

**BEFORE THE WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,

Complainant,

v.

AVISTA CORPORATION, DBA AVISTA UTILITIES

Respondent.

DOCKETS UE-150204 and
UG-150205 (*Consolidated*)

POST-HEARING BRIEF OF AVISTA CORPORATION

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1 COMES NOW Respondent, Avista Corporation (hereinafter “Avista” or “the Company”),
and respectfully submits this Post-Hearing Brief in the above-captioned matter.

I. INTRODUCTION

2 *“For this case Staff determined that the revenue requirement calculated using a
modified historical test period was insufficient for both electric and natural gas
service. Therefore, Staff recommends the Commission exercise its discretion in setting
rates and provide an attrition allowance for both electric and gas service.”*
(McGuire, Exh. No. CRM-1T, p. 9:14-17)

Staff Witness McGuire has described the essence of the issue surrounding the determination of
the revenue requirement in this case. For rates to be “fair, just, reasonable, and sufficient”
including providing Avista with a reasonable opportunity to earn its authorized rate of return
during the 2016 rate year, an attrition adjustment is essential.

3 This Brief will demonstrate, based on evidence of record, why the sole use of a modified
historical test period with limited pro forma adjustments, as proposed by Public Counsel, ICNU
and NWIGU, will not produce a revenue requirement that is sufficient to allow the Company a

reasonable opportunity to earn the return agreed to by the parties in the May 1, 2015, Multiparty Settlement Stipulation. (See, Bench Exh. No. 1)¹ Moreover, this Brief will explain how the Staff and the Company are fundamentally aligned in their methodology for calculating attrition, save for one significant issue: the calculation of the appropriate O&M trending factor. The Commission has, within its authority, discretion to employ an “attrition” adjustment, under the circumstances of this case, in order to meet its obligation to provide the Company with a reasonable opportunity to earn the agreed-upon rate of return.

4

This Post-Hearing Brief will emphasize the following issues:

- It will explain why an attrition analysis should be used to determine the electric and natural gas revenue requirements in these dockets, as opposed to a modified historical test period with limited pro forma adjustments.
- It will explain why the O&M escalator proposed by the Company on rebuttal for the attrition adjustment, is a better indicator of expense levels for the 2016 rate year. This O&M escalator issue alone explains \$7.3 million of the difference in the revenue requirement derived by Staff and the Company – representing the only significant difference between the two attrition analyses. Staff’s use of an unreasonably low escalation factor for O&M expense was based on developing a “trend” of O&M for a one-year period from 2013 to 2014. Anomalies in this one year change in costs do not reflect O&M expense levels that will occur in the 2016 rate year.
- Expenses associated with major thermal maintenance should be “normalized” for both customers and the Company. Failing to do so, would result in the Company experiencing the full expense in the year in which it occurs, without the opportunity for cost recovery, thereby causing it to under-earn its allowed return.

¹ The Multiparty Settlement (Bench Exh. No. 1) resolved all issues among the parties relating to cost of capital, power supply costs, rate spread and rate design. The agreed-upon cost of capital called for a ROE of 9.5%, a 48.5% equity component, and a 5.2% cost of debt, resulting in a ROR of 7.29%. Several adjustments were made to establish a newer base level of power supply costs, with the further understanding that the Company would file to update the power supply adjustment in November to reflect then-current natural gas and electric market prices and new power supply and transmission contracts. Finally, O&M costs related to Coyote Springs II and Colstrip were removed from base power supply costs, with the understanding that they would be addressed in the remainder of the case. (See also, Joint Testimony, Bench Exh. No. 2)

- The Company is requesting that the Commission approve its decision, in principle, to move forward with Advanced Metering Infrastructure (AMI), with the understanding that Avista would present a showing in its next general rate case of the prudence of its decision, based on updated information with respect to costs and benefits. Whether that guidance is provided in this docket or not, the Company, nevertheless, requires approval, in these dockets, of the proposed accounting treatment related to the planned replacement of existing electric meters, without which, the AMI Project would be delayed or terminated.
- Contrary to the assertions of Staff Witness Mr. Gomez, Avista has demonstrated that its investment in Project Compass was prudently incurred and should be fully recovered.
- Avista supports a multi-year increase in funding for its Low Income Rate Assistance Program (LIRAP), which will provide a substantial increase to funding over the next several years.

5 The revenue requirements positions of the parties in this case are as follows: Avista proposes a \$3.6 million base revenue increase on rebuttal for its electric operations and a \$10.0 million base revenue increase for its natural gas operations. This was predicated on its attrition analysis, accompanied by Cross Check Studies to confirm the reasonableness of its analysis. Staff argues for a \$6.2 million revenue decrease for electric service and a \$9.0 million revenue increase for natural gas operations, using an attrition adjustment in addition to an adjusted historical test period. Public Counsel argues for a \$29.7 million revenue decrease for electric and a \$3.3 million revenue increase for natural gas, based strictly on an historical test period with limited pro forma adjustments. ICNU recommends a \$17.4 million revenue decrease for electric, and NWIGU recommends no revenue adjustment for natural gas, or, in the alternative, an attrition adjustment of \$3.6 million.²

6 Since the filing of Avista's original request for a \$33.2 million increase in its electric revenue requirement and a \$12 million increase in its natural gas revenue requirement,

² (See Norwood Exh. No. KON-1T, pp. 18-19) (See also Smith, Exh. No. JSS-4T, p. 6)

circumstances have changed. The evolution of Avista's request for rate relief is summarized in Table No. 5 (appended as Attachment A) and discussed in Mr. Norwood's testimony.^{3/4} The Multiparty Partial Settlement, if approved, would serve to reduce Avista's request, in and of itself, to \$16.8 million for electric and \$11.3 million for natural gas. Further reductions were made based on, in part, updated information provided to the parties resulting from revised allocation factors shifting costs from the Washington jurisdiction to Idaho, as well as updated information relating to tax adjustments and the timing of additions to net plant in service. This resulted in a revised revenue requirement, as of July of 2015, of \$10.0 million for electric and \$9.7 million for natural gas.⁵ Subsequently, Avista, in its rebuttal testimony, now proposes to exclude new plant investment and new operating expenses relating to AMI in the determination of its electric and natural gas revenue requirements for the 2016 rate period.⁶ This serves to remove an additional \$4.1 million from its electric revenue requirement.⁷ Avista, however, does need the Commission to approve its request for an accounting order relating to the planned replacement of existing electric meters, as explained later in this Brief.⁸ Finally, the electric revenue requirement is further reduced by \$3.0 million to reflect the proposed normalization of thermal maintenance associated with the Company's thermal projects.

7 The impact of the previous adjustments, as shown in the attached Table No. 5, is reflected in Avista's rebuttal position of a \$3.6 million electric base increase, and a \$10.0 million base

³ (Ibid.)

⁴ (Reproduced as Attachment A to this Brief) On October 29, 2015, the Company filed an updated power supply adjustment pursuant to the Partial Settlement Stipulation that further reduced the level of power supply expense by \$12.3 million. As shown in this attachment, the overall net impact on billed electric rates proposed by the Company in this case is \$0.0.

⁵ (Ibid.)

⁶ (Ibid.)

⁷ (Ibid.)

⁸ (Ibid.)

increase for natural gas.⁹ The \$3.6 million electric revenue requirement represents a 0.7% increase overall base rates for electric service and a 5.9% overall increase in base rates for natural gas service (6.3% for residential).¹⁰

8 Avista is requesting an effective date of January 1, 2016 (approximately one, and one-half weeks prior to the scheduled end of the statutory suspension period of January 11, 2016). This effective date of January 1 will minimize the number of bill changes for customers, by matching the January 1 scheduled expiration date of the ERM rebate.¹¹

II. AN ATTRITION ADJUSTMENT IS AN APPROPRIATE VEHICLE TO PROVIDE THE COMPANY WITH A REASONABLE OPPORTUNITY TO EARN A FAIR RATE OF RETURN

9 Staff Witness McGuire recognizes that rates calculated using a modified historical test year will generate revenues that will “fall short” of those necessary to provide Avista “with a reasonable opportunity to earn a fair rate of return.”¹² Mr. McGuire observed that “Avista has been experiencing very low load growth over the last several years, and if that load growth continues at a slow pace, the Company is not going to be able to generate the revenues necessary to cover the expenses moving forward.” (TR 445:24 – 446:3) In the circumstances of this case, where evidence demonstrates that rate base and expenses are rising much faster than revenues between the historical test period and the rate period, the Commission should look to an attrition

⁹ Table No. 5 also reflects additional LIRAP funding for electric and natural gas, as well as reductions associated with the power supply update filed October 29, 2015, and the expiration of the ERM rebate on December 31, 2015. This Table, when prepared, showed an estimated rate adjustment as of January 1, 2016, of \$2.2 million for electric and \$10.3 million for natural gas. This would represent an overall percentage change in billed rates of 0.4% for electric customers (0.5% for residential) and 5.9% for natural gas customers (6.4% for residential). (Exh. No. KON-1T, p. 38:4-12) Subsequently, on October 29, 2015, the Company filed the updated power supply adjustment called for in the Multiparty Settlement (see note 1, supra) which changed the previously estimated power supply adjustment from (\$10 million) to (\$12.3 million). This further reduced the total change in electric billed rates from a 0.4% increase to 0.0%.

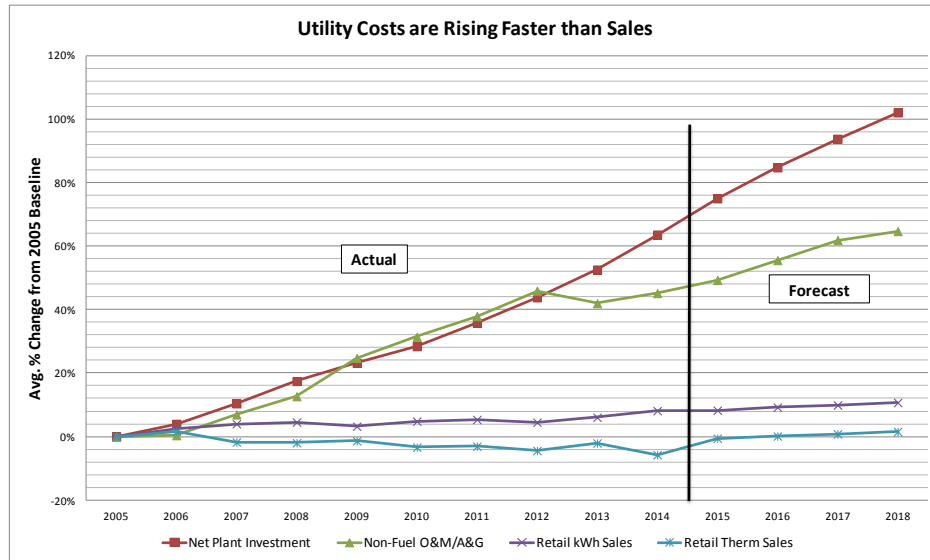
¹⁰ (Exh. No. KON-1T, p. 37:6-26)

¹¹ (Id., at p. 38:14-18)

¹² (McGuire Exh. No. CRM-1T, p. 28:8-10)

adjustment for ratemaking purposes. This is illustrated below (excerpted from Exh. No. SLM-1T, p. 11):

Illustration No. 7



10 As recently as its Order 08, dated May 7, 2012, in Dockets UE-111048 and UG-111049, at ¶489, the Commission recognized that an attrition adjustment is “one among the several possible responses” to address under-earning during the rate year:

11 We nevertheless find it appropriate to discuss the subject because an attrition adjustment is one among several possible responses the Commission could make to address a demonstrated trend of under earning due to circumstances beyond the Company’s ability to control. This form of adjustment was available to utilities during the early 1980s in an environment of exceptional inflation and high interest rates; it is equally available today if shown to be a needed response to the challenges posed by PSE’s current intensive capital investment program to replace aging infrastructure (emphasis supplied).

Accordingly, an attrition adjustment is not a “relic” of ratemaking in the early 1980s; rather, it remains a viable tool today to address the shortcomings of a historical test period with limited

pro forma adjustments.¹³ Moreover, in Avista's recent Dockets UE-120436 and UG-120437, the Commission approved a settlement agreement that included revenue increases that were based, in large part, on attrition, noting:

12 Here, both the Company and Staff performed attrition studies to project 2013 rates. We agree with the Company and Staff that the proposed 2013 rate increase is based significantly on attrition. (Para. 70 of Order 14)

Furthermore, Mr. Norwood discussed in his testimony the Commission's recent approval of a "K-Factor" mechanism for use by Puget Sound Energy in Docket Nos. UE-130137 and UG-130138, which was designed to accomplish the same thing as an attrition adjustment.¹⁴ The approved "K-Factor" relies on trends in growth rates of rate base, expenses and revenues over time. As such, it is representative of the difference in the annual growth rates of rate base and expenses versus revenues.¹⁵ As does an attrition adjustment, the K-Factor mechanism determines a revenue increase that is necessary to provide the utility with the opportunity to earn the allowed rate of return during the prospective rate year. It recognizes the fact that rate base and expenses will grow at a faster pace than revenue.^{16/17}

¹³ When discussing the allowed attrition adjustments in the context of prior orders of this Commission in the 1980s, Mr. McGuire observed that load growth during that period was "between 5 and 8 percent," and that comparing those numbers to numbers experienced today, Avista is experiencing "less than 1 percent annual load growth." (See TR 466:18-25) He went on to observe that, ". . . this Commission has provided attrition allowances when there's evidence of different rates of growth in revenues, expenses, and rate base such that test-year relationships are not likely to hold during the rate-affected period." (TR 467:12-17)

¹⁴ (Exh. No. KON-1T, pp. 21-22)

¹⁵ (Ibid.)

¹⁶ (Ibid.)

¹⁷ Public Counsel appealed Puget Sound Energy's approved "rate plan" in Docket Nos. UE-130137 and UG-130138, supra, to the Thurston County Superior Court, arguing, inter alia, that the "K-Factor" violated Commission precedent. (See, Cross Exh. KON-7CX). In its Brief to the Thurston County Superior Court, Public Counsel argued that the K-Factor "lacks an 'attrition study,' the evidentiary support that the Commission has always required before making attrition adjustments, and therefore it was not supported by substantial evidence." (Ibid.) The Thurston County Superior Court, nevertheless, rejected these arguments and affirmed the Commission's use of an attrition adjustment. The Thurston County Superior Court entered its order in Case Nos. 13-2-01576-2 and 13-2-01582 on July 25, 2014, Granting in Part and Denying in Part Petitions for Judicial Review.

13

It is also instructive to note what this Commission did and did not say about attrition in its most recent March 2015 Order concerning Pacific Power & Light (PP&L).¹⁸ NWIGU Witness Mullins suggested that the “facts in this case [Avista] are not materially different than in the 2014 Pacific Power General Rate Case.”¹⁹ That is simply not the case. In the recently-concluded PP&L case, the Commission found that the Company had not presented a study demonstrating that it was experiencing attrition:

14

The Company did not present persuasive evidence that it is suffering attrition in earnings. In particular, the Company did not present an attrition study. Moreover, the fact that the Company failed in the past to earn its authorized return cannot justify use of EOP absent a showing that, due to factors beyond the Company’s control, the Commission can expect this condition to continue into the future. There is no such evidence in the record of this case. (Emphasis added) (See ¶146 of Order 08 in Docket UE-140762)

This should be contrasted with the instant case, where both Avista and Staff have presented substantial evidence that the Company has and will continue to experience attrition.

