BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, v. AVISTA CORPORATION d/b/a AVISTA UTILITIES, Respondent.	DOCKETS UE-240006, UG-240007, (*Consolidated*)

INITIAL POST-HEARING BRIEF
OF PUBLIC COUNSEL

October 28, 2024

Shaded information is Designated as Confidential per WAC 480-07-160

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I. INTRODUCTION

1. Two generations ago, Dr. Martin Luther King popularized an American sentiment: "the arc of the moral universe is long, but it bends toward justice." Dr. King's abiding faith in the possibility of the steady march of progress inspired generations. And yet, if thoughtful, informed, and well-intentioned people could endorse increasing the transfer of wealth from a population in which one in two residents qualify for assistance and four in five earn less than $66,000 a year to shareholders who have extracted $1 billion in dividend payments in the last decade as "fair, just, reasonable, and sufficient," one cannot help but wonder at the fragility of Dr. King's vision in the face of increasing concentration of wealth and whether the arc bends both ways. If fear of a utility bill motivates a 72-year-old woman to set her thermostat at 55 degrees and cook only one meal a day, how can it be "fair" for a utility to make $145 million in dividend payments this year? How can it be "just" to set a Rate of Return (ROR) for shareholders that exceeds the rate at which that utility deems it necessary to fund the pension plans of its employees? The anger and frustration in the public comments over the un-"reasonability" of near constant rate increases by a company led by executives making base salaries of between $255,000 and $884,000 before incentives is understandable. Unless one is willing to abandon Dr. King's hope or accept that increasing income inequality is somehow a marker of progress, all the parties and decisionmakers in this case should very carefully and thoughtfully limit what is "sufficient" to only that which is strictly necessary to keep the lights on.

2. The Washington State Attorney General's Public Counsel Unit (Public Counsel) requests that the Washington Utilities and Transportation Commission (Commission) limit Avista's rate increases in this General Rate Case (GRC) to only what is strictly necessary under Commission precedent. The Commission should reject Avista's portfolio error adjustment and proposed

alterations of the Energy Recovery Mechanism (ERM) that would increase ratepayers' exposure to fluctuating power costs. The Commission should set a Return on Equity (ROE) that is limited to Avista's actual cost of capital. Public Counsel asks the Commission to adjust Avista's revenue requirement downward by removing unsupported cost escalators, disallowing increased executive compensation, properly allocating director and officer costs to shareholders, and properly accounting for energy imbalance market benefits. Unless the Commission is convinced that an unequal adjustment will not overshoot parity, the Commission must approve an equal allocation of rate increases among the rate classes. Finally, the Commission should impose conditions requiring a full analysis of wildfire spending and should approve individual project rather than portfolio reviews for provisional capital projects.

3. It is a daunting task to guide a public utility through everchanging market conditions while also addressing the pressing need to stop spewing millions of tons of pollution into our climate. Treating Washington residents and small businesses as bottomless sources of future income for shareholders is not and cannot be the solution. Public Counsel is confident that Avista, which is a financially sound and already fairly compensated company, will continue to succeed without the massive rate increase it has requested in this case.

II. STATEMENT OF RELEVANT FACTS

A. Unaffordability in Avista's Service Territory is Deep and Broad

4. The Public Comment exhibit in this rate case[1] illustrates that rate increases and inflation are forcing Avista customers to make affordability choices that impact their ability to sustain a decent lifestyle, which is at the heart of energy justice.[2] Cynthia Freyer, a 72-year-old retiree

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[1] Public Counsel, Public Comment Exh. BR-1 (filed Oct. 8, 2024) (hereinafter Public Counsel, Exh. BR-1).
[2] *Wash. Utils. & Transp. Comm'n v. Cascade Nat. Gas Corp.*, Docket UG-210755, Order 09: Final Order ¶ 56 (Aug. 23, 2022) (hereinafter *Cascade Final Order*).

who is on Avista's "comfort plan," writes of the decisions she makes as a direct result of higher utility bills, "I do not use my oven. I use an air fryer instead and cook only one meal daily."[3] She sets her thermostat at 55 degrees during the night, and asks if Avista will provide her with thermal underwear.[4] Mary Arlt from Ritzville reports that she is freezing, and resorted to using her free standing gas stove for heat until she saw her Avista bill and "freaked."[5] Ms. Arlt makes it clear that these energy bills are rising in the context of higher grocery and gas bills and notes that raising rates, "really hurts the person who doesn't qualify for…the rate deduction plan."[6] Barbara De Vore writes that even with assistance from Avista, "I'm usually still paying off winter bills from Avista in June."[7]

5. The Energy Project (TEP) witness Roger Colton establishes that what Ms. Freyer, Ms. Arlt, and Ms. De Vore report are consistent with "deep" and "broad" unaffordability in Avista's service territory.[8] The depth of unaffordability refers to the impact that the rate increases proposed in this case will have on the lowest income customers, which Mr. Colton defines as households with below $35,000 in annual income.[9] For these customers, the energy burden ranges from 56.2 percent to 5.1 percent of their income.[10] And there are a lot of these customers, with 18,695 homeowners and 24,335 renters falling into this category.[11] Avista provides no contrary evidence to dispute that there are 43,030 customers for whom electricity and gas is deeply unaffordable.

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[3] Public Counsel, Exh. BR-1, Attach. 1 at 2.
[4] *Id*. Attach 1, at 2.
[5] *Id.* Attach 1, at 9–10.
[6] *Id.* Attach 2, at 6 (Letter from Mary Arlt).
[7] *Id.* Attach 1, at 14.
[8] Direct Testimony of Roger Colton, Exh. RDC-1T at 16:3–5.
[9] *Id.* at 17:3–19:3
[10] *Id.* at 18, Table 2 and Table 3.
[11] *Id.* at 19:11–14, 20:8–11.

6. The depth of energy unaffordability is exacerbated by what Avista's Chief Financial Officer, Kevin Christie called "an inflationary environment" in which the inflation rate has lessened, but the impact remains.[12] As Mr. Colton demonstrates, the "impact of inflation is felt most severely by low-income households."[13] As Ms. Arlt noted in her comments, household goods such as food are heavily impacted by inflation and the costs competing with utility payments "really hurt."[14] The recent round of inflation for necessities rose higher than overall inflation rates[15] and lower-income households are less able to adjust to the impact, such that the burden "is particularly great for households with more limited resources."[16]

7. Predictably, the depth of the unaffordability is reflected in arrearages and disconnections for nonpayment. Those census tracts in Avista's service territory with the highest energy burdens have disproportionally higher levels of arrears and those debts are disproportionally older.[17] Disconnections for nonpayment likewise are concentrated in those areas with the highest energy burdens, highest energy bills, and lowest incomes.[18] The consequences of increasing rates for Avista's lowest income customers are debt, disconnection, and, ultimately, denial of the ability to sustain a decent lifestyle.[19]

8. Avista's response to the depth of unaffordability in its service area is, laudably, expanding its bill discount rate and arrearage management programs. In a September 20, 2024, update, Avista reported that there are 50,931 consumers enrolled in its discount programs and

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[12] Kevin Christie, TR. 99:11–20.
[13] Colton, Exh. RDC-1T at 23:7.
[14] Public Counsel, Exh. BR-1, Attach 2 at 6 (Letter from Mary Arlt).
[15] Colton, Exh. RDC-1T at 24:1–6.
[16] *Id.* at 26:8–9 (quoting Lael Brainard, a member of the Board of Governors for the Federal Reserve System).
[17] *Id.* at 8:2–9.
[18] *Id.* at 8:14–19.
[19] *Cascade Final Order*, ¶ 56.

1,396 consumers received an average of $615 in arrearage assistance.[20] In the 11 months from October 1, 2023, when the program started and the contested rate hearing at the end of September 2024, Avista provided $27 million in assistance.[21] By September 2025, Avista anticipates that its annual spend on low-income programs will reach $35.8 million per year and will reach 75,187 customers.[22]

9. Despite this expansion of low-income programming, however, the record before the Commission establishes that this assistance is not meeting the need. There are between 302,000 and 284,456 Avista customers in Washington.[23] Avista estimates that there are 141,863 customers who qualify for low-income assistance.[24] This means that between 46.9 percent and 49.8 percent of Avista's customers cannot pay their current utility bill in full. This is a remarkable statistic: one out of every two residents cannot pay their current utility bill without assistance. Until Avista's assistance programs reach more of those in need, increasing rates will result in more debt, more disconnections, and more customers having to forego heat for fear of their utility bills.

10. While the depth of the unaffordability in Avista's service territory is concerning, equally troubling is the breadth. Using Avista's reported data, Mr. Colton was able to calculate the average income of households Avista serves.[25] Per his testimony, for those households below $35,000, Avista's current requested rate increase is unaffordable. But the data show a troubling pattern for those above that threshold as well. The income distribution is heavily weighted toward the lower end. In fact, 83 percent of Avista's households have an average annual income

[20] Cross-Examination of Shawn J. Bonfield, Exh. SJB-12X at 11, 14.
[21] Bonfield, TR. 341:3–5.
[22] *Id.* at 343:9–22, 344:9–11.
[23] Bonfield, TR. 339:1–3 (302,000); Colton, Exh. RDC-1T at 31, Table 7 (284,456).
[24] Bonfield, TR. 343:9–22.
[25] Colton, Exh. RDC-1T at 32, Table 8.

of below $66,000.[26] Households between $36,000 and $66,000 make up 62.3 percent of accounts in arrears–the inability to pay utility bills is a significant problem afflicting households above Mr. Colton's threshold. [27] As Barbara De Vore notes, higher rates force customers into debt, forcing them to pay their January bills in June.[28] The currently requested rate increase will have real impacts for four in five of Avista's customers.

11. The challenge of affordability for Avista's customers will only worsen in the future. Avista currently plans to add $1.1 billion in capital expenditures in 2025 and 2026, which will result in a five percent increase in rate base.[29] In 2015, Avista's rate base was $2.5 billion.[30] It is currently $4.3 billion, a 60 percent increase over the last decade.[31] The pace of additional investment will only accelerate as Avista pursues Washington's clean energy goals. These capital investments mean that rates will rise faster than inflation.[32] Avista's continued rate increases are significantly eroding, and in many cases eliminating, the majority of customers' already minimal financial cushion to absorb price shocks–Avista has reached a point at which it is fundamentally inequitable to continue raising rates for most of its customers.

12. The growing income inequality in Avista's service territory defines Avista's financial circumstances and influences this Commission's decision making as much as growth of regional energy markets and regional scarcity. Avista's utility rates clearly exacerbate income inequality, redistributing wealth from poorer Washingtonians to shareholders. In 2024, Avista will pay

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[26] *Id*. at 32, Table 8.
[27] *Id.* at 32, Table 8 (summing the "Sum of Pct CT Arrs of total").
[28] Public Counsel, Exh. BR-1 Attach 1, at 14.
[29] Cross-Examination of Dennis P. Vermillion, Exh. DPV-3X (2024 Second Quarter Earnings).
[30] Cross-Examination of Adrien M. McKenzie, Exh. AMM-28X at 6:12–37 (Mckenzie's 2015 testimony).
[31] Vermillion, Exh. DPV-1T at 4:17.
[32] Direct Testimony of Mark E. Garrett, Exh. MEG-1T at 12:3–5 (Calculating an expected inflation rate of 2.5 percent through 2026).

$145 million in shareholder dividends.[33] Avista currently projects that from October 2024 to September 2025, it will spend $38.5 million on low-income assistance programs, or one quarter of the profits paid to shareholders.[34] This program spending will only reach just over half of qualifying participants and will be insufficient to prevent people like Ms. Freyer, who already receives assistance, from continuing to make sacrifices.[35] It is time to readjust investor expectations for such a massive annual wealth transfer.

13. Expansion of low-assistance programs are necessary; in fact, they are statutorily mandated.[36] However, these programs will also exacerbate income inequality since they are funded by ratepayers. Given that half of Avista's population qualifies for income assistance and considering the substantial depth of need among Avista's lowest income customers, expanding assistance programs will squeeze the vanishing middle class even further. The Commission must carefully consider this dynamic–where a smaller number of ratepayers are forced to subsidize both shareholder dividends and low-income customers who cannot reasonably afford rates–in this and in all future rate cases. As Public Counsel noted in its opening statement, ratepayers are not bottomless sources of future income. Rates cannot continue to increase at their current pace.

B. Avista is a Fundamentally Sound Utility

14. Even though half of the population in Avista's service territory currently needs active assistance, and 83 percent of households earn under $66,000 a year, Avista's financial situation is undeniably healthy. In the words of Dennis Vermillion, Avista's "financial results demonstrate the strength of [Avista's] core utility operations."[37] In addition to adding $1.8 billion to its rate

[33] Christie, TR. 123:24–124:3.
[34] Bonfield, TR. 344:9–11.
[35] *Id.* at 342:11–18.
[36] RCW 80.28.425(2). Requiring an increase in low-income bill assistance for every rate increase.
[37] Christie, TR. 131:12–18.

base in the past decade, a 60 percent increase, Avista has distributed $997 million in dividend payments in that time frame.[38] In fact, Avista has been able to increase its dividend every year for the past 22 years, including during the Great Recession and COVID-19.[39]

15. Contrary to Mr. Vermillion's presentation to shareholders about Avista's strength, in its testimony, Avista claims to be facing significant, "headwinds" from inflation, interest rate hikes, and rising power costs.[40] Noting that Standard and Poor's (S&P) rating agency placed Avista's credit into a negative outlook in 2023, Avista asks for a more "supportive regulatory environment."[41]

16. Avista's testimonial claims to financial weakness were significantly undermined during the hearing. Initially, Chief Financial Officer Kevin Christie admitted Avista's earnings per share were up in 2024 through the second quarter and that its utility margin had improved by $54 million over the prior year.[42] Avista procured a new large utility customer that substantially offset all the forecast power costs in 2024.[43] Indeed, despite the "headwinds," Avista confirmed its earnings guidance for 2024.[44]

17. Additionally, although Avista's initial testimony relied on Mr. McKenzie to claim that Avista needed a higher return on equity to "maintain financial integrity,"[45] at the hearing, Mr. McKenzie clarified his testimony did not make "any predictions about Avista's financial soundness based on a specific Return on Equity outcome."[46] In fact, as Mr. McKenzie admitted,

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[38] Christie, TR. 113:3–7.
[39] *Id*. at. 111:13–18.
[40] Vermillion, Exh. DPV-1T at 5:18–6:11.
[41] *Id*. at 6:23–7:1–3.
[42] Christie, TR. 126:5–25.
[43] *Id.* at 129:16–21.
[44] Vermillion, Exh. DPV-5X at 1.
[45] *See e.g.* Vermillion, Exh. DPV-1T at 9:2–11.
[46] McKenzie, TR. 151:1–6.

Avista's financial information is known to investors, and Avista has been able to increase its capital base and maintain its access to capital with current level of returns.[47]

18. Avista's credit situation is not so negative as to need immediate support, either. Although one credit agency, S&P, placed Avista in a negative outlook, Moody's Credit agency affirmed in September 2024 that Avista's credit is stable.[48] As Moody's noted, the primary challenge to Avista's cash flow in recent years was payments necessary to pay a customer tax credit.[49] But as the Company admits, that challenge is ending this year and its end will ameliorate Avista's cash flow.[50] In fact, Chief Financial Officer Kevin Christie admitted that despite the higher power costs, the inflationary pressures, and the low hydro year, barring an unforeseen event, Avista will be "at or above threshold" for the credit agencies.[51] When asked to indicate how much over threshold Avista would be, Mr. Christie declined to answer, citing confidentiality.[52] Avista's refusal to provide the Commission with a target number for meeting credit thresholds should be held against the Company. Unless Avista provides sufficient evidence to assess the need for a credit report, the Commission can give no weight to this claim. But even on the merits, Avista's concerns are overstated. With respect to S&P's rating, Mr. Christie admitted that Avista will meet the agency's base case assumptions, including the use of adders and regulatory mechanisms[53], capital spend,[54] equity issuance and dividend targets,[55] debt maturities,[56] and cash flow.[57]

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[47] *Id.* at 155:9–17, 152:17–21.
[48] Christie, TR. 116:11–17, 117:1–2.
[49] *Id.* at 117:3–18.
[50] *Id.* at 102:3–15, 16–19.
[51] *Id.* at 119:4–8 (Moody's), 121:13–15 (S&P).
[52] *Id*. at 120:7–15.
[53] *Id.* at 122:1–5.
[54] *Id.* at 123:18–24.
[55] *Id.* at 123:24–124:10.
[56] *Id.* at 124:14.
[57] *Id.* at 124:23–25.

