BEFORE THE WASHINGTON

UTILITIES & TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,

Complainant,

v.

AVISTA CORPORATION, d/b/a AVISTA UTILITIES

Respondent.

DOCKETS UE-240006 & UG-240007 (*Consolidated*)

CROSS-EXAMINATION EXHIBIT OF KEVIN J. CHRISTIE
ON BEHALF OF THE
WASHINGTON STATE OFFICE OF THE ATTORNEY GENERAL
PUBLIC COUNSEL UNIT

KJC-__X

Avista's Response to UTC Staff Data Request No. 10, Attachment L

September 16, 2024

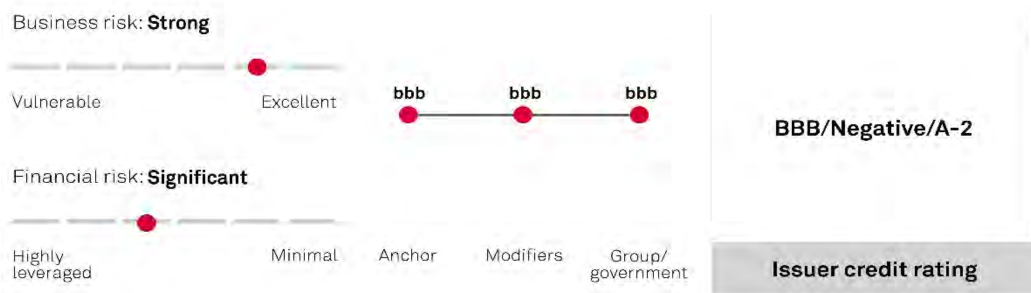
S&P Global
Ratings

RatingsDirect®

Avista Corp.

December 8, 2023

Ratings Score Snapshot



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Credit Highlights

Overview

Key strengths	Key risks
Mostly lower-risk regulated utility, with nonregulated operations contributing less than 5% of the company's consolidated EBITDA.	Expected near-term weakness in credit metrics at the current rating.
Modest regulatory, operating, and geographic diversity, with Washington and Idaho accounting for most of Avista Corp.'s regulated footprint.	Service territory is susceptible to wildfire risk.
Avista engages in adequate regulatory risk management with mechanisms like decoupling and interim adjustments for purchased power and gas costs.	Significant dependence on hydroelectric generation, which introduces some fuel replacement risk.
	Negative discretionary cash flow expected over the next few years, indicating a reliance on external funding.
	Energy transition risk primarily in Washington and Oregon.

Avista's service territory remains highly susceptible to wildfire risks. In August 2023, The Gray Wildfire and the Oregon Road Wildfire caused widespread damage around Spokane County, Washington. Reports from the Washington State Department of Natural Resources indicate that over 185 structures were damaged, and more than 20,000 acres of land were ravaged by these wildfires. Although there is no evidence suggesting Avista Corp. is responsible for or contributed to these wildfires, such incidents of wildfires highlight Avista's vulnerability to physical risks– which we believe is an ongoing concern for the company. Separately, we are monitoring legal proceedings related to the September 2020 Babb Road fire (220 structures damaged or destroyed), including 11 lawsuits that have been filed naming the company as a defendant. All 11 lawsuits are now consolidated and could face trial over the coming months. While our base case incorporates the possibility of a manageable outcome, the company's financial measures are weak for the current rating. As such, an adverse outcome could further weaken Avista's financial measures, constraining the company's credit quality.

Recently approved rate cases to provide support to the company's weak credit metrics. In August 2023, the Idaho Public Utilities Commission (IPUC) approved a $26.4 million increase in electric rates and $1.3 million increase in the gas rates over two years beginning September 2023. This rate increase was premised on a 9.4% return on equity (ROE) and 50% equity ratio. During the same month the Regulatory Commission of Alaska (RCA) approved an electric rate increase for Alaska Electric Light and Power Company (AEL&P) for $2.1 million based on a 11.45% ROE and 60.7% equity ratio. Further, in October 2023, the Oregon Public Utility Commission (OPUC) approved a natural gas revenue increase of $7.2 million, based on a 9.5% ROE and 50% equity ratio. S&P Global Ratings expects the cumulative increase from these rate cases coupled with expiration of customer tax credits in 2024 to partially mitigate the company's weak financial measures, given other offsetting factors such as its elevated capital spending of about $500 million, regulatory-lag, and that the company experienced higher operating costs and interest rates in 2023. Overall, we expect the company's financial measures will remain at the lower end of the range for its financial risk profile category, including funds from operations (FFO) to debt of 13%-14% for 2023-2024.

