

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In re the Matter of	)	DOCKET NO. UE-010395
	)	
AVISTA CORPORATION d/b/a	)	POSTHEARING BRIEF OF THE
AVISTA UTILITIES	)	INDUSTRIAL CUSTOMERS OF
	)	NORTHWEST UTILITIES
Request Regarding the Recovery of Power	)	
Costs Through the Deferral Mechanism	)	
_____	)	

**I. INTRODUCTION**

On July 17, 2001, Avista Corporation (“Avista” or the “Company”) filed a petition (the “Petition”) requesting that the Commission approve a 36.9% rate surcharge for the Company’s Washington ratepayers for a period of 27 months, and that the Company be allowed to accelerate the amortization of the credit related to the monetization of the Company’s power sale to Portland General Electric Company (“PGE”). The Industrial Customers of Northwest Utilities (“ICNU”) submits this posthearing brief and requests that the Washington Utilities and Transportation Commission (“WUTC” or “Commission”) deny the relief requested in the Petition. If the WUTC does not deny the Petition, in the alternative, ICNU requests that the Commission adopt the proposal made by ICNU witness Don Schoenbeck (the “Schoenbeck Proposal”).

If the Commission elects to grant Avista some form of rate relief, the following factors suggest that it would be inappropriate to give Avista all of the relief that it requests:

1. The evidence shows that Staff, as well as other parties, had insufficient time to analyze all of the factors set forth in WUTC v. Pacific Northwest Bell Tel. Co., WUTC Docket No. U-72-30tr, Second Supp. Order Denying Petition for Emergency Rate Relief at 3 (Oct. 10, 1972) (“PNB”). The adequate hearing requirement of the PNB standard has not been met.

- 1 2. Avista’s unregulated operations were a substantial cause of Avista’s current  
2 financial crisis. Despite the claims of Avista Witness John Eliassen at the  
3 hearing, the rating agency reports establish that the decline in Avista’s credit  
4 rating from an A rating in 1998 to its current BBB- rating was in large part  
5 due to the losses and increased risks of Avista’s unregulated operations.  
6 Absent Avista’s unregulated operations, it would be in a much better financial  
7 position to deal with its alleged lack of liquidity.
- 8 3. In April 2001, Avista entered into a Stipulation under which it intended to  
9 avoid any power cost rate increases until 2003. Avista apparently was not  
10 forthcoming to the Commission, Commission Staff (“Staff”), Public Counsel  
11 or ICNU about the risks involved in the implementation of the Stipulation. In  
12 particular, Avista failed to disclose its internal projections of worsening hydro  
13 conditions.
- 14 4. Adoption of either the Avista or Staff proposals will result in rate shock. The  
15 speed and size of the proposed rate increase is particularly shocking because  
16 the Company informed its customers in May 2001 that rates would likely not  
17 increase due to power costs until at least 2003. Staff’s proposal to apply the  
18 rate surcharge on an equal cents per kilowatt hour basis, instead of an equal  
19 percentage basis, exacerbates the rate shock for large industrial and  
20 institutional customers purchasing power under Schedule 25.
- 21 5. The Commission has not determined that recovery of power costs through a  
22 deferral mechanism is appropriate or that Avista’s deferred power costs were  
23 prudent. Thus, the conditions for recovery of deferred power costs have not  
24 been met, and approving Schedule 93 as proposed is premature.
- 25 6. Avista may have viable alternatives other than a rate increase to deal with its  
26 alleged poor liquidity, including, but not limited to: 1) tapping into substantial  
27 earnings from subsidiaries; 2) cutting costs and delaying capital spending;  
28 3) issuing new equity; 4) issuing more debt; and 5) selling either part or all of  
29 its equity investment in Coyote Springs II. The evidence presented at the  
30 hearing shows that Avista is investigating or implementing many of these  
31 alternatives, and they are not included in the financial analysis performed by  
32 Staff. Thus, Avista’s poor financial situation may be overstated, or may  
33 improve in the near future.
- 34 7. Avista’s proposal for a 36.9% rate surcharge for 27 months is based on past  
35 costs that may not be prudent, and on highly speculative forecasts of future  
36 market and hydro conditions that may not prove accurate.
- 37 8. The relief requested by Avista, including a request for interim rate relief, is  
38 more appropriately addressed in conjunction with a general rate case, because

1 it will allow the Commission to evaluate all of the statutory and Commission  
2 established factors for interim rate relief and power cost deferrals.

- 3 9. As noted by Mr. Schoenbeck, given the magnitude and timing of the rate  
4 surcharge, and the economic conditions in the Spokane area, the subject to  
5 refund requirement is not an adequate remedy.

6 The factors described above support a Commission determination that no rate  
7 relief should be granted to Avista at this time. However, if the Commission is inclined to grant  
8 some relief, it should be held to the absolute minimum necessary. Under these circumstances,  
9 the proposal advanced by ICNU witness Don Schoenbeck is the most reasonable solution,  
10 because it is tied to costs actually incurred by Avista and levels of deferred power cost recovery  
11 that Avista is likely to receive in the future. Accordingly, ICNU requests that the Commission  
12 deny the Petition, or in the alternative, adopt the Schoenbeck Proposal. Furthermore, the  
13 Commission should direct Avista to investigate, and where appropriate implement, alternatives  
14 other than rate increases to address its alleged short-term lack of liquidity.

## 15 **II. BACKGROUND**

### 16 **A. Procedural Summary**

17 On June 22, 2000, Avista filed a petition in Docket No. UE-000972 requesting  
18 authorization to defer certain power costs related to higher wholesale market prices. Re Avista,  
19 WUTC Docket No. UE-000972, Petition of Avista Corporation (June 22, 2000). Avista  
20 estimated that the amount of the deferral would be \$29 million for the period from July 2000  
21 through December 2000. Id. at 2. On August 9, 2000, over the objections of Public Counsel and  
22 ICNU, the WUTC approved the power cost deferral for the period from July 1, 2000, ending  
23 June 30, 2001, pending a demonstration, *inter alia*, that the deferred costs were prudently  
24 incurred and that recovery of those costs through a deferral mechanism was appropriate.

1 Re Avista, WUTC Docket No. UE-000972, Order Granting Deferral Of Power Cost Expenses  
2 Pending Demonstration of Prudence (Aug. 9, 2000).

3           On December 20, 2000, Avista requested authority to modify the deferral to  
4 include costs related to increased system load requirements. Re Avista, WUTC Docket No.  
5 UE-000972, Request for Modification of Original Petition of Avista Corporation (Dec. 20,  
6 2000). Staff concluded that Avista’s “proposal [was not] in the public interest and recommended  
7 setting the matter for hearing.” Re Avista, WUTC Docket No. UE-000972, Order Granting  
8 Request To Modify Power Cost Deferral Mechanism (Jan. 24, 2001). Staff maintained that the  
9 modified deferral mechanism “resemble[d] those that were either rejected, found inappropriate,  
10 or terminated in the past because of failure to satisfy certain criteria enunciated by this  
11 Commission.” Id. at 1. As a result, the Commission adopted Staff’s alternative recommendation  
12 to approve the modification, but ordered Avista to file a proposal that would address certain  
13 power cost issues by March 20, 2001. Those issues included: a) the prudence of the incurred  
14 power costs; b) the optimization of the Company-owned resources to the benefit of retail  
15 customers; c) the appropriateness of recovery of power costs through a deferral mechanism; d) a  
16 proposal for cost of capital offsets to recognize the shift in risk from shareholders to ratepayers;  
17 and e) a Company plan to mitigate the deferred power costs. Id. at 2-3. On March 22, 2001,  
18 Avista filed testimony addressing the power cost issues and its proposal to recover those costs.  
19 This filing was docketed as UE-010395.

20           ICNU intervened in Docket No. UE-010395 on March 30, 2001. Re Avista,  
21 WUTC Docket No. UE-010395, Petition to Intervene of ICNU (Mar. 30, 2001). On April 26,  
22 2001, Avista, Staff, Public Counsel and ICNU (collectively “the Parties”) entered into a  
23 settlement stipulation (“Stipulation”) that resolved all issues related to recovery of deferred  
PAGE 4—POST-HEARING BRIEF OF ICNU

1 power costs. The Parties agreed that rather than requesting a rate increase, Avista would utilize  
2 the proceeds of surplus power sales beginning in 2002 to recover deferred power costs, and that  
3 absent further action by the Commission, the Stipulation balance would be deemed to be zero by  
4 February 28, 2003. Stipulation at 2. On May 23, 2001, the Commission approved the  
5 Stipulation. Re Avista, WUTC Docket No. UE-010395, First Supp. Order Approving and  
6 Adopting Settlement Stipulation (May 23, 2001).