15

There is a sound basis for the use of an attrition analysis that examines rate base, expenses and revenues during the rate-effective period of 2016. As noted by Company Witness Norwood, “through the attrition analysis, changes in rate base, operating expenses and revenues between the historical test period and the prospective rate year are all captured in the analysis, and provide for a matching during the prospective rate period.”^{20/21}

¹⁸ Wash. Utils. & Transp. Comm’n v. Pacific Power & Light Co., Dockets UE-140762, Order 08 (March 2015)

¹⁹ (Exh. No. BGM-1T)

²⁰ (Exh. No. KON-1T, p. 23:17-20)

²¹ The Rate Case and Audit Manual prepared by the NARUC Staff Subcommittee on Accounting and Finance enunciated certain principles meant to ensure that new retail rates resulting from a general rate case provide a utility with a reasonable opportunity to earn a fair return:

In looking at the months beyond the end of the test year, have the growth rates for rate-base, expenses, and revenues all remained fairly close and constant, maintaining the test year relationship among the three elements, or has one element changed dramatically, making the test year out of kilter with current operations? If so, can this situation be resolved through adjustments to the test year? . . . Whether using a future or historic test year, the auditor should judge the appropriateness of the test year that has been

It has been suggested by other parties in this case, such as Public Counsel Witness Ramas, that mechanisms such as decoupling, the Purchased Gas Adjustment (PGA), and the Energy Recovery Mechanism (ERM) will somehow “offset the impacts of attrition and potential regulatory lag.”²² This reflects a fundamental misunderstanding on the part of Ms. Ramas of what these mechanisms are designed to do. As explained by Mr. Norwood, none of these mechanisms have anything whatsoever to do with new rate base investment, which is the primary driver of Avista’s attrition.²³ Simply put, no rate base items are tracked through decoupling, the PGA or the ERM. Moreover, the secondary driver to attrition are increases in utility operating costs, excluding power supply costs and natural gas commodity costs. Again, none of these utility operating costs are tracked through decoupling, the PGA or the ERM.²⁴ The PGA mechanism operates independently of base natural gas retail rates and the ERM simply tracks differences in power supply costs between rate cases and, as such, is independent of the drivers of attrition. Finally, the decoupling mechanism only tracks changes in revenue directly related to variances in use-per-customer following a general rate case; it does not otherwise mitigate attrition.²⁵

Mr. Mullins, on behalf of ICNU, suggests that the downward trend in natural gas commodity costs is somehow relevant to the attrition analysis.²⁶ Here again, the trend in commodity costs has nothing whatsoever to do with the attrition Avista is experiencing. The drivers of attrition are changes in capital investment and increases in utility operating costs,

proposed. Is it representative, after adjustments, of the period in which rates take effect?
Page 10 of Audit Manual (quoted in Testimony of Andrews, Exh. No. EMA-1T, p. 10)

²² (Exh. No. DMR-1T, p. 22)

²³ (Exh. No. KON-1T, p.26:19-22)

²⁴ (Id., at 27:1-13)

²⁵ (Ibid.)

²⁶ (See Exh. BGM-1T, p. 11)

excluding power supply commodity costs and natural gas commodity costs.²⁷ Finally, for reasons discussed below, an attrition adjustment is to be distinguished from the use of a “future test year.” In his testimony, Staff Witness McGuire noted that the Commission has stated “unequivocally” that “such historical analysis is what distinguishes an attrition adjustment from the use of a future test year.”²⁸ The current growth factor proposals to the Commission by both Staff and the Company are based on a historical trend analysis.²⁹

III. GROWTH IN RATE BASE EXCEEDS REVENUES

18

The Company has presented substantial evidence relating to its actual and expected level of capital investment. Mr. Norwood provided information on the overall level of capital investment from 2011-2014, showing an increase in actual capital investment from \$247 million to \$352 million³⁰:

Table No. 1 – Capital Investment and Capital Requests

Year	Actual Capital Investment	Total Requests	Funded Requests	Unfunded Requests
2011	\$247	\$291	\$230	\$61
2012	\$262	\$269	\$250	\$19
2013	\$296	\$320	\$266	\$54
2014	\$352	\$386	\$331	\$55

This table also demonstrates that the Company has still left as “unfunded” as much as \$50-60 million of capital requests. As noted by Mr. Norwood, capital projects must be “prioritized.”³¹ Furthermore, as some scheduled capital projects experience unexpected delays, a

²⁷ (Exh. No. KON-1T p. 27:20 – p. 28:2)

²⁸ (Citing Wash. Util. & Transp. Comm’n. v. Puget Sound Energy, Dockets UE-111048/UG-111049, Order 08 (May 7, 2012), 181, fn. 673).

²⁹ (Exhibit CRM-1T, p. 33:6-15)

³⁰ (Exh. No. KON-1T, p. 8:12-18)

³¹ (Ibid.)

“reprioritization” occurs within the Company’s Capital Planning Group, which manages the total capital.³² Moreover, what the Company plans to spend on capital is quite close to its actual expenditures over time, as shown in the table below³³:

Table No. 2 - Planned vs. Actual Expenditures

	Planned Expenditures (\$ millions)	Actual as a Percentage of Planned
2006	\$160.00	99%
2007	183.10	108%
2008	190.00	108%
2009	220.00	91%
2010	235.00	88%
2011	260.00	95%
2012	255.00	103%
2013	275.00	108%
2014	336.00	105%
Nine Year Average	\$234.90	101%

This information demonstrates that, although individual project timing and dollar amounts may vary both within a year and from year to year, the Company does “manage its overall spend to be close to the overall planned amount” as testified to by Mr. Norwood.³⁴ This evidence provides substantial support that the planned capital spending in 2016 will actually occur.

19

Finally, we should not lose sight of the fact that, other than a portion of the capital associated with Project Compass, the parties did not otherwise challenge the prudence of any specific capital projects. Avista provided extensive evidence supporting its current and planned capital additions. Company Witness Mr. Kinney provided details related to generating plant capital additions, Company Witness Mr. Cox did so for transmission plant, Mr. Kensok provided information for technology investments, and Ms. Schuh provided information for common plant and other capital investment.³⁵ Moreover, business cases were also provided for all projects

³² (Id. at 9:7-13)

³³ (Id. at 10)

³⁴ (Id. at 10:22-24)

³⁵ (See Exh. Nos. JMK-1T, JMK-2 – JMK-5, SJK-1T, BAC-1T, KKS-1T – KKS-4)

totaling more than 300 pages of information.³⁶ In fact, the extent of the evidence even prompted Mr. Mullins to comment on the “voluminous amount of data for the 150 capital projects proposed for 2015 and 2016.”³⁷

20

The impact of the limited capital adjustments of Staff, ICNU and Public Counsel, as part of the traditional pro forma historic test period, is noteworthy.³⁸ Company Witness Schuh provided illustrations demonstrating how the parties’ pro forma net plant adjustments do not reflect the level of plant that will be in service during the 2016 rate year:³⁹

Illustration No. 3:

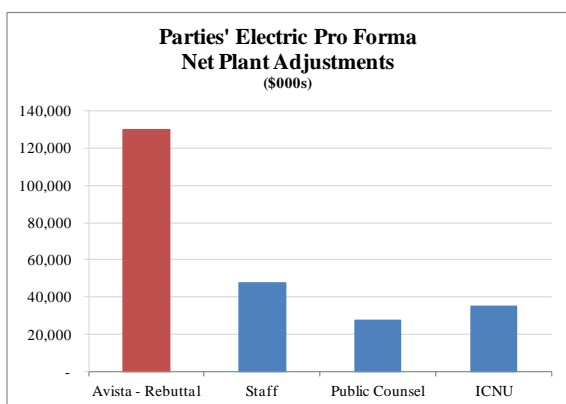
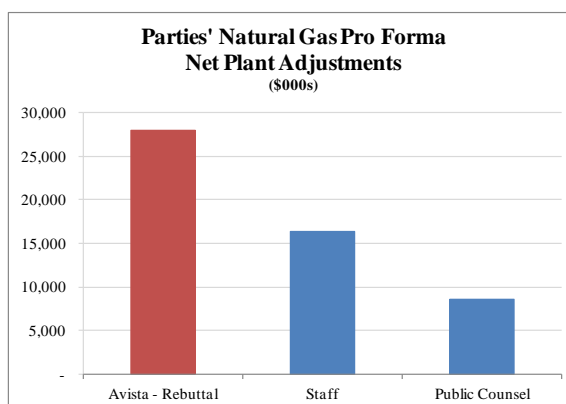


Illustration No. 4:



As testified by Company Witness Schuh, “clearly, the ‘pro forma’ analyses performed by the other parties will not address the level of rate base attrition that will be experienced by the

³⁶ (See Exh. No. KKS-5)

³⁷ (Exh. No. BGM-1T, p. 23)

³⁸ Before applying its attrition adjustment, Staff started with Avista’s December 31, 2014 end-of-period capital and made limited pro forma adjustments on only 14 major capital projects from January 1, 2015, through June 30, 2015. In doing so, it excluded the remaining July through December 2015 additions, as well as all capital additions for the 2016 rate period. (Schuh Exh. No. KKS-6T, p. 8:1-6)

ICNU proposed the use of an AMA basis for the 12 months ended September 30, 2014, with an additional adjustment for ADFIT; however, it excluded all post-test year capital additions, with the exception of Project Compass. (Mullins Exh. No. BGM-1CT, p. 18) It also proposed to exclude, for Project Compass, the depreciation expense and deferred federal income taxes accrued for the project in 2015. (*Ibid.*)

Finally, Public Counsel proposed that the electric adjustment for plant-and-service from the test year (AMA 12 months ended September 30, 2014) to EOP December 31, 2014, be rejected. For natural gas, it did propose that an adjustment be made from AMA to EOP for the 2014 test year. It also proposed the exclusion of post-test year capital adjustments with the exception of three projects.

³⁹ (Exh. No. KKS-6T, p. 10)

Company during the 2016 rate year.”⁴⁰ As she further notes, this was recognized by Staff Witness McGuire⁴¹ and the Company, which both proposed a revenue requirement based on attrition studies, instead. Simply put, “using an historical test year with limited pro forma adjustments for capital investment severely understates the capital investment that will occur through the rate year, resulting in considerable attrition,”⁴² as testified to by Company Witness Schuh.⁴³

IV. STAFF AND THE COMPANY EMPLOY SIMILAR APPROACHES TO ANALYZING ATTRITION

21 This is not a case where the Commission is dealing with divergent attrition methodologies. Rather, both the approaches of Staff and the Company are fundamentally similar, with only a few differences in trending assumptions.⁴⁴ These will be discussed below. It is also important to clarify, at the outset, that while, in its direct case, the Company employed certain “projections” in its attrition analysis (see Exh. Nos. EMA-2 AND EMA-3), on rebuttal the Company revised its attrition study based on Staff’s analysis and used only historical data for trending purposes. (See Exh. Nos. EMA-6 and EMA-7) As will be discussed below, the only differences that remain deal with the choice of trending years (2007 – 2014 versus 2009 – 2014) and the appropriate O&M trending percentage.

⁴⁰ (Exh. No. KKS-6T, p. 11:1-6)

⁴¹ Mr. McGuire put it this way: “So for electric service, if we were to say that Avista’s current expected revenue growth between the test year and the rate year will be sufficient to cover costs, particularly net plant, the growth in net plant between the test year and the rate year would be zero percent. So what you’re asking the Company to do is to scale back its capital investments to zero. Now, I would argue that that’s unreasonable, and that’s what I’m arguing here is that, without doing any sort of analysis, providing any sort of analysis of what might happen in the rate year, you don’t know whether or not the Company can even achieve what you’re expecting them to achieve.” (TR 447:2-14)

⁴² Ms. Schuh explained why she included plant for 2016 in the cross check study: “This is all the plant that we expect – expect to be in service during the rate year. We did this as a comparable approach to the attrition study, as kind of an apples-to-apples comparison, to show the level of plant that will be in service during the 2016 rate year. . . .” (TR 219:18-22)

⁴³ (Exh. No. KKS-6T, p. 14:10-12)

⁴⁴ (Exh. No. EMA-5T, p. 3:17 – p. 4:7)

22 Company Witness Andrews, underscored that the Company, on rebuttal, “begins by accepting Staff’s methodology for computing attrition.”⁴⁵ She notes that:

23 Both Staff and the Company rely on attrition analyses to set the proposed retail rates for 2016; both models use a trending approach using historical data; and both models recognize that in order to allow Avista an opportunity to earn the agreed-to 9.5% ROE, it is important to reflect what is expected to happen in the rate year, rather than relying solely on an historical pro forma study with limited pro forma adjustments approach.⁴⁶

The Company’s Exh. No. EMA-6 (electric) and Exh. No. EMA-7 (natural gas) present the results of the Company’s revised electric and natural gas attrition studies as well as the underlying supporting data. Exhibit No. EMA-8 provides a detailed description of the revised electric and natural gas attrition models.

24 In order to demonstrate how closely aligned the two attrition methodologies of Staff and the Company are, Ms. Andrews provided a simplified matrix at p. 16 of her rebuttal testimony (Exh. No. EMA-5T):

Table No. 4 - Avista/Staff Attrition Model Alignment

Electric	Staff	Avista	Natural Gas	Staff	Avista
Historical vs 2016 Expected Trending	X		Historical vs 2016 Expected Trending	X	
Linear vs Non-Linear Regression Analysis	X		Linear vs Non-Linear Regression Analysis	X	
Compounding	X		Compounding	X	
Use of Years		X	Use of Years		X
O&M Growth Factor %		X	O&M Growth Factor %	X	
After Attrition Adj. for Project Compass	X¹		After Attrition Adj. for Project Compass	X¹	

¹Avista used total costs for Project Compass versus Staff's partial disallowance.

