BEFORE THE WASHINGTON

UTILITIES & TRANSPORTATION COMMISSION

WASHINGTON UTILIITES AND TRANSPORTATION COMMISSION,

Complainant,

v.

AVISTA CORPORATION d/b/a AVISTA UTILITIES,

Respondent.

DOCKET NOS. UE-200900 and UG-200901

RESPONSE TESTIMONY OF ANDREA C. CRANE
ON BEHALF OF THE
WASHINGTON STATE OFFICE OF THE ATTORNEY GENERAL
PUBLIC COUNSEL UNIT

EXHIBIT ACC-1T

April 21, 2021

RESPONSE TESTIMONY OF ANDREA C. CRANE

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RESPONSE TESTIMONY OF ANDREA C. CRANE

DOCKET NOS. UE-200900 and UG-200901

EXHIBIT ACC-1T

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I. STATEMENT OF QUALIFICATIONS

Q. Please state your name and business address.

A. My name is Andrea C. Crane and my business address is 2805 East Oakland Park Boulevard, #401, Ft. Lauderdale, Florida 33306.

Q. By whom are you employed and in what capacity?

A. I am President of The Columbia Group, Inc., a financial consulting firm that specializes in utility regulation. In this capacity, I analyze rate filings, prepare expert testimony, and undertake various studies relating to utility rates and regulatory policy. I have held several positions of increasing responsibility since I joined The Columbia Group, Inc. in January 1989. I became President of the firm in March 2008.

Q. Please summarize your professional experience in the utility industry.

A. Prior to my association with The Columbia Group, Inc., I held the position of Economic Policy and Analysis Staff Manager for GTE Service Corporation, from December 1987 to January 1989. From June 1982 to September 1987, I was employed by various Bell Atlantic (now Verizon) subsidiaries. While at Bell Atlantic, I held assignments in the Product Management, Treasury, and Regulatory Departments.

Q. Have you previously testified in regulatory proceedings?

A. Yes, since joining The Columbia Group, Inc., I have testified in over 400 regulatory proceedings in the states of Arizona, Arkansas, Connecticut, Delaware, Florida, Hawaii, Kansas, Kentucky, Maryland, New Jersey, New Mexico, New York, Oklahoma, Pennsylvania, Rhode Island, South Carolina, Vermont, Washington, West Virginia and the District of Columbia. These proceedings involved electric, gas, water, wastewater, telephone, solid waste, cable television, and navigation utilities. A list of dockets in which I have filed testimony over the past five years is included in Exhibit ACC-2.

Q. What is your educational background?

A. I received a Master of Business Administration degree, with a concentration in Finance, from Temple University in Philadelphia, Pennsylvania. My undergraduate degree is a B.A. in Chemistry from Temple University.

II. PURPOSE OF TESTIMONY

Q. What is the purpose of your testimony?

A. On October 30, 2020, Avista Utilities ("Avista" or "Company") filed a Petition with the Washington Utilities & Transportation Commission ("Commission") requesting increases in its base rates for electric and natural gas utility services of $44.183 million and $12.270 million respectively. The Company concurrently filed two additional petitions with the Commission. First, it filed a Wildfire Deferral Petition seeking authorization to defer certain costs associated with Avista's Wildfire Resiliency Plan beginning on January 1, 2021, and to seek recovery of those costs in a future rate proceeding.[1] That petition was subsequently consolidated with this rate filing. Second, Avista filed a Tax Accounting Petition seeking authorization to flow-through certain tax benefits to Washington customers through a tariff rider. The Tax Accounting Petition was approved

[1] Docket No. UE-200984.

by the Commission on March 11, 2021 in Docket Nos. UE-200895 and UG-200896.

The Columbia Group, Inc. was engaged by the Washington State Office of the Attorney General, Public Counsel Unit ("Public Counsel") to review the Company's rate case petition and to provide recommendations to the Commission regarding the Company's revenue requirement claims. In addition, we were engaged to offer a recommendation regarding the Tax Accounting Petition and the appropriate period over which the associated deferred income taxes should be flowed-through to customers.

In developing my recommendations, I relied upon, and incorporated, the conclusions and recommendations of various other Public Counsel witnesses. Dr. J. Randall Woolridge is filing testimony on cost of capital and capital structure issues. Mr. Paul Alvarez is filing testimony on several issues including the Company's proposed Wildfire Resiliency Plan, and certain capital expenditures related to substation rebuilds and grid modernization. Ms. Rachel Wilson is filing testimony on Gas Supply issues and Ms. Shay Bauman is filing testimony on Advanced Metering Infrastructure (AMI) recovery and policy issues. Finally, Mr. Glenn Watkins is filing testimony on class cost of service and rate design issues.

Q. Please provide a brief summary of the Company's filing.

A. Avista is seeking an electric base revenue increase of $44.183 million and an increase in its base revenues for gas service of $12.790 million. The Company's filing would result in an electric base revenue increase of approximately 8.13 percent, and in a gas base revenue increase of approximately 12.16 percent. These rate increases would constitute the tenth electric and gas base rate increases for Avista's Washington's ratepayers since 2009. Avista's filing is based on a test period ending December 31, 2019.

In this filing, Avista is seeking authorization to begin to earn a return on, and a return of, its investment in AMI. The Company is also seeking to begin recovery of deferred costs related to AMI deployment. In addition, Avista is seeking to include extensive post-test-period 2020 plant additions, as well as certain plant additions projected for 2021 related specifically to AMI, membership in the Western Energy Imbalance Market ("EIM"), the Wildfire Resiliency Plan and Colstrip Units 3 and 4. Avista is also proposing to include 2022 plant additions associated with the EIM and Colstrip in its pro forma rate base. The Company is planning to join the EIM in March of 2022.

Avista is proposing a ten-year Wildfire Resiliency Plan and is seeking to defer certain costs associated with the Wildfire Plan for recovery in a future base rate case. Specifically, the Company is proposing to defer Wildfire operating expenses from January 1, 2021 through September 30, 2021. Avista is also seeking authorization to establish a two-way "balancing account" to track and defer the difference between actual annual Wildfire Resiliency Plan operating expenses and those reflected in base rates.

Finally, Avista is seeking to implement a Tax Credit rider to return to ratepayers certain non-protected deferred taxes associated with meters and Industry Director Directive No. 5 ("IDD No. 5"), which are mixed services costs primarily relating to inventory allocation and engineering. The Company is proposing to flow-through the balance of these deferred taxes through a Tax Credit that would completely offset its requested base revenue increases in this case. In addition, the Company is proposing that future additional deferred tax balances related to meters and IDD No. 5 be amortized to ratepayers over a period of ten years.

Q. What are the most significant issues in this rate proceeding?

A. The most significant revenue requirement issues in this case are (1) the Company's claim for a return on equity of 9.90 percent and a capital structure reflecting 50 percent common equity, (2) Avista's request to include AMI investment in rate base and to begin amortizing deferred AMI costs, (3) the Company's claim for inclusion of significant post-test period plant in rate base, (4) Avista's proposals to include speculative post-test period operating expenses in utility rates, including 2022 costs in some cases, (5) inclusion of significant incentive compensation costs in rates, and (6) the Company's proposal to implement a Tax Credit rider.

III. SUMMARY OF CONCLUSIONS

Q. What are your conclusions concerning the Company's revenue requirement and its need for rate relief?

A. Based on my analysis of the Company's filing and data request responses, on the testimony submitted by other Public Counsel witnesses, and on other relevant documentation in this case, my conclusions are as follows:

1. The 12-month period ending December 31, 2019, is a reasonable test period to

use in this case to evaluate the reasonableness of the Company's claims.