7 Less than two months later, on July 17, 2001, Avista filed a petition requesting  
8 that the WUTC impose a power cost surcharge, and, by implication, amend or terminate the  
9 Stipulation. Petition at 1. On August 2, 2001, Avista filed direct testimony in support of its  
10 Petition. Staff and intervenor direct testimony was filed on August 24, 2001, and the Company  
11 rebuttal was filed on August 30, 2001. A public hearing was held on September 5-6, 2001, in  
12 which the Commission heard cross-examination of the Parties' witnesses.

13 **B. Avista's Petition and Schedule 93**

14 Avista's Petition maintains that drastic changes in hydro generation conditions  
15 and wholesale power prices since the Stipulation was adopted have caused an increase in the  
16 actual and projected deferral balances warranting immediate rate relief. Avista requests that the  
17 Commission grant two forms of relief in order to reduce the power cost deferral balances and  
18 generate cash flow for the Company to address the alleged financial emergency.

19 Avista requests Commission approval of Schedule 93 (Power Cost  
20 Surcharge-Washington) ("Schedule 93"). Petition at 1. Schedule 93 imposes a 36.9% electric  
21 rate surcharge on Avista's Washington ratepayers for twenty-seven months. Id. at 4. Avista  
22 proposes that the surcharge remain in effect until the deferral balance reaches \$0, which Avista  
23 expects to occur by December 31, 2003. See Id. at 16; Stipulation at 3. Avista's proposal

1 includes recovery of many traditional general rate case revenue requirement items such as  
2 Coyote Springs II and other capital expenditures. See Exhibit 651-T at 17; Tr. at 517:8-22.

3 Avista also requests that the Commission allow accelerated amortization of the  
4 PGE monetization credit. Petition at 15; See WUTC v. Avista, WUTC Docket Nos.  
5 UE-991606/991607, Third Supp. Order at 36 (Sept. 29, 2000). Avista proposes that the  
6 accelerated amortization begin in October 2001, and that the credit be fully returned to  
7 ratepayers by December 31, 2002. Petition at 15. This accelerated amortization reduces the  
8 power cost deferral balance by \$53.8 million by December 31, 2002. Id. Absent the accelerated  
9 amortization of the PGE monetization credit, the overall rate increase for customers under the  
10 Avista proposal would be 48%. Exhibit 250-T at 7.

11 Finally, Avista proposes that Schedule 93 and the accelerated amortization be  
12 implemented “subject to refund.” Petition at 4. This allows for a refund of the surcharge  
13 revenues if the Commission subsequently determines that Avista incurred any deferred power  
14 costs imprudently or that such costs are not otherwise recoverable. Id. Avista suggests that the  
15 Commission perform a prudence review in a general rate case that the Company plans to file in  
16 November 2001. Petition at 4. Avista also suggests that the Commission utilize the November  
17 2001 rate case to address a number of unresolved issues from prior dockets related to Avista’s  
18 rates. Id. at 4-5.

19 **C. Staff and ICNU Proposals**

20 In response to the Petition, Staff and ICNU made alternative proposals in their  
21 direct testimony submitted on August 24, 2001. Due to the accelerated schedule of Phase I of  
22 this proceeding, these proposals were based on a cursory review of both the facts and the  
23 standards set out in the PNB case.

PAGE 6—POST-HEARING BRIEF OF ICNU

1           **1.     The Staff Proposal**

2           Staff proposes that the Commission impose a 32.6% surcharge on Avista's  
3     ratepayers on an equal cents per kWh basis, for a period of ninety days, subject to continuation.  
4     Exhibit 451-T at 3. However, Avista would not be allowed to immediately credit surcharge  
5     revenues to decrease the deferral balances until the Company has proven its entitlement to  
6     recovery. Id. at 13. Instead, Staff would require Avista to separately book any surcharge  
7     revenue in a separate account until the Commission can determine which costs were prudently  
8     incurred, if any. Exhibit 551-T at 3. In addition, Staff would terminate Avista's current deferred  
9     accounting of excess net power costs effective June 30, 2001. Exhibit 451-T at 4. Staff also  
10    would require Avista to expeditiously address the issues in contention in Phase II of this Docket  
11    by either affirming the Company's March 23, 2001 filing as its case on those issues, or by filing  
12    a new direct case altogether. Id. Staff's proposal also requires Avista to file a general rate case  
13    by September 28, 2001, in which the Commission would address the outstanding issues from  
14    prior dockets, as well as any request to continue the proposed surcharge beyond ninety days. Id.  
15    Finally, Staff would not allow Avista to accelerate amortization of the PGE credit to decrease the  
16    overall amount of the surcharge. Exhibit 401-T at 24.

17           **2.     The Schoenbeck and Thornton Proposals**

18           The Schoenbeck Proposal recommends that an 11.9% rate increase be put in place  
19    subject to refund over a fifteen-month period. Exhibit 651-T at 3. This increase compensates  
20    Avista for its actual deferred power costs incurred through June 31, 2001, subject to refund  
21    pending a prudence review. Id.; Tr. at 493:21-24. In addition, the Schoenbeck Proposal allows  
22    the Company to continue to defer power costs incurred after June 30, 2001, for possible recovery  
23    in a later proceeding. The Schoenbeck Proposal also incorporates Avista's suggestion to  
PAGE 7—POST-HEARING BRIEF OF ICNU

1 amortize the \$53.8 million PGE monetization credit on an accelerated basis in an effort to  
2 minimize the overall impact on ratepayers. Exhibit 651-T at 15. Finally, Mr. Schoenbeck adopts  
3 Avista’s proposal to apply the surcharge on an equal percentage basis. Id. Adoption of the  
4 Schoenbeck Proposal provides the Company with approximately \$28.3 in additional revenue per  
5 year, and would offset the deferral balance by \$83 million over the entire 15-month period.  
6 Exhibit 651-T at 3; Tr. at 502:12-13.

7 ICNU and Public Counsel jointly sponsored the testimony of John Thornton, who  
8 proposed a number of options and alternatives for the Commission to consider. Exhibit 601-T at  
9 12-14. First, Mr. Thornton suggests that the Commission could take no action at this time, and  
10 postpone the Avista request until full review in a general rate case. Id. at 12. Second, Mr.  
11 Thornton recommends that the Commission consider accelerated depreciation of the Company’s  
12 distribution assets as an alternative source from which to generate cash. Id. at 13. Third, Mr.  
13 Thornton suggests granting limited interim relief conditioned on Avista taking actions such as  
14 reducing Company dividends, issuing new equity, or selling Coyote Springs II. Id. at 13.  
15 Finally, Mr. Thornton suggests that the Commission could grant limited relief at a lower level  
16 necessary to meet the fixed charge coverage ratios. Id. at 14.

17 **III. ARGUMENT**

18 As noted above, Avista’s Petition should be rejected for a variety of reasons:  
19 1) Avista’s Petition is not consistent with the terms of the Stipulation; 2) Avista has not asserted,  
20 nor has there been time to review, sufficient facts to meet the Commission’s standard for interim  
21 rate relief; and 3) Avista’s questionable current financial problems are in large part attributable to  
22 the Company’s unregulated activities, rather than to market volatility or hydro conditions. For  
23 these reasons, the issues raised by the Petition should be addressed in a general rate case rather  
PAGE 8—POST-HEARING BRIEF OF ICNU



1 than in this expedited proceeding. Nevertheless, ICNU would support adoption of the proposal  
2 sponsored by ICNU witness Don Schoenbeck to give the Company some flexibility to address its  
3 alleged lack of short-term liquidity, subject to a later prudence review. Any remaining measures  
4 to address Avista’s financial condition should be the responsibility of shareholders and  
5 management.

6 **A. Avista’s Request Does Not Meet the WUTC Standard for Interim Rate Relief**

7 The Commission has consistently relied upon a strict standard for granting the  
8 type of interim rate relief that Avista seeks. See PNB at 3. The Commission has hesitated to  
9 grant interim relief for fear of liberalizing the PNB standard and being required to grant interim  
10 rate relief “pending the final determination of a general rate increase request in virtually every  
11 utility rate filing to come before this Commission.” WUTC v. Pacific Northwest Bell Tel. Co.,  
12 WUTC Docket No. U-75-40 at 12 (Sept. 26, 1975).