Potential energy transition risks in Washington and Oregon could affect credit quality over time. This reflects recent passage of the Washington Climate Commitment Act (WCCA), and the Oregon Climate Protection Plan (OCPP), both of which seek to reduce carbon emissions.

Outlook

The negative outlook reflects our expectation that Avista's weakening financial performance will cause its metrics to fall below our downgrade thresholds because of inflation, rising interest rates, and regulatory lag. Under our base case, we assume FFO to debt of 13%-14% in 2024.

Downside scenario

We could lower our ratings on Avista over the next 12 to 24 months if adverse regulatory outcomes, regulatory lag, or rising expenses pressure its financial measures such that its FFO to debt remains consistently below 14% without a material reduction in its business risk.

Upside scenario

We could affirm our ratings and revise our outlook to stable over the next 12 to 24 months if Avista improves its financial measures such that its FFO to debt remains consistently above 14% without increasing its business risk.

Our Base-Case Scenario

Assumptions

- Continued use of existing regulatory mechanisms;
- Periodic and timely rate case filings;
- Implementation of multiyear rate case increase in Washington;
- Refund of customer tax credits;
- No material weakening in the company's capital structure;
- Capital spending averaging about $500 million annually;
- Dividends averaging around $145 million annually;
- Equity issuance of about $120 million in 2023;
- Refinancing of all debt maturities; and
- Negative discretionary cash flow over the forecast period.

Key metrics

Period ending	**Dec-31-2021**	**Dec-31-2022**	**Dec-31-2023**	**Dec-31-2024**	**Dec-31-2025**	**Dec-31-2026**
(Mil. $)	2021a	2022a	2023e	2024f	2025f	2026f
EBITDA (reported)	460	443	493	557	627	685
Plus: Operating lease adjustment (OLA) rent	5	5	5	5	5	5
Plus/(less): Other	18	24	15	16	22	22
EBITDA	484	472	514	578	654	713
Funds from operations (FFO)	393	352	366	414	458	518
Debt	2,796	3,048	2,933	3,085	3,209	3,310
Adjusted ratios						
Debt/EBITDA (x)	5.8	6.5	5.7	5.4	4.9	4.7
FFO/debt (%)	14.0	11.6	12.5	13.4	14.3	15.7

Company Description

Avista Corp. is a vertically integrated regulated electric and natural gas utility that operates in two segments: Avista Utilities and Alaska Electric Light & Power Co. (AEL&P). Avista Utilities generates, transmits, and distributes electricity to customers in Eastern Washington and Northern Idaho (as well as few in Montana). The company also provides natural gas distribution services to retail customers in parts of Eastern Washington, Northern Idaho, and Northeastern and Southwestern Oregon. In total, Avista Utilities supplies retail electric service to about 403,000 customers and retail natural gas service to about 369,000 customers. AEL&P generates, transmits, and distributes electricity in Juneau, Alaska to about 17,000 customers.