2. Based on the testimony of Dr. Woolridge, the Company has a cost of equity of 9.0 percent, a capital structure consisting of 48.5 percent common equity, and an overall cost of capital of 6.92 percent.[2]

3. Avista has pro forma electric distribution rate base of $1.742 billion[3] and a pro forma gas distribution rate base of $416.198 million.[4]

4. The Company has pro forma electric distribution operating income at present rates of $115.110 million[5] and pro forma gas distribution operating income at present rates of $25.782 million.[6]

5. As discussed by Ms. Bauman, the Commission should exclude a return on the new AMI meters at this time.

6. As discussed by Mr. Alvarez, the Commission should exclude many of the capital projects proposed in the Company's Wildfire Resiliency Plan. In addition, the Commission should approve the Company's request to defer expenses from January 1, 2021 through September 30, 2021 for possible recovery in the future, and the Commission should adopt the tracking mechanism recommended by Mr. Alvarez.

7. As discussed by Ms. Wilson, the Commission should exclude EIM costs from the

[2] Andrea C. Crane, Exh. ACC-3, at 2; Exh. ACC-6, at 2.
[3] Crane, Exh. ACC-3, at 1.
[4] Crane, Exh. ACC-6, at 1.
[5] Crane, Exh. ACC-3, at 1.
[6] Crane, Exh. ACC-6, at 1.

Company's base rates at this time.

8. Avista has a pro forma, electric base distribution revenue deficiency of $7.225 million and a pro forma, gas base distribution revenue deficiency of $4.007 million.[7]

9. The electric and gas base revenue increases authorized by the Commission should be offset with a Tax Credit rider adjustment.

10. The Commission should revisit the appropriate amortization period over which to return accumulated deferred federal income taxes ("ADFIT") associated with meters and IDD No. 5 in the Company's next base rate case. In addition, in future cases, the Commission should also consider extending flow-through treatment to other categories of ADFIT.

Q. Please explain how your schedules are structured.

A. I have attempted to mirror the adjustment schedules presented by Ms. Andrews in Exhibit EMA-2 and EMA-3 for electric and gas respectively. Ms. Andrews began with the actual test period Results of Operation (1.00). She then made a series of adjustments to include individual normalizing and restating adjustments that are standard components of the Company's annual reporting to the Commission. These adjustments are shown in the 1.XX and 2.XX series of adjustments on Exhibits EMA-2 and EMA-3 of her testimony.

[7] Crane, Exh. ACC-3, at 1; Exh. ACC-6, at 1.

Finally, Ms. Andrews reflected a series of post-test period, pro forma adjustments, which are shown in the 3.XX series of adjustments in her exhibits.

My schedules provide similar information. Exhibit ACC-3 (for electric) and Exhibit ACC-6 (for gas) summarize Public Counsel's recommended Revenue Requirement. Exhibit ACC-4 (for electric) and Exhibit ACC-7 (for gas) show the details of the accounting adjustments proposed by Avista. I highlighted those individual normalizing, restating, and pro forma adjustments with which I disagree by identifying each of Ms. Andrews' adjustments that I propose to modify at the top of each relevant column. My adjustments are identified as either "ROR", "Correction", or "Adjustment" as discussed in more detail below. Exhibits ACC-3, ACC-4, ACC-6, and ACC-7 are all based on Avista's excel models, adjusted for Public Counsel's recommendations. In Exhibit ACC-5 (for electric) and Exhibit ACC-8 (for gas), I have summarized each of my proposed adjustments, and I have provided the revenue requirement difference between each of my recommendations and those of Ms. Andrews. I have also prepared workpapers for my adjustments that are provided to the Parties in this case. For the most part, these workpapers were also based on the underlying Excel models provided by Ms. Andrews. Following is a discussion of Public Counsel's revenue requirement recommendations.

IV. REVENUE REQUIREMENT ISSUES

A. Capital Structure and Cost of Capital

Q. What is the cost of capital and capital structure that Avista is requesting in this case?

A. The Company utilized the following capital structure and cost of capital in its filing:

Table 1: Company Cost of Capital / Capital Structure

	Percent of Total	Cost Rate	Weighted Cost
Long Term Debt	50.00%	4.97%	2.48%
Common Equity	50.00%	9.90%	4.95%
Total	100.00%		7.43%

Q. What is the capital structure and overall cost of capital that Public Counsel is recommending for Avista?

A. As shown on Exhibit JRW-1 of Dr. Woolridge's testimony, Public Counsel is recommending an overall cost of capital for Avista of 6.92 percent, based on the following capital structure and cost rates:

Table 2: Public Counsel Cost of Capital / Capital Structure

	Percent of Total	Cost Rate	Weighted Cost
Long Term Debt	51.5%	4.97%	2.56%
Common Equity	48.5%	9.00%	4.37%
Total	100.00%		6.92%[8]

[8] Does not add due to rounding.

Dr. Woolridge recommends that the Commission adopt a common equity ratio of 48.50 percent, which is the equity ratio adopted in the Company's last rate case and is consistent with Avista's actual capitalization in recent years. In addition, he is recommending that the Commission authorize a cost of equity of 9.0 percent. Dr. Woolridge's adjustments result in a pro forma overall cost of capital of 6.92 percent.[9] I have used Dr. Woolridge's recommended cost of capital of 6.92 percent to determine the Company's pro forma required income.[10]

Q. What is the revenue requirement impact of the cost of capital adjustment?

A. The Company's actual Results of Operation demonstrate an overall rate of return for the electric utility of 6.73 percent, resulting in a revenue shortfall of $4.438 million.[11] Avista is claiming that the Results of Operation indicated an electric revenue shortfall of $15.941 million. Therefore, cost of capital and capital structure issues will reduce the Company's electric revenue claim by a total of $11.503 million.[12] In addition, there will be impacts to certain other components of the revenue requirement as discussed below.

With regard to the gas utility, Avista's Results of Operations indicate an earned return of 6.03 percent, resulting in a revenue shortfall of $4.798 million, while the Company is claiming a revenue shortfall of $7.528 million. Therefore, the difference between Public Counsel's overall cost of capital and Avista's recommended cost of

[9] Crane, Exh. ACC-3, at 2; Exh. ACC-6, at 2.
[10] Crane, Exh. ACC-3, at 1 (electric); Exh. ACC-6, at 1 (gas).
[11] Crane, Exh. ACC-4, at 1.
[12] Crane, Exh. ACC-5.

capital results in a revenue difference of $2.730 million for the gas utility, based on the Actual Results of Operation, in addition to the impact on other post-test period adjustments.

Table 3: Adjustment to Results of Operations to Earn Recommended ROR ($000)

	Public Counsel (6.92%)	Avista (7.43%)	Difference
Electric	$4.438	$15.941	($11.503)
Gas	$4.798	$7.528	($2.730)

Q. What other adjustments are impacted by the modifications that Public Counsel is recommending in this case for capital structure and cost of capital?

A. There are several rate base adjustments that I have accepted, but where the revenue requirement impact of the adjustment differs between Avista and Public Counsel due to the different recommended capital structures and costs of capital. Since the revenue requirement impact of rate base adjustments depends on the overall cost of capital and capital structure, the revenue requirement impact of these adjustments will differ even though we have accepted the underlying rate base adjustment. For the electric utility, these include Working Capital (1.03), the Removal of AMI from Rate Base (1.04), the Restatement of Interest Expense (2.14), Deferred Debits, Credits, and Regulatory Amortizations (3.02), and the Restatement of 2019 ADIT (3.21). For the gas utility, these include Deferred FIT Rate Base (1.01), Working Capital (1.03), Removal of AMI from Rate Base (1.04), the Restatement of Interest Expense (2.14), the Restatement of 2019 AMA Rate Base to End of Period (“EOP”) (2.15), LEAP Deferral Amortization (3.17) and Restatement of 2019 ADIT (3.21). Following is a comparison of these revenue requirement adjustments as quantified by Public Counsel and Avista:

Table 4: Electric Revenue Requirement Impact ($000)

	Public Counsel	Avista	Difference
Working Capital (1.03)	(317)	(343)	26
Remove AMI Rate Base	(4,082)	(4,417)	335
Restate Interest Expense	870	1,237	(367)
Deferred Debits, Credits, and Reg. Assets	(2,593)	(2,598)	5
Restate 2019 ADIT	(2,582)	(2,794)	212

Table 5: Gas Revenue Requirement Impact ($000)

	Public Counsel	Avista	Difference
Deferred FIT Rate Base (1.01)	(84)	(91)	7
Working Capital (1.03)	(97)	(105)	8
Remove AMI Rate Base (1.04)	(1,555)	(1,683)	128
Restate Debt Interest (2.14)	206	294	(88)
Restate 2019 AMA Rate Base to EOP (2.15)	802	890	(88)
LEAP Deferral (3.17)	1,286	1,259	27
Restate 2019 ADIT (3.21)	(1,287)	1,393	106

For these items, our disagreement with Avista is limited to the use of a different capital structure and cost of capital. These adjustments are labeled “ROR” in Exhibit ACC-4 (electric) and Exhibit ACC-7 (gas).

