Exhibit BGM-9T
Dockets UE-170485/UG-170486
Witness: Bradley G. Mullins

BEFORE THE

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION Complainant, v. AVISTA CORPORATION d/b/a AVISTA UTILITIES Respondent.	)	DOCKETS UE-170485 and UG-170486 (*Consolidated*)

CROSS-ANSWERING TESTIMONY OF BRADLEY G. MULLINS

ON BEHALF OF

THE INDUSTRIAL CUSTOMERS OF NORTHWEST UTILITIES

AND

THE NORTHWEST INDUSTRIAL GAS USERS

December 1, 2017

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CROSS-ANSWERING TESTIMONY OF BRADLEY G. MULLINS

I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Bradley G. Mullins, and my business address is 333 SW Taylor Street, Suite 400, Portland, Oregon 97204.

Q. ARE YOU THE SAME BRADLEY G. MULLINS WHO PREVIOUSLY FILED TESTIMONY IN THIS PROCEEDING?

A. Yes. I previously filed Response Testimony on behalf of the Industrial Customers of Northwest Utilities and the Northwest Industrial Gas Users on revenue requirement issues associated with the rate filing of Avista Corporation ("Avista" or the "Company") in this matter before the Washington Utilities and Transportation Commission (the "WUTC" or the "Commission").

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

A. I respond to the Response Testimony of the Staff of the WUTC ("Staff") on revenue requirement issues, particularly in regard to Staff's rate plan proposal. More specifically, I discuss the Response Testimony of Staff witnesses Christopher S. Hancock and Kathi B. Scanlan.

II. STAFF'S RATE PLAN PROPOSAL

Q. DOES STAFF SUPPORT A MULTI-YEAR RATE PLAN FOR THE COMPANY?

A. Yes. Staff witness Christopher Hancock testifies that "[t]he Commission should approve a multi-year rate plan."[1/]

1/ Hancock, Exh. CSH-1T at 19:1.

Q. ON WHAT BASIS DOES STAFF RECOMMEND APPROVAL OF A MULTI-YEAR RATE PLAN?

A. Staff's basis is not entirely clear. For instance, Staff testifies that "one of the primary purposes of a multi-year rate plan" is to "combat attrition,"[2/] yet Staff seems to disclaim any attrition-related basis for its multi-year rate plan recommendation: "To be clear, Staff's multi-year rate plan is not based on an attrition analysis and does not include any attrition adjustments."[3/]

Likewise, Staff explains that a multi-year rate plan "is a solution to regulatory lag, in that the prices a utility charges its customers are updated in a manner consistent with the changes that the utility itself faces."[4/] Notwithstanding, Staff testifies that "[r]egulatory lag is neither good nor bad," and even emphasizes: "<u>Regulatory lag serves as an important tool for regulators and the public</u>."[5/] More specifically, Staff believes that regulatory lag is only "bad" when "costs are unavoidable, *and* when those costs threaten a regulated utility's financial position," such that "regulatory lag causes attrition."[6/] As just noted, however, Staff disclaims an attrition-related basis for its multi-year rate plan recommendation, meaning Staff itself is not claiming any need to address "bad" regulatory lag caused by allegedly unavoidable costs beyond the control of the utility, or which threaten Avista's financial position.

2/ <u>Id.</u> at 13:4-5.

3/ <u>Id.</u> at 8:2-3.

4/ <u>Id.</u> at 17:4-6.

5/ <u>Id.</u> at 7:10, 14 (emphasis by Staff).

6/ <u>Id.</u> at 7:15-17 (emphasis by Staff).

Accordingly, I am uncertain as to why Staff feels any need to support a multi-year rate plan as "a solution to regulatory lag" in this proceeding. In fact, I agree with Staff that "[t]he argument for regulatory lag …. [I]s equally deserving of hearing," since it "imposes discipline on utility operations and investment decisions, thus encouraging efficiency."[7/] This would seem to compel allowance for the "positive advantage" of regulatory lag to take effect, rather than attempting to solve a non-existent regulatory lag problem via unnecessary rate escalation, for the very reasons Staff cites: "Freezing rates for the period of the lag imposes penalties for inefficiency … and offers rewards for their opposites: companies can for a time keep the higher profits they reap from a superior performance and have to suffer the losses from a poor one."[8/]

Q. HAS AVISTA BEEN SUFFERING FROM RECENT LOSSES?

No. As I demonstrated in my Response Testimony, Avista most recently reported "a position of severe overearning in 2016," which has been even more pronounced for the electric business line since 2013.[9/] The Company's "historical pattern of actual earnings indicate a very healthy utility,"[10/] such that I am at a loss to reasonably explain why Staff would surmise that there is a regulatory lag problem which must be "solved" by the establishment of a multi-year rate plan.

