year average of actual nominal dollar
19 (rather than six year average percent) payout as the basis for the incentive adjustment and
20 rejects Adjustment 3.05 Forma Incentive.[91]

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[89] White, Exh. AIW-1T, pp. 5-8.
[90] There is an immaterial difference between Avista and Staff's revenue requirement for electric (-$9,000) and gas (+$9,000) from revising uncollectible expense. It is assumed to be related to the impact of the conversion factor.
[91] Huang, Exh. JH-1T, p. 12, ll. 10-12.

1 The Company agrees with Staff to use a six-year average of actual nominal dollars
2 rather than the average percent payout for its Restating Incentive adjustment. Further, to
3 minimize the issues in this case, the Company also accepts Staff's removal of the
4 Company's Pro Forma Incentive adjustments.[92] The net impact to the Company's as-filed
5 revenue requirement of accepting both restating and pro forma incentive adjustments,
6 reduces the electric and natural gas as-filed revenue requirement by $77,000 and $20,000,
7 respectively. However, the Company believes it is important to clear up some
8 misunderstandings in Ms. Huang's testimony.

9 **Q. Ms. Huang stated she took issue with the "2016 Target – at 100%"**
10 **asserting "the HR Department controls the targeted expense level, which potentially**
11 **creates budget-based ratemaking."[93] Is this true?**

12 A. No, it is not true. The Company's objective in this adjustment is to restate
13 test year incentive compensation to reflect a six-year average of payout, and remove the
14 impact of any prior period adjustments. In order to accomplish this, the Company <u>first</u>
15 determines the base amount of incentive expense if 100% of metrics were achieved
16 ("Target"). This was calculated by the Human Resources Department in accordance with
17 guidelines established in the 2016 Short Term Incentive Plan Document ("STIP"). It is
18 important to note that <u>all inputs are known and measurable</u> – the <u>actual</u> 2016 regular
19 earnings, <u>approved</u> eligibility percent per employee, and all <u>approved</u> metrics and associated
20 weighting. These metrics are the basis for a calculated payout expense.

[92] *Id.* p. 14, ll. 8-12.
[93] *Id.* p. 14, ll. 16-18.

1 Once the base is established (effectively eliminating prior period adjustments and the
2 embedded actual payout percent),[94] the second step is to apply the six-year average to the
3 result for determining the restated level of incentives. The combination of the two steps
4 effectively removes the prior period adjustments and replaces the actual level incentive
5 expense with the six-year average level of expense.

6 **Q. Does the Human Resources Department have the ability to "manipulate"**
7 **the calculated base incentive pay ("Target") in order to achieve "any desired expense**
8 **level" as suggested by Staff?[95]**

9 A. No, they cannot. The Human Resource calculated the "Target" payout
10 amount in accordance with the STIP document which was approved by the Company's
11 Board of Directors and subsequently verified by the Company's Internal Audit Department.
12 Human Resources cannot change what an individual was actually paid in earnings during
13 2016, an individual's eligibility percent (unless an employee was promoted into a position
14 that has a different payout percentage), or the metric/weighting of individual metrics. It is
15 not based on any budget estimates, as Staff asserts. The actual payout percent in 2016 was
16 simply replaced with "Target" (or 100%) in order to provide a base to apply the six-year
17 average payout to in order to eliminate the double-counting of the 2016 payout.

18 **Q. Please continue with your discussion of the adjustments accepted by**
19 **Avista on rebuttal.**

20 **d) Pro Forma Director Fees (3.12 electric and natural gas)**

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[94] Absent this first step, applying a six year average to the actual payout expense embedded in the test period, would effectively double-count the impact of the 2016 payout since both the expense and the six-year average percent would contain the impact of 2016.

[95] Huang, Exh. JH-1T, p. 14, ll. 1-2.

1 Ms. Huang, as well as Mr. Mullins on behalf of ICNU/NWIGU and Mr. Mark
2 Garrett on behalf of Public Counsel, oppose the Company's electric and natural gas Pro
3 Forma Director Fee adjustment (3.12)[96]. On rebuttal the Company agrees to remove this
4 adjustment. As discussed by Mr. Thies, a separate docket has been filed with the WUTC on
5 the pending merger with Hydro One. It would be inappropriate at this time to decide on the
6 pro forma level of director fee expense proposed by the Company in its direct filing. The
7 Company believes it would be more appropriate to take this issue up, if it so chooses, in its
8 next general rate case filing, after completion of the merger and the new Board of Directors
9 is established. The impact of removing this adjustment, reduces the Company's as-filed
10 revenue requirement by $394,000 for electric and $113,000 for natural gas.