B. Corrections Made by Avista

Q. Did you include any additional adjustments based on corrections made by Avista in discovery?

A. Yes, I included two such adjustments in my revenue requirement. These adjustments are labeled "Correction" in Exhibit ACC-4 (electric) and Exhibit ACC-7 (gas). First, in a footnote on page 50 of Ms. Andrews' testimony, she noted that after the Company had completed the calculation of its revenue requirement, it had discovered an error in Adjustment No. 2.19 (Electric), Restating AMA Rate Base to EOP, which restates the Company's rate base from an average monthly rate base to an end-of-period Rate Base. Specifically, certain costs associated with the Cabinet Gorge Gantry Crane Replacement Project completed in 2019 had been overstated, and certain costs that should have been booked to expense were capitalized. This error was corrected in 2020 but the correction was not reflected in Ms. Andrews' rate case schedules. In response to Staff-39, Avista quantified the impact of this adjustment, which affects only the electric utility. I have reflected this correction in my revenue requirement calculation, based on the cost of capital and capital structure recommended by Dr. Woolridge. While the Company stated in response to Commission Staff Data Request No. 39 that this correction would increase its revenue requirement by $862,425,[13] I have included an increase of only $722,000 due to the lower capital costs being recommended by Public Counsel.[14]

Q. What is the second correction that you included in your revenue requirement?

A. In a footnote on page 54 of her testimony, Ms. Andrews indicated that a small adjustment would need to be made to Adjustment 3.03 (Pro Forma ARAM Adjustment) if the Commission approved the Company's Tax Accounting Petition. In response to

[13] Crane, Exh. ACC-9, Avista Response to Commission Staff Data Request No. 39.
[14] Crane, Exh. ACC-4, at 3.

Commission Staff Data Request No. 38 Supplemental, Avista quantified the impact of this correction, stating that the impact was an increase of $20,000 to the electric revenue requirement and a reduction of $61,000 to the gas revenue requirement.[15] I have included both of these adjustments in my revenue requirement calculations.[16]

C. Injuries and Damages Expense (2.05)

Q. How did the Company determine its claim for injuries and damages expense?

A. Avista calculated its claim based on a six-year rolling average of injuries and damages expenses not covered by insurance.

Q. What is the rationale for normalizing injuries and damages expense based on a six-year average?

A. Injuries and damages expense can vary significantly from year-to-year. The purpose of a normalization adjustment is to smooth out fluctuations that occur from year-to-year so that a "normal" level of injuries and damages expense can be reflected in prospective rates. In normalizing these costs, it is not unusual for a multi-year average to be utilized in order to mitigate the impact of normal fluctuations that occur from year-to-year.

Q. Do you believe that a six-year average is a reasonable normalization period for these costs?

A. A six-year average may be reasonable if the data utilized did in fact represent normal year-to-year fluctuations in injuries and damages expenses. However, in this case, I do

[15] Crane, Exh. ACC-10, Avista Supplemental Response to Commission Staff Data Request No. 38.
[16] Crane, Exh. ACC-4, at 4 (electric adjustment); Crane, Exh. ACC-7, at 3 (gas adjustment).

not believe that the use of a six-year average is reasonable. A review of the data suggests that the 2014 electric expense does not represent normal annual fluctuations — rather it appears to represent an abnormal or extraordinary year. The 2014 electric expense is almost double the six-year average, and is 46 percent higher than the second highest year out of the past six years. Abnormal or extraordinary costs should be excluded from the normalization mechanism. Therefore, in this case, I recommend that the five-year average be utilized for both electric and gas injuries and damages expense. My adjustment will result in a decrease to electric expense but virtually no change to the Company's claimed gas expense, as shown below:

Table 6: Injuries and Damages Expense

	Electric	Gas
2014	$295,491	$23,907
2015	$82,249	$29,008
2016	$143,873	$5,992
2017	$202,277	$21,509
2018	$129,573	$9,318
2019	$97,945	$41,667
6 Year Average	$158,568	$21,900
5 Year Average	$131,184	$21,499

This adjustment is shown in Exhibit ACC-4, page 2 (electric). No corresponding gas adjustment is shown in my Exhibit ACC-7 because the difference between my recommendation and the Company's claim is immaterial.

Q. Did you make a similar recommendation in the Company's last base rate case?

A. Yes, I did. In that case, the Company's claim, which was based on a six-year average, was $164,796 for the electric utility and $69,101 for the gas utility. I recommended that a five-year average be used, resulting in a cost of $170,693 for electric and of $17,947 for gas. That case was settled without an explicit ruling on this issue. Nevertheless, while total electric and gas costs in 2019 were well below both the five-year and six-year averages as determined in the last case, the total 2019 cost was much closer to the five-year average than the six-year average, lending further support to my adjustment.

D. Incentive Compensation Expense (2.13)

Q. Please explain the Company's adjustment relating to incentive compensation.

A. The Company's adjustment restates incentive compensation to reflect a six-year average of actual incentive compensation payments. The Company claims that this treatment is consistent with Staff's methodology approved by the Commission in Order No. 07 in Dockets UE-170485 and UG-170486.[17] In addition, the Company stated that incentive compensation awards that are dependent on financial benchmarks have been excluded from its revenue requirement claim. We are recommending that 100 percent of executive officer incentive compensation expense and 50 percent of non-executive incentive compensation expense be excluded from the revenue requirement and borne by shareholders.

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[17] *Wash. Utils. and Transp. Comm'n v. Avista Corp. d/b/a Avista Utils.*, Dockets UE-170485 and UG-170486 (*Consolidated*), Order 07, Final Order (Apr. 26, 2018).

Q. Please describe the Company's incentive compensation programs.

A. The Company's executive incentive compensation plan includes two incentive compensation programs—a Short-term Incentive Compensation Plan ("STIP") and a Long-term Incentive Compensation Plan ("LTIP"). The LTIP has two components. First, performance shares, which account for 75 percent of the LTIP, are based on financial metrics related to cumulative earnings per share and total shareholder return. Second, restricted stock units, which are based on continued service at Avista, account for the remaining 25 percent of the LTIP award. Costs for the LTIP are not included in the Company's claim in this case, since these awards are based on financial parameters or metrics that otherwise do not necessarily benefit ratepayers.

With regard to the STIP for officers, these awards are limited to approximately 13 individuals, as shown in the Company's workpapers. Annual salaries in 2020 for these individuals ranged from $200,000 to $750,000 according to the Company's workpapers, and we are not recommending any adjustment to these underlying base salary levels for officers.[18]

In addition to these base salaries and the LTIP, this small group of executives is eligible for STIP awards. 60 percent of the STIP awards for officers is based on an earnings-per-share criteria. This portion of the incentive award costs has not been included in the Company's claim. The remaining 40 percent is based on O&M

[18] Ms. Andrews' Workpaper to Adjustment 3.05 (FLB Forecast Labor Executive).

(20 percent), Customer Satisfaction (eight percent), Reliability (eight percent), and Response Time (four percent). With regard to non-executive STIP awards, 50 percent of these awards are based on O&M costs per customer, 20 percent on customer satisfaction, 20 percent on a reliability index, and 10 percent on response time.