7/ Id. at 9:9-12.

8/ Id. at 9:13-19 (quoting Alred Kahn, *The Economics of Regulation: Principles and Institutions*, Vol. II, p. 48 (1988)).

9/ Mullins, Exh. BGM-1T at 7:2-8 & Table 1.

10/ Id. at 7:5.

Q. DOES STAFF PROVIDE ANY OTHER RATIONALE IN SUPPORT OF ITS MULTI-YEAR RATE PLAN RECOMMENDATION?

A. Yes. Staff believes a multi-year rate plan is "a good idea" in this proceeding for the following reasons: 1) "More predictable revenues for utilities, bolstering their financial health"; 2) "More predictable rates for customers"; 3) "Stronger performance incentives"; 4) "Timely recovery of costs for new capital projects"; and 5) "Fewer general rate cases over time."[11/]

Q. DO YOU AGREE WITH THESE PURPORTED BASES FOR ADOPTION OF A MULTI-YEAR RATE PLAN FOR AVISTA?

A. No, neither individually nor in sum. First, the Company is in no need of "bolstering their financial health" by means of a rate plan, especially on the electric side, given an average return on equity equal to 10.7% since 2013.[12/] Indeed, Staff's own cost of capital witness has recommended a substantial reduction to the Company's authorized return on equity in this proceeding, from 9.5% down to 9.1%.[13/]

Second, providing "more predictable rates for customers" cannot be presented as any benefit to customers if "predictable" rate increases within a rate plan proposal are not actually justified. My Response Testimony explains, in some detail, why the Company's rate plan proposal is unjustified.[14/] Moreover, as I explain below, Staff's alternative rate plan escalation factors are also unsupportable, rendering no customer benefit to be assigned to rate increase "predictability." In fact, Staff presents the "more predictable

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11/ Hancock, Exh. CSH-1T at 17:8-10, 16:6-11 (citing Ken Costello, National Regulatory Research Institute, *Multiyear Rate Plans and the Public Interest* at 16 (October 2016)).

12/ Mullins, Exh. BGM-1T at 7:6-7.

13/ Parcell, Exh. DCP-1T at 4:12-13.

14/ See Mullins, Exh. BGM-1T at 13:1-21:13.

rates for customers" basis for a rate plan as being among the "benefits identified from a *utility* perspective,"[15/] not a ratepayer perspective.

Third, supplying "stronger performance incentives" via a rate plan is wholly unnecessary, for the reason Staff itself supplies as an argument "for" regulatory lag: "Freezing rates for the period of the lag imposes penalties for inefficiency … and offers rewards for their opposites: companies can for a time keep the higher profits they reap from a superior performance and have to suffer the losses from a poor one."[16/] Further, as Staff also explains, "[r]egulatory lag also serves as a disincentive to overcapitalization, or 'gold-plating.'"[17/] As the Commission is probably aware, "gold-plating" is a charge that has been aimed at the Company for years.

Fourth, I am deeply concerned about the propriety of allowing for recovery of new capital project costs through escalation factors supporting multi-year rate plan increases, given the inability to justify such rate increases on the basis of known and measurable and used and useful plant. Mr. Hancock identifies various methods of escalating plant in future rate years, and testifies that "Staff adopts a form of the second approach identified … otherwise known as 'the Avista approach.'"[18/] Staff defines "the Avista approach" as "Avista's projected net plant additions through the course of the rate plan …."[19/] By adopting the Avista approach, Mr. Hancock concedes that Staff is "…

[15/] Hancock, Exh. CSH-1T at 16:4-5 (emphasis added).

[16/] Id. at 9:13-19 (quoting Alred Kahn, *The Economics of Regulation: Principles and Institutions*, Vol. II, p. 48 (1988)).

[17/] Id. at 10:4-5.

[18/] Id. at 40:3-10, 41:11-13.

[19/] Id. at 40:6-7.

forgoing *any* consideration of historical rates of plant addition."[20] Thus, Staff's support for a rate plan, on the basis of alleged timely recovery for new capital projects, is completely untethered to the Commission's reliance on a modified historical test year. Also, intentionally forgoing "any" consideration of historical plant means that Staff's capital escalators have absolutely no nexus to foundational WUTC ratemaking principles—such as including only costs which are known and measurable or used and useful in rates.

