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AVISTA
Corp.

April 4, 2006

State of Washington
Washington Utilities & Transportation Commission
1300 S. Evergreen Park Drive
Olympia, Washington 98504-8002

Attention: Ms. Carole Washburn, Executive Secretary

Enclosed is a petition of Avista Utilities requesting the Commission to approve a proposed Natural Gas Decoupling Mechanism and to authorize the Company to begin recording accounting entries associated with the Mechanism in July 2006.

If you have any questions regarding this filing, please contact Brian Hirschkorn at 509-495-4723.

Sincerely,

Kelly Norwood

Kelly Norwood
Vice-President, State & Federal Regulation

Enc.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have served Avista Corporation's Petition for an Order Authorizing Implementation of a Natural Gas Decoupling Mechanism and to Record Accounting Entries Associated with the Mechanism, by mailing a copy thereof, postage prepaid to the following:

Ms. Carole J. Washburn, Executive Secretary
Washington Utilities & Transportation Commission
1300 S. Evergreen Park Drive SW
P.O. Box 47250
Olympia, WA 98504-7250

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Washington Energy Policy Group, CTED
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Olympia, WA 98504

Chris Davis
Spokane Neighborhood Action Program
2116 East First
Spokane, WA 99202

Dated at Spokane, Washington this 4th day of April 2006.

Patty Olsness
Rates Coordinator

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Petition of AVISTA Corporation (dba Avista Utilities) For an Order Authorizing Implementation Of a Natural Gas Decoupling Mechanism And To Record Accounting Entries Associated With the Mechanism	DOCKET NO. UG-06_____ PETITION OF AVISTA CORPORATION

I. PETITIONER

1 In accordance with WAC 480-09-420, the name and address of Petitioner, Avista Corporation ("Avista Corp." "Avista," or "Company"), is as shown below. Please direct all correspondence related to this Petition as follows:

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II. COMPANY'S REQUEST

2 Pursuant to WAC 480-09-420, Avista Corp. hereby requests that the Commission issue an order authorizing Avista to implement a natural gas decoupling mechanism, and to begin recording accounting entries associated with the mechanism, effective July 2006. The Company's proposed decoupling mechanism is consistent with state and regional energy efficiency objectives, and provides the Company with an opportunity to continue to recover the fixed costs of providing service to customers, following a decline in usage resulting from

conservation and price elasticity. The proposed mechanism does not track changes in margin related to variations in customer natural gas usage caused by weather.

III. THE NEED FOR A NATURAL GAS DECOUPLING MECHANISM

3 The increase in the cost of natural gas over the past several years makes consideration of a natural gas decoupling mechanism especially important at this time. The increased cost of natural gas, projections of continued high prices in the future, and the fragile balance between supply and demand, make it increasingly important to focus on effective long-term efficiency and conservation measures. However, because the Company's current rate structure(s) provide recovery of the majority of Avista's fixed costs on a per-therm (sales volume) basis, energy efficiency and conservation objectives are directly at odds with the recovery of the LDC's fixed costs of providing service. Decoupling breaks the link between the volume of therm sales and the recovery of fixed costs and would provide for an increased focus on energy efficiency and conservation. Increased conservation would not only benefit the individual customers participating in those measures through reduced bills, but would also reduce the overall demand for natural gas which would help to reduce natural gas prices for all customers.

4 Avista has had natural gas Demand-Side Management (DSM) programs in place since the mid-1990's, and has worked closely with other stakeholders on DSM policies and programs. Funding for the DSM programs is provided through the DSM tariff rider approved by the Commission in 1995. Although Avista has been among the leaders in the Northwest in implementing and supporting DSM programs, the proposed decoupling mechanism would provide the Company with incentives to achieve even greater DSM goals. As described later,

the level of fixed costs recovered through the Company's proposed mechanism would be directly tied to the Company's success in achieving the "target" level of natural gas DSM savings during the prior year. A decoupling mechanism would also allow the Company to provide a stronger message to customers regarding conservation.