11 **e) <u>EOP 2017 Capital Net Rate Base (3.15 electric / 3.14 natural gas)</u>**

12 As previously described, Staff, as well as ICNU/NWIGU and Public Counsel oppose
13 the Company's EOP 2017 Capital Net Rate base adjustment.[97] The Company agrees on
14 rebuttal to remove this adjustment. The impact of removing this adjustment, reduces the
15 Company's as-filed revenue requirement by $21,517,000 for electric and $3,260,000 for
16 natural gas. The impact of removing this adjustment also reduces the Company's as-filed
17 rate base balances by $119,874,000 for electric and $13,626,000 for natural gas.

18 **B. <u>Contested Adjustments Opposed By Avista</u>**

19 **Q. Please explain the contested adjustments opposed by the Company on**
20 **rebuttal.**

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[96] Huang, Exh. JH-1T, p. 18, ll. 1-3; Mullins, Exh. BGM-1T, p. 30, ll. 4-7; Garrett, Exh. MEG-1T, p. 24, ll. 18.
[97] Scanlan, Exh. KBS-1T, p. 26, ll. 1-4; Mullins, Exh. BGM-1T, p. 12, ll. 1-3; Garrett, Exh. MEG-1T, p. 22:10-23:7.

1 A. Table No. 12 below provides a listing of adjustments opposed by Avista that
2 are proposed by various parties.

3 **Table No. 12**

	Electric and Natural Gas Contested Adjustments Opposed by Avista			
Item:	Adjustment Number Electric	Adjustment Number Natural Gas	Adjustment Name	Party Contesting
a)	1.03	1.03	Working Capital	Staff
b)	2.17	2.15	Restate Debt Interest (flow through)	Staff / ICNU / NWIGU
c)	2.19	2.16	Restate 2016 AMA Rate Base to EOP	Staff added adj
d)	3.02	3.02	Pro Forma Labor Non-Exec	ICNU / NWIGU / Public Counsel
e)	3.06		Pro Forma Property Tax	Staff / Public Counsel
f)	3.10	3.10	Pro Forma 2017 Threshhold Capital Adds	Staff / ICNU / NWIGU
g)	3.11	3.11	Pro Forma O&M Offsets	Staff
h)	New-A1		New MT Aquatic Invasive Fee	Avista adjustment added on rebuttal
i.)	4.00		Pro Forma Power Supply & Transm Revs	Staff / ICNU / NWIGU / Public Counsel

10 **Q. Please provide a description of each adjustment shown in Table No. 12.**

11 A. The descriptions that follow explain the individual adjustments and Avista's
12 opposition with each as proposed by the contesting party. If applicable, the description also
13 provides the impact on Avista's as-filed revenue requirement for any adjustment the
14 Company is making with regards to the specific adjustment. Exh. EMA-15, page 3 (electric)
15 and page 4 (natural gas) summarizes the contested adjustments by the individual parties and
16 the impact on their specific revenue requirement positions.

17 **a) Working Capital (1.03 electric and natural gas)**

18 This adjustment relates to the proper calculation for working capital based on the
19 Investor Supplied Working Capital (ISWC) method. Both Avista and Staff agree it is
20 appropriate to use the ISWC method, however, disagree on 1) certain account classifications
21 and 2) the method by which the working capital balance is allocated between Avista's five

1 operating divisions: Washington electric, Washington natural gas, Idaho electric, Idaho
2 natural gas, and Oregon natural gas.[98]

3 **Q. Staff witness Ms. Erdahl discusses several reclassification of accounts**
4 **that impact the Company's working capital adjustment. Please describe those**
5 **adjustments for which the Company agrees.**

6 A. The Company reclassified several general ledger (GL) accounts and provided
7 them to Staff in response to Staff Data Request No. 244, which Staff witness Ms. Erdahl
8 included as Exh. BAE-7. As can be seen in Table No. 13 below, these reclassifications,
9 agreed to by Staff and Avista, reduce the rate base for working capital for electric by
10 $4,951,000 and natural gas by $1,143,000. This is the extent of the changes made by Avista
11 on rebuttal. These changes have the effect of reducing the Company's as-filed revenue
12 requirement by $540,000 for electric and natural gas by $125,000.[99]