Peer Comparison

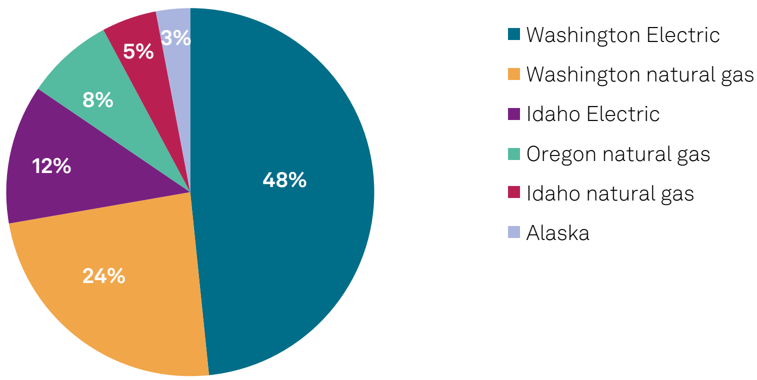
Avista Corp.--Peer Comparisons

	Avista Corp.	Puget Energy Inc.	IDACORP Inc.	Northwest Natural Gas Co.
Foreign currency issuer credit rating	BBB/Negative/A-2	BBB-/Stable/--	BBB/Stable/A-2	A+/Negative/A-1
Local currency issuer credit rating	BBB/Negative/A-2	BBB-/Stable/--	BBB/Stable/A-2	A+/Negative/A-1
Period	Annual	Annual	Annual	Annual
Period ending	2022-12-31	2022-12-31	2022-12-31	2022-12-31
Mil.	$	$	$	$
Revenue	1,710	4,221	1,644	1,014
EBITDA	472	1,407	524	292
Funds from operations (FFO)	352	998	377	236
Interest	126	376	104	52
Cash interest paid	118	362	101	51
Operating cash flow (OCF)	134	833	336	146
Capital expenditure	459	1,051	429	319
Free operating cash flow (FOCF)	(326)	(218)	(92)	(173)
Discretionary cash flow (DCF)	(455)	(234)	(250)	(236)
Cash and short-term investments	13	106	178	13
Gross available cash	13	106	178	13
Debt	3,048	7,831	2,239	1,397
Equity	2,335	4,964	2,815	1,191
EBITDA margin (%)	27.6	33.3	31.9	28.8
Return on capital (%)	5.0	4.4	8.0	7.2
EBITDA interest coverage (x)	3.7	3.7	5.0	5.6
FFO cash interest coverage (x)	4.0	3.8	4.7	5.6
Debt/EBITDA (x)	6.5	5.6	4.3	4.8
FFO/debt (%)	11.6	12.7	16.8	16.9
OCF/debt (%)	4.4	10.6	15.0	10.5
FOCF/debt (%)	(10.7)	(2.8)	(4.1)	(12.4)
DCF/debt (%)	(14.9)	(3.0)	(11.1)	(16.9)

Business Risk

Avista's business risk profile reflects its low-risk, regulated electric and gas utility operations, which contribute more than 95% of the company's consolidated EBITDA. Our assessment also reflects the company's diverse geographic footprint, with regulated operations across five different states, despite Washington and Idaho accounting for around 90% of its rate base.

Avista Utilities Rate Base



Source: Company presentation and reports

Over 90% of Avista's utility revenue is covered by regulatory mechanisms. In Washington, the company has access to an energy recovery mechanism. This is a regulatory construct that allows Avista to track certain differences in its net power supply costs compared to the costs included in base retail rates and allows the utility to true-up these amounts periodically. Similarly, the company has access to a power cost adjustment mechanism in Idaho, which allows for the deferral of 90% of its energy cost differences for future recovery. On the gas side, a purchased gas adjustment mechanism is available in all its jurisdictions, which allows the company to mitigate the risk of fluctuating gas prices. Furthermore, Avista benefits from decoupling mechanisms in Washington, Idaho, and Oregon, which provide some downside protection from reduced sales volumes. Partially offsetting is the company's exposure to physical risk, and that the company potentially faces energy transition risks that must be managed.

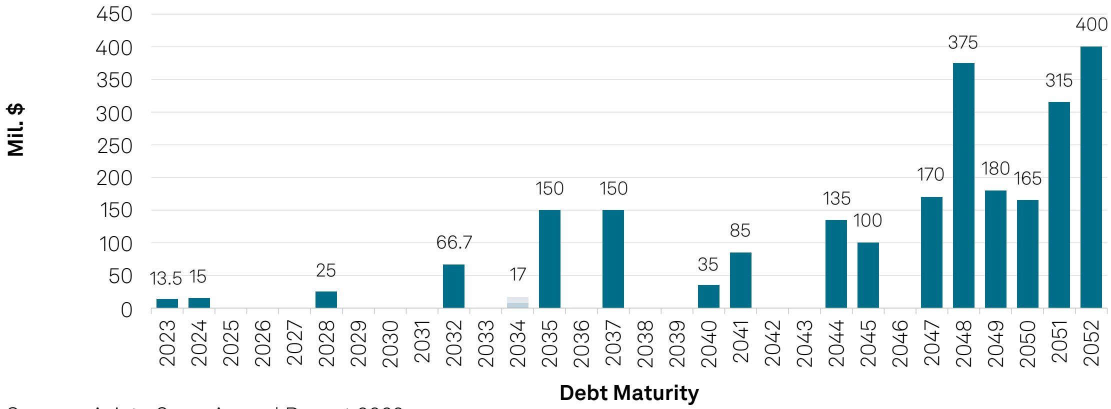
The company's electricity generation mix consists of approximately 48% hydro generation, exposing it to potential fuel replacement risks during periods of unfavorable hydro flows. Additionally, in our evaluation of Avista's business risk, we take into account its exposure to high wildfire risk territories, which remains an ongoing concern.