5 As noted earlier, the majority of Avista's fixed costs of providing natural gas service are recovered through a rate per therm for each therm sold. Ideally, from the Company's cost recovery perspective, the fixed costs of providing service would be recovered through a fixed charge each month, since the facilities and support services must be available to serve customers irrespective of how much energy they use. However, that fixed charge would need to be approximately $20 per month in order to recover the fixed costs of providing gas distribution service. Avista presently has a monthly customer (fixed) charge of $5.50 per month, and the remainder of the fixed costs are recovered on a per therm basis. A substantial increase in the customer charge, however, would require a substantial decrease in the usage charge, which would not encourage additional conservation. Because of this and other issues surrounding higher monthly customer charges, decoupling is a preferable alternative to a $20 customer charge and can be implemented without altering existing rate structures.

6 The rates established in a general rate proceeding are designed to provide full recovery of the costs of providing service to customers. When the majority of fixed costs are recovered through sales volumes, and sales volumes are lower than expected, the recovery of fixed costs falls short of the level authorized by the Commission. An effective decoupling mechanism, which separates the recovery of fixed costs from sales volumes, is consistent with the ratemaking objective of authorizing rates that are designed to recover the fixed costs of providing service.

7 From 1999 to 2005, the Company's Washington residential and small commercial (Schedule 101) gas customers reduced their average usage by 13.5%, on a weather-corrected basis. During the past two years, Avista has implemented natural gas general rate increases for Washington customers totaling approximately 5%. A primary cause of these increases was the reduction in customer usage that resulted in an under-recovery of fixed costs (margin). While a decoupling mechanism would not altogether eliminate the need for future general filings, it would serve to reduce the frequency and magnitude of general rate requests, resulting in smaller incremental rate increases over time.

IV. 2005 COMMISSION RULEMAKING TO REVIEW NATURAL GAS DECOUPLING

8 The Commission opened a rulemaking proceeding in 2005 to review decoupling for natural gas utilities. Avista filed comments dated June 10, 2005 in support of a natural gas decoupling mechanism. On October 17, 2005, the Commission issued a letter that closed the rulemaking proceeding and stated that it would consider specific utility (decoupling) proposals included in a general rate filing.

9 Avista requests that the Commission consider and approve its proposed natural gas decoupling mechanism "outside" of a general rate filing. The Company believes it has addressed and resolved the two primary issues related to a decoupling mechanism that would otherwise be examined in a general rate proceeding. These two issues are: 1) the need for a recent "test-year" to establish a reliable base from which to measure a decoupling adjustment going forward, and 2) an assessment of the potential change in the gas utility's business risk given a decoupling mechanism. With regard to 1), Avista has recently completed a natural gas

general rate case based on a 2004 test year with rates effective January 1, 2006. Accordingly, it has established a reliable base for the proposed decoupling mechanism.

10 With regard to 2), the Company's proposed mechanism does not significantly affect the Company's business risk going forward. The Company's proposed mechanism captures only the change in residential and commercial customers' usage resulting from natural gas conservation, energy efficiency and price elasticity. It does not capture: 1) changes in large customer usage often resulting from changes in business or economic conditions, or 2) changes in customer usage resulting from abnormal weather. These changes in customer usage that are not included in the Company's mechanism can be more substantial and affect the Company's business risk going forward. Therefore, an adjustment to the Company's authorized Return on Equity (ROE) would not be warranted. Additionally, as will be described later, the mechanism includes an "earnings-test" - a provision that will not allow the Company to implement a decoupling rate adjustment if its earnings exceed its authorized rate of return.

11 Because the Company has a recently completed rate case to use as a base for its decoupling mechanism, and the proposed mechanism will not significantly affect the Company's business risk going forward, the Company believes that it is appropriate for the Commission to approve implementation of the proposed mechanism outside of a general rate filing.