19. Based on the evidence in the record, the Commission should conclude, as a factual matter, Avista's financial standing is sound. At its core, Avista's GRC filing is written to justify what it would like, not what is sufficient. Far from being similar to the Western Energy crisis at the turn of the millennium, Avista is on course to maintain its 22-year streak of raising its dividends.

C. Avista Has Historically Inflated its GRC Filings

20. Avista's fundamental financial stability casts significant doubt on the reliability of Avista's general rate filings. In this case, Avista filed an initial set of papers supported by testimony claiming that Avista faces a series of financial and regulatory pressures and headwinds that make "strong regulatory support" paramount.[58] In January 2024, Avista filed an initial request for $177.1 million in additional revenue over two years.[59] In August 2024, upon further review, Avista voluntarily reduced its request to $133 million over two years against citing headwinds.[60] Avista asserts that a two-year rate plan, is "tremendously important" because ratings agencies are worried about regulated utilities' financial outlooks.[61] But nothing in Avista's filings explains why $44.1 million worth of January headwinds dissipated by August. Moreover, in the hearing, Avista's Chief Financial Officer, Kevin Christie testified that the $133 million in the rebuttal case was not actually necessary to maintain Avista's current credit rating, "move forward, and raise capital on behalf of our customers."[62] Pressed, Mr. Christie could only say he believes they need "a majority" of that requested amount.[63]

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[58] Vermillion, Exh. DPV-1T at 8:5–11.
[59] Christie, Exh. KJC-1T at 2, Table 1 (summarizing revenue requirements).
[60] Rebuttal Testimony of Kevin Christie, KJC-1T at 2:17-3.3
[61] *Id.* at 3:16–18.
[62] Christie, TR. 134:25–135:4.
[63] *Id.* at 135:2.

21. The issue of inflation of GRC filings above what is necessary is a pattern of behavior. In each of the preceding four GRCs, Avista has initially asked for far more than what the Commission awarded. The following chart shows the difference between Avista's initial testimonial position and what was ordered:

Table 1: Avista's Pattern of Over-Estimation

Year	Initial Requested Revenue Requirement (millions)	Awarded Revenue Requirement (millions)	Percentage Discounted from Initial Request
2017	69.7 [64]	8.7[65]	87.5%
2019	84.1[66]	36.5[67] (settlement)	56.9%
2020	56.97[68]	21.7[69] (settlement	61.9%
2022	83.1[70]	59.5[71] (settlement)	28.3%

Yet, despite receiving substantially less than the amounts initially requested, as described above, Avista has remained financially stable, able to access credit, and able to expand its rate base. The Commission is forced into the unenviable role of the villagers in Aesop's fable with a shepherd seeing wolves in every pasture. Given the increasing size and complexity of these rate cases, the proliferation of trackers and deferral mechanisms, and utilities' creative framing of their urgent

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[64] Elizabeth M. Andrews, Exh. EMA-1T at 14:13–23, *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Dockets UE-170485 & UG-170486 (filed May 26, 2017). The initial request was for a three-year plan, or $106.67 million. The Commission ultimately authorized a one-year rate plan, so Public Counsel used the amount requested for the first year.
[65] *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Dockets UE-170485 & UG-170486 (*consol.*) Final Order 07, ¶ 6, (Apr. 26, 2018).
[66] Andrews, Exh. EMA-1T at 3:11–4:1, *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Dockets UE-190334 & UG-190335 (filed Apr. 30, 2019).
[67] *Wash. Utils. & Transp. Comm'n v. Avista Corp,* Dockets UE-190334, UG-190335, & UE-190222, (*consol.*) Final Order 09, ¶ 175 (Mar. 25, 2020).
[68] Andrews, Exh. EMA-1T at 4:16–17, *Wash. Utils. & Trans. Comm'n v. Avista Corp.,* Dockets UE-200900 & UG-200901 (filed Oct. 30, 2020).
[69] *Wash. Utils. & Transp. Comm'n v. Avista Corp,* Dockets UE-200900, UG-200901 & UE-200894 (*consol.*) Final Order 08/05, ¶ 346 (Sept. 27, 2021).
[70] Andrews, Exh. EMA-1T at 3:13–16, *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Dockets UE-220053 & UG-220054 (filed Jan 25, 2022).
[71] *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Dockets UE-220053, UG-220054, & UE-210854 (*consol.*) Final Order 10/04 ¶ 216 (Dec 12, 2022).

need for regulatory support, the task of parsing out what is sufficient and what is preferred is increasingly difficult.

22. At this point, it is an inescapable conclusion that Avista inflates its general rate filings, at least with respect to those aspects of the rate request justified by the need for "strong regulatory support" or for Avista's financial health. The Commission should examine, with skepticism, such claims of financial vulnerability.

D. The ERM is Functioning as Intended and Avista's Power Costs Have Not Fundamentally Changed to Justify its Alteration

23. While it is true that energy markets are constantly changing, and Public Counsel does not dispute that regional power scarcity will affect electricity prices, the performance of Avista's power forecasts is not novel and is, as a factual matter, the kind of risk that the ERM was designed to allocate. Avista's power costs have traditionally been sensitive to natural gas prices and price spreads. While 2022, which saw a large spike in costs, was unusual due to the constellation of higher natural gas prices, low hydro, and the disruption caused by a once in a century pandemic, that unusual year has not repeated, and the magnitude of the surcharge has decreased. Avista needs adjust its modelling, but the ERM has worked. Changes to it are premature.

1. The ERM allocates risk of commodity prices.

24. The ERM and other risk sharing mechanisms are intended to allocate the risk of fluctuations in commodity prices such as those at issue in this case. The Commission described the primary purpose of the ERM as "allocate[ing] appropriately between shareholders and ratepayers the risk of power cost variability."[72] The Commission affirmed this purpose earlier

[72] *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Docket UE-060181, Order 3, ¶ 23 (June 16, 2006).

this year, describing PacifiCorp's power cost adjustment as being designed "to distribute equitably the risks of fluctuating power costs between the customer and Company."[73] Noting that a power cost adjustment mechanism like the ERM "benefit[s] utilities" the Commission also uses dead and sharing bands as "cost-sharing tools that prevent the utility customer from absorbing the risk from fuel adjustment mechanisms."[74]

25. Risk allocation is consistent with Avista's own understanding of the ERM. When the ERM resulted in several consecutive years of refunds, and Avista defended its design, Avista described that the purpose of the ERM was to "pick up variability in hydro generation, weather and other changes that cannot be forecasted, *or change in commodity prices that the Company has limited ability to control."*[75] At that time, Avista explained that the ERM "should not be changed based on how current conditions benefit one party or another, particularly in the absence of alternative model recommendations."[76] This is a principal that Avista continues to espouse in other contexts, asserting "one should be cautious when using a short historical dataset, especially when conditions do not reflect median conditions."[77] At the hearing, Avista admitted that the power cost adjustment mechanism is, on balance, beneficial to the Company.[78]

26. The record here establishes that the ERM is functioning as intended–equitably allocating the risk of variability in commodity prices. Although Avista attempts to cloak recent surcharges in economic-sounding terms like "implied market heat rates," it is no more than commodity price

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[73] *Wash. Utils. & Transp. Comm'n v. PacifiCorp*, Dockets UE-230172 & UE-210852, Order 08, ¶ 389 (Mar. 19, 2024) (emphasis added).
[74] *Id.* ¶ 389.
[75] Cross-Examination of Scott J. Kinney, Exh. SJK-24X at 15:9–11.
[76] *Avista Corp.*, Dockets UE-170485, et. al. Final Order 07/02/02, ¶ 125 (Apr. 26, 2018).
[77] Kalich, Exh. CGK-7T at 54:10–15.
[78] Kalich, TR. 254:25–255:1.

fluctuation. As Mr. Kalich explained, the problem "is not rocket science. It's the mid-C price divided by the price of natural gas and it's a fairly simple piece of math."[79]

27. Avista's exposure to price fluctuations in natural gas prices is not a recent problem. In 2017, before the supposed change in market fundamentals, Avista launched a workshop on its power modelling. Avista's third party expert reported that the Company's modelling was susceptible to "fluctuations in continental commodities in markets—particularly natural gas prices and natural gas basis spreads—which have a downstream impact on electricity market prices."[80] In fact, as a general matter, Avista under-forecasts power costs prices when gas prices are rising and over-forecasts when natural gas prices are falling.[81] Although due to different dynamics, Avista's last "sustained trend"[82] of surcharges in 2002 to 2008 was due to variation in natural gas prices.[83]

28. Additionally, according to Avista's own data, the magnitude of the ERM variance is not novel either. In fact, ERM "errors" were worse in the years from 2002 to 2008 when Avista last experienced surcharges. In 2002, the ERM error was 77 percent above forecast, before falling to 47 percent in 2003, and 31 percent in 2024.[84] By contrast the ERM "errors," during the recent three years of what Avista calls fundamental changes, was 17 percent, 68 percent, and 22 percent, which are all smaller than two decades ago. While the raw numbers are higher in the decade of the 2020s because of Avista's robust growth, the current volatility is not unprecedented.

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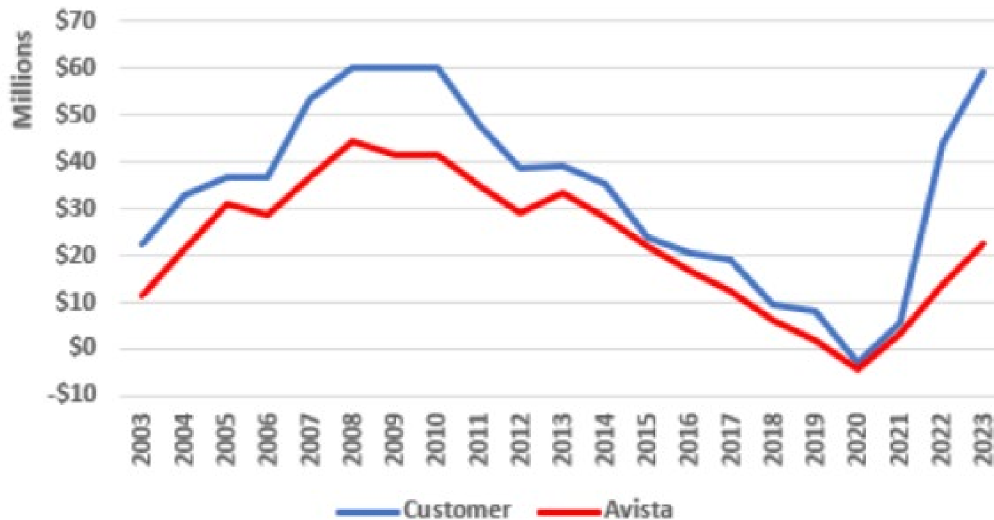
[79] *Id.* at 283:14–17.
[80] Kinney, TR. 204:2–17.
[81] Kinney, Exh. SJK-20X ¶ 3.
[82] Kalich, TR. 267:8–10.
[83] *Id*. at 298:4–13.
[84] Kalich, Exh. CGK-7T at 19 (Illustration 1).

29. The recent surcharges were also driven by fluctuations in commodity prices, and natural gas, in particular. As Mr. Kinney explained, in 2022, the problem was not a collapsing forward price of electricity, but a natural gas price spike caused by the Ukraine war in which natural gas prices rose 95 percent above forecast.[85] In 2023, natural gas prices had normalized, but electricity prices fell at the same time that Avista experienced a low hydro year.[86] After being passed through the ERM, which captured the offsets, this led to an ERM surcharge of $48.8 million in 2022 with a smaller $23.9 million surcharge in 2023.[87]

2. The evidence establishes the ERM risk allocation has been functioning.

30. In allocating the risk caused by these commodity price variations, Avista does not dispute that the ERM has, in fact, allocated the costs of variation between shareholders and customers in a fairly equitable manner. Avista prepared and filed the following chart[88] describing the relative allocations through the ERM:

<u>Illustration No. 3: ERM Cumulative Cost Share</u>



[85] Kinney, Exh. SJK-1T at 69:5–9.
[86] *Id.* at 69:10–14.
[87] Kalich, Exh. CGK-7T at 19 (Illustration 1).
[88] Kalich, Exh. CGK-20X.

31. As this chart illustrates, the ERM has successfully aligned Avista's interests with ratepayers. Indeed, the majority of risk fell on ratepayers, particularly during the recent spate of surcharges. Ratepayers are feeling body blows equally or slightly larger than Avista.

3. Avista proposed to alter the ERM is unsupported by evidence.

32. Even though the ERM has effectively allocated for more than 20 years, Avista now proposes to alter the ERM in two significant ways. First, Avista proposes to adopt a portfolio adjustment error based on a three-year average of actual ERM variances, increasing the power cost baseline by $29.7 million.[89] Second, Avista proposes to alter the dead and sharing bands to increase Avista's ability to allocate more costs to consumers.[90] Both changes are based on "how current conditions benefit one party or another….in the absence of alternative model recommendations,"[91] and the Commission should reject both proposed changes.

33. In its written testimony, Avista claims that these alterations are necessary because the market has changed such that Avista cannot control power costs because the variances are too large for the company to absorb.[92] Avista suggests that the portfolio adjustment error is necessary to accurately set the net power cost baseline.[93] Avista asserts that the dead bands must be adjusted because of its relative size in comparison to other utilities. As is discussed below, the actual reason for the requested changes is that Avista wants the ability to pass along more costs to consumers.

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[89] Kinney, Exh. SJK-17T at 11:8–12.

[90] Specifically, Avista proposes to alter the from the current symmetrical $4 million deadband, with sharing from $4 million to $10 million and a 10 percent company risk above $10 million with a single asymmetrical deadband of $2.5 million for a surcharge and $2 million for a refund with a 10 percent company share after the deadband. Kinney, Exh. SJK-1T at 51:2–12 (existing deadband); Kinney, Exh. SJK-17T at 17 Figure 1 (proposed deadband).

[91] *Avista Corp.*, Dockets UE-170485, et. al. Final Order 07/02/02, ¶ 125 (Apr. 26, 2018).

[92] *See eg.,* Kinney, Exh. SJK-17T at 5:12–13.

[93] *Id.* at 6:14–17.

a. Avista's power modelling is flawed, not the market.