Fifth, I addressed the shortcomings of a multi-year rate plan justified on the basis of producing "fewer general rate cases over time" in Response Testimony. For example, while annual rate case filings may not be ideal, requiring Avista to justify proposed rate increases has notable benefits, as this deters frivolous escalations, encourages rate stability, and allows the Commission to establish rates holistically and equitably.[21]

Q. PLEASE ELABORATE ON YOUR STATEMENT THAT "STAFF'S ALTERNATIVE RATE PLAN ESCALATION FACTORS ARE ALSO UNSUPPORTABLE."

A. Essentially, Staff's rate plan escalation factors do not differ substantially from Avista's—as affirmed by Mr. Hancock's admission to adopting a form of "the Avista approach" in this proceeding—which is why I stated that Staff's factors are "also" unsupportable.

As discussed in my Response Testimony, the escalation factors supporting the Company's multi-year rate plan proposal are materially flawed,[22] and these same flaws

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20/ Id. at 40:18-19 (emphasis added).

21/ Mullins, Exh. BGM-1T at 19:3-9.

22/ See id. at 13:1-21:13.

apply to Staff's similar approach. For instance, Avista's K-factor revenue increases "do not represent discrete capital additions or revenue requirement items," in contrast to a recent rate plan that the Commission approved for Pacific Power and Light Company.[23/] Also, the Avista escalation approach is actually a step backwards, or a regression from the more granular approach supporting similar attrition analyses in prior rate cases, meaning that, regardless of the flaws I would attribute to prior escalation studies, "… the driving factors behind the results of the K-factor study are even more difficult to ascertain."[24/] This lack of granularity—common to both the Avista and Staff approach, which "aggregates the historical trending data,"[25/] instead of detailing the historical trends by more specific major cost categories—makes it impossible to determine whether escalations over the multi-year rate plan "are due to factors beyond Avista's control," which would presumably need to be proven in order to depart from the modified historical ratemaking approach.[26/]

Q. DO YOU CONSIDER THE ALLEGED DISTINCTIONS BETWEEN STAFF AND AVISTA ESCALATION FACTORS TO BE MEANINGFUL?

A. No. Staff acknowledges that its "rate plan structure is similar to that of the company," but claims there are "… meaningful distinctions."[27/] In my opinion, however, the alleged distinctions amount to semantics more than substantive and meaningful differences that would be relevant to the Commission's consideration of salient ratemaking principles.

23/ Id. at 19:10-12.

24/ Id. at 15:13-14.

25/ Id. at 14:12-15.

26/ Id. at 15:15-19.

27/ Hancock, Exh. CSH-1T at 34:19-20.

For example, Staff rejects an escalation methodology that "… skirts too close to weighing in on the prudency of plant additions that have [not] yet occurred."[28/] Notwithstanding, Mr. Hancock admits that Staff is adopting a methodological approach similar to Avista's, which "is tantamount to authorizing interim recovery of capital costs, while deferring a permanent decision on the prudency of specific capital additions until a later rate case."[29/] From a customer perspective, this alleged distinction between the method Staff rejects and the method adopted, which is similar to Avista's, is functionally irrelevant. Either way, customers are forced to pay for capital additions prior to a prudency decision based on known and measurable costs. Worse, the burden of proof is also effectively flipped onto ratepayers, to disprove the fairness of rates already collected during some future case.

Likewise, Mr. Hancock attempts to distinguish Staff's escalation approach from Avista's, by stating that "Staff is not setting revenue requirements based on the projected level of rate base and net plant in future years, as is effectively the case with Avista's proposal."[30/] Yet, immediately thereafter, Mr. Hancock testifies that Staff is developing an escalation rate "by finding the percent growth in rate base *that Avista expects* over the course of the rate plan."[31/] Putting strained semantics aside, such testimony plainly seems to indicate that Staff's escalation method *does* rely on "projected" costs in future years, just like Avista's proposal. In fact, Staff pointedly rejects an approach of "not

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28/ Id. at 41:21-23.
29/ Id. at 42:15-21.
30/ Id. at 43:9-10 (emphasis omitted).
31/ Id. at 43:11-13 (emphasis added).

escalating plant at all," precisely because of "Avista's representations about its capital spending program."[32/] Accordingly, quite contrary to the Commission's recent concerns about allowing for a "self-fulfilling prophecy," in which Avista rates simply match what the Company chooses to project in future spending,[33/] Staff's multi-year rate plan approach would seem to facilitate that end, by developing escalation rates purposely based on Avista expectations of future spending representations.