25 By way of quantification of the impact on revenue requirement, the electric O&M escalation used by Avista accounts for \$7.27 million of the electric revenue requirement difference between Staff and Avista. The use of 2007 versus 2009 as the starting point for the

⁴⁵ (Exh. No. EMA-5T, pp. 3-4)

⁴⁶ (Ibid.)

trended data, otherwise accounts for an increase of \$277,000 for electric and a reduction of \$670,000 for natural gas, as between Avista and Staff.⁴⁷ Table No. 5, excerpted from p. 17 of Ms. Andrews’ rebuttal testimony (Exh. No. EMA-5T), provides a tabulation of the revenue requirement differences between Staff’s and Avista’s attrition analyses:

TABLE NO. 5 - Avista versus Staff Attrition Revenue Requirement		
	Electric	Natural Gas
Staff Filed:	\$ (6,209)	\$ 9,040
Corrections		
a) Benefit of Debt interest on Project Compass	\$ (540)	\$ (163)
b) Remove AMI Deferral	\$ (4,119)	\$ -
c) Formula errors	\$ 4,406	\$ -
d) Include Growth in gas costs to match Staff proposed load growth	\$ -	\$ 1,428
Net Corrections	\$ (253)	\$ 1,265
Corrected Staff Model:	\$ (6,462)	\$ 10,305
Avista Proposed Adjustments to Staff's total:		
<i>Data Assumption Changes:</i>		
1) Colstrip Refund Non-Reoccurring Item Correction	\$ 1,126	\$ -
2) Include Total (100%) Project Compass	\$ 1,428	\$ 374
Staff revised for Colstrip Refund & Total Project Compass	\$ (3,908)	\$ 10,679
<i>Model Assumption Changes:</i>		
3) Use of Years: Avista (2007-2014) versus Staff (2009-2014)	\$ 277	\$ (670)
4) Annual O&M %: Avista (5.16%) versus Staff (2.41%)	\$ 7,270	\$ -
Revised Avista Historical Model (Rebuttal)	\$ 3,639	\$ 10,009

26

Again, both Staff and the Company used historical data only (omitting projected 2016 information) and incorporated an “After Attrition Adjustment” for Project Compass to reflect Washington electric and natural gas capital transfers to plant. With respect to this adjustment, Mr. McGuire noted, at page 54 of his testimony (CRM-1T) that “I determined that this was appropriate because Project Compass appears to be an abnormality with respect to the Company’s ongoing capital growth pattern.” This was the only capital adjustment made by either

⁴⁷ (Exh. No. EMA-5T, p. 16:9-15)

Staff or the Company to the trended capital data.⁴⁸ Moreover, both the Company and the Staff employ a similar regression trending analysis.⁴⁹ That leaves only two differences between the Staff and the Company in the development of the attrition analyses: The first relates to the starting point for the historical trend period (2007 versus 2009), and the second relates to the O&M growth rate. The latter (reflecting a difference of \$7.27 million) accounts for the majority of the difference in electric revenue requirement between Staff and the Company.⁵⁰

A. Starting Point for Trending of Historical Years.

27 2007 – 2014 was the historical time period used for purposes of trending rate base and expenses in Avista’s study. As noted by Company Witness Dr. Grant Forsyth, the:

28 “. . . annual capital investment for the 2001 – 2013 period clearly shows a significant shift in the expenditure trend starting in 2007. This is the case for both electric and natural gas operations. Specifically, in 2007, capital investments started increasing at a significantly faster pace compared to the 2001 – 2006 period. . . . Given current and planned expenditures by the Company, we do not foresee a return to the expenditure trend of the 2001 – 2006 period in the near term.”⁵¹ (Emphasis added)

29 Staff Witness McGuire, on the other hand, used 2009 as the starting point for his trend analysis, in order to avoid what he termed “statistical complications caused by changes in normalization methodology.”⁵² He was referring to what he believed were changes in the weather normalization methodology. On rebuttal, however, the Company clarified – and Mr. McGuire agreed – that changes to the weather normalization methodology had been consistently reflected since the 2006 calendar year report. (See TR 461-462) Moreover, as noted by the

⁴⁸ The adoption of an attrition allowance does not mean that the Commission is prevented from otherwise disallowing particular items deemed imprudent. An example of this is Staff’s recommended disallowance of a portion of Project Compass costs (albeit an example with which the Company takes strong exception). Staff Witness McGuire explains how those proposed disallowances are not incompatible with an attrition study. (TR 458:6-21)

⁴⁹ (Exh. No. EMA-5T, p. 20:14-17)

⁵⁰ (Id. at 21)

⁵¹ (Exh. No. GDF-1T, p. 4:13-15)

⁵² (Exh. No. CRM-1T, pp. 37-38)

Company, the weather normalization process is “completely irrelevant to the trended analysis” used within Avista’s or Staff’s attrition studies; it only affects retail revenue and power supply/purchased gas expenses, both of which are treated independently from the Commission-basis trend factors in the attrition studies.⁵³ Accordingly, no “statistical complications” are introduced between 2007 and 2009 with regard to the weather normalization processes.⁵⁴

30 During cross-examination, Mr. McGuire acknowledged that the Company was correct, and withdrew his concerns over “statistical complications” associated with a starting point of 2007:

31 . . . I chose that time period because data were normalized in a consistent manner between 2009 and – and 2014; however, I agree with the Company’s assessment that it is irrelevant. The – the normalization consistency is irrelevant here. You normalize things that are not escalated in the attrition study and I – I failed to recognize that in my study. (TR 461:20 – 462:5)

As noted above, while the starting point for the historical trending analysis (2007 versus 2009) may have a relatively small impact on revenue requirement for purpose of trending rate base, the choice of period does have a greater impact when determining the appropriate O&M percentage trending factor, as will be discussed below.

B. O&M Annual Growth Rate.

32 On rebuttal, the Company employed a 5.16% electric O&M escalation growth rate. This was arrived at by an equal “weighting” of the 2007 – 2014 growth rate (excluding benefits⁵⁵) of 4.32% and the 2013 – 2014 growth rate of 5.99% (again excluding benefits). Staff used a different “weighting.” It used the 3% growth rate initially employed (but since removed) in the Company’s direct case, and “weighted” it with the unadjusted 2013 – 2014 one year change in

⁵³ (Exh. No. EMA-5T, p. 27:12-19)

⁵⁴ (Id.)

⁵⁵ “Benefits” include pension and post-retirement medical, as discussed, infra.

O&M of 1.82%. This resulted in an overall Staff growth rate of 2.41%.⁵⁶ The following table sets forth the electric O&M escalation growth rates discussed in the various analyses.⁵⁷

Table No. 6

Summary of Electric O&M Escalation Growth Rates		
Rate #	O&M Expense	Growth Rate
1	Avista Direct Case	3.00%
2	Total 2007-2014	4.60%
3	2007-2014 - Excluding Benefits	4.32%
4	Total 2013-2014	1.82%
5	2013-2014 - Excluding Benefits	5.99%
6	Financial Forecasted O&M Expenses 2014-2016	4.45%
A*	Avista Rebuttal Position - (Weighted (3 & 5))	5.16%
S*	Staff Position - (Weighted (1 & 4))	2.41%

*Avista on rebuttal and Staff propose 2.17% for the annual natural gas growth rate.

33 While the Company first employed a 3% O&M growth rate in its direct filing in order to be conservative, as it later updated its analysis through the course of these proceedings, it concluded that a 3% growth rate was no longer representative of the trend in O&M expense. Ms. Andrews explained that, as part of the Company’s initial filing, it used a “conservative” 3% escalation factor for O&M:

34 So we were definitely being conservative on our direct filing, but on rebuttal, just as we reevaluated what our trending should look like or using historical data for all other categories – capital, depreciation, other taxes, etc. – we also reevaluated the appropriate level for O&M. . . . [For] electric, we had significantly understated what the expectation was for 2016.⁵⁸

35 Staff, however, continues to use the 3% growth rate, but blends or “weights” it with a one-year change between 2013 – 2014 in O&M escalation of only 1.82%. Neither growth factor (3% nor 1.82%) are representative of what the most recent analyses support as the appropriate level of

⁵⁶ (See Exh. No. EMA-5T, p. 32)

⁵⁷ (*Ibid.*)

⁵⁸ (TR 157:6 – 158:3)

O&M annual increase.⁵⁹ This issue matters greatly to the determination of the electric revenue requirement. The difference between Staff’s proposed escalator of 2.41% (average of 1.82% and 3.00%) and Avista’s proposed escalator of 5.16% (weighting of 4.32% and 5.99%) reflects a difference in revenue requirement of approximately \$7.27 million. Staff improperly focuses on the one year difference between Avista’s 2013 and 2014 actual results, which only showed an average increase of 1.82%. This is not representative of historical or future growth rates. As testified to by Company Witness Andrews, “between 2013 to 2014 net benefit costs dropped significantly for this one year (over \$4.6 million electric), before returning in 2015 to higher levels, higher than that in 2013.” (Emphasis added)⁶⁰ Indeed, the Company’s own current financial forecast for the annual increase in O&M from 2014 to 2016 is 4.45% for the combined electric and natural gas systems.⁶¹ (See also TR 204:5-11)

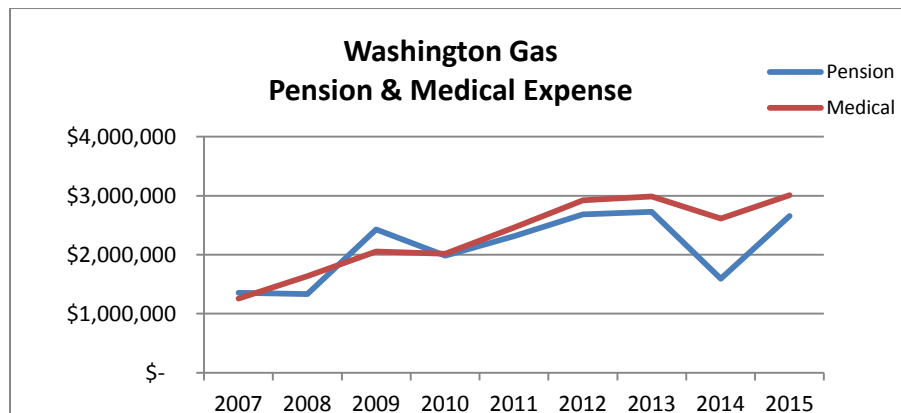
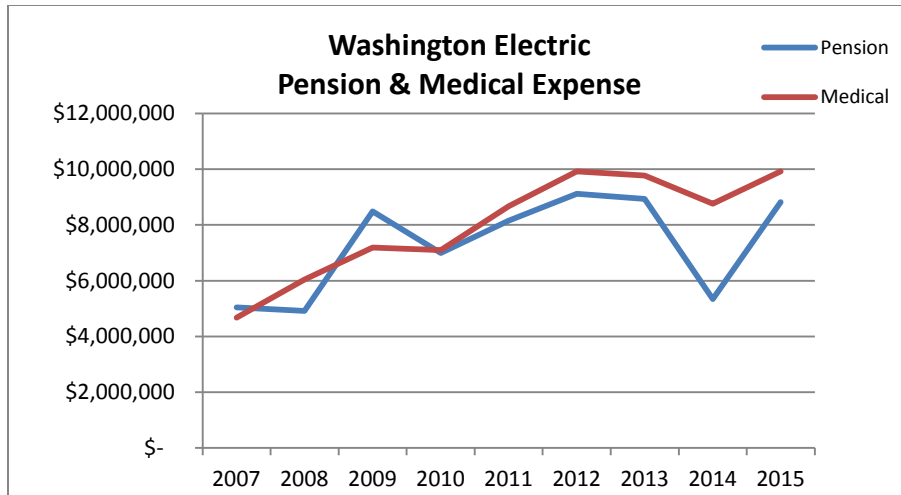
36

In response to Bench Request No. 6 (Exh. No. 9), the Company provided information with respect to pension and post-retirement medical expense through the year 2015. This clearly demonstrates that the drop in pension and post-retirement medical expense between 2013 and 2014 was an aberration. By 2015, those benefit levels had returned to, or exceeded levels prior to 2013. The information contained within the Company’s response to Bench Request No. 6 for the period 2007 – 2015, with respect to these “net benefits” is graphically displayed below:

⁵⁹ Mr. McGuire acknowledged that he used the Company’s 3% O&M escalator and averaged it with his own calculation in order to arrive at his factor of 2.41%, even though he had earlier questioned the use of a 3% growth rate by Avista. (See TR 483:14 – 484:6)

⁶⁰ (Exhibit No. EMA-5T, p. 31:15-17)

⁶¹ (Id., at p. 32:1-2)



37 Ms. Andrews explained, in response to questions from Commissioner Jones, that “there was a significant drop in net benefit costs from the year ’13 to 2014 that has since come back up, and our expense level in ’15 will be basically similar or higher than what – what we experienced in ’13.” (TR 197:14-21)

38 This is further evidence that Mr. McGuire’s use of the one year change from 2013 to 2014 for purposes of establishing an O&M growth factor is misleading and not representative of the overall annual trend in O&M expense, unless an adjustment is made to exclude this one year aberration in net benefits. Mr. McGuire acknowledged that he “used some amount of judgment” when arriving at a growth rate for electric O&M. He even “recognized” that “it’s problematic to use a single year’s rate of growth - it’s much better to have more years” (TR 484:46):

39

So I – I, to be honest, used some amount of judgment. I found a rate of growth between 2013 and 2014, recognized that it’s problematic to use a single year’s rate of growth – it’s much better to have more years, so I just – and looking at the historical data, I noted that there’s likely to be upward pressure on operating expenses, just the – the shape of the data, historically, seemed to be quite a bit steeper than the rate of growth annually. (TR 484:4-11)

40

If, however, one were to make any use of the one year change from 2013 to 2014 for purposes of arriving at a growth factor, it would be important to remove from that one year the aberration in “net benefit costs.” Doing so would result in a year-over-year change between 2013 and 2014 of 5.99% (not Staff’s 1.82%), as shown in Table No. 6, above.⁶²

41

It is important to exclude the variability of these “net benefits” in 2013-2014, because of the distortion that it introduces into the analysis. This is what the Company has done, on rebuttal, by averaging 2007 – 2014 (excluding benefits) (for purposes of incorporating a longer term trend) with the one-year change from 2013 – 2014 (again excluding benefits). At the end of the day the evidence demonstrates the following:

- If one is to make any use of the one year change from 2013 – 2014 as part of the analysis, it must be adjusted to exclude “net benefits” associated with one year aberration in pension and post-retirement medical. These net benefits showed an abnormal variance for the one year and have since increased in 2015 to levels above that even shown in 2013;
- Avista’s use of 3% in its direct case was overly-conservative and no longer represents the growth rate anticipated in 2016 (current financial forecast shows a 4.45% annual increase in O&M from 2014 to 2016).
- Accordingly, there is no justification for Staff to combine or average 3% with the unadjusted one year change from 2013 – 2014 (of 1.82%) to arrive at a weighted average of 2.41%.
- The Company’s rebuttal position takes into account a longer data series of 2007 – 2014, while still weighting it with the one year change from 2013 and 2014 – but in both cases excluding the aberration in net benefits, in order to arrive at an electric O&M growth rate of 5.16%.

⁶² (See also Exh. No. EMA-5T, p. 31:16-18)

An alternative for the Commission to consider, as presented by the Company, to remain true in principle to the consistent use of the 2007 – 2014 historical trending data, would be to simply employ the unadjusted 2007 – 2014 growth rates for O&M, in the same manner as was done for rate base and other expenses. Such an approach would be more consistent with the overall trending of data used throughout the attrition study. Doing so would result in an electric O&M escalation rate of 4.6% which is lower than the Company’s proposed rebuttal position of 5.16%, but higher than Staff’s position of 2.41%. The use of 4.6% would reduce Avista’s electric revenue requirement from \$3.69 million to \$2.10 million. (See TR 162:7-21) For purposes of resolving this issue, Avista would find that acceptable.