13 **Q. What additional changes to the Company's working capital does Ms.**
14 **Erdahl propose that the Company does not agree with?**

15 A. First, Ms. Erdahl reclassified four additional GL accounts (Issue #1) and
16 <u>second</u>, revised the method for allocating working capital between Avista's five operating
17 divisions (Issue #2).[100] A summary of these changes compared to Avista's position follows:
18

[98] Erdahl, Exh. BAE-1T, p. 3:18 - 4:3.
[99] See Andrews, Exh. EMA-16, pp. 1-4 for rebuttal adjustment support.
[100] Erdahl, Exh. BAE-1T, starting at p. 7, line 16.

1 **Table No. 13**

	Working Capital (000s)				
		Electric		**Natural Gas**	
	Working Capital - As Filed	$	62.5	$	14.8
	Avista's Proposed Adjustments	$	(5.0)		(1.1)
	Avista's Revised Position - Rebuttal	**$**	**57.5**	**$**	**13.7**
Issue #	**Staff's Proposed Adjustments:**				
1)	Reclassify Cash/Temporary Investments & Idaho Earnings		(2.1)		(0.4)
2)	Revised Allocation Methodology		2.7		(1.8)
	Total Staff's Proposed Adjustments		0.7		(2.2)
	Staff's Position	**$**	**58.2**	**$**	**11.5**

7 Regarding Issue #1, the four accounts reclassified by Ms. Erdahl can be separated
8 into two groups. The first group (Issue #1) includes FERC Account No. 131400 – Cash –
9 Canadian Account and FERC Account No. 136000 – Temporary Cash Investments. Staff
10 has removed these accounts from working capital. The Company has classified these
11 accounts as cash working capital since the interest rate is so low (1.0% interest or less),
12 consistent with the treatment proposed and accepted by Staff in previous Avista dockets
13 before this Commission.[101]

14 The second group of accounts (Issue #1), reclassified by Ms. Erdahl to working
15 capital, includes two Idaho liability accounts for earnings tests in that State, including an
16 account for electric and natural gas. The Company opposes this restatement by Staff for two
17 reasons. First, when the earnings test was ordered in Idaho, interest was not addressed by the
18 Commission, therefore no interest is accrued on this account. The Company, therefore,
19 excludes it from working capital, because to do so would include these accounts in rate base,
20 allowing it to earn a full rate of return, which would be inappropriate based on that ordered

[101] These accounts were included in this manner in Avista Docket Nos. UE-150204 and UG-150205, in which working capital was an uncontested adjustment. This is also the classification used when reviewed and accepted by Ms. Erdahl in Avista Docket Nos. UE-140188 and UG-140189, which was ultimately agreed to through settlement.

1 by the Idaho Commission. The second reason leads us to Issue #2, Avista's issue with Ms.
2 Erdahl's proposal to revise Avista's method for allocating working capital between Avista's
3 five operating divisions: these two accounts are Idaho-related and should have no bearing on
4 Washington operations.

5 **Q. Regarding "Issue #2", please explain why Avista does not agree with Ms.**
6 **Erdahl's proposed method of allocating working capital between Avista's five**
7 **jurisdictions.**

8 A. As explained by Ms. Erdahl, cash working capital is "calculated by
9 subtracting current liabilities from current assets."[102] Current assets include non-interest
10 bearing bank accounts, customer accounts receivable, prepaid expenses, etc. Current
11 liabilities include vendor accounts payable, interest payable, taxes payable, etc. After
12 determining the total overall working capital, Ms. Erdahl proposes to allocate utility working
13 capital between Avista's five jurisdictions based on their respective rate base balances.[103]
14 As I will explain later, Staff, in Avista's 2010 – 2012 general rate cases, expressed
15 opposition to allocating based on rate base. Further, in 2014, Ms. Erdahl said Avista's
16 ISWC in that case was "correct."[104]

17 The Company has gone to great lengths in past years to determine, for each
18 individual asset and liability FERC account included in working capital, what state
19 jurisdiction and service it directly impacts, or if it should be allocated, based on its income
20 statement counterpart. This has the impact of appropriately assigning the proper amount by

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[102] Erdahl, Exh. BAE-1T, p. 5, ll. 13-15.
[103] Erdahl, Exh. BAE-1T, p. 7, ll. 17-19.
[104] Docket Nos. UE-140188 and UG-140189, Erdahl Exhibit No. (BAE-1T), p. 4, line 5.