13 The Avista Petition fails to meet the standards set out in PNB and its progeny,  
14 because: 1) There has not been an adequate hearing because the Parties have had insufficient  
15 time to analyze the PNB factors; 2) there has been no showing that an actual emergency exists,  
16 or that it cannot be mitigated through other measures; and 3) the proposed surcharge will cause  
17 rate shock, which is not in the public interest. In addition, the Petition fails to satisfy the PNB  
18 standard because it relies on speculation and projections to predict uncertain harms to the  
19 Company. Further, Avista’s proposal to use the surcharge as a “stopgap” to its alleged financial  
20 deterioration is inconsistent with both prior Commission precedent and the Commission’s  
21 statutory directives.

22 **1. The PNB Standard**

1           In PNB, the Commission denied Pacific Northwest Bell Telephone Company’s  
2 (“Pac Bell”) Petition for Emergency Rate Relief despite Pac Bell’s claims that the company was  
3 “desperate,” and had taken “radical steps” to remedy its financial position. PNB at 3. In support  
4 of its petition, Pac Bell alleged that it had not met its authorized rate of return, that it could not  
5 obtain permanent financing, and that it was concerned about a downgrade of its investment  
6 rating. Id. at 4-5. The Commission concluded that there was “no significant evidence of service  
7 impairment,” and denied Pac Bell’s request. Id. at 14-15.

8           In denying Pac Bell’s request, the Commission drew six conclusions regarding  
9 interim rate relief. These conclusions have come to make up the PNB standard, and have been  
10 consistently reaffirmed in subsequent Commission decisions. See WUTC v. Cascade Natural  
11 Gas Corp., WUTC Docket No. U-74-20, Second Supp. Order; Petition for Interim Rate Relief  
12 (July 23, 1974). The six conclusions are as follows:

- 13           1. This Commission has the authority, in proper circumstances, to grant  
14 interim rate relief to a utility, but this should be done only after an  
15 opportunity for adequate hearing.
- 16           2. An interim rate increase is an extraordinary remedy and should be  
17 granted only where an actual emergency exists or where necessary to  
18 prevent gross hardship or gross inequity.
- 19           3. The mere failure of a utility’s currently realized rate of return to equal  
20 that rate of return previously authorized to the utility by this  
21 Commission as adequate is not sufficient, standing alone, to justify the  
22 granting of interim relief.
- 23           4. The Commission should review all financial indices as they concern  
24 the applicant, including rate of return, interest coverage, earnings  
25 coverage, and the growth, stability, or deterioration of each, together  
26 with the immediate and short-term demands for new financing and  
27 whether the grant or denial of interim relief will have such an effect on  
28 financing demands as to substantially affect the public interest.

1           5.     In the current economic climate the financial health of a utility may  
2           decline very swiftly, and interim relief stands as a useful tool in an  
3           appropriate case to stave off impending disaster. This tool, however,  
4           must be used with caution, and it must be applied only in cases where  
5           the denial of interim relief would cause clear jeopardy to the utility and  
6           detriment to its ratepayers and its stockholders. This is not to say that  
7           interim relief should be granted only after disaster has struck or is  
8           imminent but neither should interim relief be granted in any case  
9           where full hearing can be accomplished and the case in chief resolved  
10          without clear jeopardy to the utility.

11          6.     As in all matters before this Commission, we must reach our  
12          conclusion while keeping in mind the statutory charge to this  
13          Commission that we must “regulate in the public interest.” This is our  
14          ultimate responsibility, and a reasoned judgment must give appropriate  
15          weight to all relevant factors.

16    PNB at 13. Essentially, the PNB standard dictates that interim rate relief may be granted, but  
17    only when it will “prevent gross hardship or gross inequity,” “impending disaster,” or upon a  
18    determination that “denial of interim relief would cause clear jeopardy to the utility and  
19    detriment to its ratepayers and its stockholders.” Id. Furthermore, in interim rate relief cases, the  
20    Commission only considers actual, existing conditions, and short-range projections at the time of  
21    the application, not extended projections or speculation. WUTC v. Wash. Water Power Co.,  
22    WUTC Docket No. U-80-13, Second Supp. Order Granting Petition for Emergency Rate Relief  
23    in Part (June 2, 1980).

24           **2.     Avista’s Proposed Surcharge Does Not Meet the PNB Standard**

25           Avista’s Petition and the proceedings related to it are not sufficient to satisfy the  
26    PNB standard. Avista has not established that denial of its request would cause “clear jeopardy.”  
27    In addition, the expedited schedule in this Docket has not allowed an “adequate hearing” to fully  
28    examine Avista’s financial condition. Moreover, although Avista has alleged that it is  
29    financially impaired, the Company has offered “no significant evidence of service impairment.”

1 PNB at 14-15. Finally, even if Avista has established that an emergency condition exists, the  
2 interim rate relief measures that Avista proposes to implement are improper. Accordingly, the  
3 Petition should either be denied, or the Commission should grant limited relief as described in  
4 the Schoenbeck Proposal.

5           The financial data and projections that the Company submitted establish neither  
6 “emergency conditions,” nor that the Company is in “clear jeopardy.” In evaluating petitions for  
7 interim rate relief, the Commission concerns “itself only with an analysis of existing and actual  
8 conditions and short-range projections . . . .” Id. at 3. In general, to grant interim rate relief, the  
9 Commission relies on only actual, ongoing financial problems.

10           In support of its Petition, Avista generally cites the increased deferral balances as  
11 the source of a host of potential financial problems. See Petition at 10-14. Avista indicates that  
12 “lenders are concerned about the size of the deferral balances,” the Company “could be  
13 precluded from borrowing under its primary commercial bank credit line,” and the Company is  
14 in danger of losing its investment grade debt rating. Id. at 6, 13. In addition, Avista asserts that  
15 immediate imposition of a 36.9% electric rate surcharge on retail ratepayers would “be a signal  
16 to the financial community that the Commission will continue to take prompt actions to support  
17 the financial health of the Company.” Id. at 14.

18           Lender concerns, possible preclusion from borrowing and potential downgrades  
19 of investment ratings do not constitute an “emergency” as defined by the PNB standard. Avista  
20 has not shown that an actual emergency exists at this time, or that gross hardship will occur  
21 without immediate rate relief. The Avista Rebuttal testimony only vaguely refers to  
22 conversations in which potential lenders indicated that they were unwilling to grant further loans  
23 to the Company. Exhibit 152-T at 2-4. There are few, if any, documents in the record that  
PAGE 12—POST-HEARING BRIEF OF ICNU

1 support these claims. Additionally, the Commission previously rejected a petition for interim  
2 rate relief based on speculation about potential downgrading of an investment rating because  
3 such a situation did not pose “clear jeopardy” to the utility. See WUTC v. Pacific Northwest  
4 Bell Tel. Co., WUTC Docket No. U-75-40 at 1.

5           The testimony of Avista’s witnesses at hearing was contradictory at best. While  
6 claims were made regarding a current lack of liquidity, there was testimony regarding substantial  
7 mitigating factors. For example, Mr. Ely testified that Avista was pursuing cost reductions and  
8 deferral of capital expenses that would save \$60 million over the next 16 months. Tr. at  
9 170:9-11. These cost savings were not included in the financial exhibits that support the petition.  
10 Tr. at 169:16-18. Likewise, the Company is pursuing waivers that would allow continued use of  
11 approximately \$115 million under its revolving line of credit. Tr. at 246:13-16, 208:3-8.  
12 Finally, Avista Energy has experienced substantial earnings, and Avista is seeking the ability to  
13 dividend approximately \$145 million to the utility in the next year. Tr. at 728:16-25, 200:22-25;  
14 208:3-8.

15           Avista admits that its alleged liquidity problems are a short-term issue. Tr. at  
16 212:10-16. The factors noted above show that even in the short term there are many mitigating  
17 factors that have not been included in the financial analysis supporting the Petition.  
18 Furthermore, Avista may have additional options to improve its financial situation, such as  
19 issuing equity 1/ and selling part or all of its equity interest in Coyote Springs II.