Q. Do you believe that the incentive compensation program costs are appropriate costs to pass through to ratepayers?

A. No, I do not. I have several concerns about including costs for these types of programs in regulated utility rates. First, with regard to Avista executives, these individuals are well compensated, even without consideration of incentive compensation awards. Moreover, incentive compensation programs proliferated as the result of tax changes that imposed limitations on the amount of compensation that was tax deductible unless such compensation was performance-based. Thus, to some extent, it appears that the growth in performance-based compensation was an attempt by companies to circumvent limitations on the tax deductibility of executive compensation. The more generous tax treatment afforded performance-based compensation was eliminated by the Tax Cuts and Jobs Act of 2017, and it will be interesting to see if the popularity of performance-based programs erodes over time with the new tax law. Third, performance-based compensation is clearly less transparent than base salary programs. Therefore, it is more difficult for ratepayers to evaluate a utility's compensation programs if incentive compensation awards comprise a significant component of total compensation.

Q. Doesn't the Company use a compensation consulting firm to benchmark its compensation programs?

A. Yes, it does. Avista utilizes a compensation consulting firm to benchmark its compensation relative to other companies with similar business profiles, similar revenue size and market capitalization. However, in my view, the use of such benchmarks has a detrimental effect on ratepayers as compensation costs spiral, especially at the executive level.

Q. Why do you believe that the use of benchmarking results in spiraling executive compensation costs?

A. Companies state that they must benchmark their compensation in order to be competitive. However, such benchmarking actually results in ever-increasing executive compensation levels. This is because companies generally target their compensation to the 50th percentile of companies in the proxy group selected for benchmarking. Such practices tend to escalate increases in compensation, especially for highly-paid officers. These studies compare the subject company's compensation to compensation in a broad range of other firms. Since most companies do not want to find themselves in the lower half of the benchmark group, companies that typically fall below the average raise their compensation—and hence the average of the benchmark companies continually increases. This sets off a chain of events that results in ever-increasing compensation levels as additional companies must increase their compensation to avoid falling below the 50th percentile. The Commission should be particularly wary of any compensation plans that utilities attempt to justify by means of comparison to benchmark studies. It is not surprising that concurrent with the practice of benchmarking, executive compensation levels have risen dramatically over the past several years.

Q. Do you have similar concerns about incentive compensation awards for non-executive employees?

A. Yes, I do. Although the issues are a bit different, the use of benchmarking studies also means that non-executive employee salaries tend to suffer from the same upward spiral as compensation programs for executives. There is no indication that the employees of Avista are underpaid or that the Company would have difficulty attracting qualified employees in the absence of these programs. In addition, at least 50 percent of the STIP award criteria for non-executives relates to financial criteria (O&M per customer) that directly benefits shareholders between base rate case filings.

Q. What do you recommend?

A. The Company's employees are already well compensated and the level of service being received by Washington ratepayers does not justify the payment of additional incentive awards. Nevertheless, I have not disallowed 100 percent of incentive compensation award costs for non-executive personnel because the Company does consider non-financial factors in the incentive compensation awards made to many of its non-executive employees. Therefore, I recommend that the Commission disallow 50 percent of incentive compensation award costs for non-executive employees, reflecting the O&M component of the STIP. Although the O&M per customer criteria can provide a benefit to both shareholders and ratepayers, since shareholders benefit between base rate case filings but ratepayers benefit when operating costs are reset in a base rate case, the fact is that control of O&M costs has not reduced the frequency of base rate case filings, as evidenced by the numerous rate increases that have been borne by these customers over the past decade. My adjustment to disallow 50 percent of the non-officer incentive compensation costs is shown in Exhibit ACC-4 (electric) and Exhibit ACC-7 (gas), Adjustment 2.13.

In addition, I recommend that 100 percent of the Company's claim for officer incentive compensation awards be denied. My adjustment to eliminate officer incentive compensation costs is also shown in Exhibit ACC-4, page 3 and Exhibit ACC-7, page 2, Adjustment 2.13. These officers are already very well compensated in their base salaries. Therefore, I believe it is appropriate to eliminate 100 percent of the officer incentive compensation awards reflected in the Company's filing. My recommendation will also increase the transparency of the compensation paid to Avista's officers for Washington ratepayers, particularly compensation that is recovered though regulated rates.

E. Non-Executive Salary and Wage Expense (3.04)

Q. How did the Company determine its salary and wage claim in this case?

A. The Company's methodology is described beginning on page 48 of Ms. Andrews' testimony. To develop its salary and wage claim for non-executive, non-union employees, Avista first annualized the impact of a March 2019 non-union increase of three percent and included a further three percent increase that was effective in March 2020. In addition, the Company included an estimated increase of three percent for 2021.

For union employees, the Company annualized the impact of a three percent increase in 2019 and 2020, as well as an estimated three percent increase when the current contract with the International Brotherhood of Electrical Workers Union 77 expires in 2021. The Company's adjustments reflected increases of $3,267,390 for the electric utility and of $977,889 for the gas utility.

Q. Are you recommending any adjustment to the Company's claim for non-executive labor costs?

A. Yes, I am recommending that the Company's 2021 payroll increase be eliminated from rates resulting from this case. The test period in this case ended on December 31 2019. In my view, reaching out to 2021, more than a year past the end of the test period, violates the test year matching principle. While I have included salary and wage adjustments for 2020 in my revenue requirement recommendation, reflecting labor adjustments that will occur in 2021 reaches too far beyond the end of the test period and these 2021 labor increases should be excluded.[19]

Q. Did the Company reach well beyond the end of the test year with regard to many of its pro forma adjustments?

A. Yes, it did. Many of Avista's expense adjustments are based on projected costs in 2021

[19] My adjustments are shown in Crane, Exh. ACC-4, at 4 and Exh. ACC-7, at 3.

and in some cases 2022. I have attempted to consistently eliminate these 2021 and 2022 increases, including the 2021 increase projected for labor costs.

F. Employee Benefits Expense (3.06)

Q. What is included in Employee Benefits Expense?

A. The Company's employee benefits expense adjustment includes health insurance costs, pension costs, other post-employment benefit costs ("OPEBs"), and 401k costs. Avista included 2022 estimated costs in its claim. The Company is proposing benefit increases of $1.120 million for its electric utility and of $342,000 for its gas utility. These increases are being driven primarily by the Company's forecasts for health insurance costs and for OPEBs. Avista's employee benefits claim assumes a reduction in pension costs of $1.317 million. The Company closed its defined benefit pension plan to all non-union employees hired on or after January 1, 2014, and instituted a 401K plan for these new hires. A defined contribution plan (401K plan) replaced the defined benefit plan for employees hired on or after January 1, 2014. In addition to the defined contribution 401K plan, Avista also matches a portion of payroll that is contributed on a discretionary basis by each participant.

Health insurance estimates were provided by Mercer while pension and OPEB estimates were provided by Willis Towers Watson. 401K costs were internally developed by the Company.

Q. What adjustments are you recommending to the Company's claim?

A. I recommend that the Company's 2022 projected benefit costs be rejected by the Commission. These 2022 costs are speculative and reach too far beyond the end of the test period in this case. With regard to health care costs, the Company's plan is self-funded. Therefore, actual costs may vary from year-to-year based on both the level of services utilized by employees as well as the underlying cost structure. With regard to pension and OBEP costs, as discussed on page 60 of Ms. Andrews' testimony, these costs are impacted by both financial market conditions as well as underlying assumptions about inputs such as discount rates.[20] In fact, changes in assumptions can have a significant impact on the annual pension and OPEB costs incurred by a utility.

Instead of the Company's speculative projections, I recommend that the Commission utilize the actual 2020 employee benefit costs to determine the Company's revenue requirement in this case. This recommendation is generally consistent with my recommendation regarding other labor costs. As of the preparation date of this testimony, I do not have the actual 2020 costs by employee benefit category and therefore I have reflected the actual test period costs in Adjustments 3.06 in Exhibit ACC-4, page 4 (electric) and Exhibit ACC-7 (gas), page 3. However, I have no objection to the Commission utilizing the actual 2020 employee benefit costs once the actual costs are provided, unless there are anomalies in the actual costs, such as material non-recurring

[20] Direct Testimony of Elizabeth M. Andrews, Exh. EMA-1T at 60:2–6.

factors that would lead the Commission to conclude that the 2020 costs are not representative of normal operating conditions.[21]

G. Insurance Expense (3.07)

Q. How did the Company develop its claim for pro forma insurance costs?

A. Avista generally reflected the anticipated December 2021 insurance premiums in its claim. With regard to Directors and Officers Insurance, the Company allocated 10 percent of these costs to non-utility operations.