34. The problem is not with the market, but with Avista's power modelling, a function that is entirely within the Company's control. In practice, Avista is able to transact on the market and sell power to make money selling electricity on behalf of its customers.[94] High electricity prices caused by resource scarcity would ordinarily result in higher sales profits, increasing the value of Avista's thermal fleet, which is "good for our customers."[95]

35. But while Avista is able to make money selling power, it is unable to "capture" all of the value it expects because its predictions are poor.[96] Avista's model sees high electricity prices and low natural gas prices and projects that Avista can sell that power for large benefits for Washington consumers.[97] Its model is wrong. Mr. Kalich posited that other utilities are reluctant to sell their power forward when there is resource scarcity.[98] As the sales approach real time, "everybody's out rushing to balance" by selling their excess power, and the "price of electricity has collapsed on us."[99] This drives a collapse of the "operating margin of our thermal fleet in Aurora."[100] Apparently, the fear of resource scarcity is more powerful than the actual scarcity for Avista's model. The fix for this problem is, however, not in the market, but in the model. As Avista admitted on rebuttal, "without some additional changes to input assumptions" Avista's modelling is simply inadequate.[101]

36. Frustratingly, Avista knew of the flaw in its forecasting and chose not to address it. Avista's Vice President of Energy Resources, Scott Kinney, admitted Avista was aware of its

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[94] Kinney, TR. 207:24–208:3.
[95] *Id.* at 220:22–24.
[96] *Id.* at 229:24–230:5.
[97] Kalich, TR. 283:10–25.
[98] *Id*. at 284:1–20.
[99] *Id*. at 284:17–285:9.
[100] Kinney, Exh. SJK-17T at 5:15–6:17.
[101] *Id*. at 13–15.

exposure to natural gas price spreads.[102] When asked whether Avista adjusted its modelling, he explained, "We didn't—we didn't adjust. We modeled based on the forward market prices."[103] Now that Avista's thermal fleet is more valuable, rather than even attempting to fix its model, Avista now asks the Commission to compensate for Avista's own admitted and known error.[104]

b. Avista has not established that power cost surcharges will be persistent or unmanageable.

37. It is important to note here, that Avista has not established that the magnitude of the error is as dire a problem as pled. In fact, the evidence suggests that it is somewhat transitory. In its initial testimony, Avista focused on the modelling error itself, noting that in 2021, the model underpredicted thermal value by $56 million, in 2022 by $202.7 million, and in 2023 by $213.8 million.[105] If Avista's theory of out-of-control power costs were accurate, the ERM balances should follow a similar track line. However, the ERM balances for these corresponding years do not follow the same trajectory. The surcharges were $16.8 million in 2021, peaked at $48.8 million in 2022, and dropped to $23.9 million in 2023.[106] And in the hearing, Avista admitted that the ERM balance was at $17 million, a further drop in surcharge. Avista reported that part of that drop was because "forward market prices have not changed significantly since last quarter" and that "the impact of the ERM on earnings is expected to be $0.07 per diluted share within the 90 percent/10 percent sharing band."[107] Whether because forward market prices are adjusting to the market dynamics that Avista has identified or stability in gas prices has restored more

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[102] Kinney, TR. 204:15–24.
[103] *Id.* at 205:22–206:1.
[104] Kinney, Exh. SJK-1T at 16:16–22.
[105] *Id.* at 68, Table 1.
[106] Kinney, Exh. SJK-17T at 6:9–13.
[107] Vermillion, Exh. DPV-5X at 3.

accuracy to Avista's model, it is clear that Avista's ability to manage power costs has not been completely shattered after a particularly unusual 2022.

38. It is equally possible that the pattern from which Avista observed results isa short-term disruption in the market. Avista concedes that the large variance in 2022 was caused by the Ukraine war and natural gas price spikes, the recovery from COVID-19 inflation and supply chain issues, low hydro conditions, and extreme weather events. These are a unique constellation of events. To quote Mr. Kalich, "one should be cautious when using a short historical dataset, especially when conditions do not reflect median conditions."[108] While it is possible that market conditions have fundamentally changed, the most that Avista has established is that the issue needs further study.

c. The proposed portfolio forecast error will not address flawed modelling or set an accurate baseline.

39. If Avista is struggling with power forecasts, its proposed change to the ERM will make no progress toward solving the problem. First, Avista's portfolio forecast error mechanism does not make any changes to modelling inputs, it simply adjusts the output to be more favorable to Avista.[109] Second, the proposed adjustment is most remarkable for what it does not do. It does not help predict future gas prices or electricity prices.[110] It does not help predict the implied market heat rate.[111] It does not help predict the rate at which forward prices collapse.[112] It does not alter the way that forward prices are used, even though, "that would be a good thing to consider going forward."[113]

[108] Kalich, Exh. CGK-7T at 54:10–15.
[109] Kinney, TR. 182:11–15.
[110] *Id.* at 212:13–22.
[111] *Id.* at 213:1–3.
[112] Kalich, TR. 285:10–17.
[113] *Id.* at 300:11–15.

40. Third, the proposed adjustment is not supported by any analysis that it will make the ERM baseline more accurate or less volatile. Avista has done no analysis to determine if a three-year average of ERM variance will actually smooth out swings in refunds or surcharges.[114] And Avista admits that if additional years were added, the adjustment would be materially affected downward.[115] Avista has no receipts, contracts, ledgers, or other documents to demonstrate how the ERM variance reflects actual costs.[116]

41. Avista further admits that it has made no effort to consult with experts or other parties on how best to adjust its modelling. In 2017, Avista insisted that the Commission reject proposed modifications to the ERM that were not "fully vetted by all parties."[117] Although Avista controls the timing and pacing of its filing, and this matter could have been raised in a subsequent ERM proceeding, Avista chose not to engage in power workshops because it "did not have enough time."[118] The delay from the filing of this case to the present is attributable to Avista. If, as Mr. Kalich claims, there are fundamental market dynamic changes that "we have to figure out as an industry how to solve,"[119] the current proceeding has wasted a year of time that could have been used to make progress.

42. The pecuniary nature of Avista's portfolio adjustment error is further illustrated by Avista's course of conduct. Initially, Avista proposed a $65.8 million portfolio adjustment based on a calculation of five years of its forecast error, which UTC Staff (Staff) and Public Counsel opposed.[120] Without conferring with the objecting parties, Avista altered its methodology to a

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[114] Kinney, TR. 218:1–17.
[115] Kalich, TR. 296:4–7.
[116] Kinney, TR. 200:7–21, 193:3–12.
[117] *Id.* at 198:11–20.
[118] Kalich, TR. 300:20–21.
[119] *Id.* at 268:3–20.
[120] Kinney, Exh. SJK-17T at 8–11.

three-year average of ERM variances to reduce the adjustment to $29.7 million.[121] Avista makes no effort to establish that a three-year ERM variance will result in a more accurate forecast or ERM baseline. In fact, at the hearing, Mr. Kalich maintained that the original proposal was more accurate, but that the new proposal was "more achievable" and "better than nothing."[122] If Avista's actual goal was to improve the ERM baseline, this answer is unintelligible.

43. The Commission should understand Avista's portfolio error adjustment for what it is, a method of arbitrarily moving the ERM goalposts to ensure that Avista falls on the "winning" side of the ERM dead bands.[123] As Mr. Kalich simplified, "we just need to have better recovery of our costs."[124] Staff Witness John D. Wilson is correct that what Avista is really proposing is a pre-payment of a revenue requirement that Avista anticipates rather than a part of its known or measurable power costs.[125] From Avista's perspective, the costs to obtain power for customers are prudently incurred, and the customers "should pay for those costs."[126]

d. Avista fails to prove that hedging is impossible.

44. Aside from the inadequacy of Avista's adjustment in addressing its forecasting challenges, Avista also failed to show that its ability to manage costs is beyond its control. Avista claims that the traditional tool for managing variability, hedging, is no longer available because of a paucity of bilateral trading partners.[127] Avista's claim falls apart upon inspection. First, Avista's attempted claim of hedging impossibility is false. Even though other utilities like Puget

[121] *Id*. at 11:8–12.
[122] Kalich, TR. 273:17–25.
[123] Kinney, Exh. SJK-1T at 53:23–54:1.
[124] Kalich, TR. 303:14–28.
[125] Response Testimony of John D. Wilson, Exh. JDW-1TCr at 10–16.
[126] Kalich, TR. 301:13–23.
[127] Kinney, TR. 291:2–292:4.

Sound Energy trade in the same market and are subject to the same restrictions, they are able to find hedging partners and create significant offsets to its power costs.[128]

45. Second, Avista's purported inability to hedge is based on a critical qualification, "under favorable terms."[129] What Avista explains in a footnote is that "our risk management and hedging plants prevent such activity when prices are not favorable."[130] But what is favorable depends on the level of risk being assumed. If, as Avista now asserts, the losses in power costs have increased by an order of magnitude, it is time to adjust at what price hedging should take place, not abandon hedging altogether.[131]

46. Additionally, although Avista focuses on its relative lack of recent hedging purchases,[132] hedging works in the sales context as well. Avista's purported issue is an inability to capture value in its thermal fleet because the price of electricity falls below forecasted levels as the Company approaches real time. Avista may have to accept prices below its inaccurate forecast to avoid transacting in real time when prices have fully collapsed. Hedging is obviously complicated, but Avista's filing in this case fails to prove that it is impossible or so unaffordable that Avista has lost all control over power costs.

e. Avista fails to introduce evidence that the dead and sharing bands should be modified.

47. Turning to Avista's contention that the ERM dead and sharing bands must be adjusted, again the record is devoid of a reason for such an alteration. Not in testimony, but in oral argument, Avista asserts that it "cannot absorb the body blows" occasioned by the current dead

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[128] Kalich, TR. 293:21–294:11.
[129] *Id.* at 291:17–22.
[130] Kalich, Exh. CGK-7T at 22 fn.22.
[131] Response Testimony of Robert Earle, Exh. RLE-1CT at 14:12–19.
[132] Kalich, Exh CGK-7T at 28:17–29:3.

and sharing bands. Initially, those "body blows" benefit the Company equally during refund years. As Avista admitted, "having the ERM in place is of benefit to the Company."[133]

48. More fundamentally, the current dead and sharing bands are not so large as to threaten Avista's bottom line. Although Avista discusses $300 million thermal value numbers, the actual dead bands only affect $7 million of the first $10 million in a surcharge situation. As discussed above, Avista is a healthy utility with adequate access to capital, robust and growing dividends, and a rapidly expanding rate base. Avista makes no effort to demonstrate that reducing its potential exposure from $7 million to $2.5 million is so consequential to Avista's bottom line that the ERM must now be changed. Even without any modification to the ERM, in 2024, Avista is on course to meet its credit thresholds,[134] to meet its earnings projections,[135] and to "substantially offset all of the forecasted power costs in 2024."[136]

49. It is precisely because of the difficulty of predicting commodity prices and the complexity of managing power costs that the Commission authorized the ERM in the first place. As the Commission explained,

> [W]ithout the guardrails of deadbands and sharing bands, the utility no longer has an economic stake in a major resource decision. As a result, the utility is more likely to ignore fossil fuel price volatility because it knows, regardless of price fluctuations, that it will be made whole by ratepayers.[137]

The incentives should be appropriately sized to achieve the goal of encouraging Avista to perfect its forecast modelling and acquire new resources during times of regional scarcity.

50. Avista suggests that based on the size of other utilities, its dead bands are too large, but this record is devoid of factual support for such a claim. As Public Counsel's expert, Robert

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[133] Kalich, TR. 254:25–255:1.
[134] Christie, TR. 119:4–8 (Moody's), 121:13–15 (S&P).
[135] Vermillion, Exh. DPV-5X at 1.
[136] Christie, TR. 129:16–21.
[137] *PacifiCorp*, Dockets UE-230172 & UE-210852, Order 08, ¶ 390 (Mar. 19, 2024).

Earle, pointed out, it is equally likely that other utility dead bands are too small.[138] In fact, in the most recent Commission decision on power cost adjustment mechanisms, the Commission called into question whether PacifiCorp's current mechanism was too small, noting that when it was initially set, PacifiCorp's dead band was set at a higher percentage of its net power costs.[139] As the absolute size of PacifiCorp's net power costs increased, the percentage has shrunk such that the Commission invited the parties to consider whether "some adjustment must be made."[140] From context, that is an invitation to increase PacifiCorp's dead bands. Shrinking Avista's dead bands to match PacifiCorp's too small bands risks perverting the ERM's intended incentive without good cause.

III. STANDARD OF REVIEW

A. The Commission Sets Fair, Just, Reasonable, and Sufficient Rates

51. The Commission is charged with regulating investor-owned utilities like Avista and must regulate in the public interest.[141] Rates must be fair, just, reasonable, and sufficient, and the Commission is authorized to set rates after hearing by order.[142] The Commission has defined fair, just, reasonable, and sufficient to mean,

> [F]air to customers and to the Company's owners; just in the sense of being based solely on the record developed in the proceeding following principles of due process of law, reasonable in light of the range of possible outcomes supported by the evidence, and sufficient to meet the needs of the Company to cover its expenses and attract necessary capital on reasonable terms.[143]

The Commission's findings must be based on evidence in the record.[144]

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[138] Earle, Exh. RLE-17T at 4:1–3.
[139] *PacifiCorp*, Dockets UE-230172 & UE-210852, Order 08, ¶ 392 (Mar. 19, 2024).
[140] *Id.* ¶ 392.
[141] RCW 80.01.040(3).
[142] RCW 80.28.020.
[143] *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy, Inc.*, Dockets UE-090704 & UG-090705 (*consol.*), Order 11, ¶ 18 (Apr. 2, 2010) (emphasis added).
[144] RCW 34.05.461(4).

52. The Commission's task requires it to balance consumer and investor interests.[145] This does not, however, mean that the Commission determines what is best for investors; to the contrary, the Commission considers what is necessary such that "the regulated utilities earn enough to remain in business."[146] This includes a ROR sufficient to maintain credit and financial integrity while assuring Avista is financially motivated to provide fair prices and service to customers.[147] Thus, while a higher ROR or upward adjustments to a revenue requirement might be beneficial to Avista's bottom line, it is only a relevant consideration if it is necessary to maintain Avista's financial integrity.

B. The Commission Incorporates Equity and Energy Justice into Ratemaking Decisions, Avista Bears the Burden of Proof

53. In assessing the public interest, the Commission foregrounds the issue of equity and energy justice. In 2021, when the Legislature authorized multiyear rate plans, it directed that the Commission determine whether rates were in the public interest.[148] Following the Legislative directive, the Commission acknowledged that its definition of public interest included "equity considerations."[149] The Commission determined to "apply an equity lens in all public interest considerations going forward."[150] Integral to equity in ratemaking, the Commission explained, was the concept of "energy justice and its core tenets" which included whether "individuals have access to energy that is affordable, safe, sustainable, and affords them the ability to sustain a decent lifestyle."[151]

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[145] *U.S. West Commc'ns, Inc. v. Wash. Utils. & Transp. Comm'n*, 134 Wn.2d 74, 121 (1997).
[146] *Id*. at 121.
[147] *Id*. at 121.
[148] RCW 80.28.425(1).
[149] *Cascade Final Order,* ¶¶ 52–58.
[150] *Cascade Final Order*, ¶ 58.
[151] *Id.* ¶ 56

54. The legislative and regulatory focus on equity concerns naturally directs attention to a utility's low-income customers. The Legislature specifically identified its concern with the "energy burden of low-income residential customers" and provided that for any increase in rates, the Commission "must approve an increase in the amount of low-income bill assistance."[152] In tying rate increases to corresponding increases in low-income assistance, the Legislature emphasized the necessary balancing of ratepayer interests with those of Avista's shareholders. What is "fair to customers and utility shareholders"[153] must consider how rate increases will impact low-income customers.