Financial Risk

We assess Avista's financial risk profile as significant, under medial volatility financial ratio benchmarks, reflecting the company's mostly lower-risk cash flow sources and our view of its overall management of regulatory risk. Under our base case, we assume capital spending averaging around about $500 million, dividend payments of about $145 million, $120 million of equity issuance in 2023, timely recovery of costs incurred during the second quarter, and implementation of recent electric and gas rate increases. Overall, we expect Avista's financial measures to remain weak for 2023 and 2024 due to the effect of customer refunds stemming primarily from the company's prior rate case outcome in Washington and continued cost pressures. However, beginning in 2025 we expect credit metrics to improve, with FFO to debt ranging from 14%-16% during the 2025-2027 period.

Debt maturities

Debt Maturities
As of December 2022



Source. Avista Corp. Annual Report 2022

Avista Corp.--Financial Summary

Period ending	Dec-31-2017	Dec-31-2018	Dec-31-2019	Dec-31-2020	Dec-31-2021	Dec-31-2022
Reporting period	2017a	2018a	2019a	2020a	2021a	2022a
Display currency (mil.)	$	$	$	$	$	$
Revenues	1,446	1,397	1,346	1,322	1,439	1,710
EBITDA	500	475	447	492	484	472
Funds from operations (FFO)	436	350	314	384	393	352
Interest expense	104	110	109	112	114	126
Cash interest paid	106	110	107	108	110	118
Operating cash flow (OCF)	418	370	409	350	274	134
Capital expenditure	420	431	449	420	445	459
Free operating cash flow (FOCF)	(1)	(61)	(40)	(70)	(171)	(326)
Discretionary cash flow (DCF)	(94)	(159)	(143)	(180)	(289)	(455)
Cash and short-term investments	16	15	10	14	22	13
Gross available cash	16	15	10	14	22	13
Debt	2,177	2,412	2,509	2,641	2,796	3,048
Common equity	1,730	1,774	1,939	2,030	2,155	2,335
Adjusted ratios						
EBITDA margin (%)	34.6	34.0	33.2	37.2	33.6	27.6
Return on capital (%)	8.2	6.8	5.5	5.5	5.6	5.0
EBITDA interest coverage (x)	4.8	4.3	4.1	4.4	4.2	3.7
FFO cash interest coverage (x)	5.1	4.2	3.9	4.6	4.6	4.0
Debt/EBITDA (x)	4.4	5.1	5.6	5.4	5.8	6.5
FFO/debt (%)	20.0	14.5	12.5	14.5	14.0	11.6
OCF/debt (%)	19.2	15.3	16.3	13.2	9.8	4.4

Avista Corp.--Financial Summary

FOCF/debt (%)	(0.1)	(2.5)	(1.6)	(2.7)	(6.1)	(10.7)
DCF/debt (%)	(4.3)	(6.6)	(5.7)	(6.8)	(10.3)	(14.9)

Reconciliation Of Avista Corp. Reported Amounts With S&P Global Adjusted Amounts (Mil. $)