V. AVISTA'S PROPOSED DECOUPLING MECHANISM

A. Overview

12 The ultimate design of the mechanism itself should be understandable and remove the disincentive to fully pursue energy efficiency and conservation. The mechanism must also

balance simplicity and completeness. The Company's proposed mechanism removes the disincentive related to fully promoting energy efficiency, and provides the Company with the opportunity to recover the fixed costs of providing natural gas service. The mechanism is relatively easy to understand and implement, directly ties the recovery of fixed costs to both an annual earnings-test and pre-established DSM targets, and provides adequate time for audit prior to implementing any rate adjustment. The mechanism would not require any changes to existing rate structures or the Company's billing system. The proposed mechanism results in a single annual rate adjustment that would be implemented coincident with the annual PGA adjustment. The rate adjustment would reflect the difference between the weather-normalized margin (revenue less purchased gas costs) received by the Company during the prior year compared to the level of margin approved by the Commission in the Company's last general filing (2004). The incremental amount of the annual rate adjustment would be limited to no more than a 2% rate increase.

13 A decoupling mechanism could incorporate abnormal weather to provide the utility a more reasonable opportunity to recover fixed costs, regardless of weather. However, Avista's proposed mechanism excludes a deferral for abnormal weather, i.e., current sales volumes are first adjusted for abnormal weather, and only the variance in sales volumes created by conservation/price elasticity is measured and reflected in the deferral. The variability in customer usage caused by abnormal weather can be several times that caused by conservation/price elasticity. By excluding the variation in sales volume/margin caused by abnormal weather, the Company is still retaining the majority of risk associated with sales variability. As discussed earlier, by retaining this risk, the Company believes that an adjustment to the Company's authorized return-on-equity is not warranted.

14 The mechanism would apply to the Company's natural gas Schedules 101 and 111, which include all residential and commercial customers, as well as small industrial customers. The mechanism would not be applicable to the Company's approximately 70 large industrial customers served under High Load Factor Schedule 121, Interruptible Schedule 131, Transportation Service Schedule 146, or special contracts. As previously mentioned, changes in large customers' usage is often caused by business and/or economic condition. These changes in usage can be substantial, such as the closure of a large manufacturing plant, and are outside of the scope of the mechanism.

B. Proposed Term of the Mechanism

15 The Company is proposing a three-year "pilot-term" for the mechanism. This three-year period would extend from July 2006 through June 2009 for the recording of deferred revenue. As the initial rate adjustment for the July 2006 – June 2007 deferral period would not begin until the fall of 2007 (coincident with the PGA adjustment), the three-year pilot period would not be complete until the fall of 2010, upon completion of the third-year rate adjustment.

16 On or before March 31, 2009 (three months prior to the end of the deferral period), the Company would have the opportunity to file a request to continue the decoupling mechanism beyond the three-year pilot term. That filing would include a qualitative and quantitative assessment of the mechanism.

C. Calculation of Monthly Revenue Deferral

17 The starting point for the proposed mechanism is the volume of therm sales for each month of the year from the Company's last general rate case (2004 test year). The Company has calculated the weather-normalized calendar therm sales (Base Therm Sales) for each

month of the 2004 test year, with the total for the months matching the annual amount reflected in the approved rates resulting from Company's last general filing.

18 Following the end of each month, beginning with July 2006, the actual volume of weather-corrected therm sales for the calendar month (Current Therm Sales) would be determined and compared with the Base Therm Sales for the corresponding month. The coefficients (usage per degree-day per customer) used to determine the weather adjustment are the same as those used in the test year, thereby providing an "apples-to-apples" comparison between the two years. Only one additional adjustment, other than the weather adjustment, would be made to the Current Therm Sales. To the extent the Company has added customers since the test year, these new customers would increase Current Therm Sales as compared to the Base Therm Sales. Again, in order to have an "apples-to-apples" comparison of Current vs Base Therm Sales, an adjustment is necessary to remove the usage associated with the new customers.