42

The Company, for the natural gas O&M escalator, accepts Staff’s use of 2.17%, noting that electric operations require a higher O&M escalation rate than that experienced by the Company’s natural gas operations, given higher maintenance and other mandated compliance requirements associated with the operation of generation and transmission facilities. (See Exh. No. EMA-5T, pp. 33-34) The weighted average of annual O&M increases of 2.17% for natural gas and 5.16% for electric results in an overall weighted average of 4.26%.⁶³ (Id., at Exh. No. EMA-5T, p. 34) This 4.26% growth rate is less than the financial forecast of 4.45% annually between 2014 and 2016. It is very close to the actual 2007-2014 growth rate of 4.32% (excluding net benefits). (Exh. No. EMA-5T, p. 34:16-18)⁶⁴

⁶³ Given the “one-way” earnings tests in place, it is important to establish the correct O&M growth escalation factor for each service, electric and natural gas. If Avista, for example, “over-earns” in its natural gas operations because a higher O&M escalation growth factor is used, it would be required to return half of its over earnings, thereby protecting customers. If, however, Avista were to “under-earn” in its electric operations because a low O&M escalation growth factor was used, there would be no protection for the Company under these circumstances. (Exh. No. EMA-5T, p. 35:4-9)

⁶⁴ As noted in Avista’s response to Bench Request No. 17, if the Company were to employ the unadjusted 2007-2014 natural gas growth rate for O&M as well, the resulting growth factor would be 3.5% versus the 2.17% used by both Avista and Staff. Doing so would increase Avista’s natural gas revenue requirement from \$10.0 million to \$10.9 million. Furthermore, employing a consistent 2007-2014 growth rate for electric of 4.6% and natural gas

43

Finally, Mr. Gorman’s testimony, on behalf of NWIGU, clearly reflects a misunderstanding of Avista’s natural gas attrition study. He begins by erroneously asserting that the Company’s attrition methodology adjusted costs to the end-of-period rate base (EOP) for 2016, and that Avista should have adjusted rate base on an AMA basis.⁶⁵ This isn’t correct. Avista presented its rate base on an AMA basis for 2016 – not on a 2016 EOP.⁶⁶ He also arbitrarily reduces depreciation and amortization expense, as well as O&M expense to represent a mid-year 2016 test year. He didn’t recognize that Avista’s study already adjusted net rate base to a 2016 AMA basis. These shortcomings are explained by Ms. Andrews in her rebuttal testimony.⁶⁷ These examples illustrate why his analysis should be accorded little weight.

V. AVISTA PERFORMED “CROSS CHECK” STUDIES THAT SUPPORT THE REASONABLENESS OF ITS ATTRITION STUDIES

44

Avista’s proposed revenue requirement is based on its attrition analyses. The accompanying electric and natural gas “Cross Check” Studies were intended to provide another view of what the revenue increase would look like if one were to adjust the historical period to capture 2016 levels of rate base and expense. They were performed as a “bottoms up” analyses starting with the 2014 historic test period and adjusting rate base and expenses to 2016 rate year levels. In this way, the results could be compared with each attrition study’s need for rate relief for the same 2016 rate period. The updated Attrition Studies and Cross Check studies supported by the Company on rebuttal are independent of one another and performed differently: the “Cross Check” Studies employed a historic test period with adjustments to capture the 2016 rate

of 3.5% would result in an overall weighted average of 4.27% for Washington operations ((4.6%*70%)+(3.5%*30%). This 4.27% overall growth rate is still less than the Company’s financial forecast of 4.45% annually between 2014 and 2016.

⁶⁵ (Exh. No. MPG-1T, pp. 2-3, and 14)

⁶⁶ (Exh. No. EMA-5T, p. 36)

⁶⁷ (Id. at 37)

period; the attrition studies used trended historical information from 2007 through 2014. Mr. Norwood explained the purpose of the “Cross Check” Study this way:

45 Avista’s Pro Forma Cross Check Study was prepared as a ‘cross check’ and a second analysis to compare with the attrition analysis. The Cross Check Study includes a comprehensive set of adjustments for the prospective rate year, based on the best and most recent information available, to determine the revenues sufficient for Avista to earn its allowed return. The Cross Check Study confirms that there will be a continuation of attrition through the prospective rate year for Avista. (Emphasis added)⁶⁸

46 In order to prepare this Cross Check Study, Avista included all plant additions on an AMA basis through the 2016 rate year, providing a reasonable basis for comparison of plant to the attrition studies.⁶⁹ Were it to do otherwise – and only pro form certain plant through part of 2015 – the analysis would simply never get to the 2016 rate year, in order to allow for a comparison with the attrition study. In terms of total net plant, the Cross Check Studies show total electric net plant after ADFIT of \$1.353 billion; this compares quite closely with the net plant after ADFIT in the attrition study of \$1.341 billion. Similarly, for natural gas, the Cross Check Study shows total net plant after ADFIT of \$249 million, as compared with the attrition analysis during the rate year of \$260 million.⁷⁰ Simply put, the balances of net plant after ADFIT included in the Company’s attrition studies are quite comparable with the plant balances independently arrived at through the Cross Check Studies for the 2016 rate year.⁷¹

47 Company Witness Smith provides summary tables that identify each of the adjustments the Company has made in the Cross Check Studies to reflect the 2016 rate year.⁷² (See Table

⁶⁸ (Exh. KON-1T, p. 29:7-12)

⁶⁹ (Exh. No. KKS-6T, p. 2:6-11)

⁷⁰ (Id. at 7:5-10)

⁷¹ (Ibid.)

⁷² For a discussion of other adjustments suggested by the parties (and opposed by Avista), please see: Rebuttal Testimony of Jennifer Smith (Exh. No. JSS-4T): Long-Term Incentive Plan (Id. at 28-31); Corporate Aircraft (Id. at 31-32); Pro Forma Labor (Id. at 32-38); Pro Forma Property Taxes (Id. at 38-40); Pro Forma Information Technology/Services (Id. at 40-41); and Project Compass Deferral/Regulatory Amortization (Id. at 41). See also,

No. 3 for the summary of adjustments for the electric Cross Check Study and Table No. 4 for the adjustments for the natural gas Cross Check Study.) (Exh. No. JSS-4T, pp. 8-9) (The Cross Check Studies themselves are included as Exh. No. JSS-5 (electric) and JSS-6 (natural gas).) Ultimately, the results performed by the two independent analyses (cross check and attrition) result in similar findings. Company Witness Smith reconciled the Cross Check Studies to the attrition analyses and found that the results were quite similar.⁷³

VI. ACTUAL EARNED RETURNS FOR 2013 AND 2014 DEMONSTRATE THAT A REVENUE REQUIREMENT BASED ON ATTRITION IS SERVING ITS INTENDED PURPOSE

48

Certain parties assert that Avista “over-earned” during 2013 and 2014, attempting to draw inferences from those results as bearing on the use of an attrition adjustment.⁷⁴ In order to provide perspective, Mr. Norwood, on rebuttal, furnished a table containing 2013 and 2014 earned returns on equity on a normalized basis for electric and gas. The results are shown below:

<u>Table No. 3 – 2013 and 2014 Earned Return on Equity⁷⁵</u>			
	<u>Electric</u> <u>ROE</u>	<u>Natural Gas</u> <u>ROE</u>	<u>Total Utility</u> <u>(Weighted)</u>
2013	9.9%	7.2%	9.5%
2014	<u>10.6%</u>	<u>6.4%</u>	<u>9.9%</u>
Two-Year Rate Plan Wtd ROE	10.3%	6.9%	9.7%

This table shows that, while Avista “over-earned” for its electric operations and “under-earned” for its natural gas operations, as a whole, the results were 9.5% for 2013 and 9.9% for 2014, as

Rebuttal Testimony of Karen K. Schuh (Exh. No. KKS-6T): Accumulated Deferred Federal Income Taxes (Id. at 17-18).

⁷³ She noted that the reconciliation would require an increase in expense of only \$4,123,000 for electric and \$1,072,000 for natural gas, while electric total rate base would decrease by \$10.9 million and natural gas total rate base would increase by \$12.5 million, in order to equate with the total level of attrition deficiency, as determined in the attrition studies. (Exh. No. JSS-4T, p. 27:12-15) These are relatively small differences in total rate base between the two studies when compared with the total rate base for electric of approximately \$1.4 billion and natural gas of approximately \$280 million. (Exh. No. EMA-6 and EMA-7)

⁷⁴ (See, e.g., Exh. No. DMR-1T, p. 25; Exh. No. BGM-1T, p. 8; and Exh. No. CRM-1T, p. 10)

⁷⁵ (Exh. No. KON-1T, p. 13:9-16)

compared to the authorized ROE of 9.8% at the time.⁷⁶ It should be recalled that in December of 2012, the Commission approved a two-year rate plan for 2013 and 2014; Avista's average ROE for this two-year period was 9.7%, as shown in the table above, which is slightly below the authorized return of 9.8%.⁷⁷ The important point as testified to by Mr. Norwood, is as follows:

49 The earned ROEs for Avista for 2013 and 2014 of 9.5% and 9.9%, respectively, are an after-the-fact confirmation that the revenue increases granted based on recognition of attrition provided earned returns very close to the authorized ROE of 9.8%. Without the recognition of attrition, Avista's earned returns for 2013 and 2014 would have been substantially below its authorized return, as noted by Moody's in their comments above. (Emphasis supplied)⁷⁸

Mr. Norwood was referring to rating agencies who have recognized that the revenue increases granted in Avista's last two general rate cases took into account the impacts of attrition – namely, that investment and operating costs are growing faster than revenue growth.^{79/80} Moreover, in the prior settlement of Docket No(s). UE-120436 and UG-120437, with a two year rate plan for 2013 and 2014, increased revenues associated with the effects of attrition were also embedded in the end result, as recognized in the Commission's Order:

50 Here, both the Company and Staff performed attrition studies to project 2013 rates. We agree with the Company and Staff that the proposed 2013 rate increases are based significantly on attrition.^{81/82}

⁷⁶ (Id., at 13:17-20)

⁷⁷ (Ibid.)

⁷⁸ (Exh. No. KON-1T, p. 15:18-22)

⁷⁹ (Id. at 14:23-25)

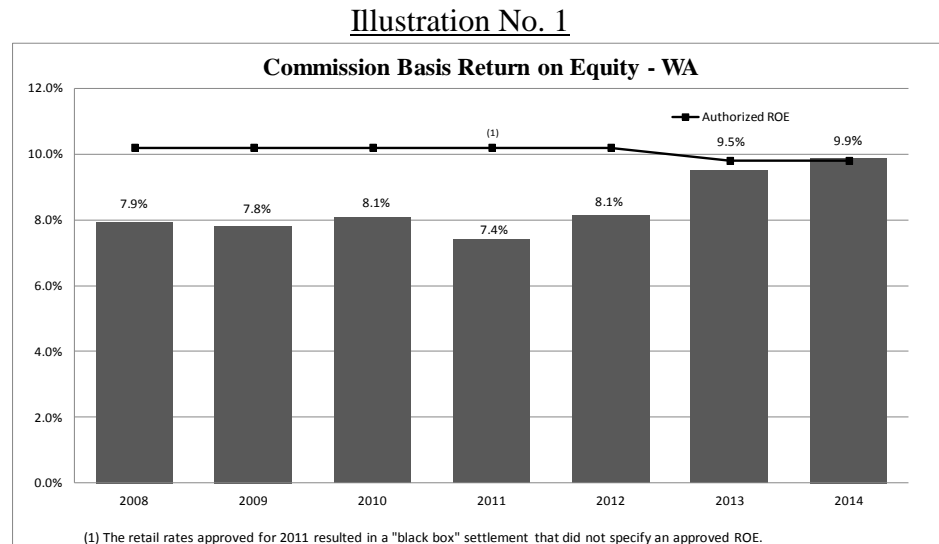
⁸⁰ While the Settlement Agreement in the Company's last rate case, with rates effective January 1, 2015, did not include specific agreement on an attrition methodology or a specific attrition adjustment, the increased revenues associated with the effects of attrition were embedded in the final "black box" revenue requirement numbers. (Exh. No. KON-1T, p. 14:26 – p. 15:2)

⁸¹ Mr. Norwood testified that S&P and Moody's viewed recent orders from this Commission "as being constructive" because recent orders were "a departure from the prior use of using historical data to set future rates." (TR 127:9-22)

⁸² (¶70 of Order 14, dated December 26, 2012, in Dockets No. UE-120436 and UG-120437)

It is also important to note that earned returns for Avista’s utility operations in Washington in years prior to 2013 fell significantly short of matching the authorized returns.

This is shown below in Illustration No. 1 excerpted from Mr. Norwood’s testimony⁸³:



This proves the point that without some recognition of attrition, the standard ratemaking approach in place in prior years, which allowed for only limited pro forma adjustments to a historical test period, simply did not provide a reasonable opportunity for Avista to earn its authorized returns.

Public Counsel asserts that Cross Exhibit KON-5CX, which splits apart the Commission-basis returns on equity for the Company’s electric and natural gas operations, somehow undermines this point. In that response, the Company provided Commission-basis returns on equity for Washington electric operations of 9.9% for 2013 and 10.6% for 2014, which are identical to what the Company provided in Table No. 3, shown on page 26 above, in its rebuttal testimony. Avista’s normalized ROE for its electric operations was 10.6% in 2014, as shown in Exh. No. KON-5CX, but there “were some unusual circumstances that drove that in 2014 that

⁸³ (See Exh. No. KON-1T, p. 16:11-20)

were not adjusted out” as explained by Mr. Norwood. (TR 83:14-16) Mr. Norwood explained why the returns in 2014 were in excess of the then-allowed ROE:

53 Two primary items in 2014. One is, with our pension post-retirement medical assets that fund those obligations, the return – stock market returns on those assets for 2014 were very positive, and as we all know, the stock market was very strong that year. That resulted in a reduction in expense for pension post-retirement medical in 2014.

54 Since that time, market returns have been much lower and – and have returned to what would be viewed as more normal, so the expense has gone back up in ’15 and ’16. So just that one issue alone in ’14 is approximately \$5 million in the electric operations, which by itself, would reduce return from 10.6 down to about 10.1.

55 Secondly, we’ve talked about the Ecova sale, and we also acquired Alaska Electric Light & Power in 2014, so we had two transactions in ’14, 2014, where there were staff time, executive time, dedicated to those transactions, which do not affect – they’re unrelated to the Avista Utilities operations.

56 The bottom line is, you had people assigning or directly assigning their time to those transactions, which reduce the expense in 2014 related to the operations. And the Commission-based reports, which don’t normalize the pension post-retirement medical issue, nor do we normalize out those types of transactions where there was a benefit to customers. So if you normalize those out, the normalized returns in 2014 would have been very close to the authorized return. (TR 106:4 – 107:8)

57 The decline (aberration) in pension and post-retirement medical expense for 2014, discussed earlier in relation to the O&M escalator for attrition, is not something that could have been predicated at the time the two-year rate plan (for 2013 and 2014) was developed and approved. This expense is driven largely by the return on assets for the plans and the discount rate (changes in interest rates).⁸⁴ In addition, the transactions to sell Ecova and purchase the Alaska Utility also could not be predicated. Removing (normalizing out) the reductions in utility

⁸⁴ (TR 203:25 – 204:4)

expense during 2014 would result in Avista earning very close to its allowed electric return, and result in further under-earning in its natural gas operations.

58 Public Counsel and ICNU paid much less attention to the Commission-basis returns on equity for Washington natural gas operations in 2013 and 2014, which remained at only 7.2% and 6.4%, respectively.

59 Moreover, it should be remembered that a utility is to be provided with a reasonable opportunity to earn its authorized rate of return. The fact that Avista, in 2013 and 2014, for its electric operations, realized a return at or slightly above its authorized return is not a bad thing; rather, regulation is working as intended. Indeed, if ratemaking is done correctly, one would expect the utility to earn close to its authorized rate of return if it prudently manages its operations – sometimes earning slightly over and sometimes earning slightly below its authorized return.