1 service and jurisdiction to the appropriate operating jurisdiction across Avista's service
2 territories.

3 Table No. 14 below highlights the impact between Avista's method and Staff's
4 method of assigning working capital between Avista's operating divisions.

5 **Table No. 14**

AVISTA METHOD (000s)								
Line #	FERC	Account Description	2016 AMA	ED-WA	ED-ID	GD-WA	GD-ID	GD-OR
1	128150	SPECIAL FUNDS-CS2 GE LTSA ADVA	$ 7.7	$ 5.1	$ 2.6	$ -	$ -	$ -
2	128155	SPECIAL FUNDS-CS2 LTSA ADV-O&M	1.8	1.2	0.6	-	-	-
3	151120	FUEL STOCK COAL-COLSTRIP	2.5	1.6	0.8	-	-	-
4	232110	ACCTS PAY-POWER TRANSACTIONS	(8.4)	(5.6)	(2.9)	-	-	-
5	232130	ACCTS PAY-GAS SUPPLY TRANSACTI	(15.7)	-	-	(7.7)	(3.2)	(4.8)
6		Total - Avista Method	$ (12.2)	$ 2.3	$ 1.2	$ (7.7)	$ (3.2)	$ (4.8)
STAFF METHOD (000s)								
Line #	FERC	Account Description	2016 AMA	ED-WA	ED-ID	GD-WA	GD-ID	GD-OR
7	128150	SPECIAL FUNDS-CS2 GE LTSA ADVA	$ 7.7	$ 3.9	$ 2.0	$ 0.8	$ 0.4	$ 0.6
8	128155	SPECIAL FUNDS-CS2 LTSA ADV-O&M	1.8	0.9	0.5	0.2	0.1	0.1
9	151120	FUEL STOCK COAL-COLSTRIP	2.5	1.3	0.6	0.2	0.1	0.2
10	232110	ACCTS PAY-POWER TRANSACTIONS	(8.4)	(4.3)	(2.2)	(0.9)	(0.4)	(0.7)
11	232130	ACCTS PAY-GAS SUPPLY TRANSACTI	(15.7)	(8.0)	(4.1)	(1.6)	(0.8)	(1.2)
12		Total - Staff Method	$ (12.2)	$ (6.2)	$ (3.2)	$ (1.2)	$ (0.6)	$ (0.9)

13 Within Table No. 14 are five general ledger accounts that have been classified as
14 working capital. The general ledger accounts on lines 1 through 4 are deposits, inventory
15 and accounts payable specifically used for electric service. The general ledger account on
16 line 5 is accounts payable specific to natural gas service. Under Avista's method, it directly
17 assigns each of the five electric or natural gas related balance sheet accounts to their
18 appropriate service, and then allocates the balance sheet based on the appropriate allocation
19 methodology approved by this Commission (similar to their income statement counterparts).
20 For example, line item #1 "Special Funds-CS2 GE LTSA" is related to the Company's
21 electric Coyote Springs 2 generating facility, and so is directly assigned to electric and then
22 allocated based on the Company's Production/Transmission (P/T) Ratio to assign between

1 Washington and Idaho. Staff's method, on the other hand, allocates each balance sheet
2 account based on the rate base method proposed by Ms. Erdahl, thus resulting in
3 inappropriately allocating electric sources of working capital to natural gas, and vice versa.

4 **Q. Ms. Erdahl explains that it is appropriate to use her proposed**
5 **methodology for Avista because it is consistent with the Commission's accepted**
6 **approach to ISWC for Pacific Power, Puget, and Cascade Natural Gas Corporation.[105]**
7 **Do you agree?**

8 A. No, I do not. First, every utility is different and should not be held to the same
9 methodology when that methodology would produce less accurate results. For example,
10 Puget only serves customers in Washington. Cascade Natural gas serves natural gas
11 customers only. Pacific Power is a multi-state, multi-service utility. However, it is my
12 understanding that they allocate across their service territories very differently than Avista,
13 making it even more difficult for Pacific Power to directly assign by balance sheet account,
14 as Avista has done. There may be various reasonable approaches to produce similar results –
15 whereas a one-size fits all approach does not always necessarily work for each utility. This
16 Commission on many occasions treats its Washington utilities differently with regards to
17 various mechanisms, because they operate differently.