19 The adjustment for new customers would be based on the average actual (weather-corrected) use-per-customer for the current month multiplied by the number of customers added since the corresponding month of the test year. Following the adjustment for new customers, the Current Therm Sales for the month are compared with the Base Therm Sales to determine the difference in therm sales. This comparison captures only the effect of conservation and price elasticity since the 2004 test year. This difference is multiplied by the margin rate (sales rate less purchase gas cost per therm) resulting from the approved rates in the last rate case, to calculate the fixed distribution costs that are either under-recovered or over-recovered as compared to the test year. As Schedule 101 consists of a single rate for all usage, the margin rate is also the same for all usage. As Schedule 111 consists of three

usage/rate blocks, the Company proposes to use the (lowest) margin from the tail-block in order to avoid the complexities of determining weather-normalized usage by rate block. Ninety percent (90%) of these dollars, either positive or negative, are then recorded in a separate account for later recovery (or rebate). As will be described later, the deferral level of 90% was chosen to allow for an additional incentive to exceed certain gas DSM goals.

20 In summary, there are essentially seven simple steps to calculating the amount of the monthly revenue deferral for each of the two rate schedules (101 &111) included in the mechanism. These steps are as follows and are illustrated in the example shown on Exhibit No. 1:

Step 1 – Calculate current month weather-normalized sales volumes ("Current Therm Sales")

Step 2 – Calculate average use per customer for current month

Step 3 – Calculate total usage for new customers by multiplying average use per customer by the number of new customers added since the test year

Step 4 – Calculate current month usage excluding new customers

Step 5 – Calculate difference in usage between current month and test year

Step 6 – Calculate the margin difference resulting from the usage difference

Step 7 – Record deferred revenue for 90% of the margin difference

21 The resulting monthly deferred revenue would be accumulated for each twelve-month period beginning July 2006 through June 2007. Interest would be accrued on the deferred balance at the same rate applied to the PGA deferral account. Following June 2007, the Company would calculate a proposed rate adjustment to amortize that amount over a prospective twelve-month period beginning in the fall of 2007, subject to the "earnings" and "DSM" tests described below.

D. Earnings and DSM Tests

22 The Company would implement a surcharge beginning in the fall of 2007 (coincident with PGA) only if: 1) it did not "over-earn" for its Washington gas operations during 2006, based on the recent Commission authorized rate of return for Avista of 9.11%, and 2) it meets pre-established gas DSM savings targets during 2006. The authorized rate of return of 9.11% is derived from the Commission's Order No. 05 in Docket No. UG-050483. These tests would be repeated for the subsequent two years, i.e., 2008 surcharge based on earnings and DSM tests for 2007, etc. The "earnings-test" would be based on the Company's annual "Commission-basis" operating results, which are currently filed with the Commission by April 30 for the previous year. If the Commission-basis rate of return for the Company's Washington gas operations exceeds 9.11% for 2006, Avista would reduce the amount of the proposed surcharge (amount transferred to the balancing account) to bring the rate of return down to 9.11%. If this calculation were to reduce the deferred revenue amount to zero, no surcharge would be implemented.[1]

23 Where the amount of the surcharge is reduced as described above, the cumulative amount of deferred revenue remaining from the prior year will be used to offset future deferrals (carryover), rather than written off the Company's books. For example, if the Company recorded deferred revenue for the prior July 2006-June 2007 period of $1 million, but could only surcharge $585,000 for the October 2007-September 2008 period, no additional deferrals would be recorded beginning in July 2007 until the cumulative balance of new deferrals exceeds $415,000 ($1 million less $585,000). An example calculation of the surcharge

[1] Avista acknowledges there is a difference in the deferral period (July-June) and the earnings and DSM test period (prior calendar year). However, the Company believes that the use of the existing information and processes, i.e.,

amount where the Company does not meet the earnings test is shown on page 1 of Exhibit No. 2.

24 The second "test" regarding implementation of a decoupling surcharge relates to the Company achieving pre-established natural gas DSM target savings during the prior year. The test provides financial incentives to not only meet, but exceed gas DSM goals. The Company's 2006 Integrated Resource Plan (IRP) sets forth a natural gas (Washington & Idaho) target savings level of 1,062,000 therms for calendar years 2006 and 2007. These targets are developed with input from other interested parties through the IRP process. This target savings level will be used for determining the level of the fall-2007 and 2008 surcharge; the target savings level included in the Company's 2008 IRP will be used for the 2009 surcharge. Assuming the surcharge level is not reduced based on the "earnings test" described above, the surcharge level could also vary depending on the actual level of gas DSM savings achieved compared to the target levels described above. The following table shows the level of the surcharge based on a comparison of actual gas DSM savings compared to the target savings:

Actual vs Target DSM Savings	Surcharge vs Margin Shortfall
90% - 110%	90% (as deferred)
70% - 90%	70%
50% - 70%	50%
< 50%	0%
> 110%	100% (additional 10% incentive)

Commission-basis and DSM reports, provide a reasonable and sound basis for the application of the earnings and DSM tests.