Q. What are you recommending with regard to pro forma insurance expense?

A. I am recommending two adjustments. First, in response to Commission Staff Data Request No. 44, the Company provided actual updated premium costs for its general liability and property insurance.[22] I have reflected these updated, actual premiums in my revenue requirement. An updated premium has not yet been provided for Directors and Officers Insurance. Therefore, my analysis utilizes the most recent actual premium as of December 31, 2020.

In addition, I am recommending that 50 percent, instead of 10 percent, of the Directors and Officers insurance costs be excluded from the Company's revenue requirement. This is consistent with the Company's adjustment to exclude 50 percent of

[21] The 2020 actual cost was provided in the response to Public Counsel Data Request No. 315, which was received on April 15, 2021, after our revenue requirement schedules were completed. *See* Crane, Exh. ACC-17. However, Public Counsel will update its revenue requirement to include the actual 2020 costs per this response in its cross answering testimony on May 28, 2021. The update does not change the nature or underlying rationale of the adjustments described in this testimony and revenue requirement schedules.
[22] Crane, Exh. ACC-11, Avista Response to Commission Staff Data Request No. 44.

Directors fees and other related Directors' costs from utility rates. Directors and Officers insurance provides significant benefit to the Company's shareholders and this benefit should be recognized by a reasonable allocation of these costs to non-utility parties. Therefore, in Adjustment 3.07, I have reflected a 50 percent allocation of Directors and Officers expense to shareholders.[23]

H. Information Systems/Information Technology (IS/IT) Expense (3.08)

Q. How did the Company determine its claim for IS/IT Expenses?

A. According to Ms. Andrews, the Company adjusted its test period IS/IT expenses to reflect the level of costs expected during the rate-effective period beginning October 1, 2021. As shown on her workpapers, the Company's claim is based on projected costs that are approximately 30 percent higher than the actual test period costs.[24] Total test period costs were $12,962,722. Avista projected cost increases of $1,963,005 in 2020 and increases of another $1,912,827 in 2021. This represents total increases of $3,875,832 over the actual test period costs of $12,962,722.

Q. Are you recommending any adjustment to the Company's claim?

A. Yes, I believe that once again Avista has reached too far past the end of the test period with regard to its claim for IS/IT costs. While I have accepted certain post-test period adjustments to IS/IT costs, I recommend that these incremental costs be limited to 2020

[23] My adjustments are shown in Crane, Exh. ACC-4, at 5 (for electric) and Exh. ACC-7, at 4 (for gas).
[24] Ms. Andrews' Workpaper to Adjustment No. 3.08.(PF IS-IT).

cost increases. Therefore, I have made an adjustment to Adjustment 3.08 to exclude 2021 cost increases from my revenue requirement recommendation.[25]

I. Property Tax Expense (3.09)

Q. How did the Company develop its property tax claim?

A. According to Ms. Andrews' testimony at page 66, the Company's claim is based on projected rate year property tax expense. Ms. Andrews goes on to state that the property on which the tax is calculated reflects the property value at December 31, 2020, taxed at existing rates.[26]

Q. What pro forma property tax level have you included in your revenue requirement recommendation?

A. In response to Commission Staff Data Request No. 49, the Company updated its property tax expense claim based on property tax assessments received in December 2020.[27] As a result, the Company reduced its electric revenue requirement claim by $746,000 and reduced its gas revenue requirement by $215,000. I have reflected these updates in my revenue requirement.[28]

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[25] Crane, Exh. ACC-4, at 5 for electric and Crane, Exh. ACC-7, at 4 for gas.
[26] Andrews, Exh. EMA-1T at 66:15–20.
[27] Crane, Exh. ACC-12, Avista Response to Commission Staff Data Request No. 49.
[28] My adjustments are shown in Crane, Exh. ACC-4, at 5 (electric) and Exh. ACC-7, at 4 (gas).

J. Capital Additions (3.11-3.15)

Q. Please describe the post-test period capital additions that Avista included in its revenue requirement claim in this case.

A. Avista included extensive capital additions that were expected to go into service after December 31, 2019, the end of the test period in this case. First, the Company included five categories of projects that were expected to go into service during 2020. As described by Ms. Andrews on pages 27–28 of her testimony, these included:

- Pro Forma 2020 Customer At Center (3.11) — This adjustment includes the investment in large and distinct projects specific to the Company's focus on its customers at the center of Avista's business and priorities. This includes $9.316 million of electric rate base additions (including plant-in-service, accumulated depreciation, and deferred income taxes) and $2.923 million of gas rate base additions.
- Pro Forma Large and Distinct (3.12) — This adjustment includes large and distinct projects, such as the electric Rattlesnake Flat Wind Farm project; the electric Labor Day 2020 Storm Damage project (replacing Avista's Chelan-Stratford 115kV transmission line), and the natural gas Cheney High-Pressure Reinforcement project. The Company included $23.308 million of electric rate base additions and $7.191 million of gas rate base additions in its claim.
- Pro Forma 2020 Programmatic Projects (3.13) — This adjustment includes projects associated with on-going, reoccurring annual projects, such as Wood Pole

Management, substation rebuilds, and distribution grid modernization. Avista included $51.538 million of electric rate base additions and $7.194 million of gas rate base additions in its revenue requirement claim.

- Pro Forma 2020 Mandatory and Compliance Projects (3.14) — This adjustment includes projects that are mainly associated with on-going, reoccurring annual projects that are required to meet regulatory and other mandatory obligations, such as compliance with mandatory federal standards for transmission planning and operations. Examples of these projects include Isolated Steel Replacement, Aldyl-A Pipe Replacement, and the Spokane River and Clark Fork PM&E implementation agreement projects. The Company's electric rate base claim includes $35.584 million of mandatory and compliance projects and its gas rate base claim includes $13.123 million.
- Pro Forma 2020 Short-Lived Projects (3.15) — This adjustment includes short-lived projects (mainly five-year lives), such as Endpoint Compute and Productivity Systems, Project Atlas, and Enterprise Security System projects. The Company included $10.886 million of electric rate base additions and $3.408 million of gas rate base additions related to short-lived projects in its filing.

Q. Did the Company include any plant additions that were not expected to be completed by December 30, 2020?

A. Yes, in addition to the 2020 pro forma adjustments described above, Avista also included several other pro forma adjustments related to capital projects that were expected to go into service in 2021 or 2022. The Company included 2021 plant additions related to four areas—AMI, EIM, the Wildfire Resiliency Plan, and Colstrip. Moreover, the Company also included 2022 projects related to EIM and Colstrip.

Q. What is the Company's rationale for including this post-test period plant in rate base?

A. As discussed on pages 22–23 of Ms. Andrews' testimony, Avista states that the Company is undertaking substantial capital investments in its electric and gas utilities. Ms. Andrews states that it is important "for this new investment to be reflected in retail rates in a timely manner, or this new investment, causing significant regulatory lag, will have a negative impact on Avista's earnings, particularly because the new plant is typically far more costly to install than the cost of similar plant that was embedded in rates decades earlier."[29]

Q. What concerns do you have regarding the Company's proposal?

A. Ratemaking is based on a regulatory triad that attempts to match revenues, expenses, and rate base investment during a 12-month test period. If any one of these components is substantially modified, then the relationship that existed during the test period is not being properly incorporated into prospective rates. This is especially true in the case of Avista, which has filed rate cases almost annually over the past decade. Regulatory lag, which can be both positive and negative for a utility, is more of an issue when a utility

[29] Andrews, Exh. EMA-1T at 23:6–10.

files less frequent rate cases.

Moreover, in evaluating the Company's request for post-test period plant additions, the Commission should be mindful that utility companies, Avista included, are increasingly focused on increasing capital investment as a means to increase shareholder earnings. Shareholder earnings are ultimately driven by capital investment. In the ratemaking process, a utility's authorized equity earnings are directly tied to two factors—the authorized weighted cost of equity and the amount of rate base authorized by the regulatory commission. Given current historic low interest rates, which prevent utilities from increasing their authorized cost of equity, companies can still seek to increase their authorized returns by increasing investment in the utility.