60 Mr. Norwood, in his rebuttal testimony, examined the probable earning shortfall for Avista in 2016 if the Commission were to adopt, instead, the recommendations of Public Counsel, ICNU and NWIGU. (See, Table No. 4 at p. 31 of Exh. KON-1T) Public Counsel's electric rate decrease recommendation of \$29.7 million would translate to only a 6.45% ROE – well below the 9.5% stipulated ROE. Similarly, with respect to ICNU's recommendation of a \$17.4 million decrease, this would result in an ROE in 2016 of only 7.58%, again well below the stipulated 9.5%. Finally, NWIGU's recommendation of no rate increase would result in a 2016 ROE earnings opportunity of only 5.01% versus 9.50%. By the agreed-upon measure of the stipulated ROE of 9.5%, each of these recommendations is woefully deficient.⁸⁵

⁸⁵ (Exh. No. KON-1T, p. 31:17-22)

VII. THE COMMISSION SHOULD APPROVE AVISTA'S THERMAL MAINTENANCE DEFERRAL PROPOSAL

61 As originally filed, the Company proposed including O&M expense at Colstrip and Coyote Springs II (CS2) as part of base power supply expense and tracking any differences from the base expenses through the Energy Recovery Mechanism (ERM).⁸⁶ Subsequently, and as part of the Partial Settlement Stipulation, the parties agreed that O&M costs related to CS2 and Colstrip would be removed from base power supply costs, and that the revenue requirement related to these costs would be addressed during the remainder of this case. This resulted in a reduction in power supply expense for the Partial Settlement of \$3.6 million. Following the Partial Settlement Stipulation, the Company removed CS2 and Colstrip maintenance expenses from power supply amounts, and included the incremental amount of CS2 and Colstrip maintenance expense as an After-Attrition Adjustment.⁸⁷

62 Both Staff and ICNU proposed that these “overhauls” should be “normalized” over the expected maintenance cycles for the plants. Staff Witness Ball argues that the normalization of these costs provides for a consistent matching of revenues and expenses with the appropriate time period.⁸⁸ Mr. Mullins, on behalf of ICNU, recommends, as well, that the Commission require the Company to “normalize” these major maintenance expenses by spreading its cost over the maintenance cycle of the various plants.⁸⁹

⁸⁶ (See Exh. No. WGJ-1T, p. 14:7 – p. 15:21)

⁸⁷ With respect to “hot gas path” maintenance on CS2, the maintenance is dependent on the number of “run-hours” on the gas turbine, and occurs every 24,000 hours, or on approximately a four-year cycle. This last occurred in 2012 at a cost of approximately \$3.9 million (system). It is expected that the CS2 turbine will reach 72,000 hours of run time in 2016, requiring maintenance at an expected cost of approximately \$3.5 million (system). With regard to Colstrip, major overhauls occur every three years; there was a major overhaul in 2014 and another overhaul is planned in 2016. (Exh. No. KON-1T, pp. 43-44)

⁸⁸ (See Exh. No. JLB-1T, p. 13:11-15)

⁸⁹ (See Exh. No. BJM-1T, p. 5:24-27)

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While it is true that the proposed “normalization of major maintenance expenses by Staff and ICNU normalize the costs for customers, as pointed out by Mr. Norwood, their proposals do not address the impact of these major maintenance costs on the Company. (Exh. No. KON-1T, p. 44:18 – p. 45:14) According to Mr. Norwood:

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Without Commission approval to defer these major maintenance expenses, and amortize them over the appropriate time period, Avista would be required to recognize the entire expense in the year the expenses are incurred. While customers would pay for the expense over a number of years through normalization of the expenses, Avista would bear the full expense in the year the maintenance occurs. (Emphasis added)⁹⁰

As concerns maintenance on CS2 in 2016 at a cost of \$3.5 million, under Staff’s approach the Company would recover revenues from customers only over a four-year period, collecting approximately \$875,000 annually over four years; however, the Company would record net expenses of \$2.6 million in the first year (\$3.5 million - \$875,000) and revenues in years two through four of \$875,000. This would result in a “mismatch” of costs and benefits for the Company.⁹¹ There should be a proper matching of costs and benefits for both customers and the Company.⁹²

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To recognize Staff’s and ICNU’s concerns regarding “normalization” of overhauls and to otherwise address variability in thermal maintenance costs experienced by Avista, the Company has proposed on rebuttal to defer only the “hours of operation based” major maintenance expenses required for its thermal generation facilities going forward. The Company would defer Washington’s share of the actual major maintenance expenses associated with these projects in the year they occur, with the first expected in 2016. The balance would be amortized over a four-year period beginning January 1st of the following year, without a carrying charge on the

⁹⁰ (Ibid.)

⁹¹ (Ibid.)

⁹² (Ibid.)

unamortized balance.⁹³ Mr. Norwood explained why deferred accounting is appropriate because of the variability in maintenance schedules:

66 By deferring and amortizing the variability in these maintenance expenses, and recovering them over a four year period, these cost swings can be smoothed, or normalized, for both the Company and for customers. (Smoothing the ‘lumpiness’ of these expenses over time) – a win-win for both customers and the Company. (Emphasis in original)⁹⁴

The net effect is that there would be no increase in cost to customers in this docket for rate year 2016 as a result of the deferral and amortization of these costs. Instead, the actual expenses for these projects would be deferred in 2016, with the amortization to start on January 1, 2017. This would ensure that the costs in the year deferred, and the amortization in the following year, would be known and based on actual expenditures.⁹⁵

67 It should be remembered that, in Avista’s prior Docket UE-110876 (Avista’s 2011 General Rate Case), the Commission approved a deferred accounting mechanism related to thermal generating plant maintenance costs.⁹⁶ Indeed, in that docket, Mr. Schoenbeck, a witness appearing on behalf of ICNU, testified that they were “supportive of the maintenance deferral we came up with [in] this case for several years So in my mind it was a win-win for the – for the customers.”⁹⁷ Likewise, Mr. Schooley, on behalf of Staff, also supported this mechanism in

⁹³ (Exh. No. KON-1T at p. 46:3-9)

⁹⁴ (Id., at p. 46:11-15); see also TR 131:20 – 132:6

⁹⁵ The CS2 Hot Gas Path is planned in 2016 at a cost of \$3.5 million. For Rathdrum, the planned level of expense is \$0.7 million, and the overhaul of Boulder Park is \$0.2 million. A four-year amortization of all of these costs starting on January 1, 2017, would be approximately \$705,000 (Washington’s share). (Exh. KON-1T, p. 47:3-6) (Id.)

⁹⁶ As part of the agreed to settlement in the subsequent Rate Case Docket (Docket No. UE-120436) the parties, however, agreed to eliminate the deferral mechanism as part of an overall settlement of all issues. (Exh. No. KON-1T, p. 47, fn. 41) (Id., at p. 47:22-24)

⁹⁷ (Exh. KON-1T, p. 48:9-14)

the prior docket (UE-110876), and noted that the mechanism creates an acceptable “smoothing effect” for these costs.⁹⁸

68 During the cross-examination, Mr. Norwood observed that, absent a “preferability letter” regarding accounting for deferrals for thermal maintenance, the Company would be required to recognize the expense of the overhaul in the year in which it occurred. Mr. Norwood explained how, under accounting rules, the Company needs an order to allow it to defer and amortize thermal maintenance:

69 “But under – under the accounting rules currently, we operate where you expense it as incurred. We don’t defer it. For us to make that decision, that would be a change in accounting, and under those accounting rules, we would need to have our outside auditor, Deloitte, give us what’s called a preferability letter. And so that – they would need to agree that the preferred method of accounting would be this deferral and amortization piece outside of a Commission order, and the indication from them is that is not the preferred approach for . . . accounting purposes. So we’re not in a position where we can elect to make this accounting change, and so in order for us to accomplish this normalization or a smoothing for the Company, we need a Commission order which allows us to defer it, set it aside, amortize it over a future period. And we’re okay without a return, because then it doesn’t increase the cost to the customer.” (TR 135:22 – 136:15)

70 In response to Bench Request No. 2 (Exh. No. 4), Jason Ball, on behalf of Staff, responded as follows:

71 If the Commission is concerned about the Company’s ability to use this type of FASB accounting, then Staff can accept the creation of a regulatory asset similar to the approach Avista recommends in its rebuttal case. However, Staff advocates a separate regulatory asset for each overhaul with an amortization schedule matching the expected cycle of maintenance of each plant . . .

⁹⁸ (Id., at p. 48: 17-20)

**VIII. THE COSTS ASSOCIATED WITH PROJECT COMPASS WERE PRUDENTLY
INCURRED AND SHOULD BE RECOVERED IN RATES**

A. Introduction: Positions of the Parties.

72 Avista’s “legacy” customer service and work management system was originally placed into service in 1994, and through continuing efforts to refresh and expand its capabilities, it remained in service for 20 years.⁹⁹ Avista began its efforts to replace the system in 2010 and in 2012, after selecting primary vendors, it prepared an initial implementation plan and capital budget.¹⁰⁰ In June of 2014, the Company extended its in-service date (the “Go-Live”) from July 2014 to early 2015, with a corresponding increase in the amount of the initial budget estimate. The final addition to the budget estimate was made in November of 2014 and the system was successfully implemented on February 2, 2015.

73 Staff Witness Gomez alleges that the actual time and cost required to successfully implement the new systems were excessive, due primarily to the performance of one contractor that he believed the Company failed to properly manage.¹⁰¹ He argues that a portion of the implementation costs were not prudently incurred, and should not be recovered by the Company, recommending a disallowance of \$12.7 million.¹⁰²

⁹⁹ (Exh. No. JMK-6T, p. 6:20-29) Chairman Danner inquired how long the existing “legacy” system would have continued to work: In response, Mr. Kensok replied:

The system was designed in the late eighties. It ran on a main frame. We felt like the most we could extend it was a few years. It was never designed for customers to be able to log into. It was designed for six months of training with a call center representative to learn how to use it. So for years, we did a whole lot of Band-Aids on the front end to give the customers the opportunity to pay on the web, for example, or to tie our interactive voice responses to it. Had no security at the detail levels for protecting customer records. We had to do that all on the outside.

So I’d say, from business – from business perspective, a few years. From a technology perspective, it had already been frozen. (TR 274:10-24) (See also TR 277:19 – 278:11)

¹⁰⁰ Avista chose Oracle’s “Customer Care and Billing” system (“CC&B”), and the “Maximo” Work and Asset Management Application (“Maximo”) sold by IBM. The firm EP2M was selected as the primary installation contractor for CC&B, and IBM was hired to install its Maximo system. (Exh. No. JMK-6T, p. 6:25-29).

¹⁰¹ (See Exh. No. DCG-1TC, p. 52:17 – p. 53:2)

¹⁰² (Id. at 49:8-12)

More specifically, Mr. Gomez asserts that a “conflict of interest” arose with Five Point, suggesting that it may have engaged with another company (EP2M) to influence Avista’s vendor selection process.¹⁰³ He asserts that the Company otherwise failed to manage the risks of this potential conflict of interest.¹⁰⁴ He also claims that Five Point failed to perform under the terms of its contract and that Avista did not properly manage the performance of Five Point or otherwise exercise its remedies under the contract.¹⁰⁵ He asserts that Five Point’s failure to perform under its contract was the primary reason for increased costs and an extension of the time to complete the project.¹⁰⁶ Finally he argues that Avista should not recover any bonuses paid to employees under the bonus plan, because the Project’s in-service date was extended and the final budget exceeded estimates.¹⁰⁷

In response, the Company presented the rebuttal testimony of Mr. Kensok.¹⁰⁸ Mr. Kensok is the Company’s Vice President and Chief Information and Security Officer. Mr. Kensok has experience in the direct application and management of Information Services over the course of his 32 year information technology career.¹⁰⁹ Over the last 17 years of his career with Avista, he has overseen the Information Services Department, performing a variety of management roles, directing and leading information technology and systems, planning, operations, system analysis, complex communication networks, cyber security, contract negotiations and data management.¹¹⁰ For Project Compass, in particular, he served as a member of the Executive Steering Committee for the Project, which was established to ensure appropriate executive

¹⁰³ (Id., 53:15-16)

¹⁰⁴ (Id., at 52:12-17)

¹⁰⁵ (Id., at 52 and p. 57)

¹⁰⁶ (Id., at 52:8-11)

¹⁰⁷ (Id., at 60:5-11)

¹⁰⁸ (See Exh. No. JMK-6)

¹⁰⁹ (Id., at 1:10-12)

¹¹⁰ (Ibid.)

oversight of Project Compass.¹¹¹ This Committee met regularly with the Compass leadership team, in order to ensure direct accountability for performance of the project, and to ensure that the Company's management had the information and understanding required to make effective and timely decisions.¹¹² Mr. Kensok also represented the Executive Steering Committee in presentations and discussions with the Company's Board of Directors relating to Project Compass.¹¹³

76 The evidence provided by Mr. Kensok demonstrates that: (1) the project timeline and costs were reasonable and prudent; (2) Avista made prudent decisions with respect to managing all agreements involving Five Point; (3) the increased project cost and delay was not caused primarily by Five Point; (4) the Company made prudent decisions managing the performance of Five Point (and its successor, Ernst & Young); and (5) employee bonuses were directly related to the successful completion of the project, and were administered pursuant to a detailed plan.¹¹⁴

77 Before discussing each of these points in turn, there is one salient fact that is undisputed, even by Mr. Gomez: The project was successfully launched on February 2, 2015 and has performed very well since that time.¹¹⁵

78 In short, the Company made a conscious decision to extend the project by seven months in order to ensure that all of the applications were ready to perform as intended, and that the necessary testing and "dress rehearsals" to ensure a successful launch could occur.¹¹⁶ And that

¹¹¹ (Id., at 3:8-20)

¹¹² (Id., at 17-21)

¹¹³ (Ibid.)

¹¹⁴ (Id., at 6:6-15)

¹¹⁵ (Id., at 5:23-25)

¹¹⁶ Mr. Kensok explained that the Company conducted not just one dress rehearsal, but ran "three dress rehearsals," with each one taking over 10 days to prepare for: "Effectively, we shut down the entire production environment over a weekend, just as though it was live, going to go live, brought up all the test – or brought up all the systems – CC&B, Maximo, and everything else – tested it all, shut it all down, and put it back together. We did that three times during that time frame." (TR 268:20 – 269:3)

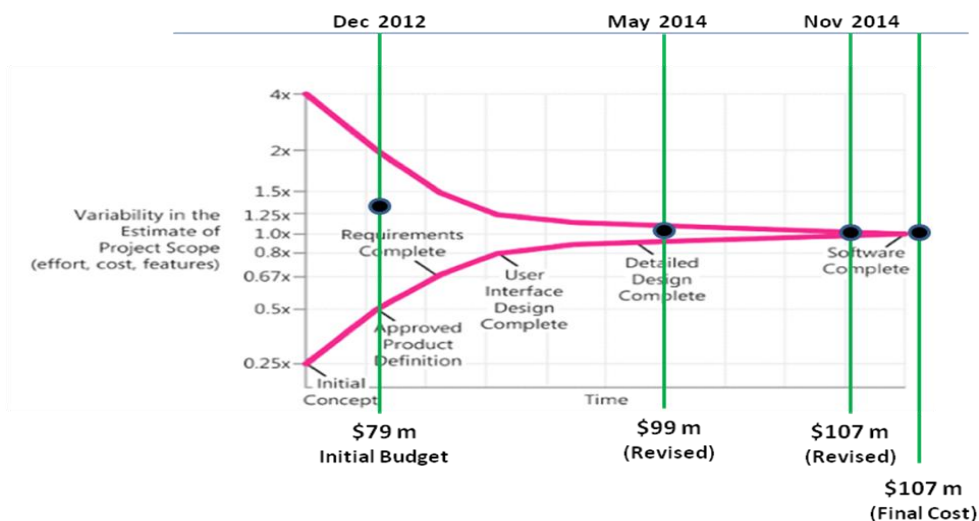
effort paid off. Nor, as explained below, was the final cost of the project excessive for complex projects of this type.