C. The Modifications to the Test Year Must be Known and Measurable

55. To accomplish its task of determining what is a fair and reasonable rate, the Commission uses a modified historic test year methodology.[154] Starting with the audited results from a recent 12-month period, the Commission allows the Company to modify those results to reflect changes supported by the evidence for costs that will occur during the future rate years.[155] Avista may not adjust or pro form revenues in a rate case unless there is a "mechanism ensuring, and evidence establishing, that [an adjustment] does not disturb test year relationships."[156] This requires that the utility show that the adjustment must be known and measurable.[157] An event is "known" if it occurred during or shortly after the historical test year and it is "measurable" if it is not an estimate, projection, or product of a budget forecast.[158] Additionally, an adjustment must be

[152] RCW 80.28.425(2).
[153] *Puget Sound Energy*, Docket UE-090704 & UG-090705, Order 11, ¶ 18 (Apr. 2, 2010) (citing *Hope* and *Bluefield*).
[154] *Wash. Utils. & Transp. Comm'n v. Pacific Power & Light Co.*, Docket UE-140762, Order 08 ¶ 18 (Mar. 25, 2015).
[155] *Puget Sound Energy*, Dockets UE-090704 & UG-090705, Order 11, ¶ 23 (Apr. 2, 2010).
[156] *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Dockets UE-090134 & UG 090135 *(consol.)* Final Order 10 ¶ 43 (Dec. 22, 2009).
[157] *Id.* ¶ 45.
[158] *Id.* ¶ 45.

matched with offsetting factors that would diminish the impact of the known measurable event.[159] Generally, the more uncertain and unknown actual utility costs and offsetting factors are, there is a greater risk that an adjustment is impermissible and disturbs the test year relationships, and there is a greater burden on the Company to prove these costs are actually known and measurable.[160]

D. Avista Bears the Burden of Proof for All Aspects of its Case

56. As with all requests for increased rates, Avista bears the burden to prove the requested rates are fair, just, reasonable, and sufficient.[161] This includes both the burden of production and the burden of persuasion, and requires Avista to demonstrate a revenue deficiency in the rate effective years following both the "known and measurable" and "used and useful" standards.[162] The Commission has long held that this requires a utility to make an affirmative showing of the reasonableness and prudence of its costs, even in the absence of a challenge.[163]

57. As a necessary corollary to this general principle, this means that the Commission should hold any failure to produce evidence on a topic or gaps in the evidentiary record against Avista. The intervening parties and Staff bear no burden of proof to disprove the need for a rate increase. If, when questioned, Avista chooses not to answer, or admits that it did not produce evidence or analysis, that is a sufficient reason to reject a requested rate increase. Thus, for example, it is not enough to assert that Avista might face a ratings downgrade. Conjecturing that there might be an

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[159] *Id.* ¶ 46.
[160] *Id.* ¶ 47.
[161] RCW 80.04.130(4). ("At any hearing involving any change in any schedule, classification, rule, or regulation the effect of which is to increase any rate, charge, rental, or toll theretofore charged, the burden of proof to show that such increase is just and reasonable shall be upon the public service company."); *see also* RCW 80.28.010(1); RCW 80.28.020.
[162] *Wash Util. & Transp. Comm'n v. Cascade Nat'l Gas Corp.*, Docket UG-210755, Order 09, ¶ 108 (Aug. 23, 2022).
[163] *Wash. Utils. & Transp. Comm'n v. Puget Sound Power and Light Co.*, Dockets UE-920499 & UE-921262 Eleventh Suppl. Order, at 19 (Sept. 21, 1993).

adverse impact is insufficient as a matter of law; to meet its burden, Avista must prove that the adverse consequence *will* happen absent the specifically requested rate increase.

IV. THE COMMISSION SHOULD REJECT MODIFICATIONS TO THE ERM

58. This is not a close decision. Both as a matter of law and as a factual matter, the Commission should reject Avista's proposed portfolio error adjustment. Adjustments to revenue, expense, or rate base "typically cannot be an estimate, a projection, the product of a budget forecast, or some other similar exercise of judgments—even informed judgment."[164] Exceptions to this rule are "few and demand a high degree of analytical rigor."[165] Despite this clear legal requirement, Avista, relying on Mr. Kalich's informed judgment and Mr. Kinney's calculation of a three-year average ERM variances, asks the Commission to adjust its pro forma net power costs and ERM baseline by $29.7 million. As a matter of law, Avista's proposed "portfolio forecast error" adjustment must be rejected as an estimate and projection. As a matter of policy, this adjustment undermines the purpose of the ERM and unfairly allocates risk to consumers. As a matter of fact, Avista has failed to prove that this adjustment would improve Avista's power cost forecasts or help set the ERM baseline more accurately. The Commission should reject the proposed portfolio adjustment.

59. The Commission should also reject alterations to the ERM dead and sharing bands. Avista has failed to prove that the current sharing bands actually threaten Avista's financial integrity or that a reduction is necessary for Avista's provision of service. Avista's expanding rate base and ever-increasing rates suggest, if anything, that the ERM dead and sharing bands should increase to properly incentivize prudent power cost management.

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[164] *Puget Sound Energy,* Dockets UE-090704 & UG 090705 (*consol.*) Final Order 11 ¶ 26 (Apr. 8, 2010).
[165] *Id.* ¶ 26.

A. The Commission Should Reject the Forecast Error Adjustment Proposal

60. Since its inception in 2002, the ERM was and remains an instrument to allocate "risk between shareholders and ratepayers."[166] In addition to its primary purpose of "allocate[ing] appropriately between shareholders and ratepayers the risk of power cost variability the ERM is meant to address" the ERM has the added benefit of "motivate[ing] Avista to effective[ly] manage or even reduce its power costs."[167] This makes logical sense as ratepayers have no ability to mitigate power cost variability, but Avista does, even if its power is not absolute. To achieve the goal of appropriately allocating risk, "setting a proper baseline is necessary for the ERM to function as intended."[168] Constantly moving the baseline up and down in GRCs, leads to distorted results–the Commission should allow baseline adjustments "only in extraordinary circumstances."[169]

61. While the Commission has acknowledged that a forward-looking approach to power costs can be appropriate, these adjustments are "few and demand a high degree of analytical rigor."[170] This is part and parcel of the "known and measurable" standard applied to pro forma alterations to the test year. As the Commission explained, to be "measurable" does not mean simply that an expense is quantifiable as estimates and budget forecasts are numerical, but are not sufficient.[171] Additionally, any such projection must be tied to offsetting factors.[172] This is because the value of using the test year process is that it captures the complex relationships

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[166] *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Docket UE-011595, Final Order: Fifth Suppl. ¶ 7, (June 18, 2022).
[167] *Wash. Utils. & Transp. Comm'n v. Avista Corp.* Docket UE-060181, Order 3 ¶ 23 (June 16, 2006).
[168] *Avista Corp.,* Dockets UE-170485, et al., Order 7/02/02 ¶ 160 (Apr. 26, 2018).
[169] *Id.* ¶ 160.
[170] *Puget Sound Energy,* Dockets UE-090704 & UG-090705, Order 11 ¶ 26 (Apr. 2, 2010).
[171] *Id.* ¶ 26.
[172] *Id.* ¶ 28.

among the various aspects of utility costs, revenue, load, and other factors.[173] The less certainty there is that actual costs and offsetting factors are known, the greater the risk that an adjustment will disturb that relationship and the less appropriate the adjustment.[174] This principle is maintained in power cost forecasting, if the "model inputs are reasonable and the modelling is comparable in analytical rigor" to the other adjustments which include "rigorously matching costs and revenues."[175]

62. Here, on every point, Avista's proposed portfolio error adjustment fails as a matter of law. First, the proposed adjustment possesses no analytical rigor. It is, to quote Avista, "simpleton" math involving the averaging of the past three years of ERM variance and spreading the impact over the next years.[176] This does not meet the legal requirement for an adjustment to revenue. It does not, as required by the Commission, alter the power forecast modelling inputs in a principled way, and focuses instead on modifying the outputs to Avista's benefit.[177] It does not help predict future gas or electricity prices, the implied market heat rate, or how forward prices are inadequate inputs because they collapse as they reach real time.[178] Avista provided no analysis to support a three-year average, no evidence to show that using a three-year average would reduce variance or predict how variance will behave in future years.[179] In short, under Commission precedent, the Commission should reject the portfolio adjustment error as analytically deficient.

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[173] *Avista Corp.,* Dockets UE-090134 & UG 090135 *(consol.)* Final Order 10 ¶ 41 (Dec. 22, 2009).
[174] *Id.* ¶ 47.
[175] *Id.* ¶ 49.
[176] Kalich, TR. 289:25–290:12.
[177] Kinney, TR. 182:11–15.
[178] *Id.* at 182:11–15, 212:13–22, 213:1–3.
[179] *Id.* at 218:1–17, 200:7–21, 193:3–12; Kalich, TR. 296:4–7.

63. Avista's proposed adjustment also fails to meet the known and measurable standard and the requirement that any increase in costs must be matched with offsets. Avista attempts to argue that because each ERM year already paired costs with offsets, Avista's proposed methodology is "known and measurable."[180] This argument misses the mark. Each test year contains a different complex set of relationships among the various aspects of utility costs and benefits.[181] Any adjustments made to revenues from a test year require rigorous analysis to be certain that the relationship between costs and benefits is maintained. In other words, each year must be considered, examined, and explained separately. This is evident in power costs here, where 2022 power costs were driven by a spike in gas prices which were not offset by higher electricity prices, as well as 2023 power costs which were caused by falling electricity prices in the context of stable gas prices.[182] Avista's approach requires abandoning the Commission's ratemaking standard of setting each year's rates in accordance with the costs and benefits specific to that year. Avista is, in effect, asking the Commission to reduce "known and measurable" costs to "quantifiable" costs and abandon the Commission matching principle. The Commission should reject this attempt to rewrite its test.

64. Here, Avista was unable to explain how averaging the 2022 or 2023 costs would ensure that costs in 2025 and 2026 would be appropriately matched to benefits in those years.[183] In fact, Avista admitted that under its definition of "known and measurable," the Commission could "potentially" "set rates based on events unrelated to rate year costs."[184] This kind of hypothetical adjustment is particularly flawed in this case because it would require future ratepayers to pay

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[180] Kinney, Exh. SJK-17T at 11:1–8.
[181] *Avista Corp.*, Dockets UE-090134 & UG-0910135, Order 10 ¶ 41 (Dec. 22, 2009).
[182] Kinney, Exh. SJK-1T at 69:5–14.
[183] Kinney, TR. 190:13–191:17.
[184] *Id.* at 188:23–189:1.

for unrelated events as 2021, 2022, and 2023 power costs, the years encompassing COVID-19, a war in Ukraine, and COVID-induced inflation.

65. Significantly, there is good reason to doubt that the years 2021, 2022, and 2023 are, in fact, emblematic of a fundamentally new market–rather, they represent a short historical dataset about which one must be cautious.[185] As noted above, Avista's modelling error, if that is the core challenge Avista faces, is not well correlated with ERM variances. In fact, the extreme variability seems to be moderating. For example, in 2024, Avista admitted that it added a large customer that "offset substantially all of the forecast impact of higher power supply costs on results in 2024."[186] Additionally, Avista's 2024 quarterly report noted that forecast power prices had not changed significantly during the second quarter, resulting in a lower impact of power costs and reducing variance from its 2022 peak.[187] Avista's proposed methodology has no mechanism for capturing offsets like new contracts, improved forecast pricing, or any other as yet unknown developments. Accordingly, the Commission should reject Avista's proposed portfolio adjustment error for violating the known and measurable standard.

66. Avista is correct to note that power cost forecasts do use estimates and inputs, but that does not justify its proposed adjustment. Avista's forecast methodology is the result of reasonable inputs and rigorous methodology. But Avista is not trying to adjust inputs, it is modifying its outputs to its benefit. [188] There is a fundamental difference between using data to

[185] Kalich, Exh. CGK-7T at 54:10–15.
[186] Christie, TR. 129:11–21. Public Counsel notes separately that Avista's decision not to include this development in its testimony is deeply problematic. If, in fact, as Mr. Christie testified, the new customer would create an additional two to three million dollar impact in 2025 and beyond, it should be included in the rates. Avista is free to forego recovery of expenses, but if this new increased revenue exclusions of future revenues is not something that Avista can "set aside and manage in a future case." Presumably, any refund for 2024 costs will be addressed in the 2024 ERM filing, but if there is a future impact, the Commission should order Avista to calculate the impact of this new contract and require a compliance filing.
[187] Christie, TR. 132:3–21; Kalich, Exh. CGK-7T at 19 (Illustration 1).
[188] Kinney, TR. 182:11–15.

determine a median hydro year because it helps predict future hydro years and authorizing Avista to collect more money upfront so that predictive accuracy is no longer necessary. Moreover, the hearing clarified that the proposed adjustment will not improve its forecast; at most, Avista model changes, "would be a good thing to consider going forward."[189] If Avista were to engage in a workshop and present its case for how its modelling could be improved, the Commission could consider whether such improvements were appropriate. Until then, the Commission should reject Avista's forecast error adjustment.

67. Similarly, the Commission must reject Avista's proposal to alter the ERM baseline due to its portfolio error adjustment. The Commission has clarified that it is important that the ERM baseline be as accurate as possible.[190] The Commission has indicated that too many baseline adjustments can be excessive and that it would "carefully consider" any baseline adjustments and change it 'only in extraordinary circumstances" such as "more closely matching the baseline to actual collections."[191] As with the forecast error adjustment discussed above, the proposed ERM baseline adjustment is fatally flawed under Commission precedent. Avista has failed to show how the proposed adjustment would be more "accurate." As Staff's Attorney pointed out on cross examination, Avista's willingness to abandon its original methodology for a more palatable lesser number is fatal to a baseline adjustment.[192] Avista could not say which proposal would make the ERM more accurate.[193] Without an improvement in accuracy, alterations to the ERM baseline should be rejected.

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[189] Kalich, TR. 300:11–15.
[190] *Avista Corp.,* Dockets UE-170485, et al., Order 7/02/02 ¶ 160 (Apr. 26, 2018).
[191] *Id.* ¶ *160*.
[192] Kalich, TR. 273:17–25.
[193] *Id*. at 273:1–23.

68. Avista's only real justification is that their proposal would improve their outcome. But, to borrow Avista's own admonition, the ERM "should not be changed based on how current conditions benefit one party or another, particularly in the absence of alternative model recommendations."[194] Avista suggests that if the Commission adopted their proposal it would result in fair recovery with no loss assigned to either party.[195] But that is patently false; Here, a $29.7 million adjustment would not cause 2024 costs to match the forecast. Instead, it would turn a $17 million surcharge, of which Avista would have to bear $7.7 million, and make it a refund of $12.7 million, of which Avista gets to keep $5.7 million. As this illustrates, Avista's proposal is not an attempt to improve its forecasts, but an attempt to capture a windfall–an unearned, unjustified swing in its favor. The Commission should not permit an alteration to the ERM baseline on such pretense at "accuracy."

B. The Commission Should Reject Avista Modifications to the ERM Dead and Sharing Bands

69. In addition to rejecting the proposed portfolio error adjustment, the Commission should also reject modifications to the ERM dead and sharing bands. On this record, modifying the dead and sharing bands would frustrate the basic policy purpose of the ERM, which is to equitably allocate the risk of changes in commodity prices and to incentivize Avista to use its available tools to control costs.[196] Avista has not met its burden of proof to show either that it has no control over power costs or that modification of the ERM dead and sharing bands is necessary to account for some change in circumstances. In the absence of such proof, the Commission should maintain the dead and sharing bands as currently constituted.

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[194] *Avista Corp.*, Dockets UE-170485, et. al. Final Order 07/02/02 ¶ 125 (Apr. 26, 2018).
[195] Kalich, TR. 279:11–18.
[196] *PacifiCorp*, Dockets UE-230172 & UE-210852, Order 08 ¶ 389 (Mar. 19, 2024).

70. The Commission explained the ERM has two purposes, one of which is to share the risk of power price volatility[197] and the second is for the dead and sharing bands to act as "guardrails" to ensure that the utility does not ignore price volatility because it knows it will be made whole by ratepayers.[198] This does not require Avista to have total control over the market or its power costs; otherwise the ERM would not be a risk allocation. Avista has previously accepted that the ERM assigns variability over which Avista had limited control.[199] The ERM was a bargain in which Avista received faster reimbursement of power costs in exchange for a cost sharing tool like the ERM to "prevent the utility customer from absorbing the risk of fuel adjustment mechanisms…that benefit utilities."[200] Avista is attempting to alter that bargain without cause.