Q. Doesn't the Commission have the statutory authority to consider pro forma adjustments up to forty-eight months after the rate-effective date?

A. I have been advised by Public Counsel that the Commission does have such authority, but that the Commission is not required to reflect such adjustments in utility rates. Therefore, I have attempted to provide a balance between the Company's stated objective to reduce regulatory lag, the legislative authority granted to the Commission, and the right of ratepayers to have utility rates that are just and reasonable. In this case, the Company is seeking significant electric and gas increases of 8.31 percent and 12.16 percent respectively, while many Avista ratepayers are undoubtedly still being impacted by the COVID-19 pandemic. Moreover, Avista ratepayers have had a decade of significant electric and gas rate increases. Therefore, the Commission should consider all of these factors as it evaluates the Company's request for significant post-test period adjustments.

Regulatory lag is not new. However, the Company is under increased pressure to grow shareholder earnings, a situation that is complicated by the fact that annual energy sales are not increasing as quickly as they did in the past. In addition, the current focus on energy efficiency and demand side management efforts puts further pressure on utility earnings. If revenues are not growing as quickly as they were in the past, utilities must seek alternative ways to grow shareholder earnings. Avista's stock dividend has grown each year over the past five years, and is currently 23.3 percent above 2016 levels.[30] Moreover, Avista indicated that it expects continued growth in earnings and dividends.[31] However, given the very low interest rates we have experienced over the past several years, along with reductions in the return on equity awards made by many state regulatory commissions, utilities are focusing their efforts on increasing rate base as a means to increase shareholder earnings. To put this issue in a broader context, for most of the past century, utilities had traditionally recovered the cost of their investment in infrastructure through base rate cases using a historic test year. Between base rate cases, utilities funded infrastructure investment that was necessary to provide safe and reliable utility service to regulated ratepayers. As plant was completed and placed into utility service, the utility began to record depreciation expense, which reflected recovery of the

[30] Nasdaq, *Avista Corporation Common Stock (AVA)*, available at https://www.nasdaq.com/market-activity/stocks/ava/dividend-history (Last Visited Apr., 16, 2021).
[31] Avista Corp., *Our Customers / Our People Perform / Invent*, SIEBERT WILLIAMS SHANK VIRTUAL WEST COAST UTILITIES CONFERENCE (Mar. 17, 2021), available at https://investor.avistacorp.com/events/event-details/Siebert-Williams-Shank-virtual-west-coast-utilities-conference.

investment over its useful life. When new utility rates were established in a subsequent base rate case, the utility began to recover its annual depreciation expenses from ratepayers. In addition, the new utility rates also reflected a return on the undepreciated investment included in rate base. It was up to the utility to decide when it would file for a base rate increase. Between base rate cases, utility shareholders took the risk of under-earning but shareholders also benefitted from any overearnings during this period.

Contrary to economic theory and good ratemaking practice, allowing utilities to include speculative post-test period adjustments in rate base increases shareholder return while significantly reducing risk. Shareholder return is directly proportional to the amount of investment made by the utility. Since shareholders benefit from every investment dollar that is spent by a utility, the Company's proposal to include post-test period plant in rate base will increase overall return to shareholders and accelerate recovery of that return.

The Commission should not lose sight of the fact that the there are two primary ways that shareholders can increase their returns—by increasing the rate base on which a return is earned or by increasing the rate of return that is applied to that rate base. Given the low interest rate environment, regulatory commissions are unlikely to increase return on equity awards in the near future. In fact, in this case, Public Counsel is recommending that the Commission adopt a return on equity that is lower than the currently authorized return, which was the result of a stipulation among the parties in the Company's last rate case. Given the strong possibility that the return on equity award will not be increased by the Commission, then Avista must increase its earnings by increasing the amount of investment on which it can earn a return. Every dollar of investment made by Avista results in greater potential earnings for shareholders.

Q. What do you recommend?

A. I recommend that the Commission include Avista's actual 2020 plant additions for the five categories outlined above. The Company provided updated actual 2020 results in its Third Supplemental Response to Commission Staff Data Request No. 107.[32] I have reflected these updates in my Adjustments 3.11-3.15.[33] With regard to proposed 2021-2022 plant additions that Avista included in Adjustments 3.16-3.19 (AMI, EMI, Wildfire, Colstrip), I will discuss each of these adjustments individually.

K. Advanced Metering Infrastructure (3.16)

Q. Please describe the Company's revenue requirement claim associated with its AMI project.

A. Avista is nearing the completion of a multi-year project to replace its electric and gas meters with AMI. The Commission previously approved deferred accounting for the undepreciated value of the meters retired from service as well as for the depreciation expense associated with new meters, until the AMI project and its benefits could be evaluated. Therefore, in its last few base rate cases, Avista has excluded the new AMI meters and the related deferral from its revenue requirement.

[32] Crane, Exh. ACC-13, Avista Third Supplemental Response to Commission Staff Data Request No. 107.
[33] Crane, Exh. ACC-4, at 5–6 (electric adjustments) and Exh. ACC-7, at 4 (gas adjustments).

Now that the project is nearing completion, Avista is seeking ratemaking treatment for the new meters. In addition, the Company is seeking authorization to begin amortizing the regulatory asset associated with the deferral of the depreciation expense on the new meters as well as the deferral of the unrecovered net investment related to the retired meters. The Company is proposing to amortize this deferral from October 1, 2021 through August 31, 2033, which is the date when the new meters will be fully depreciated. The Company's revenue requirement claim includes $18.537 million for the electric utility and $6.861 million for the gas utility.

Q. What adjustments are your recommending related to the Company's claim for AMI costs?

A. I have reflected two adjustments. First, in response to Commission Staff Data Request No. 107 (Third Supplemental Response), Avista provided updates for the electric and gas adjustments to reflect actual additions for 2020 and updated projections for 2021. [34] I have incorporated this update in my revenue requirement recommendations.

In addition, Ms. Bauman is testifying on behalf of Public Counsel regarding the evaluation of the AMI program and related benefits. Ms. Bauman recommends that the Commission exclude a return on the new AMI meters at this time. Therefore, in Adjustment 3.16, I have eliminated a return on the net book value of the new AMI meters.

[34] Crane, Exh. ACC-13, Avista Third Supplemental Response to Commission Staff Data Request No. 107.

Q. Did you eliminate the Company's entire AMI rate base claim when quantifying your adjustment?

A. No, to quantify my adjustment, I eliminated only the plant-in-service associated with the new AMI meters and the related accumulated depreciation. I did not eliminate the other components of the Company's rate base claim, which primarily reflects the regulatory asset associated with previously-deferred depreciation expense and the unrecovered cost of retired meters. Updating the Company's AMI claim to reflect more recent data and eliminating a return on the new meters reduces the Company's revenue requirement by $7.024 million for the electric utility and by $2.720 million for the gas utility, based on Dr. Woolridge's recommended capital structure and cost of capital.[35]

L. Wildfire Resiliency Plan (3.17E)

Q. Please discuss the Company's revenue requirement claim associated with its Wildfire Resiliency Plan.

A. The Company is proposing to implement a ten-year Wildfire Resiliency Plan to address the threat of wildfires in its service territory. In this case, Avista has included 2020 and 2021 capital additions associated with the plan, as well as transmission and distribution operating expenses for the period October 1, 2021 through September 30, 2022. In addition, Avista is seeking authorization to defer certain operating expenses associated with the Wildfire Resiliency Plan between the January 1, 2021 and September 30, 2021.

[35] My adjustments are shown in Crane, Exh. ACC-4, at 6 (electric) and Exh. ACC-7, at 5 (gas).

Avista originally filed a separate petition for approval of deferred accounting in Docket No. UE-200984 and that filing was consolidated with the base rate case by the Commission on March 11, 2021. Finally, the Company is also seeking to implement a balancing account to track the difference between actual Wildfire Plan expenses and the expenses included in base rates. The Company proposes to book a regulatory asset/liability for this difference and to refund/recover this difference in a subsequent base rate case.