20           Avista also requests that the Commission approve the surcharge in order to send  
21 “a signal to the financial community . . .” Petition at 14. This request is similarly insufficient

1 to satisfy the PNB standard. The Commission’s directive in this case, and in all cases, is to  
2 “regulate in the public interest,” not to “signal” the financial community as to the health of the  
3 companies which it regulates. RCW 80.01.040; PNB at 13. The imposition of a 36.9%  
4 surcharge on all Avista’s Washington retail ratepayers is a drastic measure that should only be  
5 undertaken after extensive review. Undue emphasis on the investment ratings services’  
6 perceptions of the Commission decision distorts the focus of this proceeding and conflicts with  
7 the WUTC’s statutory directives. The Commission should weigh the effect of any action  
8 intended to signal investment rating services in relation to the public interest.

9 In addition, the PNB standard dictates that the Commission should only grant  
10 interim relief after an “adequate hearing.” PNB at 13. The expedited schedule in this Docket  
11 has not allowed for the proper procedure to fully examine Avista’s true financial condition. As  
12 described below, although Avista attributes its financial status solely to the increasing deferral  
13 balances, the Company’s nonregulated activities have contributed to any financial decline as  
14 well. Exhibit 601-T at 3. Furthermore, Avista has shown profits and declared dividends in the  
15 last financial quarter, indicating that the reality of the Company’s financial distress is  
16 questionable. Staff concedes that they have not had adequate time to fully examine Avista’s  
17 financial condition, or each of the financial indicators described in the PNB standard. Exhibit  
18 401-T at 19, 21, 22. The adequate hearing requirement of the PNB standard prohibits any grant  
19 of interim relief based on this incomplete information and superficial analysis. As a result,  
20 Avista has not satisfied the PNB test. The Commission should not grant the extraordinary relief

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1/ While Avista maintains that it cannot currently issue equity, that conclusion is pure speculation, because Avista has not made a public offering of new equity in the last 18 years. Tr. at 253:17-19.

1 sought by Avista based on such cursory analysis of incomplete data, but rather should deny the  
2 Petition until full review can be conducted in a general rate case.

3 **3. The Commission Should Not Allow Avista to Use the Proposed Surcharge as**  
4 **a “Stopgap” for its Financial Requirements**

5 Avista maintains that implementation of a 36.9% surcharge on Washington  
6 ratepayers will generate cash flow, reduce the power cost deferral balances, and promote lender  
7 and investment rating service confidence in the Company. In essence, the surcharge will  
8 function as a quick cash generation mechanism, but will be implemented “subject to refund” in  
9 case it is later deemed unwarranted. The Commission has previously condemned the use of an  
10 interim rate surcharge in this manner. See WUTC v. Washington Natural Gas Co., WUTC  
11 Docket No. U-80-111, Second Supp. Order Denying Petition for Surcharge and Granting  
12 Temporary Interim Rate Relief (Mar. 3, 1981).

13 A surcharge is intended to compensate a utility for extraordinary and  
14 uncontrollable expenses, the costs of which should be passed on to ratepayers on an actual or  
15 reasonably known basis. Id. However, a surcharge “is not intended to be employed nor will it  
16 be considered by [the] Commission as a stopgap or piecemeal approach to a utility’s overall  
17 financial requirements . . . .” Id. Avista’s proposed Schedule 93 is partially intended to  
18 recapture deferred power costs. The Commission has never conducted a prudence review of  
19 these power costs. As a result, without a prudence review, the Commission cannot determine  
20 whether these costs can properly be passed on to ratepayers. Thus, to impose a surcharge to  
21 compensate Avista for costs which the Commission has never determined should be assessed  
22 against ratepayers would directly conflict with the Commission’s decision in U-80-111.

1           In addition, the Commission has previously refused to hold ratepayers responsible  
2 for the power cost deferrals absent a demonstration that these costs were prudently incurred. See  
3 Re Avista, WUTC Docket UE-000972, Order Granting Deferral of Power Costs Pending  
4 Demonstration of Prudence. Imposition of the proposed surcharge at this time would undermine  
5 the Commission’s earlier attempts to ensure that ratepayers were not improperly charged with  
6 imprudently incurred costs. Such a decision would conflict with both the Commission’s  
7 approach to dealing with these costs in prior dockets, as well as the Commission’s decisions with  
8 regard to surcharges in general.

9           Finally, in addition to use of the surcharge to compensate Avista for the deferral  
10 balances, the surcharge’s more immediate functions are to generate cash flow and improve the  
11 financial image of the Company. These purposes are not related to compensating the utility for  
12 extraordinary expenses, and directly conflict with the Commission’s U-80-111 Order.

13 **B. Avista’s Unregulated Operations Are a Substantial Cause of its Current Financial**  
14 **Condition**

15           Avista controls a number of affiliate and subsidiary corporations, certain of which  
16 operate as unregulated businesses. Avista Utilities is a regulated operating division of Avista,  
17 and operates the Company’s electric and natural gas generation, as well as its transmission and  
18 distribution business. Avista’s unregulated affiliate companies include Avista Advantage, Avista  
19 Labs, Avista Energy, Avista Power and Avista Communications. See Avista Corp., “Corporate  
20 Overview” (Aug. 2001).

21           Avista’s financial condition it primarily attributable to these risky ventures and  
22 poor decisionmaking related to Avista’s unregulated activity in recent years. Therefore, Avista’s  
23 portrayal of poor hydro conditions and market volatility as the sole source of its alleged financial



1 status is misleading. The activities of Avista’s unregulated affiliates undoubtedly have an effect  
2 on the overall financial health of the Company. In light of these impacts, the Commission should  
3 examine this issue in a general rate case, or minimize any relief granted until that time.

4 Avista attributes its lack of cash flow and potential investment rating downgrade  
5 to the mounting deferral balances, poor hydro conditions and wholesale power market volatility.  
6 Petition at 1. However, widely known investment ratings services describe a different basis for  
7 any downturn in Avista’s financial condition, a downturn that began in 1998. See Exhibit 604.  
8 These reports establish a pattern of gradual downgrades in Avista’s investment ratings over the  
9 last three years due to unregulated investments rather than any changes in conditions that may  
10 have occurred since approval of the Stipulation. Id. at 11, 15, 18.

11 For example, in 1998, Standard & Poor’s (“S&P”) downgraded Avista’s credit  
12 outlook due to the Company’s “increasing emphasis on inherently riskier nonregulated business  
13 activities, mainly those of Avista Energy, the energy trading unit.” Exhibit 604 at 2. Less than  
14 one year later, Moody’s Investors Service recognized that risks associated with Avista’s  
15 unregulated activities “have come to the fore during the first half of 1999, with losses at Avista  
16 Energy pressuring financial performance.” Id. at 3. The rating agencies consistently refer to the  
17 “[s]ignificant cash flow volatility” that results from Avista’s reliance on the unregulated  
18 activities, contributing to financial instability. Id. at 4-5.

19 In addition to the inherently risky nature of Avista’s unregulated activities, Avista  
20 posted poor results from these activities. In 1999, Avista Energy recorded a \$98 million pretax  
21 loss, and Avista’s infusion of significant amounts of money into that subsidiary decreased the  
22 Company’s financial flexibility. Id. at 11-12. In addition, Avista’s financial performance has  
23 been “adversely impacted by a wholesale short trading position . . . indicating questionable risk

1 management practices, procedures, and decision making.” Id. at 15-17. The ratings services  
2 acknowledge, as Avista maintains, that the increasing deferral balances are pressuring Company  
3 cash flow; however, “[f]urther liquidity stress comes from Avista Corp. providing support to  
4 unregulated subsidiaries in the telecommunications, internet-based energy management and  
5 alternative generation businesses.” Id. at 18-19. Mr. Ely was forced to concede that the  
6 unregulated trading operations had adversely affected the Company’s credit rating. Tr. at  
7 165:2-7.

8           The ratings services’ reviews demonstrate that the pursuit of riskier ventures in  
9 recent years have played largest role in any financial downturn. If Avista had not engaged in  
10 these activities, it would have a higher credit rating, and it would be better positioned to deal  
11 with adverse hydro conditions and a volatile power market. Avista ratepayers should not be  
12 required to bail out Avista shareholders due to the Company’s imprudent financial  
13 decisionmaking.

14           Despite the ratings services’ outlook, and Avista’s claim of a financial position  
15 that has deteriorated to emergency status, the Company has recently taken actions inconsistent  
16 with such positions. Avista maintains that it suffers from decreased cash flow and an inability to  
17 obtain financing for ongoing operations. Petition at 1. In reality, Avista reported net income in  
18 the second quarter of 2001, and declared dividends for shareholders. See Exhibit 4; Exhibit 603.