71. In this rate case, the evidence supports the conclusion that the ERM is working as intended. As shown in Avista's chart of cumulative risk allocated between ratepayers and Avista, the ERM has aligned Company and ratepayer interests.[201] If anything, ratepayers have borne more than an equal share of the risk, particularly during periods of surcharges.

72. Even if the ERM were not working–which it is–the alteration in the size of the dead and sharing bands does not follow from Avista's primary complaint about volatility or the fundamental change in the marketplace related to errors in predicting the value of the thermal fleet, which has increased by an order of magnitude.[202] This is a reason to refine Avista's predictions, not a valid argument to change the size of Avista's dead and sharing bands, which are fixed. The bands have the same impact if Avista under-collects power costs by $40 million or

[197] *Avista Corp.,* Docket UE-060181, Order 3 ¶ 23 (June 16, 2006).
[198] *PacifiCorp.*, Dockets UE-230172 & UE-210852, Order 08, ¶ 390 (Mar. 19, 2024).
[199] Kinney, Exh. SJK-24X at 15:9–11.
[200] *PacifiCorp.*, Dockets UE-230172 & UE-210852, Order 08, ¶ 389 (Mar. 19, 2024).
[201] Kalich, Exh. CGK-20X.
[202] Kalich, Exh. CGK-7T at 23:1–7.

by $11 million. Nor does Avista attempt to show why a $2.5 million dead band would solve its Avista's self-described problem of large variations in its forecast error. The information asymmetry between Avista, the Commission, and intervening parties demands a specific showing from Avista before such an alteration should be authorized.[203] The proposal to alter the sharing bands should be rejected on that basis alone.

73. Avista has also failed to establish that a lack of control over prices would justify reducing or limiting the dead and sharing bands. Avista argues that the ERM is punitive when the Company lacks control over power costs. But again, Avista's current problem is not with controlling power costs; it is with a self-admitted inability to model the value of its thermal fleet.[204] Moreover, Avista's testimony does not establish that it has no tools to control power costs. If, as Avista claims, there is developing regional scarcity, Avista has the power, through its planning process, to build new generation and going forward has the ability to participate in the Western Resource Adequacy Program, or WRAP.[205] Avista can also hedge even when there is some challenge of market liquidity, as other utilities are able to hedge.[206] Finally, the emergence of the energy imbalance market (EIM) provides utilities like Avista control over how it chooses to bid into these markets.[207]

74. At most, Avista reaffirms what the parties already know, which is that it can be difficult to hedge power costs and reduce variability. It may be that bilateral forward contracts are harder to obtain at levels that Avista traditionally enjoyed for its hedging policy.[208] But difficult it not

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[203] Earle, Exh. RLE-1CT at 9:13–10:16.
[204] Kinney, Exh. SJK-1T at 16:16–22.
[205] Earle, Exh. RLE-1CT at 11:9–21.
[206] *Id*. at 13:1–3
[207] *Id*. at 14:5–19.
[208] Kalich, Exh. CGK-7T at 22 fn.22.

the same as impossible, as Puget Sound Energy's 2023 success in hedging illustrates.[209] As Public Counsel Witness Earle argues Avista would need to conduct a full review of its hedging policies and practices before claiming impossibility.[210] If the market is changing, then Avista needs to start figuring out how to "solve" the new market dynamics [211] rather than seeking a handout to absolve itself of its responsibility. Reducing Avista's financial incentive absent good cause undermines the purpose of the ERM.

75. Finally, and fatally, Avista does not make a persuasive case that the ERM dead and sharing bands are too large. As noted above, despite the current ERM design, Avista has been able to maintain its access to capital, attract and compensate investors, expand its rate base, and is on course to make its earnings guidance for 2024. Undoubtedly, Avista would like to collect more power costs upfront, but Avista cannot say that the dead and sharing bands are undermining its financial health. Avista's filing lacks the kind of evidence necessary for the Commission to make an informed judgment about whether the dead and sharing band incentives are improperly designed for Avista's specific situation. There is no analysis of the relative share of power costs over time, no calculation of how much the dead bands contribute to earnings attrition, or any analysis of why the $2.5 million/$2.0 million bands Avista proposed are more appropriate. Based on this record, the Commission should reject the Company's modification of the dead and sharing bands.

[209] Kalich, TR. 293:21–294:11.
[210] Earle, Exh. RLE-1CT at 14:15–19.
[211] Kalich, TR. 268:3–20.

C. The Commission Should Reject Staff's Proposed Alteration to the ERM Dead and Sharing Bands.

76. Staff's proposal to "simplify" the ERM dead band by creating a single dead band of $3 million[212] also lacks sufficient analytical depth for Commission adoption and should likewise be rejected. The proposal takes up a single page in Staff Witness Wilson's testimony and is untethered from any analysis that would justify the proposed reduction. Mr. Wilson observes that PacifiCorp's current dead bands are approximately two percent of its net power costs and that a reduction to $3 million would result in a dead band that is slightly higher for Avista. However, Mr. Wilson ignores the Commission's order, which observed that PacifiCorp's dead and sharing bands were designed to be closer to 3.45 percent of net power costs.[213] The more accurate interpretation of the Commission's order is that PacifiCorp's bands are too low for its intended purpose. Additionally, although Wilson notes that Avista is in a surplus capacity relative to PacifiCorp and therefore Avista's circumstances differ materially, Wilson does not explain how that difference requires a smaller set of incentive bands.[214] The fact the Avista can sell excess power to help manage net power costs gives Avista more rather than less control compared to its peers. And as Public Counsel Witness Earle observes, companies like Avista try harder when incentives are greater–a reduction of the bands would reduce the effectiveness of the incentive.[215] At a minimum, an alteration such as Mr. Wilson suggests awaits additional factual development about how a smaller single band would accomplish the same incentive compared to the current design. Absent a more robust record, the Commission should reject Staff's proposal.

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[212] Wilson, Exh. JDW-1TCr at 37:1–12.
[213] *PacifiCorp*, Dockets UE-230172 & UE-210852, Order 08, ¶ 392 (Mar. 19, 2024).
[214] Wilson, Exh. JDW-1TCr at 35:1–9.
[215] Earle, Exh. RLE-17T at 3:8–14.

D. Climate Commitment Act (CCA) Costs Should Not Be Included in ERM Prudence Reviews

77. Finally, Staff also proposes adding CCA allowance cost expenses to Avista's ERM annual filings and prudence review. Public Counsel understands Staff's interest in regular reviews of CCA related allowance costs and its point that CCA allowance costs are intertwined with dispatch and power purchase decisions.[216] Unfortunately, the four year and 10-month CCA compliance period does not align with an annual review process.[217] Whether CCA costs are ultimately prudent will depend on an evaluation of Avista's prudence at the end of the CCA compliance period. Only at the end of the compliance period will the Commission know whether Avista procured the correct number of allowances and whether it did so in a cost-effective manner. Mr. Wilsons' alternative suggestion of interim annual reviews, followed by a post-CCA determination of prudence, may be appropriate. It is unclear, however, why those interim reviews would be handled better in a power cost proceeding which is reviewed on a shorter time frame without the full context of a GRC. If, as Staff observes, CCA allowance purchases impact dispatch decisions, power purchases, and resource procurement and planning decisions, the logical place for interim prudence reviews subject to later check would seem to be a GRC. The Commission may ultimately resolve this issue in its open policy docket on the CCA. Making the decision to conduct CCA compliance reviews in the Avista ERM proceedings is premature.

V. CAPITAL STRUCTURE

78. The Commission should lower Avista's ROE and set it at 8.5 percent or 9.25 percent. Over the past decade, the Commission's awarded ROE has been more than sufficient to ensure Avista's financial soundness, to support its credit, and enable it to raise sufficient capital. In the

[216] Wilson, Exh. JDW-1TCr at 24:16–25:11.
[217] Earle, Exh. RLE-17T at 7–19.

words of one of the credit rating agencies, "Avista's operating performance remains strong despite the weak financial metrics that were caused primarily by low cash flow generation due to a customer tax credit implemented in 2021."[218] As Avista admitted, even as Avista pays out the last of these COVID-era tax credits to customers,[219] barring a major event, Avista is already on course to meet its credit threshold earnings.[220] As discussed below, in fact, there is good reason to believe that the Commission's awarded ROE has been too generous to meet the required level of sufficient support mandated by Commission precedent. Public Counsel therefore urges the Commission to lower the ROE from its current 9.4 percent to a level more in line with Avista's actual level of risk.

A. The Commission Should Set Return on Equity at 8.5 Percent with the Overall Return at 6.86 Percent

79. Cost of capital has three main components, capital structure, ROE, and cost of debt, which, when blended together create an overall ROR.[221] Here Avista proposes a capital structure with 48.50 percent equity and 51.50 percent Long-Term Debt, with cost of debt at 4.99 percent and a 10.4 percent ROE which would result in an overall ROR of 7.61 Percent.[222] For the purposes of this proceeding, Public Counsel contests Avista's ROE and therefore the overall ROR. Avista's awarded ROE should be based on the actual cost of capital, which should be closely tied to economic realities.[223] As Public Counsel Witness David Garrett testified, "the problem is, with respect to regulated utilities, there has been a trend in which awarded returns fail to track closely with actual market-based capital."[224] Accordingly, a more accurate ROE,

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[218] Christie, TR 117:3–11; Vermillion, Exh. DPV-6X at 1.
[219] Christie, TR. 102:3–15; 16–19.
[220] *Id*. at 119:4–8, 121:13–15.
[221] *PacifiCorp*, Docket UE-230172 & UE-210852 (*consol*.) Order 08/06 ¶ 112. (Mar. 29, 2024).
[222] Christie, Exh. KJC-4T at 18:13–15.
[223] Response Testimony of David Garrett, Exh. DJG-1T at 5:17–6:6.
[224] *Id.* at 6:3–5.

given current economic realities would be 8.5 percent, resulting in an overall ROR of 6.86 percent.[225]

1. The Commission sets an ROE at a sufficient level.

80. The Commission standard for setting ROE is well established. The Commission and parties are guided by a centuries old precedent that utilities are entitled to a return that was "reasonably sufficient to assure confidence in the financial soundness of the utility, and should be adequate, under efficient and economical management to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties."[226] The Commission follows this standard more than 100 years later.[227]As any rational decision maker confronted with different results from the same models would do, the Commission adopted the approach of identifying a range of possible returns and then picking a return within that range.[228]

81. It is important to emphasize that the Commission's standard for setting returns is focused on what is sufficient and adequate rather than on what is better for a utility. A higher ROE will always be better for shareholders and better credit ratings will reduce the cost of debt. It is also illogical as protecting against a higher cost of debt by authorizing an even higher return on equity is a losing game. Setting the ROE above what is strictly necessary to support credit, raise capital, and maintain reasonably sufficient financial soundness, necessarily constitutes a transfer of wealth from ratepayers to shareholders.[229] In theory, any such excess transfer of wealth violates the Commission standard of "fair" rates.[230] But in the current situation in which one in two

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[225] Mark E. Garrett, MEG-3 (schedule 3.10) and MEG-4 (scheduled 4.10).
[226] *Bluefield Water Works & Imp. Co. v. Pub. Serv. Comm'n of W. Va,* 262 U.S. 679 (1923).
[227] *Wash Util. & Transp. Comm'n v. Puget Sound Energy*, Docket UE-220066 & UG-220067 (*consol.*) Final Order 10 ¶ 148 (Apr. 18, 2022).
[228] *Avista Corp.,* Docket UE-170485, et. al. Order 07/02/02 ¶ 59 (Apr. 26, 2018).
[229] Garrett, Exh. DJG-1T at 6:8–14.
[230] RCW 80.28.020.

ratepayers qualify for assistance and four in five ratepayers earn $66,000 or less annually, an unnecessary transfer of wealth becomes, in itself, an inequity.

2. Financial models are biased upward.

82. Modelling is subjective. Traditionally, the Commission relies on “familiar analytical tools such as the Discounted Cash Flow (DCF) and Capital Asset Pricing Model (CAPM) models.”[231] In theory, financial models such as the CAPM and DCF are useful because they predict the level of returns necessary to maintain investor confidence in a utility’s financial soundness and to continue to invest in the utility so that it can discharge its public duties. But although these models possess a veneer of objectivity stemming from the academic economic jargon with which they are described, as this Commission has noted, the models require “subjective judgments” and will “vary significantly” depending on how those judgments are exercised.[232]

83. The Commission is correct to question the subjective nature of this modelling because, models have a tendency toward positive bias. Despite rules and regulations governing stock analysts, multiple studies have found that equity analysts persistently overestimate the growth rate, by almost 100 percent.[233] This means that entities like *Value Line* have consistently overstated growth forecasts when compared to actual growth.[234] This can lead to errors as much as 3.0 percentage points when estimating the equity cost of capital.[235]

84. This bias in financial modelling seeps into utility regulation. A 2022 study of 3,500 electric and gas rate cases found that commissions have a two to four precent gap of excess

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[231] *Wash. Utils. & Transp. Comm’n v. Puget Sound Energy,* Dockets UE-190529, et. al., Final Order 08/05/03 ¶ 102 (July 8, 2020).

[232] *Avista Corp.,* Docket UE-170485 et. al., Order 07/02/02 ¶ 60 (Apr. 26, 2018).

[233] Marc H. Goedhart, et al., *Equity Analysts, Still Too Bullish*, McKinsey on Fin., 14–17, (Spring 2010).

[234] Andrew C. Szakmary, et. al., *An Examination of Value Line’s Long-Term Projections*, J. of Banking & Fin. 820-833 (2008).