18 Rather than consistency between peer utilities, a more important issue for the
19 Commission's consideration is the negative impact on the utility of removing consistency
20 across an individual utility's operating divisions. For example, this same method of
21 determining working capital is approved in Avista's Idaho jurisdiction. Working capital is

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[105] Erdahl, Exh. BAE-1T, Page 4, Lines 5-7.

1 computed monthly for the results of operations report. It would be an administrative burden
2 to have to compute working capital using two different methods each month. Avista
3 believes that being consistent with its other Avista jurisdictions is more important than doing
4 it the same way as other utilities in Washington.

5 **Q. Ms. Erdahl also explains that she does not believe Avista has provided**
6 **support or a detailed explanation of its "new" method which changes from allocating**
7 **by rate base to allocating by balance sheet.[106] Do you agree?**

8 A. No. Avista did not first apply this method of allocating by balance sheet
9 account in this instant case. First the working capital method, i.e., the ISWC method, has
10 been used and approved by this Commission for Avista since its 2010 general rate case.
11 With regards to how it allocates its working capital, its first application of the ISWC method
12 utilized rate base to allocate working capital. However, during each of Avista's 2010
13 through 2012 general rate cases, Staff at that time verbally expressed to the Company their
14 opposition to the use of allocating by rate base, mainly because of the issues described above
15 – electric or gas balance sheet accounts impacting the other service. The Company
16 developed the method that is currently being used today in both its Washington and Idaho
17 jurisdictions, and presented it in its 2014 general rate case (Docket Nos. UE-140188 and
18 UG-140189).

19 Ms. Erdahl in fact was the Staff assigned who reviewed Avista's ISWC in that
20 proceeding (Docket Nos. UE-140188 and UG-140189), and filed responsive testimony
21 <u>accepting</u> the Company's working capital adjustment, because, as she noted "Avista's

[106] Erdahl, Exh. BAE-1T, Page 8, Lines 7-8.

1 analysis is correct."[107] In fact her own exhibit (Exhibit BAE-3) to her testimony, in that same
2 Docket, provided a copy of the Company's adjustment utilizing the Company's allocation by
3 balance sheet method (i.e., exactly what Avista did in this case).

4 Since the 2014 general rate case, the Company has stated in its direct testimony that
5 the Company has prepared its working capital adjustment "consistent with prior rate cases
6 approved by this Commission." It had been referring to the use of the ISWC method. In
7 hind-site, based on the criticism by Ms. Erdahl, the Company should have described its
8 allocation methodology in its 2014 general rate case and again in its 2015 general rate case
9 (since the 2014 GRC was ultimately settled). Neither the 2015 ISWC adjustment, nor its
10 methodology, was contested in the Company's 2015 GRC, and was ultimately approved by
11 this Commission in Docket Nos. UE-150204 and UG-150205.

12 **Q. Please continue with your description of the contested adjustments the**
13 **Company does not agree with.**

14 A. The next contested adjustment is the result of proposed changes to the
15 Company's cost of capital.

16 **b) <u>Restate Debt Interest (2.17 electric / 2.15 natural gas)</u>**

17 The Restate Debt Interest adjustment calculates the tax effect on interest using the
18 Company's proposed weighted cost of debt. This is a flow-through adjustment and will vary
19 based on the cost of capital ultimately approved by this Commission. Currently as Avista
20 continues to propose on rebuttal the use of 5.62% cost of debt and a 50% equity/50% debt

[107] Docket Nos. UE-140188 and UG-140189, Erdahl Exhibit No. (BAE-1T), p. 4:5.

1 capital structure,[108] Avista has no change in this adjustment.

2 **c) Restate 2016 AMA Rate Base to EOP (2.19 electric / 2.16 natural gas)**

3 As previously described, Staff proposes to include its Restate 2016 AMA Rate Base
4 to EOP adjustments. Avista accepts Staff's adjustment to rate base, however, Avista strongly
5 believes it is appropriate to include an increased level of depreciation expense in order to
6 match the rate base included with its associated depreciation expense. The impact of adding
7 this adjustment by Avista, increases the Company's as-filed revenue requirement by
8 $11,635,000 for electric and $2,315,000 for natural gas. The impact of adding this
9 adjustment also increases the Company's as-filed rate base balances by $69,691,000 for
10 electric and $14,160,000 for natural gas.