B. The Project Timeline and Costs Were Reasonable and Prudent.

79 It is important to understand that estimating the cost of replacing a large, enterprise-wide customer information system with many applications, by its very nature, involves uncertainties at the outset. In the Company’s 2013 report, “Overview of Avista’s Project Compass” (Exh. No. JMK-7 at p. 37), this difficulty in estimating costs during the initial stages was squarely addressed:

80 Early in the scoping of a software project, particular details of the application being designed/installed, a detailed knowledge of the Company’s specific business requirements, details of solution sets, the management plan, identifying staffing needs, and many other variables are simply unclear. Accordingly, estimates of the potential cost of the project are highly variable. As these sources of variability continue to be investigated and reduced, the project uncertainty decreases; likewise, so does the variability and estimates of the project cost. This phenomenon, widely discussed in the literature, and often associated with author Steve McConnell, is known as the “Cone of Uncertainty” . . . (Emphasis supplied).¹¹⁷

This “Cone of Uncertainty” was depicted at page 10 of Mr. Kensok’s testimony (Exh. No, JMK-6T):



¹¹⁷ (Exh. No. JMK-6T, p. 7:14-23)

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As shown above, the preliminary initial estimate was \$79 million during the initial project assessment phase (indeed, at that point, the variability in the estimate of project costs could have ranged as high as “two-times the budget that was estimated at that point, or a total of \$157.8 million,” as explained by Mr. Kensok).¹¹⁸ Next, in May of 2014, the Company’s budget was revised to \$98.6 million after the detailed designs were completed (and, again, the degree of variability that could have been assigned to the predicted final cost at that point could have been expected to be about 10% - for a total cost of \$108.5 million).¹¹⁹ The final cost of the project was approximately \$107 million when implemented.¹²⁰ Simply put, it is to be expected that initial budget estimates for a project of this size and scope would be subject to revision as the project was refined and designs were completed. Certainly the end result was not unreasonable. As testified to by Mr. Kensok, projects of this type are difficult to implement and experience elsewhere with similar systems has proven so:

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If you look at some of the other utilities, basically, you know, for Los Angeles [W]ater and [P]ower, for example, they started at 100 million and they did it at 200 million – plus, and they were late. If you look at Oncor, they finished at 165 million for CC&B and Maximo and were a year late. (TR 259:2-7)¹²¹

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It should come as no surprise that the complexity of any project of this type could be underestimated, with a greater workload than initially budgeted.¹²² Not surprisingly, the ultimate

¹¹⁸ (Id. at 8)

¹¹⁹ (Id. at 9:4-6)

¹²⁰ (Ibid.)

¹²¹ While appearing in the confidential portion of the transcript, this information is not confidential.

¹²² In its June 2014 report titled “Revised Timeline And Budget Forecast – Avista’s Project Compass,” (Exh. No. JMK-2) some of the factors influencing the complexity of the project were explained:

While it’s common for a business to install one major system at a time, such as a customer service, financial management, supply chain or asset management system, the Company is installing two major systems simultaneously (CC&B and Maximo Asset Management). Avista is required to implement both new applications because our Legacy system contains a customer service module and work and asset management module that are highly integrated, mainframe-based, and both in need of replacement. As described above, this effort requires not only that these two systems be custom integrated, but that together, they be integrated with the approximately 100 other applications and systems required to perform the Company’s integrated business operations.

complexity of the project, and the resulting effort to complete, were greater than initially estimated.¹²³ Mr. Kensok explained that the nearly 100 applications were “extremely complex” and that “no other utility has done that.” (TR 270:2-5)

C. Avista Was Prudent In Managing Its Relationship With Five Point.

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As noted, Staff Witness Gomez was critical of Avista’s management of one of its vendors – Five Point. Five Point was hired by the Company in June of 2011, to provide support in the areas of documenting Avista’s system requirements used in the Request for Proposals process for selecting the new computer applications and key installation vendors, and assisting in the review of proposals. As discussed below, the timeline is important to understand: Vendor proposals were received by Avista in October of 2011. Winning vendors were selected in March of 2012, and contracts were negotiated and signed in July of 2012. As noted, the role of Five Point was to support Avista’s procurement process. It was not until much later in January of 2013 that Avista was first notified by EP2M that it had been purchased by Five Point. As explained by Mr. Kensok, “Prior to this time, Avista had no knowledge of any relationship between Five Point and EP2M, or at what point in time those discussions may have commenced.”¹²⁴ And Mr. Gomez can point to none.

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Nevertheless, Mr. Gomez imagines that a “conflict of interest” somehow arose when Five Point acquired EP2M, inferring that the Company’s vendor selection and contracting processes may have been negatively impacted as a result. He appears to erroneously assume that Five Point was somehow involved in the contract negotiations between Avista and EP2M. That is simply

(See Exh. No. JMK-2 at p. 7).

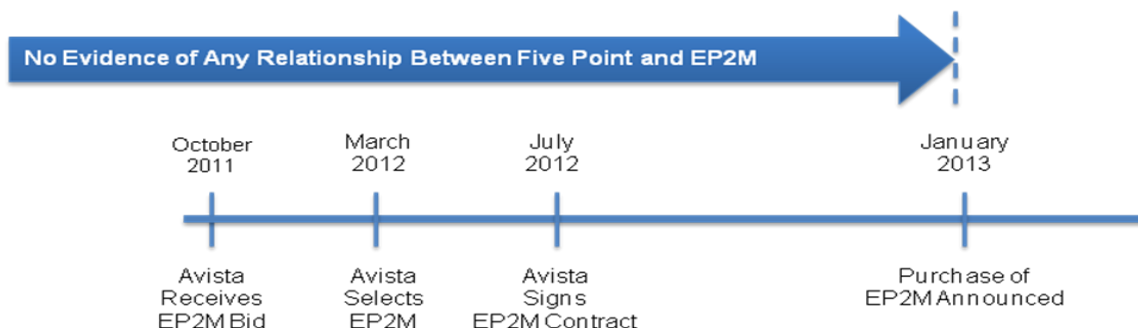
¹²³ Mr. Kensok cited two examples of added complexity and effort: First the need to upgrade the version of the Company’s ARC GIS (computer mapping) application to provide Maximo data compatibility, and the added coding for substantial extensions required to support the Company’s comfort-level-billing and credit and collections activities. (See Exh. No. JMK-6T, p. 13:8-12).

¹²⁴ (Id., at 15:6-10)

not the case. Avista’s employee team was in these negotiations to select vendors – not Five Point.¹²⁵ Moreover, as noted above, the Company first learned of the acquisition by Five Point of EP2M several months after its decision to select EP2M as a contractor. In any event, the Company’s customers were protected from any potential conflict of interest by the “rigorous and objective processes established for developing vendor proposals, evaluating and scoring proposals, making final vendor selections, and in negotiating the final contracts, purchase agreements and purchase prices,” as testified to by Mr. Kensok.¹²⁶ (See Exh. No. JMK-7 for comprehensive documentation of these processes.¹²⁷) Nowhere does Mr. Gomez challenge or otherwise dispute the actual vendor selection processes used and documented by Avista or otherwise assert that these processes were less than comprehensive and objective.

86

By way of summary, the following timeline (See Exh. No. JMK-6T, p. 17) demonstrates that there was no evidence that Avista was aware of any relationship between Five Point and EP2M until January of 2013:



¹²⁵ (Id., at 15:20-22)

¹²⁶ (Id., at 16:3-6)

¹²⁷ Over 81 pages of the Company’s 2013 report “Overview of Avista’s Project Compass” (Exh. No. JMK-7), were devoted to describing the process documentation, including information such as rating criteria, weightings, scores and Avista’s team selections.

In conclusion, Mr. Kensok testified as follows:

87 At the time EP2M submitted its bid in October 2011, there was no evidence of any relationship between EP2M and Five Point. The acquisition of EP2M by Five Point was announced in January 2013. Only Company employees scored the proposals of the vendors, based on results of a comprehensive and objective review and scoring process, which is well-documented, and has not been challenged by Staff. At the time EP2M was selected by Avista in March 2012, there was no evidence of any relationship between Five Point and EP2M.¹²⁸

At the end of the day, we are only left with Mr. Gomez's sheer speculation about any potential conflict of interest. The evidence of record belies that. The ultimate evaluation and selection of EP2M by Avista was made on the merits, without any undue influence of a third party.¹²⁹

D. The Actions of Five Point Were Not the Primary Cause for Revised Project Costs or Delays.

88 Witness Gomez claims that the performance of Five Point was the “primary contributor” to the additional time and costs required to successfully complete the project.¹³⁰ Company Witness Kensok explained why that was not the case. The greater complexity of the project, and the associated increased effort, required more time for many different Avista employee teams and project vendors – not just Five Point – to complete their work.¹³¹ In his testimony, Mr. Kensok provides examples of several key activities that were taking more time to complete than planned.¹³² Of the thirteen different key activities, six involved Five Point, but in each case the responsibility for completing the activity was shared by other organizations – not just Five Point. Mr. Gomez did not challenge this. In addition, Mr. Kensok, provided examples of eight major

¹²⁸ (Exh. No. JMK-6T, p. 16:18-23)

¹²⁹ As noted above, there was no evidence of any relationship between Five Point and EP2M at the time EP2M was selected as a vendor. Among the prudence criteria employed by this Commission is “. . . What would a reasonable Board of Directors and Company management have decided given what they knew or reasonably should have known to be true at the time they made the decision?” (Eleventh Supplemental Order, Docket No. UE-920433, September 21, 1993).

¹³⁰ (See Exh. No. DCG-1TC, p. 52:8-11)

¹³¹ (Exh. No. JMK-6T, p. 18:10-12)

¹³² (Id., at 19)

activities that had not reached a sufficient stage of development required to successfully implement the Project in July of 2014. Accordingly, it would not have been possible to successfully implement Project Compass without the completion of each of these activities.¹³³ Five Point shared the responsibility with others for completing four of these activities – it was not solely responsible for completion of these activities. Indeed, Five Point was not involved at all with the other four activities that required the extension to February 2015 for completion:

89 The remaining four activities, Field Activities, Meter Data Synchronization, Maximo Data Conversion, and ARC GIS 10.2 Upgrade, did not require the participation of Five Point in any way. The progress made on these activities was not impacted by, or dependent on the performance of Five Point. And, in addition, these four activities, which did not involve Five Point, required more time and budget to complete than the original estimate, and were not ready for implementation on the original Go-Live date in July 2014.¹³⁴

In the final analysis, as explained by Mr. Kensok, the “additional time and cost required to complete the project were not primarily due to the performance of Five Point, alone.”¹³⁵

E. The Company Was Prudent in Retaining Five Point and Ernst & Young to Complete the Project.

90 It is Mr. Gomez’s facile assertion, arrived at without the benefit of a true understanding of the dynamics of the Project, that the Company should have immediately ceased payments to Five Point under its contract when it first noted that Five Point was not completing its deliverables according to the schedule.¹³⁶ In doing so, Mr. Gomez believes this would have forced Five Point to meet its deliverables schedule and thereby avoid the need to extend the timeline and budget.

¹³³ (Exh. No. JMK-6T, p. 20:1-12) These activities included CC&B Integrations; CC&B and Maximo System Integrated Testing; Field Activities; Credit and Collections; Meter Data Synchronization; Development of Test Cases; Maximo Data Conversion; and ARC GIS 10.2 Upgrade. (Exh. No. JMK-6T, p. 20:1-10).

¹³⁴ (Id. at 20:17-26)

¹³⁵ (Id., at 21:4-9)

¹³⁶ (See Exh. No. DCG-1TC, p. 57:1-4)

91

Five Point was not alone among the major contractors working with Avista on this Project. Avista worked with all of its contractors and entered into revised contracts and change orders with the majority of its vendors as the project developed. That was to be expected as the scope of the work became better defined.¹³⁷ Indeed, Mr. Kensok provided a list of change requests showing increased costs for 25 of the contract companies who supported Project Compass; Five Point was not alone in that regard.¹³⁸ And yet, Mr. Gomez singles out only the performance of Five Point. In doing so, he conjures up arguments over “conflict of interest” that are not supported by evidence.

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With reference to Five Point, in particular, Avista worked closely with Five Point to “cure” any performance problems (in the same manner as it did with other vendors). As explained by Mr. Kensok, Five Point added staff to its complement of code developers, and Avista and Five Point worked together to improve the processing time being required to complete activities, particularly in the area of defect remediation. Moreover, at the Company’s request, Five Point replaced its project manager, and also moved its key developer to Spokane to work closely with Avista’s employees in reducing the turnaround time for resolving defects.¹³⁹ Importantly, Avista determined that Five Point had the capability needed to complete the Project, and that the Company was able to work successfully with them to optimize the completion of tasks.¹⁴⁰

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Staff Witness Gomez, however, faults Avista for not fully considering the option of exercising its contract provisions to force Five Point to perform according to the initial contract schedule. The sworn testimony of Mr. Kensok, as a member of the Executive Committee

¹³⁷ (Exh. No. JMK-6T, p. 26:11-15)

¹³⁸ (Id., at 27; see also Exh. No. JMK-9C)

¹³⁹ (Id., at 23:1-8)

¹⁴⁰ (Exh. No. JMK-6T, p. 25:1-5)

overseeing the project, described the factors that Avista took into consideration in its decision to continue to use Five Point to complete the project. These factors included: (1) the ability of Avista to work successfully with Five Point in completing the project; (2) the consequences if Avista were to terminate payment with Five Point; (3) the potential outcome of any litigation with Five Point; (4) whether it could find a suitable replacement contractor who would be available and could perform on the same timeline; (5) the significant delay and increased costs associated with changing contractors; and (6) finally, the cost of hiring a replacement contractor.¹⁴¹ Moreover, it should be remembered that Five Point staff were among the original authors of the CC&B application and were key individuals for the project. As testified to by Mr. Kensok, “. . . when considering alternatives to Five Point, we had to weigh the risks of finding a replacement team that had sufficient knowledge, experience, skills, and familiarity with the application, which was an important element of our successful implementation.”¹⁴²

94 All of the factors mentioned above were taken into consideration by the Executive Steering Committee,¹⁴³ as explained in the Company’s response to Staff D.R. 152C (included as Exh. No. JMK-11C):

95 Avista also concluded that even if another suitable contractor was immediately available to step in, that the effective transition would, in the very best case, add several months to the Project timeline (i.e., several months beyond the actual February 2, 2015 Go-Live).