[235] Peter D. Easton & Gregory A. Sommers, *Effect of Analysts’ Optimism on Estimates of the Expected Rate of Return Implied by Earnings Forecasts*, J. of Acct. Research, 45, 983-1015 (2007).

returns over in the past two decades.[236] Nationally, this translates into $2.5 billion to $8.9 billion in excess costs being borne by consumers, the majority of which occur in the electric sector.[237] What is most puzzling is that these results are incongruous with the level of risk under which utilities operate. Utilities are widely considered as the least risky investments, "prime examples of low-risk, defense firms."[238] As Mr. McKenzie conceded at the hearing, less risky companies deserve lower returns.[239] And yet, utility stocks have out-performed higher-risk, market-based returns in the long-term, outperforming the Dow Jones Industrial average.[240]

85. This general trend of utility returns surpassing market-based returns is evident when considering Avista's pension plans. Avista retains financial consultants to forecast returns so that it does not over or underfund its pension and retirement plans.[241] The projected portfolio return is ███ percent.[242] The expected return on large capital stocks, the most comparable to utilities is ███ percent, or ██ basis points below Avista's currently authorized ROE.[243]

86. There is also evidence in this record that Avista's awarded rates have consistently exceeded the rates that are necessary for capital acquisition and higher than are warranted by Avista's business risk. As Mr. McKenzie admitted in testimony, "a financial model is only valuable to the extent that it accurately predicts or explains investor behavior."[244] Here, it is

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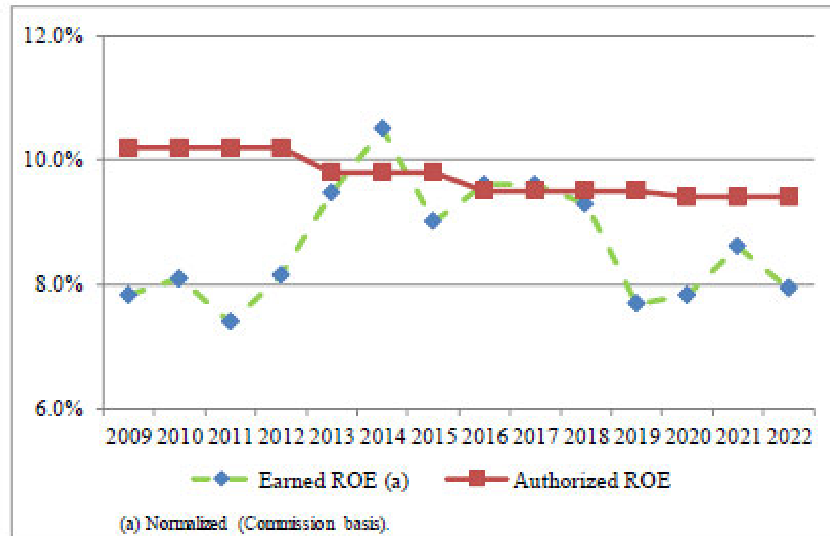
[236] McKenzie, Exh. AMM-24X; Karl Dunkle Werner & Stephen Jarvis, *Rate of Return Regulation Revisited, Working Papers*, Energy Inst., U.C. Berkeley (2022) at 27; *see also,* McKenzie, Exh. AMM-23X; David C. Rode & Paul S. Fischbeck*, Regulated Equity Returns: A Puzzle,* Energy Policy (Oct. 2019), at 5, (noting that the regulated equity premium above the riskless Treasury rate has grown from 277 basis points in 1980 to 668 basis points in 2018 despite the fact that the risk of the underlying assets has not changed.).
[237] Werner & Jarvis, *supra* note 236, at 36.
[238] Garrett, Exh. DJG-1T at 14:6–16:10.
[239] McKenzie, TR. 166:18–24.
[240] McKenzie, Exh. AMM-26X at 1.
[241] Christie TR. 136:21–25, 137:7–14. The primary consultant is Willis Towers Watson, but they also use VERIS, Sageview, and JP Morgan; Christe TR. 136:21–25, 138:1–12.
[242] McKenize, Exh. AMM-36CX at 1.
[243] *Id*. at 2.
[244] McKenzie, TR. 148:18–21.

undisputed that Avista's actual return on investment has been below the authorized threshold in 11 of the last 14 years, producing the following chart.[245]



87. Although Avista claims that this trend results in "under" earning and "attrition," this only holds true if these actual returns somehow interfered with access to capital or financial soundness. And here, it is undisputed that they have not. Avista has continued to issue new stock, at well over book value, to the tune of $595 million from 2015 to 2023.[246] Despite these actual earnings, Avista has increased its rate base by $1.8 billion from 2015 to 2024. Since 2010, Avista, despite its actual earnings has issued $1.337 billion in dividend payments.[247]

88. Moreover, in applying Mr. McKenzie's admonition that actual investor behavior is the key inquiry, the last decade proves that these actual returns, which are known to investors, have been sufficient to maintain Avista's financial soundness and access to capital.[248] These lower actual earnings are, in essence, already accounted for as part of Avista's "strong" operational

[245] McKenzie, Exh. AMM-1T at 21, Figure 2.
[246] McKenzie, Exh. AMM-13 at 1.
[247] Direct Testimony of Lance D. Kauffman, Exh. LDK-1CT at 56. From 2015, Avista issued $997 million in dividend payments.
[248] McKenzie, TR. 155:9–17.

performance and cash flow. Investor's actual behavior–continuing to invest with actual returns in the 8.0 percent range–should take priority over the calculations produced by subjective financial models.

3. The Commission should adopt Public Counsel's recommendation

89. Although the recent COVID-recovery inflation has resulted in financial models showing more risk, there is still room for the Commission to move safely downward from its current authorized return. The appropriate range is 8.0 percent to 9.2 percent.[249] Mr. Garrett recommends 8.5 percent and Mr. Kauffman 9.25 percent–Public Counsel submits that the Commission should lower ROE from the current authorized rate for three compelling reasons. First, a lower ROE is consistent with a fair rate of return for the level of risk of a utility like Avista. Second, Avista's debt-equity ratio is robust enough that it dictates a lower ROE. Third, Avista's cash flow is already sufficient to maintain credit and does not require increased support through a higher ROE.

90. The most important factor for the Commission to consider is the level of risk that an investor faces using the general principle that the lower the risk, the lower the expected return.[250] Because no investor invests solely in one stock, the kinds of risk that an investor must evaluate are market risks such as interest rates, inflation, or major socioeconomic risks rather than firm-specific risks.[251] The example that Public Counsel's Witness David Garrett provides is illustrative and compelling. When Enron collapsed from firm-specific misbehavior in 2001, only an irrational investor holding only Enron stock would suffer. A rational diversified investor would be relatively unaffected. Actual investors hold Avista stock as part of a portfolio, and

[249] Garrett, Exh. DJG-1T at 3 Figure 1.
[250] *Id.* at 10:3–6.
[251] *Id.* at 10:11–11:18.

absent extraordinary firm specific developments are not going to abandon it. And, in fact, other utilities were able to survive the Enron collapse. Accordingly, the kinds of risk that the Commission should consider are systemic risks.

91. Avista, like other utilities, is a low-risk defensive firm with a great deal of insulation from market risks such that even during a recession, they profit.[252] Avista confirmed that this is the case in the hearing, admitting that it has been able to increase dividends every year for 22 years despite the Great Recession in 2008, the worst and most disruptive health crisis in a century, and the subsequent supply chain inflation following it.[253] Because it is a low-risk firm, its returns should correspondingly be lower.

92. Additionally, Avista is a well-established company well into its mature growth stage.[254] Such companies are distinguished, as Avista is, by paying a larger portion of its earnings through dividends rather than reinvesting in operations and relying on stock price valuation.[255] When a firm reaches the point at which it is focused on redistributing wealth directly to shareholders, it is no longer appropriate to look at short-term growth metrics, but instead to use sustainable growth rates.[256] This is independent of size; the weight of the evidence supports the finding that smaller companies do not justify higher returns.[257] Even Mr. McKenzie conceded on questioning that Avista is most comparable to large capital stocks.[258] In this setting, what is fair, is to use a growth rate between the expected rate of inflation and nominal GDP growth.[259]

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[252] *Id*. at 15:1–16:10.
[253] Christie, TR. 110:10–112:7.
[254] Garrett, Exh. DJG-1T at 21–14-22:11.
[255] *Id*. at 22:4–8.
[256] *Id.* at 22:8–11.
[257] *Id.* at 30:13–41:22.
[258] McKenzie, TR. 170:6–9.
[259] Garrett, Exh. DJG-1T at 23:18–21.

93. In a related issue, the Commission should reject Avista's request for flotation costs. These costs are not out-of-pocket costs for the Company.[260] Furthermore, the flotation costs are known to both the buyer and the seller in the transaction. The Commission has no metric by which to determine which party would have negotiated to capture that additional value; i.e. would the stock price have dropped or risen slightly.[261] Only competition could fairly make that allocation.

94. Avista's business model is also different that other industries with respect to debt. Utilities, which have large fixed assets, stable earnings, and low risk, can afford higher debt ratios than other industries.[262] Both when compared to other utilities in Avista's proxy group and in comparison to non-utilities, Avista has a debt ratio significantly lower than average, 51.5 percent to 55 percent.[263] When applied through the Hamada formula, it is possible to adjust Avista's ROE to account for Avista's superior debt ratio, which results in a lower ROE of 9.2 percent through the CAPM modelling.

95. Finally, as discussed above, the reality of Avista's situation is such that the Commission's decision to keep the ROE at 9.4 percent has been more than sufficient to continue Avista's capital growth, access to capital, and ever-increasing dividend payments. Looking forward, the expected pace of inflation has returned down to 2.3 percent,[264] and as Avista admits, all other things being equal, lower inflation typically leads to lower bond rates and an improvement in Avista's credit.[265] With Avista's tax payments ceasing at the end of the year,

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[260] *Id*. at 45:1–4.
[261] *Id*. at 45:5–16.
[262] *Id*. at 51:15–52:11.
[263] *Id.* at 52:14–20.
[264] Direct Testimony of Bradley G. Mullins, Exh. BGM-1T at 19:11–20.
[265] Christie, TR. 110:17–19, McKenzie, TR. 159:16–21, 160:4–7.

Avista's cash flow will naturally improve over time.[266] These facts should reassure the Commission that it can lower Avista's ROE to align with its actual cost of capital without negatively impacting Avista's financial performance.

4. The Commission should discount Avista's modelling.

96. Avista presented the testimony of Adrien McKenzie to argue for a much higher rate of return. The Commission should discount Company witness Adrien McKenzie's testimony for two reasons. First, Mr. McKenzie's modelling has consistently failed to predict Avista's investor behavior, and, as Mr. McKenzie agreed, "a financial model is only valuable to the extent that it accurately predicts or explains investor behavior."[267] Because his modelling does not, the Commission should not follow his recommendation. Second, Mr. McKenzie admits that his modelling and testimony are not useful to the Commission in achieving the goals of *Bluefield* and the Commission's test.[268]

97. Comparing Avista's actual performance against the actual awards by this Commission expose Mr. McKenzie's bias. In each iteration of testimony, Mr. McKenzie asserts that a reasonable ROE is, "imperative to ensure the company has the capability to maintain and build its credit…while funding infrastructure development."[269] And it is hard to argue that the Commission's rulings, to date, have not met that criterion. In 2015, almost a decade ago, Mr. McKenzie identified that Avista had a rate base of approximately $2.5 billion and needed to fund $1.8 billion in planned infrastructure over the next five years (i.e. by 2021).[270] As of this year, Avista has maintained its credit, currently has an existing rate base of $4.3 billion, and plans for

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[266] Christie, TR. 102:16–19.
[267] McKenzie, TR. 148:18–21.
[268] *Id*. at 151:1–6.
[269] McKenzie, Exh. AMM-28X at 7:1–16.
[270] *Id*. at 6:12–17.

an additional $1.5 billion in the next two years. In other words, the rates actually awarded by the Commission have been sufficient to achieve what Mr. McKenzie identified as necessary a decade ago.

98. While the Commission's actual choices allowed for massive capital investment and financial stability, fully meeting the *Bluefield* directive, Mr. McKenzie's testimony about his financial models have been consistently inaccurate. Over the last decade of testimony regarding his financial modelling, Mr. McKenzie provided conservative estimates of what investors would need to invest. Mr. McKenzie was wrong. Below is a table comparing Mr. McKenzie's modelling testimony against actual results.

Table 2 McKenzie's Financial Model ling vs. Actual Investment Outcomes

Year	McKenzie model range	McKenzie recommendation	Actual award
2015	9.83% - 11.03%[271]	9.9%[272]	9.5%[273]
2017	9.6% - 10.8%[274]	9.9%[275]	9.5%[276]
2019	9.9%-10.9%[277]	9.9%[278]	9.4%[279]
2022	9.5%-10.9%[280]	10.25%[281]	9.4%[282]

99. Not once has Mr. McKenzie's estimated modelling range included the return authorized by the Commission. And despite that, Avista has retained its access to credit and grown its rate base from $2.5 billion to $4.3 billion. The Commission should conclude from this actual

[271] *Id.* at 5:22–25, 6:12–17.
[272] *Id.* at 5:22–25, 6:12–17.
[273] *Wash. Utils. & Transp. Comm'n v. Avista Corp.,* Dockets UE-150204 & UG-150205, Order 05 ¶ 5 (Jan. 6, 2016).
[274] McKenzie, Exh. AMM-29X at 5:25–6:10.
[275] *Id*. at 5:25–6:10.
[276] *Avista Corp.,* Dockets UE-170485 et. al., Order 07/02/02 ¶ 73 (Apr. 26, 2018).
[277] McKenzie, AMM-30X at 4:1–8.
[278] *Id*. 4:1–8.
[279] *Avista Corp.,* Dockets UE-190334, et. al., Final Order 09 ¶ 34 (Mar. 25, 2020).
[280] McKenzie, Exh. AMM-31X at 5:16–6:17.
[281] *Id*. at 5:16-6:17; McKenzie, Exh. AMM 30X at 4:1-8.
[282] *Avista Corp.,* Dockets UE-220053, UG-220054, & UE-210854 (*consol.*), Final Order 10/04 ¶ 156 (Dec. 12, 2022).

performance that Mr. McKenzie's modelling should be deeply discounted for the purpose of setting a sufficient ROE in a utility rate proceeding.

100. This deep discount is further bolstered by Mr. McKenzie's testimony at the evidentiary hearing. He admitted his modelling and testimony cannot be used by the Commission to help satisfy the *Bluefield* inquiries about the level of return necessary for capital acquisition or financial soundness. In Mr. McKenzie's words, "I'm not making predictions about Avista's financial soundness based on a specific ROE outcome in this case."[283] He also does not claim that Avista needs a specific ROE in order to raise capital.[284] The self-described value of his testimony is to use financial models to develop a "fair range."[285] And yet, even here, Mr. McKenzie was forced to concede that his analysis was considerably higher than Avista's own analysis for investing to fund its pension.[286]

101. The reality is that Avista is a financially healthy company that has flourished over the past decade, and which has safely emerged from the COVID-19 challenge to the American economy. The Commission should continue to lower Avista's ROE to be consistent with the actual cost of capital.

VI. REVENUE REQUIREMENT ADJUSTMENTS

102. Although not addressed in the evidentiary hearing, Public Counsel requests that the Commission make several downward revenue adjustments to Avista's revenue requirement. The Commission should reject Avista's proposed executive pay increase and both Avista and Staff's proposed Operations and Maintenance (O&M) adjustments. The Commission should allocate

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[283] McKenzie, TR. 151:1–3.
[284] *Id*. at 151:11–13.
[285] *Id*. at 151:4–5.
[286] *Id*. at 170:15–17.

more Director and Office Insurance expenses to shareholders. The Commission should remove investor relations expenses and industry dues from Avista's revenue requirement. The Commission should update the Company's Pension and Employment Benefits expenses and should adjust Avista's revenues to account for rents from electric property. A full list of the revenue adjustments appears in the cross-answering testimony of Public Counsel's Witness Mark Garrett. [287] All of these proposed adjustments are appropriate.

A. The Commission Should Reject Executive Pay Increases from Avista, and Reduce the Allocation of Director compensation and Director-Officer Insurance Expenses

103. Avista proposes a $60,000 electric and $19,000 revenue increase for executive compensation.[288] Public Counsel requests that the Commission reduce Avista's revenue requirement and order Avista to provide an executive salary survey including municipal and cooperative utility executive compensation rates. As Avista admitted during the hearing, hourly and middle management staff at municipal utilities make similar pay compared to Avista employees.[289] Although municipal executives manage utilities safely and efficiently, investor-owned utility executives are compensated at higher levels.[290] It is logical to understand the difference between municipal executive and Avista executive pay as being attributable to the dual fiduciary duties that Avista executives have to both shareholders and customers. The compensation above municipal executive pay is a reasonable estimate of the value that Avista executives provide to Avista shareholders. Ultimately, Avista shareholders should bear that cost. For now, Public Counsel asks the Commission to disallow these executive pay increases pending more information from Avista.

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[287] Garrett, Exhs. MEG-10 (Electric) and MEG-11 (natural gas).
[288] Direct Testimony of Kaylene Shultz, Exh. KJS-1T at 58:7–13.
[289] Christie, TR. 115:15–20.
[290] Garrett, Exh. MEG-1T at 7:8–8:5.

104. Avista is seeking a 90 percent recovery of $2.5 million in Board compensation and $1.2 million in director and officer liability insurance.[291] Public Counsel asks the Commission to reduce the percentage allocated to ratepayers from Board members cash compensation to 50 percent, and by 100 percent for stock-based compensation. The Commission should reduce the insurance allocation to 50 percent.