19           On July 31, 2001, Avista reported a second-quarter net income of \$22.1 million.  
20 Avista Press Release, “Avista Corp. Reports Second-Quarter 2001 Earnings,” July 31, 2001. In  
21 light of these increased earnings, Avista revised its full-year 2001 corporate earnings guidance  
22 upward to between \$1.10 and \$1.20 per share, from the previous estimate of between 80 cents  
23 and \$1.00 per share. Id.; Reuters, “Avista posts second-quarter profits, reversing loss,” July 31,  
PAGE 18—POST-HEARING BRIEF OF ICNU

1 2001. Additionally, Avista has continued to issue stockholder dividends as recently as August  
2 10, 2001. See Exhibit 603. Avista issued these dividends rather than directing the net income  
3 posted in the second quarter towards the mounting deferral balances that the Company claims are  
4 degrading its current financial position. Avista's actions in recent months call into question the  
5 seriousness of Avista's actual financial position as a whole and, therefore, the Commission  
6 should not impose a surcharge on Avista ratepayers.

7 **C. The Issues Raised by the Petition are More Appropriately Addressed in a General**  
8 **Rate Case**

9 The interaction between Avista and its affiliates, the uncertainty regarding  
10 Avista's actual financial status, and the prudence and recoverability of deferred power cost issues  
11 raised by the Petition must be resolved before the Commission approves any rate increase, much  
12 less a 36.9% emergency surcharge. The PNB Standard requires that the Commission only grant  
13 interim relief after an adequate hearing. PNB at 13. The expedited proceedings in this Docket  
14 have not afforded the Parties or the witnesses adequate time to address the Petition and formulate  
15 reasonable suggestions as to Avista's request.

16 Even excluding the Staff proposal, the Avista Petition requires consideration of  
17 the following issues:

- 18 1. The reasonableness of Schedule 93;
- 19 2. The consistency of the proposed accelerated amortization of the PGE  
20 monetization credit with the Third Supp. Order in UE-991606/991607;
- 21 3. Examination of the long-term power contracts Avista formed after the Stipulation;
- 22 4. Prudence review of the deferred power costs (UE-000972);
- 23 5. The effect of Avista unregulated activities (UE-010395 and UE-991606/991607);
- 24 6. Proposal of a PCA mechanism (UE-991606/991607);

PAGE 19—POST-HEARING BRIEF OF ICNU

- 1           7.     Development of a dispatch model (UE-991606/991607);
- 2           8.     The regulatory treatment of Avista's Coyote Springs II project; and
- 3           9.     Sale of Avista's interest in the Longview, WA power plant project.

4           Adequate consideration of all the issues pertaining to Avista's rates requires a  
5 greater time period than that allowed by the expedited proceedings in this Docket. Witnesses for  
6 all Parties in this proceeding have commented that the expedited schedule has not allowed for  
7 full examination of all the issues and alternatives associated with Avista's request. The inability  
8 to fully examine the issues involved demonstrates the need for the Commission to address these  
9 issues in a general rate case.

10           Avista currently claims that uncertain conditions have contributed to the  
11 deterioration of its present financial condition. The uncertainties associated with current power  
12 market and hydro conditions give every indication that they will continue. Prior to taking action,  
13 the Commission should be certain that any drastic short-term measures are necessary in light of  
14 the changing circumstances facing the Company. Failure to account for uncertain conditions will  
15 harm Avista ratepayers in the short-term, only to discover that these actions may have been  
16 unwarranted.

17           Staff has indicated that immediate imposition of a 37% rate increase constitutes  
18 rate shock, a result that undoubtedly conflicts with the Commission's directive to "regulate in the  
19 public interest." Exhibit 451-T at 21; RCW 80.01.040. Dramatic fluctuations in rates create  
20 uncertainty related to customers' electric service, and implementation of such measures "subject  
21 to refund" does not mitigate the impact on the customer in the short-term. Tr. at 490:22-491:3.  
22 Avista ratepayers should not be subjected to rate surcharges in September, only to be told in less  
23 than a year that the surcharge was unwarranted.

1 Avista plans on filing a general rate case in November 2001. The general rate  
2 case will provide the proper forum for the Parties and the Commission to address the new issues  
3 raised by the Petition, as well as the unresolved issues from prior Avista dockets. In addition, a  
4 general rate case will address the long-term interests of Avista and its customers. Thus, to avoid  
5 creating uncertainty for Avista ratepayers, and to fulfill the Commission's directive to regulate in  
6 the public interest, the Commission should either deny the Petition at this time or postpone  
7 examination of most of the issues in this proceeding by adopting the limited relief set out in the  
8 Schoenbeck Proposal.

9 **D. The Proposed Surcharge Violates the Stipulation**

10 Avista's proposed surcharge request violates the letter and spirit of the Stipulation  
11 it signed only three months prior to filing the Petition. Avista should allow the previously  
12 approved deferral elimination mechanisms the opportunity to take effect, instead of prematurely  
13 concluding that those mechanisms are no longer viable. Additionally, although the Stipulation  
14 allows Avista to petition to alter, amend, or terminate the Stipulation for limited reasons, in light  
15 of Avista's misrepresentation of the Company's hydro generation projections, drought-related  
16 hydro conditions and changes in wholesale power markets are insufficient justifications. Finally,  
17 if Avista is justified in seeking release from the Stipulation, the process by which the Company  
18 has chosen to do so is improper. As a result of these deficiencies, the Commission should deny  
19 the Petition.

20 **1. Avista Should Allow the Deferral Balance Elimination Plan to Work**

21 Avista has not allowed a sufficient amount of time to pass to determine whether  
22 the Company will be able to comply with the Stipulation and successfully eliminate its deferral  
23 balance. The Stipulation was designed to provide Avista an opportunity to eliminate the deferral  
PAGE 21—POST-HEARING BRIEF OF ICNU

1 balance over a twenty-two month period. Stipulation at 3. However, less than three months after  
2 signing the Stipulation, Avista alleges that due to dramatic changes in circumstances, the  
3 Stipulation deferral balance elimination plan is no longer viable. The short time lapse between  
4 Avista's commitment to handle deferred power costs without increasing customer rates and the  
5 filing of the surcharge suggests either bad faith, or a complete lack of dedication to the  
6 Company's obligations under the Stipulation.

7           When Avista signed the Stipulation, the Company did not expect to begin  
8 eliminating the deferral balance until 2002, or for almost a year. Stipulation at 2. Avista  
9 intended to eliminate the deferral balances with the proceeds of sales of surplus electricity in the  
10 wholesale market. Avista expected that new generation scheduled to come on line in June 2002  
11 would place the Company in a surplus power position, and that the sales of this surplus power  
12 would generate revenue for the Company to apply to the deferral balances. Therefore, under this  
13 plan, Avista expected to maintain high deferral balances until mid-2002.

14           Avista now maintains that based on its projections of lower wholesale power costs  
15 in 2002, it will be unable to offset the deferral balances by February 28, 2003. Avista's concerns  
16 are premature and based on speculation. There is no reason to believe Avista's predictions  
17 regarding hydro conditions, the wholesale power markets, and its future deferral balances are  
18 accurate, or that these conditions will not undergo additional changes. Avista cannot realistically  
19 predict future wholesale power market conditions to the extent necessary to conclude that the  
20 Company will be able to eliminate the deferral balance. Therefore, the Commission should  
21 reject Avista's premature efforts to abandon the Stipulation, and require Avista to allow the  
22 deferral balance elimination plan an opportunity to succeed. If, at a later date, Avista can show  
23 that its reasonable efforts have been unable to eliminate the deferral balance, then the

1 Commission should consider either reviewing the prudence of Avista’s deferred amounts or  
2 extending the deadline for deferral balance elimination.

3 **2. Avista’s Proposed Surcharge is Not Consistent with the Terms of the**  
4 **Stipulation**

5 Section 4 of the Stipulation requires the Parties “to support and actively promote”  
6 its provisions. Stipulation at 4. In addition, Section 4 allows Avista to petition the Commission  
7 to amend or terminate the Stipulation in discrete, limited circumstances. Id. Section 4 allows the  
8 Company to:

9 [P]etition the Commission to alter, amend, or terminate the  
10 Settlement Stipulation (or propose other appropriate action) should  
11 the deferral balance increase or be reasonably anticipated to  
12 increase substantially due to *unanticipated or uncontrollable*  
13 *events*, such as an unplanned outage of a large Company-owned  
14 thermal unit, or worsening drought conditions.