25 Each month, beginning in July 2006, the margin difference is calculated as shown on Exhibit No. 1, and 90% of the difference is recorded as deferred revenue. As an example of the DSM test, let's assume the total deferred revenue for July 2006 - June 2007 is $1 million, which is 90% of the total margin difference ($1.11 million) for the period. If during 2006, between 90%-110% of the gas DSM target savings are achieved, the Company would file for a decoupling surcharge to recover the total deferred amount of $1 million beginning in the fall of 2007. If between 70% and 90% of the target savings are achieved, the surcharge amount would be 70% of $1.11 million, or $777,000. If the Company achieves over 110% of the target, it would file for a surcharge of $1.11 million (100% of margin difference), thus providing a financial incentive for the Company to significantly exceed the target. Any deferred revenue not recovered as a result of not meeting at least 90% of the DSM target would be carried forward and used to offset future deferrals that would otherwise be recorded. Examples of the surcharge amount under various DSM savings levels are shown on page 2 of Exhibit No. 2.

26 The earnings and DSM tests would be calculated independently and the test resulting in the lowest surcharge amount would be used. Examples of potential surcharge levels using both the earnings and DSM savings tests are also shown on page 2 of Exhibit No. 2.

E. 2% Annual Rate Increase Limitation

27 After applying the "earnings" and "DSM" tests, the amount of the rate increase resulting from the adjustment would be subject to an annual incremental limit of 2%, i.e., the annual increase in the surcharge cannot exceed a 2% rate increase each year (cumulative of approximately 6% over the three year pilot term). The incremental surcharge (percentage) increase will be determined by dividing the total deferred revenue for the past year (July-

June), subtracting the annual amount recovered by the present surcharge rate, and dividing that amount by the total "normalized" revenue for Schedules 101 and 111 for the same period. Normalized revenue would be determined by multiplying the weather-corrected usage for the period by the present rates in effect. If the incremental surcharge would exceed a 2% rate increase, only a 2% increase would be implemented and any excess deferred revenue would remain in the deferred revenue account and could be recovered the following year, subject to the 2% limitation.

28 The Company has prepared a simulation of the deferral calculation for 2006 using projected customer usage based on normal weather. The simulation resulted in a total deferred revenue amount of approximately $550,000, or a 0.3% increase over present rates in effect.

F. Decoupling Rate Adjustment Filing & Implementation

29 On or before September 1, 2007, 2008 and 2009, the Company would file a proposed decoupling surcharge (or rebate) based on the amount of deferred revenue recorded for the prior July through June period, and the results of the "earnings", "DSM" and "2%" tests. A proposed tariff would be included in the filing. A sample tariff for the decoupling/conservation rate adjustment is attached for illustrative purposes as Exhibit No. 3. The Company presently files its Commission-Basis Earnings report (for the prior year) by April 30th and will file its annual DSM report in advance of the decoupling filing. The Commission Staff and other interested parties should have ample time to examine and audit these reports prior to the decoupling surcharge filing.

30 For the first year, July 2006-June 2007, the total net deferred revenue amount for the year would be recovered via a twelve-month surcharge implemented coincident with the Company's annual PGA adjustment in the fall of 2007. The surcharge would be a single rate

adjustment (same rate) for both Schedules 101 and 111. If the surcharge is approved by the Commission, the corresponding deferred revenue amount would be transferred to a separate account and the surcharge revenue received would reduce the deferred revenue in that account. Any deferred revenue remaining in the balancing account at the end of the year, resulting from over- or under-collection, would be added to the "new" revenue deferrals to determine the amount of the proposed surcharge for the following year.