Q. What adjustments have you made to the Company's claim for Wildfire Resiliency Plan costs?

A. Paul Alvarez is testifying on Public Counsel's recommendations regarding the proposed Wildfire Resiliency Plan and related ratemaking treatment. While Mr. Alvarez is not recommending any adjustments to the Company's proposed operating costs associated with the plan, he is recommending that a significant number of capital costs proposed by Avista be excluded from rates at this time. In Adjustment 3.17, I have incorporated Mr. Alvarez's proposed capital adjustments and the related adjustments to depreciation expense and interest on debt.[36]

M. Energy Imbalance Market (3.18E)

Q. Please explain the Company's claim associated with joining the EIM.

A. The Company plans to join the Western EIM, which is operated by the California

[36] Crane, Exh. ACC-4, at 6.

Independent System Operator ("CAISO"), in March 2022. Avista included certain EIM-related capital additions through March 2022 in its revenue requirement claim, as well as operating expenses for the rate-effective period. The Company's EIM adjustment, as filed, increased its revenue requirement by $3.781 million. This claim was later updated in Avista's Third Supplemental Response to Commission Staff Data Request No. 107 to $4.706 million.[37]

Q. What is Public Counsel's recommendation regarding these EIM costs?

A. EIM costs, and the related benefits, are discussed in the testimony of Public Counsel witness Rachel Wilson. Ms. Wilson is recommending that EIM costs be excluded from base rates at this time. Therefore, in Adjustment 3.17, I have eliminated the Company's EIM cost claim from my revenue requirement. Note that my adjustment is limited to the Company's original claim of $3.781 million, because that is the amount included in the Company's filing on which my subsequent adjustments are based.

N. Additional Electric Rate Base Adjustments

Q. Is Public Counsel recommending any additional rate base adjustments?

A. Yes, there are four additional rate base adjustments being recommended by Public Counsel, all of which impact the electric utility. First, Public Counsel is recommending that certain costs associated with substation upgrades and grid modernization be excluded from the electric utility's revenue requirement. These adjustments are described by

[37] Crane, Exh. ACC-13, Avista Third Supplemental Response to Commission Staff Data Request No. 107.

Mr. Alvarez. The proposed substation disallowances are based on the response to Public Counsel Data Request No. 241 and the proposed grid modernization disallowance are based on the response to Public Counsel Data Request No. 247.[38] Therefore, I have added two columns to Exhibit ACC-4, on page 7, to include the impact of these two adjustments that are sponsored by Mr. Alvarez.

In addition, I am recommending that 2022 Colstrip plant additions, as well as costs associated with the installation of SmartBurn at Colstrip Units 3 and 4, be excluded from rates, as discussed in more detail below.

Q. How did the Company develop its claim for Colstrip post-test period plant additions?

A. In the last case, the Commission authorized accelerated recovery for Colstrip plant investment to reflect recovery by 2025, instead of the 2034 and 2036 dates previously established for Colstrip Units 3 and 4 respectively. In addition, Avista agreed that it would not support capital expenditures at Colstrip that would extend the plant's operational life beyond December 31, 2025. In its filing in this case, Avista included several 2022 projects in its revenue requirement, arguing that these projects should be included because of the previously-approved accelerated recovery period, and the relatively short period of time over which these costs would be recovered. Ms. Andrews stated on page 30 of her testimony that the 2022 Colstrip additions increased the

[38] Crane, Exh. ACC-14, Avista Response to Public Counsel Data Request No. 241; Crane, Exh. ACC-15, Avista Response to Public Counsel Data Request No. 247.

Company's revenue requirement by approximately $900,000.

In Avista's Third Supplemental Response to Commission Staff Data Request No. 107, Avista updated its claim for Colstrip plant additions to reflect actual 2020 additions and revised projections for 2021 and 2022.[39] In that response, the Company indicated that it only included 2021 projects that were approved by the owners as of February 4, 2021. In addition, the Company indicated that it was limiting its requested 2022 addition to "only one large project that Avista anticipates the owners will approve in 2021." The changes reflected in Avista's Third Supplemental Response to Commission Staff Data Request No. 107 reduced the Company's original revenue requirement claim by approximately $837,000.[40] I have updated the Colstrip adjustment to reflect the actual 2020 plant additions as well as the 2021 projects included in this response. However, I am recommending that the request for recovery of the 2022 Colstrip project be denied, and that project has been eliminated from my revenue requirement in the Company's Colstrip Adjustment 3.19E.[41]

Q. Why are you recommending that the 2022 plant addition associated with Colstrip be excluded?

A. In the supporting schedule for Avista Third Supplemental Response to Commission Staff Data Request No. 107, the Company included a capital addition of $3.338 million in July 2022 related to Colstrip. I am recommending that these costs be excluded from the rates

[39] Crane, Exh. ACC-13, Avista Third Supplemental Response to Commission Staff Data Request No. 107.
[40] *Id*.
[41] Crane, Exh. ACC-4, at 6.

resulting from this case for three reasons. First, these costs are very far past the end of the test period in this case. This investment is not expected to be in-service until more than 30 months, or two and half years, past the end of the test period. Second, given the Company's agreement that it will not undertake projects that extend the operational life of Colstrip, it is more important than ever to closely monitor the Colstrip capital costs that are being charged to ratepayers, and to ensure that such costs are necessary only for the continued operation of Colstrip Units 3 and 4 through December 31, 2025. Third, these costs have not yet been approved by the Colstrip owners. Therefore, at this time, these costs are speculative. For all these reasons, I recommend that the Commission reject the Company's claim for inclusion of this 2022 project in utility rates resulting from this case.

Q. Please provide a brief overview of the SmartBurn investment included in the Company's revenue requirement claim.

A. As discussed beginning on page 55 of Mr. Thackston's testimony, SmartBurn "was originally developed as "part of Alliant Energy's Combustion Initiative Program focused on the reduction of nitrogen oxides ("NOx") by optimizing the combustion process in coal-fired generation plants."[42] It was anticipated that the SmartBurn technology would be used in conjunction with Selective Catalytic Reduction ("SCR"), whereby SmartBurn would reduce the amount of NOx being produced and SCR would eliminate the resultant

[42] Direct Testimony of Jason R. Thackston, Exh. JRT-1T, at 55:8–10.

NOx through a chemical reaction, resulting in NOx being broken down into molecular nitrogen (“N_2”) and water vapor.

Q. When was SmartBurn installed?

A. SmartBurn was installed on Colstrip Unit 4 in 2016 and on Colstrip Unit 3 in 2017. The total SmartBurn capital cost allocated to Washington was $2.74 million. According to Mr. Thackston, the decision to install SmartBurn was made in 2012, on the basis that the owners of Colstrip Units 3 and 4 “could be ordered to install SCR during the 2017 review period….”[43]

Q. Was SCR ultimately required on Colstrip Units 3 and 4?

A. No, it was not. As acknowledged by Mr. Thackston on page 57 of his testimony, SCR was not required.[44] The Company argues that even though SCR is not required on Colstrip Units 3 and 4, the decision to invest in SmartBurn was a prudent one and this investment should be recovered from Washington ratepayers.

Q. Do you agree?

A. No, I do not. It is the Company and its shareholders that bear the risk for recovery of its investment, and for proving that such investment is prudent and necessary for the provision of regulated utility service. The Company has not met this burden. SmartBurn was a completely discretionary project at the time that it was undertaken, and remains an unnecessary project today. While the Company may have had an expectation that it

[43] Thackston, Exh. JRT-1T at 59:13.
[44] Thackston, Exh. JRT-1T at 57:5.

would be required to install SCR in the future, which would have made the SmartBurn investment more appropriate, that ultimately is not the case. In fact, in its last base rate case, Avista received Commission authorization to accelerate recovery of its Colstrip investment to 2025, with the understanding that Colstrip Units 3 and 4 will no longer be serving Washington customers after that time. Accordingly, SmartBurn was not necessary to serve customers in the past and will not be necessary to serve customers in the future. Therefore, I recommend the Commission exclude the revenue requirement associated with the SmartBurn project from Avista's Washington-jurisdictional electric rates.