11 **d) Pro Forma Labor Non-Exec (3.02 electric and natural gas)**

12 As described in Exh. EMA-2, at page 27, the Pro Forma Labor Non-Exec adjustment
13 reflects changes to test period union and non-union wages and salaries, including actual
14 increases approved in 2017, as well as 2018 increases that will go into effect in March of
15 2018. For its part, Staff did not contest the Company's proposed Pro Forma Labor Non-
16 Exec adjustment, and the Company makes no adjustment to that as-filed amounts.

17 **Q. ICNU/NWIGU witness Mr. Mullins proposes removal of the 2018 labor**
18 **increases, assuming these increases were "wage escalations."[109] For its part, Public**
19 **Counsel witness Mr. Mark Garrett proposes the Commission remove half of the**
20 **Company's overall adjustment, stating that is representative of removing the 2018**

[108] Thies rebuttal, Exh. MTT-6T, p. 12.
[109] Mullins, Exh. BGM-1T, p. 30, ll. 8-18.

1 **proposed labor increase.[110] Does the Company agree with these adjustments?**

2 A. No, we do not. First, in response to Public Counsel, removing half of the
3 Company's adjustment is arbitrary and was not supported by analysis and actual data
4 provided through discovery. Second, all increases are known and measureable based on
5 either a union contract or approval by the Compensation Committee of the Board of
6 Directors. Non-union wage increases for 2018 were approved in May of 2017 by the
7 Compensation and Organization Committee, as reflected in its Board minutes.[111] The
8 Commission has previously held that board-approved union and non-union wage increases
9 fulfill the "known and measurable" standard in WUTC rules. The Commission stated in
10 Order 10, in Dockets UE-090134 and UG-090135, page 44, paragraph 105, that:

11 *"Staff and Public Counsel generally agree that known and measurable company*
12 *obligations, such as union wage increases resulting from collective bargaining*
13 *agreements or non-union wage increases approved by the board of directors, are*
14 *proper adjustments."*
15
16 Moreover, Staff witness Ms. LaRue stated in that Docket's hearing transcripts (TR. Vol. IX,
17 p.685, ll. 5-11) that union and non-union wage increases approved by the board are
18 obligations of the Company:

19 ***Q. [Company]:*** *So the only non-executive wage expense that you've recognized as*
20 *being an obligation, if you will, of the company is the union, the increases approved*
21 *in the union collective bargaining agreement which has been approved by the board*
22 *as well?*
23
24 ***[Ms. LaRue]:*** *Correct, and the non-union increases that were approved by the*
25 *board.*
26

[110] M. Garrett, Exh. MEG-1T, pp. 23:20 - 24:8.
[111] The Compensation Board minutes were provided to the parties through discovery by the Company in response to Staff_DR_156C Confidential Attachment A.

1 e) **Pro Forma Property Tax (3.06 electric)**

2 **Q. Please explain the revision to Staff's pro forma electric property tax**
3 **adjustment.**

4 A. Regarding the electric Pro Forma Property Tax adjustment (3.06), as noted
5 above the Company believes Staff witness Ms. White included a calculation error that once
6 corrected, would agree with Avista's electric property tax adjustment. Specifically, an
7 inconsistency was noted between the electric pro forma expense values for Montana in Ms.
8 White's Exhibit AIW-2 on page 6 at row 15, as compared to Exhibit AIW-6 on page 4.
9 Examination of Ms. White's workpapers revealed that her calculation had essentially
10 "double counted" an exclusion for intangible plant in the determination of pro forma
11 Montana property taxes. Correcting for this, Staff's adjustment would agree with the
12 updated adjustment proposed by the Company, reducing the Company's as-filed revenue
13 requirement for electric by $539,000. With this adjustment, property taxes reflect the level
14 of property tax expense during the effective rate period.[112]

15 **Q. Did other parties have proposals with regards to property tax expense?**

16 A. Yes, Public Counsel witness Mr. M. Garrett proposed to include half of the
17 Company's pro forma adjustment.[113] However, Public Counsel's property tax adjustment
18 was a simplistic reduction of the Company's proposed expense that was not supported by
19 analysis and actual data provided through discovery, unlike the proposals of Staff and the
20 Company.

21

[112] See Andrews, Exh. EMA-16, pp. 5-11 for rebuttal adjustment support.
[113] M. Garrett, Exh. MEG-1T, p. 24, ll. 9-16.