96 Moreover, it should be remembered that the extension of time was not primarily caused by Five Point. Indeed, in any litigation, the Company understood that Five Point could “reasonably point to the performance of Avista and other contractors as contributing to their need

¹⁴¹ (Exh. No. JMK-6T, p. 23:21 – p. 24:2)

¹⁴² (Id., at 24:10-12)

¹⁴³ The Executive Steering Committee was composed of Mr. Kensok, the President of Avista Utilities, the Vice President of Energy Delivery, the Vice President and Treasurer, and the Vice President of Energy Resources. (Exh. No. JMK-6T, p. 24:16-20).

for additional time to meet contract deliverables.”¹⁴⁴ Staff Witness Gomez seems to fault Avista for not having documentation of these discussions. As Mr. Kensok explained in his testimony and in the information furnished pursuant to discovery, Avista did actively consider all of its options. However, it is important to remember that it worked with Five Point to “cure” any deficiencies (as it did with other contractors) and the issue never “ripened” into the need for a full blown assessment of all litigation risks and uncertainties.

97 What is undisputed is that the replacement of Five Point would have put Project Compass further behind schedule. And Mr. Gomez does not contest this point. As noted by Mr. Kensok, compared with a decision to continue the project with Five Point, the Committee concluded that any alternative action would have seriously delayed the project and added significantly to the final cost. It was estimated that any delay beyond February 2, 2015, would cost upwards of \$3.6 million per month.¹⁴⁵ Mr. Kensok testified that had the Company fired Five Point or exercised other contractual remedies, it would have had an impact on the February 2nd go-live date: “It [the February 2nd “go-live” date] would have been impossible.” (TR 272:1-6) In the final analysis, there is simply no evidence in this record that demonstrates that a different decision by the Company would have delivered Project Compass more quickly, more successfully, or at a lesser cost.

98 Finally, Avista received additional value for its contract extension and payments to Five Point to complete the project. In the process of doing so, it was able to retain the critical members of the Five Point team for the balance of the project.¹⁴⁶ Under the contract extension,

¹⁴⁴ (Id. at 25:20-22)

¹⁴⁵ (Id., at JMK-6T, p. 25:25-29)

¹⁴⁶ Mr. Kensok explained the cost and expense associated with further delay: “. . . We’d lose all the core people or many of the core people, and their ramp-up to start back up would have been in the millions of dollars for, we estimated, at least six months to get to restart if we stop the project to deal with Five Point at that level and fired

members of the Five Point team contributed an additional 8,000 hours to the Project for which they were paid approximately \$3.9 million – which was less than the \$6.7 million estimated cost of the contract extension.¹⁴⁷

F. Bonuses Paid to Company Employees Were Prudent, Based on a Very Successful Effort in Implementing Project Compass.

99 Finally, Staff Witness Gomez recommends that the bonus amounts paid to Avista employees should not be recovered by the Company. Mr. Kensok described the rationale for the bonus plan (see Exh. No. JMK-12C) that recognized the significant challenge and effort required to complete Project Compass and the substantial and sustained contribution required of employees over a period of approximately two years. Indeed, when the timeline was extended, it required our employees to maintain the additional high level of intensity through the February 2015 implementation date. According to Mr. Kensok, the “continuity that comes with retaining the same employees over a multi-year period, on an effort as complex as Project Compass, warrants a bonus plan to help encourage employees to stay with the Project to the end.”¹⁴⁸

100 It is important to note that this bonus plan (see Exh. No. JMK-10) was based on objective and measurable benchmarks established at the beginning of the Project. Moreover, the plan was audited by the Company’s internal audit group, and approved by the Company’s senior executives and the Board of Directors. The Executive Steering Committee authorized bonuses being paid based on achievement of defined project benchmarks as required in the plan.¹⁴⁹

them. And then you got to retrain everybody. And finally, we felt it would be close to \$20 million, not the \$3.9 that we paid E.Y. to extend.” (TR 272:16-23)

¹⁴⁷ The contract extension was based on the hourly rates of named personnel and an estimate of the hours to be spent on the project for each person, based on the estimated time needed to complete the project. The Company chose a time-and-materials-based contract, because it provided greater transparency, and more control over the ultimate amount Avista would spend in successfully completing the project. (Exh. No. JMK-6T, p. 28:5-10).

¹⁴⁸ (Exh. No. JMK-6T, p. 28:23-25)

¹⁴⁹ (*Id.*, at 29:2-9)

101 In the end, bonus compensation was appropriate to provide to employees in recognition of their sustained and difficult efforts – many of whom left their assigned jobs to work full time on this project for more than two years. There is no reasonable basis for a disallowance of these costs.

IX. ADVANCED METERING INFRASTRUCTURE (AMI) IS THE NECESSARY “PLATFORM” FOR THE FUTURE IN DELIVERING CUSTOMER BENEFITS

102 Avista plans to move forward with the implementation of AMI, absent a decision from the Commission in these dockets to the contrary.¹⁵⁰ The Company, however, is not asking for preapproval of the recovery of costs; that will await the further refinement of costs and benefits to be presented in the Company’s next general rate filing. Instead, the Company is asking that the Commission, in its Order, do two things:

(1) Provide guidance with respect to Avista’s planned deployment of AMI, most notably by identifying any issues or concerns based on the evidence presented thus far; and

(2) Specifically approve, as part of this Docket, Avista’s request for an accounting order addressing the planned replacement of the Company’s existing electric meters.

A. AMI Has Become the Industry “Platform” for Delivering Customer Benefits.

103 Over the six year deployment period, the Company plans to deploy advanced meters to approximately 253,000 electric customers and 155,000 natural gas customers in the State of Washington. Advanced electric meters are digital meters capable of two-way communication, which are equipped with the ability to measure the incoming and outgoing flow of electricity

¹⁵⁰ (Exh. No. KON-1T, p. 40:9-11)

from a customer's premises in intervals that range from 5 minutes to an hour. They must be connected with specialized communication networks and information management systems to ultimately deliver value to the consumer. This entire system of meters, communications, and digital hardware and software systems, is referred to as the advanced metering infrastructure.¹⁵¹

104 The national trend in the deployment of smart metering systems is revealing. These levels have increased markedly from only 7 million in 2007, to a level of 50 million by July of 2014.¹⁵² In fact, the rate of penetration of advanced electrical meters stands at 43% for residential applications as of 2015, but is expected to increase to a range from 50% to 70% by the year 2020 (when Avista's AMI will be fully deployed).¹⁵³

105 Throughout 2015, the Company has been developing the system requirements and preparing requests for proposals from metering system vendors and evaluating systems to be implemented. The installation of AMI systems is slated to begin in 2016 along with the installation of associated communications infrastructure and systems integration. It is presently anticipated that the advanced metering project will be completed in 2020.¹⁵⁴

106 Staff and Public Counsel express concerns regarding the uncertainty surrounding the costs and benefits associated with AMI, and do not support the inclusion of new investment and

¹⁵¹ (Exh. No. DFK-1T, p. 5:13 – p. 6:2) The AMI meters to be installed in Washington should be distinguished from the automatic meter reading technology currently deployed in the Idaho and Oregon service territories, which record energy consumption and transfers that data, usually monthly, from the meter to the utility by way of one-way communication. Advanced meters (also known as Smart Meters) are capable of two-way communication, meaning that the meter can remotely transmit energy usage information to the utility and the customer can, in turn, also receive and respond to signals sent from the utility to the meter. (Exh. No. DFK-1T, p. 6:5-17).

¹⁵² (Exh. No. DFK-1T)

¹⁵³ (Exh. No. DFK-1T, p. 9:10 – p. 10:4) (See also TR 115:8-16) In fact, Avista's largest neighboring cooperative utilities with adjacent service territories – Inland Power & Light and Kootenai Electric Cooperative – either have installed advanced metering or are in the process of doing so. Elsewhere in Washington State, Tacoma Public Utilities has deployed advanced metering and Seattle City Light is in the process of selecting the advanced metering systems that they will be placing into service. (Exh. No. DFK-1T, p. 10:5-9).

¹⁵⁴ (Id. at 19:14 – 20:2)

operating costs for AMI in the 2016 revenue requirement.¹⁵⁵ The Company recognizes that, at present, the Company's estimates of costs and benefits remain preliminary and will be refined over the next several months. Accordingly, the Company has removed any AMI investment and operating costs from its revenue requirement in this case.¹⁵⁶ As will be discussed below, however, the Company does need an accounting order from this Commission addressing the planned replacement of existing electric meters. Absent such an Order, Avista will not enter into contracts with equipment vendors to replace existing meters and will suspend the project. As explained by Mr. Norwood, under Generally Accepting Accounting Principles (GAAP), once Avista selects a vendor and signs an agreement to replace its electric meters, absent an accounting order from the Commission, Avista would be required to write-off its existing \$21 million net investment in electric meters.¹⁵⁷

107 As noted by Mr. Norwood, it is the Company's desire to move ahead at this time with AMI, assuming it receives the accounting treatment it has requested.¹⁵⁸ Moreover, Mr. Norwood explained that the Company is ready to proceed with the selection and contracting with vendors once the accounting order is received:

108 Actually, we have requests for proposals out and proposals received, and so we are actually in the process right now of identifying vendors, and so we would expect, very early in the first quarter, to move ahead with executing agreements with vendors to move forward with the project.¹⁵⁹

¹⁵⁵ (See Exh. No. DN-1T, p. 4: 3-8; Exh. BRA-1T, p. 9:15 – p. 10:5)

¹⁵⁶ The associated revenue requirement, initially included with the Company's direct case, was \$4.1 million. This has been removed in the Company's revised revenue requirement. (See Exh. No. KON-1T, p. 34).

¹⁵⁷ (Exh. No. KON-1T, p. 41:8-11) In response to questioning from Commissioner Rendahl, Mr. Norwood explained that “. . . once you sign an agreement with a vendor to replace those meters, you don't write them off as you replace them. You write them off immediately because what you've done is you've made a commitment to replace them.” (TR 141:8-11)

¹⁵⁸ (TR 104:5-18)

¹⁵⁹ (TR 104:13-18)

Mr. Norwood cautioned, however, that it would not proceed without an accounting order:

109 We would not proceed if we don't receive the accounting treatment that is requested, simply because we would have a \$20 or \$21 million write-off right up front.¹⁶⁰

Furthermore, the requested accounting treatment includes not only the deferral, but a return on the unamortized balance.¹⁶¹ If the Company does not receive a return, it would result in “a \$3.7 million write-off.”¹⁶²

110 More specifically, Avista proposes that, in this case, a regulatory asset be established coincident with the month in which it signs a contract with a vendor to provide new AMI meters.¹⁶³ Avista proposes to amortize the undepreciated balance of approximately \$20 million over a 10-year period beginning January 2017, with a return on the unamortized balance. Accordingly, the cost associated with accelerating the amortization of the existing electric meters would begin in 2017, instead of 2016. Avista is also requesting a rate of return on the unamortized balance, without which Avista would suffer an immediate write-off of \$3.7 million. Absent this accounting treatment, Mr. Norwood explained that the AMI Project would be

¹⁶⁰ (TR 104:23 – 105:1)

¹⁶¹ (TR 105:15 – 106:4)

¹⁶² (TR 89:1-3)

¹⁶³ With reference to AMI, Mr. Norwood clarified with Commissioner Rendahl that it was including the specific accounting request as part of its rate case filing; it was not doing so by means of a separate accounting petition. (TR 20:1-7) As part of recent general rate case filings, the Company has requested, and the Commission has approved, deferred accounting – doing so without the need for a separate accounting petition. See, e.g., Docket UE-11087 (approved deferred accounting for Coyote Springs 2 and Colstrip 3 and 4 maintenance costs); Docket UE-080416 (approved deferral of certain settlement payments made to Coeur d'Alene Tribe).

delayed until such time as an order issued, or the Project would otherwise be terminated.¹⁶⁴ The Company would not move forward facing a \$21 million write-off.¹⁶⁵

B. Evaluation of the Costs and Benefits of Advanced Metering.

111 In Mr. La Bolle’s testimony,¹⁶⁶ he summarizes the benefits (both quantified and unquantified) as presently estimated. Over the life of the meters, he identifies not only benefits derived from operational efficiencies, but also direct customer benefits. The preliminary estimate of quantified benefits is approximately \$15.4 million annually. This is then compared with preliminary estimates of costs discussed elsewhere, to arrive at a net benefit of approximately \$3.6 million over the life of the Project.¹⁶⁷ It is important to recognize, however, that this tabulation of benefits was conservative and also did not seek to quantify at this time any of the “intangible benefits” otherwise identified.¹⁶⁸

112 It is true that the Company’s preliminary estimate of approximately \$145 million of costs associated with implementing AMI has since increased to nearly \$165 million.¹⁶⁹ This has had the effect of reducing, somewhat, the overall net benefit over the life of the AMI Project of \$7.5

¹⁶⁴ Ms. Andrews explained that there is no double counting for existing meters in the attrition analysis related to depreciation expense and the amortization expense for the regulatory asset. She explained that in the Company’s attrition study, it has included the \$20 million of rate base with respect to existing meters, but has not included a separate adjustment to add a return in for the regulatory asset or the \$2 million amortization. There’s “no double counting.” (TR 186:19-25)

¹⁶⁵ (Exh. No. KON-1T, p. 42:3-4) In response to Bench Request No. 4, the Company provided estimated net plant balances for existing meters as of February of 2016 of \$20.9 million. Attached to the response to the Bench Request was the depiction of the requested 10-year amortization period beginning January 1, 2017. This response also addresses how Avista would continue to treat net plant associated with electric meters in 2016 and the associated depreciation level. Beginning in January 2017, however, after new retail rates are set in the next rate case, the remaining \$20 million regulatory asset would be amortized over a 10-year period at approximately \$2.0 million annually, with a rate of return on the unamortized balance.

¹⁶⁶ (Exh. No. LDL-1T at p. 6)

¹⁶⁷ (See Exh. No. LDL-16CX)

¹⁶⁸ These intangible benefits include: Access to interval usage data; customer home network interface; energy alerts; customer privacy; rate options; micro grids and smart cities; data analytics; distributed generation; and engineering studies. (See Exh. No. LDL-1T, p. 6:19-21 and p. 14:13-24).

¹⁶⁹ (See Exh. No. LDL-16CX)

million down to \$3.6 million as noted above.¹⁷⁰ With respect to any assessment of “net benefits” at this point in time, the Company acknowledges that its costs are preliminary in nature, as is its assessment of benefits. While Avista continues to believe that its most up-to-date assessment of net benefits remains reasonable given what is known at this time, it will be refining this information as it develops additional costing information based on actual bids received from vendors. Likewise, it will be refining its estimate of the associated benefits of AMI. A more refined estimate of “net benefits” will be presented in the Company’s next general rate filing.