G. Accounts Used for the Decoupling Mechanism

31 The Company is proposing to record the deferred revenue in account 186 – Miscellaneous Deferred Debits. The amount approved for recovery would be transferred into a 182.3 - Regulatory Asset account for amortization via the surcharge revenue received. On the income statement, the Company is proposing to record both the deferred revenue and the amortization of the deferred revenue through Account 407 - Regulatory Debits and Credits in separate sub-accounts. Exhibit 4 illustrates examples and provides additional detail of the specific accounts proposed for the gas decoupling mechanism.

H. Future General Rate Filings

32 Should the Company file a natural gas general case, and the Commission issues its Order prior to June 2009, the approved test year therm usage from that filing will be used to calculate deferred revenue for the remaining months of the three-year deferral period. If a Commission Order is issued prior to July 2008, the new authorized rate of return would be used for the earnings test for the 2008 Commission-basis results.

VI. SUMMARY

33 The increase in the cost of natural gas over the past several years make consideration of a natural gas decoupling mechanism especially important at this time. This filing requests an order from the Commission authorizing Avista to implement its proposed natural gas decoupling mechanism, and to begin recording accounting entries associated with the mechanism, effective July 2006. The Company's proposed mechanism removes the disincentive related to fully promoting energy efficiency, and provides the Company with the opportunity to recover the fixed costs of providing natural gas service. The mechanism is relatively easy to understand and implement, directly ties the recovery of lost margin to both an annual earnings-test and pre-established DSM targets, and provides adequate time for audit prior to implementing any rate adjustment.

34 Avista has recently completed a natural gas general rate case with rates effective January 1, 2006. It has established a recent test year that can be used as a reliable base for its proposed decoupling adjustment. The Company's proposed mechanism captures only the change in customers' usage resulting from natural gas conservation, energy efficiency and price elasticity. It does not capture changes in large customer usage or changes in customer usage resulting from abnormal weather.

35 The Company is proposing a three-year "pilot-term" for the mechanism, with deferred revenue accounting entries beginning July 2006 and ending June 2009. The initial rate adjustment would not be implemented until the fall of 2007, coincident with the Company's annual PGA. Lastly, the decoupling rate adjustment would be limited to no more than a 2% annual rate increase.

VII. COMPANY'S REQUEST

36 The Company respectfully requests that the Commission issue an order authorizing Avista to implement a natural gas decoupling mechanism, and begin recording accounting entries associated with the mechanism, effective July 2006, as explained in this Petition.

DATED this 4th day of April 2006

Kelly Norwood

By: _____
Kelly Norwood
Vice President, Avista Corp.

VERIFICATION

STATE OF WASHINGTON)
Thurston)
County of ~~Spokane~~)

Kelly O. Norwood, being first duly sworn on oath, deposes and says: That he is a Vice President of Avista Corporation and makes this verification for and on behalf of said corporation, being thereto duly authorized;

That he has read the foregoing Petition, knows the contents thereof, and believes the same to be true.

Kelly O. Norwood

SIGNED AND SWORN to before me on this 4th day of April 2006

KRISTAL L. LINLEY NOTARY PUBLIC STATE OF WASHINGTON COMMISSION EXPIRES 11-9-06

NOTARY PUBLIC in and for the State of Washington, residing at ~~Spokane.~~ Olympia

Commission Expires: 11-9-06

Avista Utilities
Proposed Natural Gas Decoupling Mechanism
Example Calculation of Monthly Deferred Revenue for Decoupling