Q. How were these costs handled in the Company's last base rate case?

A. The Company's last base rate case was resolved by a stipulation. Although the stipulation was largely a "black-box" settlement, there were several provisions specified in the stipulation, including the provision stating that "the costs associated with the installation of SmartBurn on Units 3 and 4, are not included in Avista's rate base at this time."[45]

Q. Has the Commission excluded SmartBurn costs associated with Colstrip Units 3 and 4 in other rate proceedings?

A. Yes, these costs were excluded by the Commission in Puget Sound Energy's ("PSE") 2019 rate case. According to Mr. Thackston's testimony at page 61, the Commission found that PSE "failed to demonstrate that [SmartBurn] was necessary in order to comply

[45] Partial Multiparty Settlement Stipulation, at 6, *Wash. Utils. & Transp. Comm'n v. Avista Corp.* (Nov. 21, 2019)(Dockets UE-190334 and UG-190335.

with any law, State or Federal, and that PSE failed to document its decision to support SmartBurn."[46] While Avista has attempted to distinguish its decision to implement SmartBurn from the PSE case, the two cases are in fact similar. Just as the Commission found that SmartBurn should be excluded from rates in the PSE proceeding, so should the Commission find that these costs should be excluded from the Company's revenue requirement in this case.

Q. How did you quantify your adjustment?

A. In response to an informal request, the Company quantified the impact of SmartBurn as increasing the Company's revenue requirement in this case by $345,247. Since Public Counsel is recommending a different capital structure and cost of capital than Avista, the impact based on Public's Counsel's overall cost of capital is slightly less, approximately $329,000.[47]

O. Tax Flow-Through Proposal

Q. Please describe the Company's Tax Flow-through Proposal

A. As described in the testimony of Ryan Krasselt, concurrent with the base rate case filing, Avista filed a petition seeking authorization to: (1) change its accounting method from normalization to flow-through for regulatory purposes for federal income tax expense associated with Industry Director Directive No. 5 ("IDD No. 5") and meters; and (2)

[46] Thackston, Exh. JRT-1T at 61:10–12.
[47] I have included this additional adjustment to eliminate $329,000 of costs associated with SmartBurn in Crane, Exh. ACC-4, at 7.

defer the associated change in tax expense and future annual benefits.[48] Avista sought authorization for flow-through treatment in Idaho and Oregon, as well as in Washington. Idaho granted Avista's request on February 1, 2021 and Washington granted Avista's request on March 11, 2021. It is my understanding that the Oregon petition is still pending.

In this rate case, Avista estimated that the December 31, 2020 balance of ADFIT related to meters and IDD No. 5 was $45.9 million for Washington electric and $22.3 million for Washington gas, before the tax gross-up.[49] The tax grossed-up estimates were $58.1 million for electric and $28.2 million for gas. Avista proposed to return the electric balance over one and a quarter years and to return the gas balance over two years, which would exactly offset the requested revenue increases in this case. Thus, although Avista is proposing to increase electric base rates by $44.2 million and to increase gas rates by $12.8 million, there would be no initial net change in rates under the Company's proposal. Avista proposed to return future ADFIT associated with meters and IDD No. 5 over a 10-year period.

Q. Did Public Counsel support the Company's proposal to flow-through ADFIT associated with meters and IDD No. 5?

A. Yes, it is my understanding that Public Counsel supported the Company's proposal to flow-through these deferred taxes, as well as its proposal to defer the associated change

[48] Docket Nos. UE-200895 and UG-200896.
[49] Ryan L. Krasselt, Exh. RLK-2.

in tax expense and future annual benefits. However, the petition filed in UE-200895 and UG-200896 did not address the ultimate ratemaking treatment or amortization period for these tax benefits, which is to be decided in this rate case.

Q. What is your view of flow-through accounting treatment for ADFIT versus the normalization methodology?

A. I generally support flow-through accounting treatment. The flow-through methodology returns these tax benefits to ratepayers more quickly than the normalization methodology. This result promotes intergenerational equity by returning the deferred taxes sooner to the ratepayers that paid for them. In addition, the flow-through method helps to mitigate the front-end loaded nature of the return of and on investment. For any given investment, rate base and its associated revenue requirement are higher in the earlier years and lower in the later years. Flowing these deferred taxes through to customers helps to mitigate the rate impact in the earlier years, when such rate relief is needed the most. Accordingly, I generally view flow-through accounting treatment as more favorable to ratepayers than the normalization methodology.

Q. What period of time do you recommend that these deferred taxes be returned to ratepayers, based on the flow-through authorization granted by the Commission?

A. I am recommending that the Commission adopt an amortization period for the initial ADFIT balance that will eliminate any electric or gas increase in this case. Based on my recommended increases of $7.225 million for the electric utility and of $4.007 million for the gas utility, this would result in an amortization period of between seven to eight years.

Q. What period of time do you recommend for future ADFIT balances related to meters and IDD No. 5?

A. The Company has proposed that these future balances be returned over 10 years. I am not opposed to adopting a 10-year period for the return of future ADFIT balances. However, I recognize that flow-through treatment for ADFIT is a new ratemaking treatment in Washington. The Commission and all parties should therefore have the flexibility to review an appropriate amortization period and to recommend adjustments going forward, once all parties have more experience with flow-through accounting and once we have a better idea of the potential impact on rates. Therefore, I recommend that the issue of an appropriate amortization period be reviewed in the Company's next base rate case.

Q. Are you recommending that the Commission limit flow-through treatment to ADFIT associated with meters and IDD No. 5?

A. At this time, I am recommending that the Commission limit flow-through to ADFIT associated with meters and IDD No. 5. There are certain categories of deferred taxes that the Internal Revenue Service ("IRS") requires to be normalized in order for the Company to benefit from advantageous tax treatment. However, there are other categories of deferred taxes that can be flowed-through at the Company's discretion. In addition to ADFIT associated with meters and IDD No. 5, the Company has $178.4 million of other deferred taxes associated with repairs, AFUDC Debt, Pension and Medical costs, Settlements, Hydro Relic, and Others that could be flowed-through by the Commission.[50] The Company claims that flowing all these deferred taxes through to ratepayers could cause cash flow problems for Avista, and in fact deferred taxes are generally a source of cash flow for regulated utilities. At this time, I believe that it is prudent for the Commission and all parties to limit flow-through treatment to the deferred taxes associated with meters and IDD No. 5. However, the parties may want to reexamine this issue in the future as we all gain more insight and experience with Avista's flow-through of ADFIT.

Q. Please summarize your testimony regarding Avista's request to flow-through ADFIT associated with meters and IDD No. 5.

A. I support flow-through treatment for meters and IDD No. 5. I recommend that the Commission return the actual December 31, 2020 ADFIT balances over a period of time that will result in no net increase in rates as a result of this case. In addition, I am generally supportive of the Company's proposal to return future ADFIT balances associated with meters and IDD No. 5 over a 10-year period. However, I recommend that the Commission reexamine the appropriate amortization period in the next base rate case. Finally, in the future, the Commission may also want to consider adopting the flow-through treatment for additional categories of ADFIT that are not protected by the IRS.

[50] Crane, Exh. ACC-16, Avista Response to Public Counsel Data Request No. 10.

P. Summary of Revenue Requirement Recommendation

Q. What is the result of Public Counsel's revenue requirement recommendations in this case?

A. Public Counsel's recommendations result in an electric revenue base revenue increase of $7.225 million (versus the Company's $44.183 million request) and a gas base revenue increase of $4.007 million (versus the Company's $12.790 million request). These recommendations result in base distribution revenue increases of 1.36% and 3.81% for electric and gas, respectively. Public Counsel's proposed rates would go into effect October 1, 2021. In addition, Public Counsel is recommending that the Commission adopt an amortization period for certain deferred income taxes that would provide for a tax credit to match these electric and gas base revenue increases, resulting in no net increase to Washington ratepayers.

Q. Does this complete your testimony?

A. Yes, it does.