15 Id. (emphasis added). Through the Petition, Avista apparently seeks to exercise its rights under  
16 Section 4 only two months after the Stipulation was approved. Avista claims that in the last two  
17 months, both hydro conditions, and the wholesale markets, have changed in such a dramatic,  
18 uncontrollable, and unanticipated fashion, that the Company must abandon the Stipulation and  
19 obtain immediate rate relief. Petition at 3. These claims are unwarranted.

20 **a. Avista was Aware of the Deteriorating Hydro Conditions at the Time**  
21 **of the Stipulation**

22 The change in hydro conditions are not an unanticipated or uncontrollable event  
23 as contemplated by the Stipulation. On March 14, 2001, Washington Governor Gary Locke  
24 declared a drought emergency, saying that “this already is the worst drought in our state since  
25 1977, and [we will] *probably beat that record soon.*” Office of Governor Gary Locke, “Locke  
26 announces statewide drought emergency,” Mar. 14, 2001 (emphasis added). Locke also noted

1 that the “state’s snow pack is at just 50 to 60 percent of average for this time of year, which *will*  
2 *sharply reduce the amount of runoff into streams this summer.*” Id. (emphasis added). Thus, by  
3 Avista’s signing of the Stipulation on April 26, 2001, hydro conditions had already deteriorated  
4 to record levels, and officials predicted that the drought conditions would break additional  
5 records as the summer progressed. As noted below, Avista now admits that it knew hydro  
6 conditions were worsening at the time of the Stipulation. Thus, Avista’s claim that it could not  
7 have anticipated that hydro conditions would continue to deteriorate to the lowest level in  
8 seventy-three years is unfounded.

9 **b. Avista has Misrepresented a Fundamental Assumption Upon Which**  
10 **the Stipulation was Predicated**

11 The Stipulation was “based on a number of assumptions, including, but not  
12 limited to, streamflow conditions, thermal plant performance, level of retail loads, and wholesale  
13 market prices during the deferral period.” Stipulation at 2. The Company’s assumptions  
14 regarding streamflow conditions, and the conditions’ subsequent effect on hydroelectric  
15 generation are one of the fundamental premises upon which the Stipulation was formed.  
16 Notwithstanding the importance of these assumptions, Avista has misrepresented its hydro  
17 generation estimates at the time of the Stipulation in both the Petition and in its direct testimony.

18 In the Petition and direct testimony, Avista states that for “deferral estimates  
19 under the Settlement Stipulation, hydroelectric generation for 2001 was estimated to be 135  
20 aMW below normal.” Petition at 7; Exhibit 100-T at 4. In addition, Avista states that current  
21 estimates indicate that 2001 hydro generation will be 194 aMW below normal, 59 aMW below  
22 what Avista claims it projected at the time of the Stipulation. Petition at 7. Avista characterizes  
23 this 59 aMW difference as an “additional substantial reduction” in hydro conditions that requires



1 its release from the Stipulation. Id. However, Avista witnesses now admit that by at least April  
2 16, 2001, ten days before the Company signed the Stipulation, Avista actually estimated that  
3 hydro generation conditions would be 172 aMW below the yearly norm, not the 135 aMW  
4 deficit cited in the Petition. Tr. at 373:20-24; see also Exhibit 108-C. In actuality, Avista’s  
5 hydro generation estimates have declined only 22 aMW. As a result, Avista knew that hydro  
6 generation conditions had fallen to record low levels at the time of the Stipulation. This  
7 knowledge directly relates to Avista’s need to seek the relief requested in the Petition. Such a  
8 direct causal link between hydro generation estimates and the filing of the Petition demonstrates  
9 that this scenario was not unanticipated.

10 **c. The Imposition of a West-Wide Price Cap was not Unanticipated**

11 Avista also alleges that changes in wholesale market prices are an unanticipated  
12 or uncontrollable event that allows the Company to amend or terminate the Stipulation. Petition  
13 at 3. The Stipulation cites plant outages or drought conditions as potential unanticipated and  
14 uncontrollable events, but does not mention changes in market conditions. Moreover, FERC  
15 proceedings throughout the last year have put the energy community on notice of the possibility  
16 of Western price caps. See San Diego Gas & Elec. Co. v. Sellers of Energy and Ancillary  
17 Service, Docket EL00-95-031, Order Providing clarification and Preliminary Guidance (May 25,  
18 2001). At the time the Stipulation was approved in May 2001, FERC was specifically  
19 deliberating about whether to impose price caps or implement other mitigation measures. Id.  
20 Therefore, while the wholesale market has currently stabilized, Avista cannot establish that these  
21 market conditions were unanticipated or uncontrollable. Further, while market prices may be  
22 uncontrollable, the impact of market prices on Avista is a risk that the Company can manage. It

1 is far from clear whether Avista prudently managed those risks and the Commission should not  
2 terminate the Stipulation until that determination has been made.

3 **3. Avista has not Submitted a Petition to Alter, Amend, or Terminate the**  
4 **Stipulation**

5 The process by which Avista has sought Commission approval of the Petition is  
6 improper. The Stipulation allows Avista to “petition the Commission to alter, amend, or  
7 terminate the Settlement Stipulation.” Stipulation at 4. Avista’s Petition is defective because it  
8 does not seek to alter, amend, or terminate the Stipulation. In effect, the surcharge undermines  
9 Avista’s obligations with respect to the Stipulation’s deferral recovery mechanism. However,  
10 the Petition does not specify the action that the Commission should take with respect to the  
11 Stipulation, and only by implication does the Petition suggest that the Company’s proposal  
12 requires the Commission to alter or terminate the Stipulation at all.

13 The Stipulation is an agreement between Avista, Staff, Public Counsel, and  
14 ICNU. As such, the Stipulation should not be altered, amended, or terminated without the  
15 consent of all Parties. ICNU objects to any such change or termination of the Stipulation. If  
16 such action is necessary, ICNU requests that the Stipulation be terminated, because amendment  
17 of the Stipulation would deprive the Parties of the benefit of their bargain.

18 **E. The Staff Proposal is Unwarranted and Promotes Rate Shock**

19 As an alternative to the Avista proposal, Staff has formulated its own  
20 recommendation as to Avista’s need for immediate rate relief. Staff agrees that Avista should  
21 receive some interim rate relief; however, Staff’s proposal differs significantly in terms of both  
22 the amount and the form of that relief. ICNU generally objects to the Staff proposal on the same  
23 grounds asserted against Avista’s Petition above, as well as in other respects. First, the Staff

1 Proposal is not consistent with the Stipulation. Second, in formulating its proposed relief, Staff  
2 has not demonstrated that Avista meets the PNB standard, nor has Staff considered the impact of  
3 Avista’s unregulated activities on the Company’s overall financial condition. Finally, Staff’s  
4 proposal to implement a 32.6% emergency rate increase over 90 days constitutes the “stopgap”  
5 approach to ratemaking that the Commission has condemned in the past.

6 In addition to these generalized objections to Staff’s proposal as a whole, the  
7 Commission should reject Staff’s uniform cents per kWh rate design. This rate design forces  
8 Avista’s twenty largest customers to bear a disproportionate share of the burden of any increase,  
9 is unjustified, and promotes rate shock. In light of these shortcomings, the Commission should  
10 reject Staff’s proposals.

11 **1. Staff Has Not Demonstrated That Avista Meets the PNB Standard for**  
12 **Interim Rate Relief**

13 Staff’s proposed surcharge should be rejected because Staff has failed to  
14 demonstrate that Avista is in a state of financial emergency that warrants emergency rate relief.  
15 Avista has alleged only potential harms based on speculative forecasts and projections, rather  
16 than the genuine harm upon which the Commission has granted interim relief in the past.

17 Staff concedes that in performing its analysis, it did not examine many issues that  
18 would bear on Avista’s overall need for interim rate relief. First, Staff did not review all of the  
19 standards required by the PNB case. Second, Staff has not made a detailed analysis of the  
20 streamflow studies that the Company offers to support its hydro projections. Exhibit 401-T at 6.  
21 As noted earlier, hydro generation projections provide the foundation for Avista’s projections  
22 regarding the deferral balance, and Avista’s use of these projections previously in this Docket  
23 have been misleading. See Section III.D.4. Third, Staff has not given any consideration to how

1 the operations of Avista’s nonregulated affiliates impact the Company’s financial situation.  
2 Exhibit 401-T at 15-16. Finally, to the extent that Staff has examined any alternatives, Staff has  
3 not recommended any alternative ratemaking treatment for Avista other than a surcharge. Tr. at  
4 595:17-25.