Q. IS STAFF'S MULTI-YEAR RATE PLAN PROPOSAL UNDERMINED BY THE TESTIMONY OF ANY OTHER STAFF WITNESS?

A. Yes. I agree with many of the points that Ms. Scanlan makes in testimony concerning the application of Commission standards, based on modified historical test year ratemaking practice and pro forma policy. But, Ms. Scanlan's testimony severely undercuts the premise for Staff's proposed escalation factors in a multi-year rate plan.

Q. PLEASE EXPLAIN.

A. In opposing certain Avista revenue requirement increase proposals, Ms. Scanlan testifies to the Company's failure to align requests with fundamental WUTC standards such as "known and measurable" and "used and useful" ratemaking principles, which are examined in some detail in her testimony.[34/] As noted above, however, Staff's rate plan proposal is essentially premised upon wholesale projections of Company cost

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32/ Id. at 42:7-9.

33/ See, e.g., WUTC v. Avista, Dockets UE-160228 and UG-160229 (Consolidated), Order 06 at ¶ 55 (Dec. 15, 2016); WUTC v. Avista, Dockets UE-150204 and UG-150205 (Consolidated), Order 05 at ¶¶ 119-20 (Jan. 6, 2016). See also WUTC v. Wash. Water Power Comp., Cause Nos. U-81-15 and U-81-16 (Consolidated), 1981 WL 721420, Second Suppl. Order (Nov. 25, 1981) (rejecting a "projected budget" in favor of using the traditional historical test year approach, after Staff pointed out that "[f]orecasts tend to be self-fulfilling prophecies").

34/ See, e.g., Scanlan, Exh. KBS-1T at 5:20-6:14, 10:6-12:6, 14:1-15:12.

expectations, which Mr. Hancock describes as "… forgoing *any* consideration of historical rates of plant addition."[35/] By definition, there can be no support for such an approach, since there is nothing either known and measurable or used and useful about forecasts divorced entirely and purposely from "any" historical plant considerations.

In fact, Ms. Scanlan's rationale for rejecting all forecasts of the Company's capital additions, after August 31, 2017, can be fairly applied as a basis to reject Staff's proposed escalation rate in years 2 and 3 of the rate plan, since Mr. Hancock's proposed escalation rate is developed from forecasts—i.e., "by finding the percent growth in rate base that Avista expects over the course of the rate plan."[36/] That is, Ms. Scanlan argues:

> Staff rejects the remainder of the forecasted capital additions. The Company's forecasts are just that – forecasts, which have not occurred as transfers to plant. Staff cannot attest that the Company's forecasts accurately reflect actual project costs, the prudence of those final costs, offsetting factors, or whether the project will be used and useful to ratepayers in the rate year. In addition, the Company's forecasts for 2017 and previous general rate case plant transfers to plant *have been substantially inaccurate* ….[37/]

Similarly, I believe that the same ratepayer risks identified by Ms. Scanlan, in the context of potentially accepting Avista's forecasts of major pro forma proposals, would apply equally to the potential acceptance of Mr. Hancock's proposal to escalate rates based on "projected" plant growth under the Avista approach: "… the Company's proposal

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35/ Hancock, Exh. CSH-1T at 40:18-19 (emphasis added).

36/ Id. at 43:11-13.

37/ Scanlan, Exh. KBS-1T at 23:1-9 (emphasis added) includes forecasted plant balances and puts the risk of error or delayed transfers to plant *entirely on ratepayers*. Many of those forecasts have been historically inaccurate."[38]

Q. WHAT IS YOUR RECOMMENDATION REGARDING THE STAFF RATE PLAN PROPOSAL?

A. Staff's multi-year rate plan proposal should not be approved, for many of the same reasons that Avista's rate plan proposal should be rejected. Additionally, Staff has presented confusing and conflicting policy support for its own plan, which does nothing to merit the establishment of Commission precedent that would be difficult for the public and future parties to understand or apply.

Q. DOES THIS CONCLUDE YOUR CROSS-ANSWERING TESTIMONY?

A. Yes.

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[38] Id. at 30:3-5 (emphasis added).