105. Directors and officers are biased toward shareholder interests. As this Commission has previously recognized, directors and officers owe a fiduciary duty to shareholders, but do not owe a fiduciary duty to ratepayers.[292] As Avista's Chief Executive Officer explained in a recent press release announcing the 22nd consecutive year of dividend increases, the Board of Directors are committed to maximizing shareholder value.[293] It is telling that while Avista's directors manual requires directors to focus on shareholder growth, nowhere does that manual mention customers.[294] When combined with the fact that Avista's executives are compensated at higher levels than comparative municipal executives,[295] the conflict of interest among Avista's leadership between loyalties to shareholders and keeping rates low for ratepayers justifies shareholders bearing an equal share of executive level expenses. The primary value of a Board dedicated to shareholders is to the shareholders. It is inappropriate to fixate on shareholder value in a regulated monopoly permitted only because it is in the public interest. In all decision-making, the board members and officers must also maximize public value. Until Avista makes that a core tenet of these positions, Avista shareholders should pay the servants of their

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[291] Schultz, Exh. KJS-1T at 70:15–16.
[292] *Avista Corp.,* Dockets UE-090134 et. al., Order 10 ¶ 135, fn.161 (Dec. 22, 2009).
[293] Christie, TR. 114:3–6.
[294] *Id*. at 140:1–21.
[295] Garrett, Exh. MEG-1T at 7:8–8:5.

interests. Limiting the allocation of Director compensation would result in an $819,000 electric and $259,000 reduction in revenue requirement.

106. The case is even stronger regarding Avista's insurance policies. Even acknowledging that attracting and retaining effective management is beneficial to the ratepayers to some degree, the weight of authority by the utility commission favors a 50 percent or less rather than a 90 percent allocation of insurance expenses. An eclectic mix of bipartisan states, Arkansas, California, Connecticut, Nevada, New Mexico, Florida, and New York, have all concluded that an equal split is appropriate.[296] As Connecticut persuasively noted, the main beneficiaries of these insurance policies are shareholders. It is unlikely ratepayer loss is even compensable. In the end, payments from this insurance does not go to ratepayers, only to the Company. The secondary benefit of helping attract competent officers is ancillary to the main purpose of insurance. Accordingly, shareholders should pay at least half of this expense, if not the majority. Limiting reimbursement to 50 percent will result in a $237,000 electric and $75,000 gas reduction in revenue requirement.

B. The Commission Should Reject Avista's and Staff's Proposed O&M Adjustments

107. In Avista's pro forma O&M expense adjustments, Avista escalated O&M accounts by 6.3 percent for electric and 4.57 percent for natural gas operations.[297] This was based on Avista's internal averaging. This initial proposal would have resulted in a $12.4 million and a $2.3 million gas revenue increase, for a total revenue requirement increase of $16.4 million.[298] Public Counsel initially objected to this allocation including COVID-19 inflation impacted years and proposed a 2.5 percent escalation, which is dictated by reasonable expectations of inflation after

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[296] *Id*. at 30:21–33:24.
[297] Garrett, Exh. MEG-1T at 10:4–20 (summarizing those accounts exempted from escalation).
[298] Andrews, Exh. EMA-1T at 44, Table 1 (adding the "direct" testimony lines).

the Federal Reserve interest rates have reduced inflation.[299] For its part, Staff argued that this escalation was not known or measurable and that Avista's data was so variable as to render it unreliable as a forecast of future escalation.[300] Instead, Staff recommended including only "the incremental O&M expenses not already included in the Company's test year."[301]

108. In its rebuttal case, Avista accepted Staff's offer to update these expenses to the 12 months ending December 2023 and escalated the amount by the 2.5 percent suggested by Public Counsel. Updating the expense to December 2023 resulted in a $5.9 million dollar increase to electric and 467,780 decrease to gas revenue requirements.[302] Using the 2.5 percent escalation yielded a $4.6 million escalator for electricity and a $1 million escalator for gas.[303] The final result was a $10.5 million electric revenue requirement increase and a $569,000 revenue increase for natural gas, for a total increase of $11.1 million.

109. Upon review of Staff's testimony, Public Counsel is persuaded that the Commission should not award any escalation from the test year. This is because an inflation escalator, whether derived from Avista's internal averaging, or from Public Counsel's informed estimate for future inflation fail the known and measurable test. As discussed above, pro forma adjustments "typically cannot be an estimate, a projection, the product of a budget forecast, or some similar exercise of judgment—even informed judgment—concerning future revenue, expense, or rate base."[304] Until the inflation occurs, Avista will have no bills, contracts, or

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[299] Garrett, Exh. MEG-1T at 14:3–15:7.
[300] Hillstead, Exh. KMH-1T at 15:8–16:10.
[301] *Id.* at 16:14–16.
[302] Andrews, Exh. EMA-7 (12ME 06.2023 adjusted to 12 ME 12.2023 for electric and gas).
[303] *Id.*
[304] *Puget Sound Energy,* Dockets UE-090704 & UG-090705, Order 11 ¶ 26 (Apr. 2, 2010).

documents to base their recovery upon. And escalation from inflation, while likely, is not certain. As Staff pointed out, in 2023, O&M expenses shrunk by 2.39 percent.[305]

110. Public Counsel also opposes updating the O&M accounts to December 2023 for a different reason. The second part of the known and measurable standard is that expenses must be matched with revenues and offsets.[306] As the Commission explained, the value of a test year process is that it captures the complex relationships among the various aspects of utility costs and revenue.[307] Here, in order to preserve those relationships, Avista would have had to either escalated the entire test year including revenues and costs by six months or provided a full accounting of the offsets that the additional expenses in the new 12-month period provided. But Avista did neither. Thus, while it is true that Avista has the documentation for the 12 months ending in December 2023, it has not matched those expenses to changes in revenue, load, or other factors to. Under Commission precedent, however, it should deny any escalation and deny Staff's proposal to shift the operation expenses forward. The result is that the Commission should strip out the entirety of the $11.1 million revenue increase for the O&M escalation.

111. Only if the Commission is going to alter its precedent and permit an inflation escalation of operating and administrative costs would Public Counsel's position about a more reasonable inflation estimate be appropriate. As Public Counsel Witness Mark Garrett observed, using the COVID-19 affected inflation years is not defensible.

[305] Hillstead, Exh. KMH-1T at 16, Table 4.
[306] *Avista Corp.,* Dockets UE-090134 & UG 090135 *(consol.)* Final Order 10 ¶ 43 (Dec. 22, 2009).
[307] *Id.* ¶ 41.

C. The Commission Should Reduce Recovery of Investor Relations Expense and Disallow Industry Dues

112. Avista maintains an investor relations unit to provide information in the form of news releases, investor presentations, and regulatory filings for investors and potential investors.[308] This includes earnings reports for shareholders, calls with equity analysts, and investor conferences. The audience and intended beneficiary of this information are shareholders, and they should be required to share in the expense of providing these investor relations. While there is an indirect benefit to ratepayers caused by removing some friction from the process of attracting investors, Mr. McKenzie's testimony makes it clear that the core decision points for investors are the hard metrics. If Mr. McKenzie is correct, ratepayers should pay only part of this expense. A 50 percent allocation would reduce the electric revenue requirement by $201,000 and the gas by $60,000.

113. Avista seeks $240,204 for Edison Electric Institute (EEI) and $133,440 for American Gas Association (AGA) membership dues. A significant proportion of these entities' activities involved political activities and legislative lobbying.[309] Moreover, much of the lobbying appears to advocate on behalf of its members' private interests and the Federal Energy Regulatory Commission (FERC) has opened an investigatory docket on the issue.[310] A number of state commissions have already disallowed industry dues, including Kentucky, Minnesota, California, and Oregon.[311] The tax reporting that EEI and AGA use applies a narrow definition of lobbying that does not permit this Commission to determine how much of their activities serve the utilities

[308] Garrett, Exh. MEG-1T at 34:15–35:3.
[309] *Id*. at 15:16–16:2.
[310] *Id*. at 19:10–20:19.
[311] *Id*. at 11–15.

versus the public interest.[312] Until Avista can prove what portion of these industry dues serve the public interest, the Commission should disallow the entire expense.

D. The Commission Should Update the Company's Pension and Employment Benefits Based on Actuarial Reports

114. Avista provided an updated actuarial report in February 2024 regarding its pension and other post-employment benefits expense. In 2022, Avista entered a pension settlement with a non-recurring expense amortized over 12 years. Avista did not, however, include the full reduction to its pension expense on an ongoing basis.[313] Including those ongoing lower pension expenses lowers the revenue requirement by $1.285 million for electric and $407,000 for gas.[314]

VII. POWER COSTS

115. As discussed above, Public Counsel's main recommendation for power costs is for the Commission to reject Avista's proposed alterations to the ERM. Public Counsel also recommends that Avista be ordered to update power costs in 2025 and to update EIM benefits per Public Counsel Witness Earle's testimony.

A. The Commission Should Update Net Power Expense Forecast in August 2025 If the Commissions Permits a Multi-Year Rate Plan

116. Public Counsel supports Alliance of Western Energy Consumer's (AWEC) recommendation that Avista be ordered to provide an updated forecast for net power expenses. One of Avista's complaints about forecasting power expense is that it has to forecast prices as much as 35 months beforehand in order to conduct a multi-year filing.[315] One practical solution that does not require undermining the purpose and utility of the ERM is to provide for more

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[312] *Id*. at 17:7–18:11.
[313] Garrett, Exh. MEG-9T at 3:2–11.
[314] *Id*. at 2:17–20.
[315] Kinney, Exh. SJK-1T at 50:11–15.

frequent power forecast updates.[316] In addition, as AWEC observes, the removal of Colstrip in Rate Year 2 will be complex and given the significance of that milestone, it is far superior to update the forecast and mark-to-market calculation closer in time.[317]

B. The Commission Should Reject Avista's Proposed Methodology for Energy Imbalance Market Benefits.

117. EIMs have the potential to add significant efficiencies for Avista by permitting it to take advantage of real time markets using 15 and five minute-markets.[318] This permits Avista to adjust its hour-ahead schedules and capture additional value.[319] This benefit needs to be properly forecast for Avista's net power forecast to be accurate.

118. Avista's current methodology is flawed. Avista attempts to estimate benefits by running an hourly dispatch model, and then running the model with intra-hour modelling to obtain an incremental value.[320] Using, as Avista does, an average hourly price results in an undervaluation of the benefits from participation in EIM.[321] When Public Counsel's Witness Earle tested Avista's methodology against out-of-sample data, the statistical validity of Avista's methodology is called into question by its poor R-squared result.[322] Dr. Earle also noted that Avista ignored the variability of the distribution of five-minute prices within an hour, which separately results in undervaluation.[323]

119. These methodological flaws are validated by comparing Avista's valuation of benefits using its modelling and that of CAISO, the operator of the EIM. In 2025, for example, Avista

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[316] Earle, Exh. RLE-17T at 7:11–18.
[317] *Id*. at 7:5–8.
[318] Earle, Exh. RLE-1CT at 17:10–13.
[319] *Id*. at 17:14–22:9.
[320] *Id.* at 26:1–3
[321] *Id.* at 22:7–9, 27:3–14.
[322] *Id.* at 28:10–17.
[323] *Id.* at 29:1–16.

projects a $5.5 million benefit, but CAISO calculates a $22.3 million benefit in annualized benefit through March 2024.[324] While Avista complains that CAISO's data include greenhouse gas revenues no longer available to it, the effect of that is $2.2 million, which moves the needle slightly, but not enough.[325] Avista admits that in 2022 and 2023, it benefited by $24.1 million and $20.1 million.[326] Such a dramatic difference between a forecast benefit and actual results cannot be justified.

120. Public Counsel Witness Earle also provides an alternative model, using 25 months of historical data.[327] He tested this with a bootstrapping analysis to create a confidence interval, and excluded outliers.[328] This analysis produced an estimated benefit more in line with actual results, a $20.1 project EIM benefit.[329]

121. In its rebuttal case, Avista does not so much defend its methodological errors as attempt to excuse them by claiming the methodology was "approved" in the 2020 workshop.[330] That claim is dubious given that EIM was so new. Regardless, Avista claims that its model, "requires a single price to perform its math" and that this somehow justifies using hourly price assumptions known to be inaccurate.[331] This is a poor reason to continue using Avista's model. If Aurora's estimates are flawed, as they are, they need to be fixed, not excused.

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[324] Earle, Exh. RLE-1CT at 30:9–14.
[325] Kalich, Exh. CGK-7T at 54:1–12.
[326] Earle, Exh. RLE-1CT at 31:1–6.
[327] *Id*. at 31:9–15.
[328] *Id.* at 33:1–10. Though Avista complains that there are only 25 months of data used and the data is further reduced by excluding outliers. Kalich, Exh. CGK-7T at 54:6–9, Avista has stated that 12 to 24 months of data would be sufficient "to predict future opportunities." Earle, Exh. RLE-1CT at 31, fn.59. Moreover, excluding outliers is conservative in that it decreases the estimated EIM benefit. Earle, Exh. RLE-1CT at 33:1–9.
[329] *Id.* at 8:8–15.
[330] Kalich, Exh. CGK-7T at 49:17–50:5.
[331] *Id*. at 50:3.

122. Avista then accuses Public Counsel Earle's alternative method of being "a classic textbook approach with simplifications that ignore key real-world issues."[332] Avista's attempted rejoinder misses the mark. First, using inaccurate numbers as input is a more egregious simplification than Dr. Earle's use of CAISO data. If Dr. Earle assumes too much knowledge, Avista is intentionally clinging to known ignorance. And it ignores the uncomfortable reality that Dr. Earle's forecast is much, much closer to the real benefits from the EIM. If, in fact, there are "real world" issues that must be added into a forecast of EIM benefits using CAISO data, then Avista should adjust Dr. Earle's model accordingly. Flaws in a superior model are not a justification to continue using a flawed model under predicting EIM benefits by $15 million a year.

123. On the merits, Avista's critique of the CAISO methodology is unpersuasive.[333] Third party expert, E3 considers the CAISO methodology to be a good benchmark of EIM benefits.[334] Dr. Earle addressed Avista's concerns with transmission costs, differences between bidding and actual costs, and the value of a counterfactual analysis.[335] Avista's attempt to illustrate how CAISO overstates value with an example undermines its own position. Avista posits a market price of $30/MWh and a hydro generator that it bid at a cost of $50/MWh and then claims that if CAISO cleared the price at $25/MWh, CAISO's model would assume a greater benefit than actual market cost.[336] Initially, under either scenario, Avista would be losing money if it operated a generator at a cost higher than market price, making this example so contrived as to be clearly false. Avista's EIM benefit occurs when Avista rationally sells power above its cost of

[332] *Id*. at 53:15–16.
[333] *Id*. at 44:12—47:6.
[334] Earle, Exh. RLE-1CT at 35:9–11.
[335] *Id*. at 33:15–35:11.
[336] Kalich, Exh. CGK-7T at 46:15–47:6.

production. Assuming a loss in the transaction distorts the analysis. But fundamentally, the fact that CAISO's EIM obtained a lower price is, in fact, a benefit. It beats market prices. Avista's forecasting needs to take that into account, not disregard it.