1 **f) Pro Forma 2017 Threshold Capital Additions (3.10 electric and natural gas)**

2 As previously discussed by Company witness Ms. Schuh, Staff, ICNU/NWIGU and
3 Public Counsel contest the Company's electric and natural gas Pro Forma 2017 Threshold
4 Capital Additions adjustments (3.10). For Avista's part, as described above, the Company
5 has revised its electric and natural gas adjustments (3.10) to include 2017 capital additions
6 based on its revised "Functionalized Threshold." The impact of revising this adjustment for
7 electric, increases the Company's as-filed revenue requirement by $4,414,000 and rate base
8 by $27,633,000. For natural gas, the impact of revising this adjustment decreases the
9 Company's as-filed revenue requirement by $441,000 and rate base balances by $1,353,000.

10 **g) Pro Forma O&M Offsets (3.11 electric and natural gas)**

11 The Pro Forma O&M Offsets adjustments reflect offsets to O&M expense in Rate
12 Year 1, reflecting O&M savings, reduced load losses etc., as a result of completing specific
13 2017 capital additions included by the Company in its direct filed case. As explained by
14 Staff witness Ms. Scanlan, she removes this adjustment as the specific offsets relate to
15 capital projects which did not qualify as "major" projects under Staff's "0.5% threshold" for
16 2017 capital projects.[114]

17 Avista believes it is appropriate to include this O&M Offsets adjustment to reflect
18 savings associated with 2017 capital projects included in the Company's rebuttal filing. In
19 response to discovery, as well as additional review of projects included within the
20 Company's rebuttal "functionalized threshold" adjustment, the Company has revised its
21 electric and natural gas O&M Offsets adjustment (3.11), reflecting a reduction to expense of

[114] Scanlan, Exh. KBS-1T, pg 23:13-24:21.

1 $1.1 million for electric and $5,000 for natural gas. As noted previously, this adjustment
2 includes a reduction to expense of $800,000 related to the project "Street Light Conversion
3 to LED Fixtures" (ER 2584), even though this project is not included as one of the threshold
4 selected projects – i.e., no associated capital has been included. This provides a 10%
5 reduction in the electric revenue requirement amount included related to the 2017 capital
6 additions.[115]

7 The impact of updating this adjustment by Avista, decreases the Company's electric
8 as-filed revenue requirement by $120,000, while increasing the natural gas as-filed revenue
9 requirement by $28,000.[116]

10 **h) <u>Montana Aquatic Invasive Fee (New A-1)</u>**

11 As Avista noted within its direct filed case, Andrews Exh. EMA-2, page 10, footnote
12 2, after completion of the Company's revenue requirement, the Company learned of the
13 impact of a new aquatic invasive species fee, to be paid to the State of Montana, related to
14 the Company's Noxon Rapids hydroelectric generating facility, beginning July 1, 2017. The
15 fee is based on FERC-approved Name Plate Capacity, which for Noxon is 488 MW. The fee
16 is to be paid quarterly to the State at $795.76 per MW ($388,330.88), or approximately $1.6
17 million annually. Washington's share of this expense is $1,021,000. Inclusion of this
18 adjustment (New A-1) by the Company, increases its as filed electric revenue requirement by
19 $1,071,000. This known increase in expense was not addressed by Staff, or other
20 intervening party.[117]

21

[115] Electric Pro Forma threshold adjustment revenue requirement total ($11.6 million) versus electric O&M adjustment (-$1.2 million).
[116] See Andrews, Exh. EMA-16, p. 12 for rebuttal adjustment support.
[117] See Andrews, Exh. EMA-16, pp. 13-14 for rebuttal adjustment support.

1 **i) Pro Forma Power Supply and Transmission Revenues (4.00 electric)**

2 Staff, as well as ICNU/NWIGU and Public Counsel propose to remove the Pro
3 Forma Power Supply adjustment as proposed by the Company, arguing the Commission
4 should reject any update to base power supply costs.[118] Company witnesses Mr. Kalich and
5 Mr. Johnson respond to the parties' objections within their rebuttal testimonies.[119] No
6 additional adjustment is made to the Company's as-filed revenue requirement from that
7 originally filed including $16,602,000.