5 In particular, Staff’s analysis of Avista’s financial condition is not consistent with  
6 the fourth criteria of the PNB standard, which states that the Commission should:

7 [R]eview all financial indices as they concern the applicant,  
8 including rate of return, interest coverage, earnings coverage and  
9 the growth, stability or deterioration of each, together with the  
10 immediate and short term demands for new financing and whether  
11 the grant or failure to grant interim relief will have such an effect  
12 on financing demands as to substantially affect the public interest.

13 PNB at 13. Despite this admonition to review all financial indices, Staff has focused solely on  
14 Avista’s ability to meet the fixed charge coverage ratio. Exhibit 401-T at 19, 21, 22. Based on  
15 this analysis, Staff both concluded that Avista is facing an impending disaster and calculated the  
16 level of cash needed to return the fixed coverage ratio to the necessary level. Id. Although the  
17 expedited schedule in this Docket has not allowed for comprehensive analysis by any Party,  
18 Staff’s narrow focus on fixed charge coverage ratios produces an incomplete picture of Avista’s  
19 financial situation and is inconsistent with the PNB standard. As noted above there are several  
20 factors that mitigate the dire financial picture painted by Avista’s Petition and Testimony.

21 In formulating its recommendation, Staff essentially used only the information  
22 provided by Avista to examine only the Company’s ability to meet the fixed charge coverage  
23 ratio, and recommended a 32.6% surcharge be imposed without thoroughly considering any  
24 alternatives. Staff’s development of its recommendation is not consistent with the requirements  
25 of the PNB standard, and is otherwise insufficient to justify imposition of a 32.6% emergency

- 1 surcharge. As a result, the Commission should reject Staff's proposal at this time, and examine
- 2 Avista's full financial conditions in a general rate case.
- 3

1           **2.     Staff’s Uniform Cents per kWh Rate Spread is Unjustified, Unduly**  
2           **Burdensome, and Promotes Rate Shock**

3           Staff recommends that the 32.6% surcharge be imposed on a uniform cents per  
4 kWh basis, in contrast to the uniform percentage basis proposed by Avista. Exhibit 551-T at 6.  
5 Although Staff has offered a number of reasons for its uniform cents per kWh proposal, they are  
6 insufficient to justify the burden that Avista’s larger customers will bear under that rate design.  
7 In addition, imposition of the Staff or Avista proposal on a uniform cents per kWh basis only  
8 exacerbates the rate shock otherwise associated with an emergency rate increase in excess of  
9 30%. Accordingly, if interim relief is warranted, the Commission should take every action to  
10 minimize the impact on Avista ratepayers, and decline to implement any relief on a uniform  
11 cents per kWh basis.

12           **a.     Avista’s Institutional and Industrial Customers Cannot Bear the Rate**  
13           **Impact that Results from a Uniform Cents Per kWh Rate Design**

14           The impacts of a uniform cents per kWh rate design on Schedule 25 institutional  
15 and industrial customers will be wholly unprecedented and intolerable. Approximately twenty  
16 Avista customers take service under Schedule 25, Avista’s largest general service tariff in  
17 Washington. Tr. at 458:4-5; 473:8-9. Among these twenty customers are five institutional  
18 customers, which include three colleges and universities: Gonzaga University, Washington State  
19 University, and Spokane Community College, and two medical centers in Spokane: Sacred Heart  
20 and Deaconess. Tr. at 473:21-24. In addition, a number of municipalities take service under  
21 Schedule 25, including the City of Spokane. Tr. at 462:11-15.

22           Staff work papers demonstrate that under a 32.6% rate increase imposed on a  
23 uniform cents per kWh basis, Schedule 25 customers would experience a rate increase of 48%.  
24 Exhibit 552. This 48% rate increase is 15.8% higher than the 32.2% increase for Avista’s  
PAGE 30—POST-HEARING BRIEF OF ICNU

1 residential schedule, and 17% higher than Avista’s next largest tariff, Schedule 21. Id. In  
2 addition, the 32.2% rate increase for residential customers will be further reduced by the  
3 Company’s application of the BPA residential exchange settlement credit. See Petition at 18.  
4 Avista estimated that the residential exchange credit would reduce the overall rate impact to  
5 residential customers by approximately 10% in the first year. Id.; Tr. at 374:18-23, 457:22-  
6 458:1. Because Schedule 25 customers are not eligible for this credit, those customers will  
7 experience the entire burden of a 48% rate increase. In terms of actual dollars, the 48% rate  
8 increase represents an additional \$12.6 million dollars per year that would be paid by only  
9 twenty Schedule 25 customers. Exhibit 552.

10           To reduce rate shock, Avista proposed that its 36.9% surcharge be implemented  
11 on a uniform percentage basis. Exhibit 300-T at 3. If the Company’s proposed surcharge were  
12 implemented, and Staff’s uniform cents per kWh hour allocation basis was adopted, Schedule 25  
13 customers would experience a rate increase of approximately 55%. Tr. at 457:22-458:1-2. This  
14 amounts to an additional \$14.5 million that would be paid by the twenty Schedule 25 customers  
15 each year. Tr. at 459:10-14. Avista recognized that forcing Schedule 25 customers to bear such  
16 a disproportionate amount of the burden was not just and reasonable, and that the rate shock  
17 associated with such a rate increase will have dire consequences for Avista’s large customers.  
18 ICNU requests that the Commission do the same and reject Staff’s uniform cents per kWh  
19 proposal, especially since these customers have had virtually no time to plan or budget for such a  
20 huge rate increase.

21

1           **b.       Staff Has Not Justified its Uniform Cents Per kWh Proposal**

2           In contrast to the dire consequences that a uniform cents per kWh rate design will  
3       have on Avista’s largest customers, Staff has only offered administrative and historical  
4       justifications for its proposal. Staff essentially puts forth four reasons for its uniform cents per  
5       kWh rate design proposal, each of which is insufficient to justify the impact that such a rate  
6       design will have on Avista’s large customers.

7           Two of Staff’s reasons for its uniform cents per kWh proposal essentially address  
8       the administrative ease of dealing with any rate increase. First, Staff claims that the uniform  
9       cents per kWh hour rate design is “much easier to track and verify,” and is “the easiest method to  
10      track for purposes of refundability.” Exhibit 551-T at 7, 8. Avista disputes this claim, stating  
11      that a “small amount of additional administrative work” would be required to use an equal  
12      percentage method. Exhibit 252-T at 12:18-20. Second, Staff states that “a uniform rate per  
13      kWh would allow customers to easily understand and apply the rate to their expected  
14      consumption to determine the impact.” *Id.* at 8. It is hard to see, however, why a kWh charge is  
15      easier to understand than a percentage increase.

16           Staff’s other reason for its uniform cents per kWh proposal are similarly  
17      insufficient. Staff maintains that “a uniform rate per kWh is consistent with the method  
18      authorized by the Commission in past interim relief cases” and “consistent with how power  
19      supply costs were allocated in [Avista’s] last general rate case, Docket UE-991606.” *Id.* Staff’s  
20      reliance on prior Commission practice as a justification for its rate design proposal is unduly  
21      restrictive of the Commission’s ability to fashion appropriate relief in this case, and inconsistent  
22      with Staff’s position in this proceeding as a whole.



1           Throughout this proceeding, Staff has consistently recognized that Avista’s  
2 proposal is not a traditional request for interim relief because it does not arise in the context of a  
3 general rate case. Exhibit 451-T at 17. Moreover, Staff does not “think that [Avista’s] surcharge  
4 request should be processed under the interim standards,” but that the Commission should only  
5 apply those standards “with a clear recognition” that Avista’s Petition is not a typical request for  
6 interim relief. Tr. at 587:1-2; Exhibit 451-T at 17. Thus, Staff has gone to great lengths to  
7 distinguish Avista’s current request from past interim rate relief request, as well as to establish  
8 that the Avista proposal is unrelated to decisions made in a general rate case. However, despite  
9 repeatedly recognizing the unique nature of this case, Staff abruptly abandons this approach in  
10 support of its rate design proposal.

11           Finally, as a practical matter, the impacts of imposing any surcharge on a uniform  
12 cents per kWh basis will have a dramatic affect on Avista’s largest customers. The Commission  
13 should evaluate the impact of a 48% to 55% rate increase on Avista’s largest customers in  
14 relation to Staff’s justifications. ICNU maintains that the potentially devastating impact of any  
15 surcharge implemented on a uniform cents per kWh basis far outweighs Staff’s abstract notions  
16 of administrative ease and historical practice.