124. The Commission should also reject Staff's conclusions concerning Public Counsel's analysis of the EIM benefit.[337] Staff witness John D. Wilson states that "it is not necessary for Avista to calculate benefits from the WEIM and include them in the NPE forecast, because Avista's modelling is designed to capture all market power transaction opportunities as part of its production cost forecast."[338] Mr. Wilson misapprehends the situation. It is not that Avista has not included the five-minute dispatch in the EIM in its calculations,[339] it is that, as Dr. Earle explains, Avista has done so incorrectly. Mr. Wilson admits that he did not investigate the methodology for inclusion of EIM benefits, and simply assumes that Avista did so correctly. Mr. Wilson's analysis on this should be rejected by the Commission

125. Avista's response presents the Commission with a complicated decision. Avista cannot defend its own modelling, and while Avista critiques Dr. Earle's modelling, it makes no effort to improve it so as to add confidence. Between the two, Dr. Earle's approach is more in line with the reported results of the CAISO. Public Counsel submits that in this situation, the appropriate approach is to adopt Dr. Earle's methodology and impute $20.1 million as an EIM benefit to Avista. If Avisa comes up with a better model, it is free to present it to the Commission for adoption.

126. Finally, Public Counsel is compelled to note that the dispute over EIM modelling is the kind of modelling that is intended for forecast adjustments. Analytical rigor turns on debates

[337] Wilson, Exh. JDW-1TCr at 2:17–3:7.
[338] *Id.* at 3:2–4. WEIM stands for "Western Energy Imbalance Market."
[339] Wilson, Exh. JDW-1TCr at 3:17–20.

over input and assessing predictive value. This stands in stark contrast to Avista's proposed ERM modification which simply insulates Avista from its own inadequate modelling.

VIII. RATE SPREAD

127. The Commission has explained that, in principle, each customer class would pay exactly 100 percent of the costs that Avista incurs in providing it service.[340] The Commission acknowledged, however, that in practice, parity is "rarely, if ever achieved because there are simply too many variables at play and the relationships among them are dynamic, not static."[341] Accordingly, the Commission uses principles of rate stability, gradualism, and avoidance of rate shock in deciding whether to adjust a rate spread.[342]

128. Although the Commission has not acknowledged a specific set of parity ratios, in recent cases Staff[343] has taken the position that parity rations within 0.1 (i.e. .90 to 1.10) are within a range of reasonableness with anything outside of the range warranting adjustment.[344] AWEC, in its testimony accepted this formula.[345] For the purposes of this rate proceeding, Public Counsel does not see a need for the Commission to adopt or refine a formula for adjusting rate spread in a mechanical fashion. Public Counsel concedes that Avista's class cost of service study found a 0.86 rate parity ratio and that Public Counsel has offered no contrary testimony.[346] Ordinarily, this may justify some adjustment, but under the specific circumstances, the Commission should exercise caution and approve an equal allocation.

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[340] *Wash. Utils. & Transp. Comm'n v. Puget Sound Energy*, Dockets UE-170033 & UG-170034, Final Order 08 ¶ 11, fn.10 (Dec. 5, 2017).
[341] *Id.* ¶ 11, fn.10.
[342] *Wash. Utils. & Transp. Comm'n v. PacifiCorp d/b/a Pacific Power & Light Co*, Docket UE-100749, Order 06 ¶ 315. (Mar. 25, 2011).
[343] Staff has not taken a position on rate spread in this filing.
[344] *See e.g. Puget Sound Energy*, Dockets UE-190529 & UG-190530 et. al., (*consol.*) Final Order 08/05/03 ¶ 472 (July 8, 2020).
[345] Kauffman, Exh. LDK-1CT at 10:17–11:6.
[346] Cross-Answering Testimony of David E. Dismukes, Exh. DED-10T at 4:6–10.

A. The Commission Should Adopt an Equal Rate Spread as Recommended by Public Counsel

129. Public Counsel asks the Commission to exercise caution in adjusting residential class allocation for four reasons. First, the size of Avista's revenue requirement increase means that any asymmetrical rate spread will have an outsized impact on parity rates and may overshoot the mark. Second, there are very good reasons to question whether Avista's Class Cost of Service Study has accurately captured the results of the last adjustment. Third, the expiration of Colstrip and move toward renewable energy will already move residential payers toward parity. Finally, as discussed above, residential ratepayers are already distressed from existing rate increases. Any overcorrection will exacerbate inequity from rate increases.

130. In its initial filing, Avista proposed an equal rate allocation among the classes.[347] With such a large proposed rate increase, an equal allocation would move all of the rate classes toward parity on a return ratio basis.[348] Even at the amount of revenue requirement proposed in its rebuttal case, an equal rate spread would result in a modest movement toward parity on a return basis.[349] If the Commission awards a revenue requirement at Avista's rebuttal position, a differential proposal such as AWEC proposed would result in an additional $23 million being allocated to residential ratepayers over both rate years.[350] Accordingly, although Avista supports AWEC's proposal, it would not oppose an equal allocation.[351] Public Counsel concedes, as it must, that if a lower amount is awarded, the move toward parity will be more modest. If the eventual amount of the approved revenue requirement awarded exceeds $72.5 million, however,

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[347] Direct Testimony of Joseph D. Miller, Exh. JDM-1T at 1:22–2:7.
[348] *Id.* at 7:16–19.
[349] Miller, Exh. JDM-20X at 1.
[350] *Id.* at 1.
[351] *Id.* at 2.

Public Counsel asks the Commission to award an equal rate spread. Below that point, Public Counsel continues to counsel caution for the reasons discussed below.

131. Caution is particularly warranted because of the timing of Avista's cost of service study and because of the impact of Colstrip being removed from rates. As described in Public Counsel Witness Dismukes' testimony, the 2022 Avista GRC resulted in a differential allocation to residential rates of 1.49 times the system average increase in rate year one and 1.09 times the average in rate year two.[352] As Avista concedes, its current study only captured six months of the Rate Year 1 increases and none of the Rate Year 2 increases.[353] As a result, the modest move in residential rate parity from 0.84 in 2022 to 0.86 in 2024 is an understatement of what residential rate parity actually is today. Any attempt to adjust parity now runs the risk over overshooting by rate pancaking the last 18 months of differential allocation on top of the two years of this rate case. Without a means to adjust until the 2026 general rate case, this runs a very real risk of real harm to residential customers.

132. This caution must be heightened by the 2025 removal of Colstrip and by the shift toward renewable energy. As AWEC elicited during testimony, the costs of Colstrip are allocated differently than the rest of rates, and are governed by a separate settlement.[354] AWEC pointed out that, for Schedule 25, customers were allocated $10 million out of a total $236 million, or 4.2 percent, while residential customers were paying $50 million out of $2.2 billion, or 2.2 percent.[355] This illustration, however, proves Public Counsel's point. Under the current Colstrip tracker, residential customers are receiving a good deal—proportionally less of the cost allocated

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[352] Dismukes, Exh. DED-10T at 3:19–4:3.
[353] *Id*. at 5:1–6.
[354] Miller, TR. 327:16–23.
[355] Marcus Garbarino, TR. 176:21–177:24.

to the residential class than Schedule 25. When Colstrip ends, residential customers will lose that beneficial allocation going forward.[356] Although it is counter-intuitive, removing Colstrip from rates hurts residential ratepayers with respect to other classes, particularly where Colstrip will be replaced with higher power costs which are allocated less beneficially. This makes caution with allocation particularly important around the end of 2025.

133. The shift toward renewable energy will also shift costs toward residential customers over time.[357] As Public Counsel Witness Dismukes notes, Avista has increased its rate base by 12.9 percent over the past two years, while operating expenses expanded by 2.4 percent.[358] This shift, which must be completed by 2045, allocates 51.46 percent of production expenses on a renewable peak credit basis to residential customers.[359] The increase of distributed energy sources will naturally shift higher load factors onto residential and small commercial customers.[360] While in its nascent stage, this shift will bear increasing attention.

134. The rational way to proceed with uncertainty around the issue–from an awkwardly timed cost study, rate pancaking from the last rate case, the removal of Colstrip, and the continued transition to renewable energy–is to agree to an equal allocation of costs and to ensure that Avista's next cost study accounts for the removal of Colstrip. An equal allocation will move all rate cases toward parity until the Commission has better information about how the residential class has absorbed the last significant modification and responded to the changing resource mix.

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[356] Dismukes, Exh. DED-10T at 7:12–19.
[357] *Id*. at 5:20–8.
[358] *Id*. at 6:3–5.
[359] Miller, Exh. JDM-20X at 2.
[360] Dismukes, Exh. DED-10T at 7:2–4.

B. The Commission Should Not Adjust the Basic Charge

135. The Commission should reject Avista's proposal to shift more costs to the basic charge for three reasons. First, Avista overstates the cost attributable to customer-related activities and uses a skewed comparator group. In reality, Avista's current charge recovers 82.4 percent of electric customer costs and 51 percent of gas customer costs after removing administrative and general expenses not attributable to consumer service.[361] Avista's proposed increase is 31 percent higher than regional comparators.[362] Second, shifting costs from variable to fixed charges necessarily reduces conservation incentives.[363] Relying on a limited study of a subset of low-income customers, Avista suggests that low-income customers use more electricity and therefore do not conserve.[364] That argument fails in the face of robust contrary studies[365] and TEP Witness Colton's comprehensive refutation.[366] The general principle that the Commission should encourage conservation holds. In fact, as illustrated by the public comments in this matter, low-income customers resort to extreme measures to keep energy bills low. Third, and finally, increasing fixed charges is not necessary in the presence of a decoupling mechanism.[367]

136. Staff's proposal for a more modest increase to the basic charge falters on these same points. Avista's current charge already recovers the majority of Avista's fixed costs, while an increase further constrains low-income customers' ability to conserve.[368] With Avista's access to decoupling, an adjustment to the basic charge is just not warranted.

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[361] Dismukes, Exh. DED-1T at 10:21–11:4.
[362] *Id*. at 10–16.
[363] *Id*. at 13:7–12.
[364] Miller, Exh. JDM-1T at 38:15–18.
[365] *See*, Dismukes, Exh. DED-1T at 13–3.
[366] Colton, Exh. RDC-1T at 67:2–72:14.
[367] Dismukes, Exh. DED-1T at 18:6–15.
[368] Dismukes, Exh. DED-10T at 8:12–9:16.

IX. THE COMMISSION SHOULD ORDER AN UPDATED COST BENEFIT ANALYSIS OF AVISTA'S WILDFIRE PLAN

137. Public Counsel requests that the Commission incorporate into its order several conditions regarding Avista's Wildfire Resiliency Plan. Although Public Counsel acknowledges the need for wildfire planning and strongly supports the effort to reduce wildfires, the Commission should require Avista to maintain contemporaneous records of cost-benefit decisions that must necessarily be made while spending more than $400 million over a 10-year period. It is troubling that four years into this plan, Avista is still not tracking whether the outages on its system are causing wildfires or whether their deployed strategies are effective.[369] For those metrics Avista does track, such as spark events, Avista should have been tracking whether those events are causing fires.[370] During the hearing, Avista consented to remedying this lack of information, and Public Counsel requests that the Commission order Avista to (1) provide an explanation for any 15 percent variance in wildfire spending in any category of the current wildfire plan in its next GRC; (2) to begin tracking wildlife ignition events or "heat" events no later than January 2026 or provide a written explanation of the delay, and (3) complete a full cost-benefit analysis of all strategies deployed as part of the Wildfire Resiliency Plan and produce it at or before Avista's the next GRC filing. This analysis should include a risk profile for Avista's service territory and should provide sufficient analysis to allow Avista, the Commission, and intervening parties to confirm that Avista is deploying the right tools, including undergrounding, in the right areas to maximize risk reduction and cost-effectiveness.

[369] David Howell, TR. 236:25–237:4.
[370] *Id*. at 242:9–18.

X. THE COMMISSION SHOULD EXERCISE CAUTION WITH PORTFOLIO REVIEW OF PROVISIONAL CAPITAL EXPENSES

138. In a bench request, the Commission asked the parties to address any legal issues with the 2023 provisional plant review process and to provide suggestions on how to handle provisional plant reviews going forward.[371] Public Counsel agrees with AWEC that the provisional capital process arising from the 2022 GRC is problematic. As noted by Public Counsel's response, there were eight new business cases with a total Washington electric and gas spend of $4,970,212.[372] Avista's total 2023 variance above authorized net plant for Washington investment was $22,075,000 ($20,441,000 for electric and $1,634,000 for gas)–21.7 percent of which is attributable to these eight new business cases which were unaccounted for in the rates approved in Avista's prior GRC.[373] Public Counsel does not believe that the current provisional capital review process affords it sufficient time or process to assess new business cases. At a minimum, Staff's proposed longer period for review is appropriate, but the use of the tracker does seem premature in this case, as issue of tariff design would need to be resolved.

139. Public Counsel also shares AWEC's concern that a portfolio review runs the risk of running afoul of the Commission's Used and Useful Policy statement, which specified that the interim capital projects must still be known and measurable and used and useful.[374] The Commission also warned that rate-effective period investments would depend on the Company's request and type of identified property and would not be a matter of matching budgets,

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[371] Notice of Bench Request No. 2 (filed Oct. 15, 2024).
[372] Public Counsel Resp. to BR-2, Recon. Attach (filed Oct. 22, 2024).
[373] *See* Avista 2023 Wash. Provisional Cap. R., at Attach. E, Tab 2, *Wash. Utils. & Transp. Comm'n v. Avista Utils.*, Dockets UE-220053 & UG-220054. Total new business cases in WA $4.97 million/total WA variance above authorized net plant $22.075 million = 21.7 percent.
[374] Pol'y Statement Used and Useful ¶ 20, *In re the Comm'n Inquiry Used and Useful Rate Effective Date*, Docket U-190531 (filed Jan 31, 2020).

something that a portfolio review does not satisfy.[375] If there is going to be a provisional capital review process, Public Counsel agrees with AWEC that it needs to be performed on a project-by-project basis.

140. It is also possible that new capital projects should simply not be included in provisional capital reviews. If, as Avista witness Elizabeth Andrews testifies, Avista needs the flexibility "to operate its business" during a multi-year rate plan,[376] it can do so; it may wait for the next general rate case. But Ms. Andrews testified that the majority of their capital cases would be unaffected by such a rule and that there are a "pretty limited amount of new business cases."[377] If the flexibility to include a pretty limited amount of rate cases is sufficiently concerning, Avista can propose a multiyear rate plan, but ask the Commission to approve a single year rate plan.[378]

XI. CONCLUSION

141. One thing that both sides in the current polarized political climate agree on is that income inequality is accelerating rapidly and that middle class families are increasingly struggling. The economic realities of Avista's customer base demonstrate this clearly. It is deeply uncomfortable to admit that in Washington, four out of five Avista customers make less than $66,000 annually and one out of two qualify for assistance. These economic realities do not happen in a vacuum, they are caused by policies and decisions that exacerbate income inequality. Any request, and any decision that exacerbates the redistribution of wealth from poor to rich must be closely examined.

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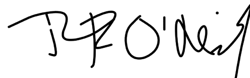
[375] *Id*. ¶ 42.
[376] Andrews, TR. 311:3–4.
[377] *Id*. at 321:13–14.
[378] Although Public Counsel has not taken a position on Staff's request for a single year rate plan in his matter, Public Counsel notes that AWEC is correct that the complexity of the removal of Colstrip does make this year a candidate for it. *See* Mullins, Exh. BGM-1T at 13:5–10.

142. As written, Avista's rebuttal request for $133 million of additional revenue over the next two years will improperly accelerate the defining inequality of our current times. At a minimum, the Commission should reject the proposed portfolio error adjustment and ERM modifications. It should also lower Avista's return on equity to 8.5 percent. The Commission should remove unsupported cost escalators, fairly allocate executive expenses to shareholders, and adopt Public Counsel's calculation of EIM benefits. The Commission should exercise caution and approve an equal allocation of rate increases. The Commission should require additional data on the efficacy of wildfire prevention and should approve individual rather than portfolio review for provisional capital projects. In the final analysis, unless the Commission limits rate increases to what is strictly necessary, the bend in the arc of our small slice of history will be toward more inequality.

DATED this 28th day of October 2024.

ROBERT W. FERGUSON
Attorney General



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