8
9 **VI. OTHER INTERVENING TESTIMONY –**
10 **MR. MULLINS ON BEHALF OF ICNU/NWIGU**
11
12 **Q. Mr. Mullins, representing ICNU and NWIGU, provided electric and**
13 **natural gas Attrition Study models. What was the purpose of these Studies?**

14 A. Mr. Mullins does not support the Three-Year Rate Plan, as proposed by
15 Avista and supported by Staff. He does however, suggest if this Commission were to
16 approve a Three-Year Rate plan, his electric and natural gas Attrition Studies "produces a
17 more informed view of revenue requirement than the K-Factor Study [prepared by
18 Avista]."[120] For Rate Year 2 (May 1, 2019), his electric and natural gas Attrition Studies
19 (including an escalation of depreciation expense and operating expenses) result in increases
20 of approximately $5.1 million and $1.4 million, respectively. For Rate Year 3 (May 1,

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[118] Gomez, Exh. DCG-1CT, p. 3, ll. 16-18; Mullins, Exh. BGM-1T, pp. 31:10-32:11; Wilson, Exh. RSW-1CT; p. 4, ll. 18-20.
[119] Kalich rebuttal, Exh. CGK-4T and Johnson rebuttal, Exh. WGJ-6T.
[120] Mullins, Exh. BGM-1T, p. 20, ll. 10.

1 2020), his electric and natural gas Attrition Studies result in increases of $5.0 million and
2 $1.4 million, respectively.[121]

3 **Q. Are the results of Mr. Mullins' Attrition Studies reasonable?**

4 A. No. Mr. Mullins merely dusted off his 2016 prior Avista general rate case
5 attrition studies, extending them out through 2020, claiming these results are superior to that
6 produced using a "K-Factor" approach as proposed by the Company (and now also
7 supported by Staff). Consistent with my testimony in Docket Nos. UE-160228 and UG-
8 160229, these studies are fraught with inconsistent trending periods and understated growth
9 factors, significantly understating the revenue requirement need and producing results that
10 are not reasonable or appropriate.

11 In the prior case, both Company witness Dr. Forsyth[122] and I discussed the
12 methodological issues with Mr. Mullins' electric and natural gas attrition analyses.
13 Specifically, inconsistencies related to the years chosen by Mr. Mullins between the periods
14 2000-2016 (Mr. Mullins updated most categories to include 2016 data in this case), which
15 vary depending upon the specific category of cost he is trending. The second issue relates to
16 his regression trending analysis applied to each category of cost,[123] which is inconsistently
17 and inappropriately applied across his electric and natural gas models.

18 As noted in Docket Nos. UE-160228 and UG-160229, Mr. Mullins varies the years

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[121] Mr. Mullins also provides Attrition Study results excluding an escalation of depreciation expenses and operating expenses. For Rate Year 2 (May 1, 2019), these electric and natural gas Attrition Studies produce revenue increases of $164,285 and $354,947, respectively. For Rate Year 3 (May 1, 2020), these electric and natural gas Attrition Studies result in increases of $161,562 and $305,667, respectively.

[122] Docket Nos. UE-160228 and UG-160229, Forsyth rebuttal, Exhibit No. (GDF-1T),

[123] Mr. Mullins disaggregates Avista's expense cost categories into multiple categories (10 electric, 11 natural gas) and separated ADFIT from Net Plant, producing multiple plant categories (6 electric, 4 natural gas).

1 he chooses to trend depending on the cost category. For electric, his data series by cost
2 category ranges anywhere from 2005-2016, as is the case with "Distribution Taxes Other
3 Than Income," to only 2013-2016 for "Accumulated Deferred Income Taxes." He even goes
4 so far as to include one data series, Distribution O&M expenses, where he includes 2011-
5 2014 and 2016, and excludes the year 2015.[124] For Natural gas, however, he has several data
6 series that range from 2000-2016, such as "Administrative and General Depreciation
7 Expense," to only 2012-2016 for "Administrative and General Expenses." For natural gas
8 "Accumulated Deferred Income Taxes", he trends the 2009-2016 time period.[125] However it
9 is unclear why Mr. Mullins chooses these variations, and especially why he uses, in several
10 instances, the entire time period for natural gas, but chooses to truncate the time period for
11 electric.

12 His inconsistencies between categories, especially as it relates to depreciation
13 expense, plant and ADFIT, produces mixed results and do not reflect what one would expect
14 during the rate effective periods.

15 **Q. Does that conclude your rebuttal testimony?**

16 A. Yes, it does.

[124] Mullins, Exh. BGM-5.
[125] Mullins, Exh. BGM-6.