Step 1 : Calculate current month weather-normalized sales volumes (Current Therm Sales)	
Billed Therms for Current Month	13,824,000
Add: Net Unbilled Therms(1)	(939,000)
Add: Weather Adjustment(2)	1,274,000
Normalized Current Month Therms	14,159,000
Step 2: Calculate average use-per-customer for current month	
Normalized Current Month Therms	14,159,000
Divided by: Number of Customers	132,300
Normalized Use per Customer	107
Step 3: Calculate total usage for new customers added since test year	
Current Month No. of Customers	132,300
Less: Test Year No. of Customers	129,000
Incremental Customers	3,300
Times: Current Normalized Use per Customer	107
Incremental Customer Usage Adjustment(3)	353,100
Step 4: Calculate customer-adjusted current month usage	
Normalized Current Month Therms	14,159,000
Less: Incremental Customer Use Adjustment	353,100
Customer-adjusted current month usage	13,805,900
Step 5: Calculate difference in usage between current month and test-year	
Normalized Test Year Therms for Month(4)	14,157,000
Less: Customer-adjusted current month usage	13,805,900
Current Month Usage Shortfall	351,100
Step 6: Calculate margin difference between current month and test-year	
Current Month Usage Shortfall	351,100
Times: Approved Margin per Therm(5)	$0.23696
Current Month Margin Shortfall	$83,197
Step 7: Calculate deferred revenue based on 90% of margin difference	
Current Month Margin Shortfall	$83,197
Times: 90% Deferral Rate	0.9
Deferred Revenue for Current Month	$74,877

(1) Addition of current month unbilled & subtraction of prior month unbilled therms
(2) Use of same methodology including coefficients (use/customer/degree day) from test year
(3) Assumes new customers use the average use for all customers
(4) Monthly therms adjusted for unbilled and weather - total for all months of the test year equals annual test year volumes from the test year
(5) Rate per therm approved in UG-050483 less puchased gas costs

Exhibit 1

Avista Utilities
Proposed Natural Gas Decoupling Mechanism
Example Application of Earnings and DSM Tests

Margin Shortfall between Current Period (July '06 - June '07) & 2004 Test Year	**$ 1,110,000**
Deferred Revenue during July '06 - June '07 Period (90% of Margin difference)	**$ 1,000,000**

Example 1 - Earnings Test not met: 2006 Commission Basis ROR exceeds 9.11%(1) (assumes 100% of DSM target met)

2006 Commission Basis ROR less Authorized ROR equals Excess ROR
9.30% - 9.11% = 0.19%

Excess ROR times Rate Base equals Excess Net Income
0.19% X $136 million = $258,000

Excess Net Income divided by revenue conversion factor = Surcharge Revenue Reduction
$258,000 / 0.621746 = $415,000

Oct. '07 - Sept. '08 Surcharge = $1,000,000 - $415,000 = $585,000

$585,000 transferred to balancing account upon implementation of surcharge
$415,000 carry-over in deferred revenue account

Example of following year revenue deferral:

	Prior Year Carry-Over Balance	90% of Current Month Margin Shortfall	Current Month Deferral Recorded	Current Year Deferral Balance
	$415,000			
July '07	$415,000	$20,000	$0	$0
Aug	$395,000	$20,000	$0	$0
Sept	$375,000	$60,000	$0	$0
Oct	$315,000	$80,000	$0	$0
Nov	$235,000	$120,000	$0	$0
Dec	$115,000	$160,000	$45,000	$45,000
Jan '08	$0	$220,000	$220,000	$265,000
Feb		$160,000	$160,000	$425,000
Mar		$120,000	$120,000	$545,000
Apr		$80,000	$80,000	$625,000
May		$60,000	$60,000	$685,000
June		$20,000	$20,000	**$705,000**

(1) Based on Commission Order No. 05 in Docket No. UG-050483

Avista Utilities
Proposed Natural Gas Decoupling Mechanism
Example Application of Earnings and DSM Tests

Margin Shortfall between Current Period (July '06 - June '07) & 2004 Test Year **$1,110,000**

Deferred Revenue during July '06 - June '07 Period (90% of Margin difference) **$1,000,000**

Example 2 - Surcharge Level based on Actual DSM savings during 2006

2006 DSM Target Savings **1,062,000 therms**

Earnings Test met - Company not over-earning					Earnings Test Not Met - from Example 1	
Actual Savings	Actual / Target	Surchg % of Margin diff.(1)	Surcharge Amount	Deferred Rev Carryover	Surcharge Amount(2)	Deferred Rev Carryover(3)
1,100,000	104%	90%	$1,000,000	$0	$585,000	$415,000
900,000	85%	70%	$777,000	$223,000	$585,000	$415,000
700,000	66%	50%	$555,000	$445,000	$555,000	$445,000
500,000	47%	0%	$0	$1,000,000	$0	$1,000,000
1,300,000	122%	100%	$1,110,000	$0	$585,000	$415,000