113 That is not to say, however, that the information provided in the record in this proceeding is not useful to allow the Commission to provide some guidance, at this point in time, with respect to any issues or concerns that it may have.¹⁷¹ That guidance would be instructive to the Company in determining not only (1) whether to proceed, but also (2) how to proceed. While it is ultimately the management’s prerogative to decide when and how to implement the program, a sufficient record has been developed in this case to allow the Commission to affirm or otherwise question the general direction of the Company with respect to AMI. The Company understands,

¹⁷⁰ (See Exh. No. DFK-1T, p. 15 and Exh. No. LDL-16CX)

¹⁷¹ According to Mr. Norwood, with reference to AMI:

We’ve made it clear that we’re not asking for a prudence determination on the investment or the costs associated with implementing AMI. Our plan is to come back at a later date and demonstrate that we took the right steps, we hired the right vendors, we selected the right equipment, and we spent the right amount of money to implement it. But based on the cost-benefit and analysis that we performed, we’ve decided that we believe now is the time to move forward with AMI, and so the cost-benefit analysis demonstrates that. And so what we’re looking for here is some kind of affirmation or indication from the Commission that, based on the analysis presented to him, that they’re in agreement to move forward with this project. (TR 91:7-20)

however, that this does not rise to the level of “pre-approval.”^{172/173}

114 Ms. Barbara Alexander, on behalf of Public Counsel, has expressed skepticism over whether Avista will actually achieve its estimated net benefits.¹⁷⁴ Interestingly enough, of the Company’s 24 areas of quantified benefits (with a cumulative annual value of approximately \$15.4 million), she has chosen to question only four areas of benefit.¹⁷⁵ The rebuttal testimony of Mr. La Bolle responds to each of these four areas, in turn, and explains why her criticisms are wide of the mark.¹⁷⁶ Those arguments will not be repeated here. What is important to note, at this time, however, is that Avista’s estimate of benefits of AMI has been conservatively tabulated.¹⁷⁷ The level of these benefits will be reexamined, along with an update of the costs associated with AMI, and presented in Avista’s next general rate case in support of recovery of the costs associated with AMI.

115 Even though Ms. Alexander professes in her testimony to not oppose AMI generally, her past experience suggests otherwise. As shown in Cross Exhibit No. BRA-CX1, she identified 27

¹⁷² Indeed, NARUC, itself has recognized that deployment of AMI technology may require the removal and disposition of existing meters that are not fully depreciated. In its February 21, 2007 Resolution, it was resolved that Commissions seeking to facilitate deployment of cost-effective advanced metering technology should consider the regulatory option to, inter alia:

. . . Provide for timely cost recovery of prudently incurred AMI expenditures, including accelerated recovery of investment in existing metering infrastructure, in order to provide cash flow to help finance new AMI deployments.

Moreover, this same Resolution encouraged Commissions to consider regulatory options for AMI that “takes into account both tangible and intangible benefits.” (See Exh. No. DFK-4).

¹⁷³ Mr. Norwood further explained that if the Commission were not to otherwise affirm, in principle, AMI, then it is being asked to “. . . let us know if there’s any red flags or material concerns that they have, at this point, about moving forward with AMI.” (TR 89:15-17)

¹⁷⁴ (See Exh. No. BRA-1T)

¹⁷⁵ (See Exh. No. LDL-1T)

¹⁷⁶ (See Exh. No. LDL-1T, pp. 7-14)

¹⁷⁷ In response to questioning by Chairman Danner, Company Witness La Bolle acknowledged that Avista was being “conservative” in how it estimated the benefits. Mr. La Bolle cited several examples in the Company’s benefit analysis and concluded as follows:

I did a little tally of the benefits where we arbitrarily decided not to claim the entire benefit as a way to be conservative and tallied those up in the model, and it adds up almost \$30 million to the net benefit of the model, so it’s pretty substantial. (TR 418:13-23)

different occasions on which she has presented AMI testimony.¹⁷⁸ Apparently in her many years of testifying on AMI, however, she has yet to find a single AMI program that she could support.

116 In conclusion, the Company recognizes that its estimates of costs and benefits (and accordingly the “net benefits”) are preliminary “estimates.” These will be refined prior to the Company seeking to recover costs associated with a “prudence” review. But that does not mean that such an effort to define “net benefits” (however preliminary) is without significance or worth. Avista believes that it has provided a sufficient record in this case to permit the Commission to express general observations or concerns regarding the direction in which the Company is heading with respect to AMI. Such guidance would prove helpful to the Company at this time.

117 Even if such general guidance is not forthcoming (and the Company recognizes that the Commission may elect not to provide such at this time), the Company does need at this time the approval of an accounting order in this Docket that would allow it to amortize its existing electric meters, along with a return on the unamortized balance. It simply cannot proceed to contract with vendors absent such an order. To do so would force an immediate write-off of nearly \$21 million.

118 In closing, Avista appreciated the opportunity to present evidence with respect to its AMI program, however preliminary in nature, and believes that the hearing process has provided further focus and clarification of the issues involved.

¹⁷⁸ On cross examination, Public Counsel Witness Alexander acknowledged that, even though she has presented AMI testimony on 27 different occasions, “In not one instance” did she ever recommend adoption of AMI for the particular utility. (TR 581:10-14) Moreover, she acknowledged that in nearly every jurisdiction in which she has presented AMI testimony, the jurisdictions have ultimately adopted, in one form or another, AMI. (TR 582:8 - 583:18)

X. OTHER ISSUES

A. Additional Capital Reporting Requirements Should Not Be Imposed At This Time.

119 Staff Witness Gomez proposes to expand the Company's capital reporting and filing requirements in between rate cases.¹⁷⁹ Such reporting would extend well beyond the recently-developed capital reporting presently provided by the Company. As explained by Company Witness Schuh, as a result of the Company's 2012 general rate case, it began providing quarterly reports related to its overall capital expenditure plan (as part of the two year rate plan adopted).¹⁸⁰ Subsequently, capital reporting was expanded to include even more detailed information by expenditure request, including transfers-to-plant, budget-versus-actual information and construction work in progress, all to be reported on a semi-annual basis.¹⁸¹ (See Exh. No. KKS-11 for an example of such an expanded report.) Accordingly, Avista already provides a wealth of capital information to Staff and interested parties outside of a general rate case. Avista believes it would prove more beneficial to develop a working understanding of the Company's Asset Management Program before requiring additional capital reporting.¹⁸²

120 On cross examination, Mr. Gomez admitted that no other utility in this jurisdiction is subject to the same capital reporting requirements.¹⁸³ Moreover, it is not at all clear what use is actually being made of the information that the Company has already been supplying. In response to questioning by Commissioner Jones, Mr. Gomez acknowledged that Staff has yet to provide an update to the Commissioners based on either the quarterly or semi-annual reports previously filed by the Company. (TR 511:1 - 512:3)

¹⁷⁹ (See Exh. No. DCG-1TC, pp. 64-65)

¹⁸⁰ (Exh. No. KKS-6T, p. 20)

¹⁸¹ (Ibid.)

¹⁸² (TR 502:1-12)

¹⁸³ (TR 506:6-9)

121

To conclude, the Company already provides extensive data surrounding its capital projects both in its rate case filings and through its extensive and detailed periodic compliance reports in between cases. The Company continues to be cooperative in providing whatever additional information on specific projects that are of interest – and will do so upon request, without yet an additional layer of formal reporting. The Company urges the Commission not to “layer-on” an additional level of formal reporting at this time.¹⁸⁴

B. Additional “Econometric” Modeling of Reliability May Be Premature at This Time.

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Staff Witness Cebulko expresses interest in developing an “econometric model” that takes into account Company-specific service territory attributes to determine appropriate, utility specific benchmarks related to reliability.¹⁸⁵ In his words, it would use data on “as many relevant variables as necessary and available, collected from regulated utilities across the country, to quantify the relationship of service territory characteristics to reliability performance.”¹⁸⁶ He concedes that this is a “laborious task and participation from the regulated utilities in identifying key data sources and developing the model will be critical.”¹⁸⁷

123

Avista, of course, will cooperate with any reasonable effort in this regard. However, Avista wishes to draw attention to the wealth of information already available for Staff to digest, before it embarks on further analysis and data gathering. As explored during cross examination, some of this information relates to the detailed “asset management program reports” that speak directly to reliability metrics that are prepared by the Company with respect to a multitude of

¹⁸⁴ Nor should the Commission accept Mr. Gomez’s recommendation that utilities should be somehow limited in the testimony they can present in future rate cases regarding pro forma capital additions. It is one thing to debate the merits of pro forma capital additions; it is yet quite another thing to seek to limit the actual evidence the Company can proffer with respect to capital projects, whether limiting them by size or other criteria.

¹⁸⁵ (Exh. No. BTC-1T, p. 8)

¹⁸⁶ (Id.) (Ibid.)

¹⁸⁷ (Id.) (Ibid.)

projects. Moreover, the Company in 2015 only recently introduced service quality measures, after consultation with Staff. The Company believes that Mr. Cebulko's ambitious undertaking should not detract from making optimal use of considerable information already available.

124 Finally, Mr. Cebulko acknowledged, on cross examination the following:

Q: [CHAIRMAN DANNER] So the only question I have is, Mr. Cebulko, is there currently a high level of concern about reliability with this utility?

A: I just – I don't know. I – I don't know their level of reliability. . . . (TR 547:10-14)

XI. THE COMMISSION SHOULD ADOPT THE COMPANY'S LOW INCOME RATE ASSISTANCE PROGRAM FUNDING PLAN

125 There appears to be no disagreement over whether additional funding should be provided under the Company's Low Income Rate Assistance Program ("LIRAP"). The recommendations of the parties, however, vary somewhat. Staff has proposed a five-year LIRAP funding plan that would increase LIRAP funding by \$475,000 per year, with a provision that if Avista files a general rate case within the five-year period, the LIRAP funding would increase by twice the percentage of the final residential revenue requirement increase, or \$475,000, whichever is greater.¹⁸⁸

126 Public Counsel and The Energy Project propose an alternative funding plan that is also a five-year plan, but would provide for annual increases in funding over the prior year's budget by an amount equal to twice the percentage increase of the final residential bill impact to customers resulting from a general rate case, or 10%, whichever is greater.^{189/190}

¹⁸⁸ See Exh. No. JMW-1T)

¹⁸⁹ (Exh. No. SMC-1T)

¹⁹⁰ Avista's present level of LIRAP funding, including the \$350,000 increase that occurred on October 1, 2015, is \$7,048,065. Of that amount, \$4,572,134 is collected from electric customers and \$2,475,931 is collected from natural gas customers. (Exh. No. PDE-8T, p. 7:17-19)

The Company recommends that the Commission approve a five-year LIRAP plan that increases Schedule 92 electric LIRAP funding each year by two times the final approved base rate increase for Schedule 1 customers, or 7.0%, whichever is greater. For natural gas, the Company recommends the LIRAP funding for Schedule 192 increase each year by two times the final approved base rate increase for Schedule 101 customers, or 7.0%, whichever is greater.^{191/192} For electric service under the Company's proposal, the overall increase in LIRAP funding would be 7%, or \$320,049. For natural gas service, the increase in natural gas funding would be \$311,400, also effective January 1st.¹⁹³ (As compared to Staff's proposed increase of \$475,000, the Company's proposal is similar to Staff in terms of funding levels: the Company compared Staff's proposed increase of \$475,000 to the total level of present funding of \$7,048,065. That ratio is approximately 6.7%. The Company simply rounded that to the nearest whole increment – i.e., 7.0%.¹⁹⁴) As testified to by Mr. Ehrbar:

The Company believes that its proposed funding plan balances both the need to provide LIRAP grants to greater number of customers while at the same time keeping the overall increase at a reasonable level of 7.0% annually, similar to Staff's proposal. The Company's proposal also specifies how the proposed increases in LIRAP funding would be recovered for each service, rather than at the total program level.¹⁹⁵

¹⁹¹ (Exh. No. PDE-8T, p. 8:1-13)

¹⁹² For 2016, the LIRAP increases would become effective at the time the rates for this general rate case become effective; proposed to be January 1, 2016. The Company proposes that the next four subsequent increases would be filed by August 15th to become effective October 1st, beginning October 1, 2016, in order to match up the increased level of funding with the LIRAP program year. Any additional LIRAP funding increases necessary to achieve two-times the base rate increase would become effective with the corresponding base rate increase. (Exh. No. PDE-8T, p. 8:7-13)

¹⁹³ (*Id.* at 8:17 – p. 9:2)

¹⁹⁴ (*Id.* at 9:17-19)

¹⁹⁵ (Exh. No. PDE-8T, p. 9:22 – 10:3)

(Cross Exhibit No. PDE-12 illustrates how the funding would be implemented each year of the program.)¹⁹⁶

XII. CONCLUSION

129

This case is, first and foremost, an opportunity for the Commission to set, “fair, just, reasonable and sufficient” rates that will provide the Company with a reasonable opportunity to earn its allowed rate of return. Under the circumstances of this case, given the demonstrated trend of capital and expense that far outstrip the growth in revenues, a modified historical test period with limited pro forma adjustments will not suffice. Staff recognizes this fact. The Company respectfully urges the Commission to employ the attrition adjustment proposed by the Company in setting a revenue requirement.

RESPECTFULLY SUBMITTED this 4th day of November 2015.

AVISTA CORPORATION

By: 

David J. Meyer
VP, Chief Counsel for Regulatory and
Governmental Affairs

¹⁹⁶ ICNU offered Cross Exh. PDE-11CCX through Company Witness Ehrbar, which provides information on Schedule 91 Demand Side Management (DSM) funding from Schedule 25 customers, as well as benefits received by Schedule 25 customers, as well as benefits received by Schedule 25 customers. The issue of whether Schedule 25 customers are paying too much under Schedule 91, or should otherwise be exempt, is not before the Commission in this general rate case. It was not made an issue in the testimony of ICNU or any other party. Moreover, recently in Docket UE-151148, ALJ Friedlander, at the prehearing conference held in September of 2015, determined that this issue was more appropriately to be addressed in the Technical Advisory Group meetings where all interested parties would be present.

ATTACHMENT A
(Table Excerpted from Exh. No. KON-1T, p. 34)

Table No. 5 – Electric and Natural Gas Revenue Requirement Reconciliation

<u>Line</u>		<u>\$Millions</u>	
		<u>Electric</u>	<u>Natural Gas</u>
1	Original Requests	\$33.2	\$12.0
2	Multi-Party Partial Settlement		
3	Cost of Capital	(\$3.8)	(\$0.7)
4	Power Supply Adjustments	(\$12.6)	
5	Subtotal May 1, 2015	\$16.8	\$11.3
6	Additional Updates/Revisions ¹	(\$6.8)	(\$1.6)
7	Revised Revenue Requirement -- July 2015	\$10.0	\$9.7
8	Avista Proposal on Rebuttal		
9	Delay Amortization of Existing Meters (AMI)	(\$4.1)	
10	Normalize “Hours-Based” Thermal Maintenance ²	(\$3.0)	
11	Other ³	\$0.7	\$0.3
12	Subtotal -- Avista Proposal on Rebuttal	\$3.6	\$10.0
13	Proposed Additional LIRAP Funding	\$0.3	\$0.3
14	Avista Proposal on Rebuttal	\$3.9	\$10.3
15	Estimated Power Supply Update – Nov 2015	(\$10.0) [\$12.3]*	
16	Expiration of ERM Rebate 12/31/15	\$8.3	
17	Estimated Rate Adjustment	\$2.2 [(\$0.0)]*	\$10.3

¹ Tax adjustments, state allocations, and changes to net plant investment, as explained by Ms. Andrews. (Exh. No. EMA-5T, p. 8)

² If Avista’s proposal on rebuttal to defer and amortize (normalize) the “hours-based” thermal maintenance is rejected by the Commission, then Avista’s electric revenue requirement on rebuttal would increase from \$3.6 million to \$6.6 million in order to provide cost recovery for these increased costs in 2016.

³ Ms. Andrews explains the adjustments in her rebuttal testimony that add up to \$0.7 million. (Exh. No. EMA-ST, p. 6)

* [Note: On October 29, 2015, the Company filed an updated power supply adjustment pursuant to the Partial Settlement Stipulation that further reduced the level of power supply expense by \$12.3 million. The overall net impact on billed electric rates proposed by the Company in this case is \$0.0.]