	Debt	Shareholder Equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
Financial year	Dec-31-2022									
Company reported amounts	2,809	2,335	1,710	443	190	115	472	124	129	452
Cash taxes paid	-	-	-	-	-	-	(2)	-	-	-
Cash interest paid	-	-	-	-	-	-	(107)	-	-	-
Lease liabilities	114	-	-	-	-	-	-	-	-	-
Operating leases	-	-	-	5	3	3	(3)	2	-	-
Postretirement benefit obligations/ deferred compensation	66	-	-	-	-	-	-	-	-	-
Accessible cash and liquid investments	(13)	-	-	-	-	-	-	-	-	-
Capitalized interest	-	-	-	-	-	4	(4)	(4)	-	(4)
Share-based compensation expense	-	-	-	9	-	-	-	-	-	-
Power purchase agreements	87	-	-	15	4	4	(4)	11	-	11
Asset-retirement obligations	12	-	-	1	1	1	-	-	-	-
Nonoperating income (expense)	-	-	-	-	60	-	-	-	-	-
Debt: other	(27)	-	-	-	-	-	-	-	-	-
Total adjustments	239	-	-	29	67	11	(120)	9	-	7
S&P Global Ratings adjusted	**Debt**	**Equity**	**Revenue**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from Operations**	**Operating cash flow**	**Dividends**	**Capital expenditure**
	3,048	2,335	1,710	472	257	126	352	134	129	459

Liquidity

We assess Avista's liquidity as adequate because its sources will likely cover uses by more than 1.1x over the next 12 months and we expect sources will cover uses even if forecasted consolidated EBITDA declines by 10%. We believe the predictable regulatory framework for Avista provides it with manageable cash flow stability even in times of economic stress. In addition, we believe Avista can absorb high-impact, low-probability events because it maintains about $525 million in committed credit facilities through 2028 and we expect it can lower its capital spending (averaging about $500 million annually) and dividends (averaging around $145 million annually) during stressful periods, which indicates a limited need for refinancing under such conditions. Furthermore, our assessment reflects the company's generally prudent risk management and sound relationships with banks. Overall, we believe the company could withstand adverse market circumstances over the next 12 months with sufficient liquidity to meet its obligations. The company does not have any material debt maturities till 2028.

Principal liquidity sources

- Cash balance of $8.6 million;
- Cash FFO of about $410 million;
- Undrawn credit facilities totaling about $300 million; and
- Working capital inflows of about $20 million.

Principal liquidity uses

- Assumed capital spending of about $500 million; and
- Dividend payments of about $145 million.

Environmental, Social, And Governance

Environmental factors are a moderately negative consideration in our credit rating analysis of Avista Corp. This reflects the company's elevated physical risks due to its service territory's exposure to higher-than-average wildfire risk. Although exposed to less-severe wildfire risk than California utilities, Avista experienced heightened wildfire activity in September 2020 and August 2023, and we believe this risk is ongoing. This risk is slightly mitigated by the company's wildfire resiliency plan, which aims to reduce its fire risk with about $330 million in capital investment over 10 years.

Issue Ratings--Subordination Risk Analysis

Capital structure

Avista's capital structure consists of about $2.7 billion of debt, most of which is secured.

Analytical conclusions

Consistent with our criteria, we rate the preferred stock issued by Avista Capital II two notches below the issuer credit rating to reflect the deferability of the dividends and because it is deeply subordinated to other instruments in the capital structure. The short-term credit rating is based on the long-term issuer credit rating.

Issue Ratings--Recovery Analysis

Key analytical factors

Avista's first-mortgage bonds benefit from a first-priority lien on substantially all of the utility's owned or subsequently acquired real property. Collateral coverage of more than 1.5x supports a recovery rating of '1+' and an issue-level rating two notches above the issuer credit rating.

Rating Component Scores

Foreign currency issuer credit rating	BBB/Negative/A-2
Local currency issuer credit rating	BBB/Negative/A-2
Business risk	Strong
Country risk	Very Low
Industry risk	Very Low
Competitive position	Satisfactory
Financial risk	Significant
Cash flow/leverage	Significant
Anchor	bbb
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Adequate (no impact)
Management and governance	Satisfactory (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile	bbb

Related Criteria

- General Criteria: Hybrid Capital: Methodology And Assumptions, March 2, 2022
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | Utilities: Key Credit Factors For The Regulated Utilities Industry, Nov. 19, 2013
- Criteria | Corporates | Utilities: Collateral Coverage And Issue Notching Rules For '1+' And '1' Recovery Ratings On Senior Bonds Secured By Utility Real Property, Feb. 14, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings Detail (as of December 08, 2023)*

Avista Corp.

Issuer Credit Rating	BBB/Negative/A-2
Senior Secured	A-

Issuer Credit Ratings History

11-Nov-2022	BBB/Negative/A-2
10-Dec-2018	BBB/Stable/A-2
15-Jun-2018	BBB/Watch Pos/A-2

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.