17 **F.    If Interim Relief Is Warranted, The Commission Should Adopt the Schoenbeck**  
18 **Proposal**

19           At the September 6, 2001 Hearing, ICNU witness Don Schoenbeck presented his  
20 proposal to alleviate Avista’s alleged financial crisis. Due to the problems with the Avista and  
21 Staff approaches noted above, the Schoenbeck Proposal represents a reasonable alternative that  
22 accommodates the interests of all Parties. If the Commission determines that Avista’s Petition is  
23 consistent with the terms of the Stipulation, and that Avista has satisfied its burden under the

1 PNB standard, then the Commission should grant Avista limited relief as described in the  
2 Schoenbeck Proposal.

3           The Schoenbeck Proposal is predicated on four primary concepts. First, the  
4 Schoenbeck Proposal utilizes Avista's own method of calculating its financial need, but limits  
5 the Company's recovery to that based on the poor hydro conditions, and delays recovery of  
6 extraneous costs. Tr. at 502:5-9. Second, because Avista requests only emergency interim  
7 relief, to the extent possible, the Commission should attempt to base any relief on reasonably  
8 known conditions and actual power cost deferrals, rather than speculative projections or  
9 forecasts. For this reason, the Schoenbeck Proposal allows recovery of Avista's actual power  
10 cost deferrals through June 2001 to reflect the certainty of conditions during that time period.  
11 Third, the Schoenbeck Proposal adjusts the amount of any relief granted to the Company to  
12 exclude the risk of poor hydro and market conditions that the Company bears in its base rates.  
13 Finally, and perhaps most critically, the Schoenbeck Proposal continues the deferral period  
14 beyond June 30, 2001, in order to allow the Company to continue to defer power costs until the  
15 Commission can fully consider those issues in the November 2001 rate case. The combination  
16 of these factors provides immediate cash to alleviate the Company's alleged liquidity problems,  
17 but still assures that ratepayers are not assessed the costs of imprudent actions or activities from  
18 which they receive no benefit.

19           **1. The Schoenbeck Proposal is Based on Actual Costs and Conditions**

20           The Schoenbeck Proposal differs in that the Avista proposal incorporates  
21 speculative forecast assumptions, questionable power purchase transactions and fuel costs into  
22 the amount of money that it seeks to recover. Exhibit 651-T at 11. These types of costs are not  
23 properly charged to ratepayers, even if assessed subject to refund. *Id.* The Schoenbeck Proposal  
PAGE 34—POST-HEARING BRIEF OF ICNU

1 focuses on the Company's actual power cost deferrals and known conditions through June 2001  
2 to provide the Company with a substantial amount of money that carries an "extraordinarily high  
3 probability" of being retained by the Company after prudence review. Tr. at 492:22-493:12. In  
4 this respect, the Schoenbeck Proposal creates certainty for both Avista and ratepayers.

5 In addition to all power costs, the Avista proposal also seeks immediate recovery  
6 of all the projected capital costs and rate of return on the Coyote Springs II project. Tr. at  
7 516:15-21. As Mr. Schoenbeck testified at hearing, these are not the types of costs that should  
8 are traditionally included in current rates, and the Commission has ample time to address the  
9 recovery of these costs in subsequent proceedings. Tr. at 517:16-22. The Coyote Springs II  
10 plant is not expected to come on line until June 2002, and incorporation of Coyote Springs II  
11 costs into any surcharge at present, essentially amounts to a prepayment of those costs to Avista.  
12 Tr. at 519:7-11. Thus, the Schoenbeck Proposal limits Avista's recovery to those costs that are  
13 reasonably known to be properly recoverable at present, and leaves projected costs to be  
14 examined in a future proceeding.

15 **2. The Schoenbeck Proposal Allocates the Proper Amount of Risk Between**  
16 **Ratepayers and the Company**

17 Avista seeks immediate recovery all of the power costs that it has been authorized  
18 to defer to date, without respect to the risk sharing that takes place between utilities and  
19 ratepayers in the traditional rate setting process. Exhibit 561-T at 12. This recovery would  
20 effectively shift the risk that the Company bears in its everyday operations to ratepayers. The  
21 Schoenbeck Proposal incorporates a "risk adjusted authorized" level to calculate the amount of  
22 the power costs through June 30, 2001, that should be borne by the Company and not ratepayers.  
23 Id. Under this risk adjusted approach, Avista ratepayers are held responsible for an appropriate

1 amount (approximately 80%) of the costs that the Company incurred in purchasing power on the  
2 volatile wholesale markets in the past year. Tr. at 502:14-16.

3 **3. The Schoenbeck Proposal Continues the Deferral Period and Allows**  
4 **Consideration of Avista's Additional Costs in the Future**

5 In addition to providing \$83 million in immediate relief, the Schoenbeck Proposal  
6 also allows Avista to continue to defer its power costs pending full Commission review of  
7 prudence in a later proceeding. Tr. at 502:21-503:6. The Commission can fully examine all  
8 issues related to Avista's current expenses and financial condition in the upcoming general rate  
9 case. Traditionally, such rate cases require eleven months for full Commission review. Tr. at  
10 506:7-8. Because the Schoenbeck Proposal provides the Company with \$83 million extended  
11 over a fifteen month period, Avista will still have the benefit of that increased cash flow during  
12 the rate case. In addition, before the fifteen-month period ends, the Commission will likely have  
13 decided the ratemaking treatment for Avista's additional costs. Tr. at 513:17-25.

14 Finally, Avista's proposed surcharge requests recovery of all costs related to  
15 construction of the Coyote Springs II plant that is not expected to come on line until June 2002.  
16 Id. at 516:15-24. Consistent with the attempt to base any relief on actual costs and conditions at  
17 present, the Schoenbeck Proposal excludes recovery of costs associated with Coyote Springs  
18 because it would constitute customer pre-payment of those costs. Tr. at 504:17-505:24.  
19 However, nothing in the Schoenbeck Proposal precludes Avista from recovering those costs at  
20 the appropriate time. Tr. at 517:16-22. The Schoenbeck Proposal does not foreclose any action  
21 by the Company in relation to any costs incurred during the fifteen month period. Moreover, the  
22 Company does not lose any opportunity to recover all costs incurred upon a demonstration of  
23 their prudence.

1 Avista criticizes Mr. Schoenbeck for failing to calculate the impact of his  
2 proposal on the Company's debt coverage ratios. Tr. at 479:11-480:25. However, it is neither  
3 the role of the Commission, nor the responsibility of ratepayers, to bail out the Company for its  
4 poor business decisions. The relief that Avista seeks is extraordinary, because it seeks to recover  
5 costs (i.e., amortize the deferral) that have not been determined to be prudent or otherwise  
6 recoverable. In this context, any relief provided by the Commission should be circumscribed and  
7 should require the management of the Company to implement other measures to solve the  
8 Company's financial problems.

#### 9 IV. CONCLUSION

10 Avista's case for interim rate relief is based on one measure of the Company's  
11 financial health: the fixed charge ratio. The Company claims that it needs immediate rate relief  
12 to meet the fixed charge ratio in its revolving credit agreement so that it will continue to have  
13 access to capital.

14 These claims are suspect because the Company has many options for addressing  
15 this issue short of an interim rate increase. These options include: issuing more debt, issuing  
16 more equity, cutting costs, deferring capital expenditures, selling assets and providing cash  
17 dividends to the utility from the unregulated affiliates. To a varying degree, each of these  
18 measures may be implemented in the short term.

19 The Commission should require Avista to solve its financial problems without a  
20 rate increase. However, if a rate increase is necessary, the Commission should adopt the  
21 Schoenbeck Proposal. The Schoenbeck Proposal is the only recommendation based on Avista's  
22 actual conditions, and if interim relief is warranted, constitutes the most just and reasonable  
23 resolution of issues in this Docket. Accordingly, if any relief is to be granted in this Docket, the  
PAGE 37—POST-HEARING BRIEF OF ICNU

1 Commission should grant reasonable relief as recommended in the Schoenbeck Proposal and  
2 require the Company to file a general rate case in November to fully examine these issues as  
3 expeditiously as possible.

4 DATED this 17th day of September, 2001.

Respectfully submitted,

DAVISON VAN CLEVE, P.C.

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