(1) Based on the following table:

Actual DSM Savings/ Target Savings	Surcharge as a % of Margin Difference
90% - 110%	90%
70% - 90%	70%
50% - 70%	50%
< 50%	0%
> 110%	100%

(2) Based on the lower result of either the earnings test ($585,000) or the DSM test

(3) Total deferred revenue amount of $1,000,000 less surcharge amount - carryover would be used to offset future deferrals as shown in Example 1

AVISTA CORPORATION
dba Avista Utilities

SCHEDULE 159

NATURAL GAS CONSERVATION RATE ADJUSTMENT

PURPOSE:

To allow the Company to recover the fixed costs of providing Natural Gas distribution service as authorized by the Commission. Recovery of these fixed distribution costs removes the financial incentive for the Company to increase natural gas sales and allows the Company to fully support all cost-effective natural gas conservation measures.

APPLICABLE:

To Natural Gas Customers served under General Service Schedule 101 and Large General Service Schedules 111 and 112.

MONTHLY RATE:

$0.___ per therm

SPECIAL TERMS AND CONDITIONS:

This Schedule reflects a rate adjustment to General Service Schedule 101 and Large General Service Schedules 111 and 112 to allow the Company to recover the fixed costs of providing Natural Gas distribution service as authorized by the Commission in Order No. ___.

The monthly rate set forth above reflects the recovery of lost revenue recorded by the Company during the past year resulting from reduced customer usage due to the implementation of natural gas conservation measures.

The monthly rate set forth above cannot reflect more than a 2% annual increase in the total rate billed to customers for natural gas service.

This Schedule is a three-year pilot program, effective October 1, 2007 through September 30, 2010, with the monthly rate subject to change annually based on Commission approval of a filing by the Company.

Avista Utilities
Proposed Natural Gas Decoupling Mechanism
Illustrative Accounting Examples

Monthly deferred revenues resulting from a margin shortfall would be recorded in the deferral account by crediting Account 407.4 - Regulatory Credits and debiting Account 186 - Miscellaneous Deferred Debits. Associated deferred tax entries would be recorded by debiting Account 410.1 - Deferred Tax Expense (Debits) and crediting Account 283 - Accumulated Deferred Taxes. These entries would increase current net income to reflect the impact of the additional deferred revenue. The same accounts would be used if the monthly calculation resulted in a reduction to deferred revenue with the debits and credits reversed.

Interest computed on the Deferred Revenue balance sheet account would be recorded by debiting Account 186 – Miscellaneous Deferred Debits and crediting the non-operating Account 419 – Interest Income. Related deferred taxes would be recorded as a debit to Account 410.2 – Deferred Tax Expense (Debits - non-operating) with the credit to Account 283- Accumulated Deferred Taxes.

When an amount is approved for recovery through a surcharge there would be an entry to transfer the allowed amount from Account 186 – Miscellaneous Deferred Debits into Account 182.3 – Other Regulatory Assets.

Finally, as revenue is collected from customers through a surcharge, the regulatory asset would be amortized by debit entries to Account 407.3 – Regulatory Debits that would offset the revenue collected from customers, and credit entries to Account 182.3 – Other Regulatory Assets. Associated deferred taxes would be recorded in Account 283 – Accumulated Deferred Taxes and Account 411.1 Deferred Tax Expense (Credits). These entries offset the effect of the surcharge revenue resulting in no current net income.

Each of the balance sheet accounts and the 407 accounts would have unique sub-accounts that would specifically identify the amounts associated with the gas decoupling mechanism.

Avista Utilities
Proposed Natural Gas Decoupling Mechanism
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If the monthly calculation results in a shortfall or surcharge direction, example $50,000

		Debit	Credit
Misc Deferred Debits - Decoupling Deferred Revenue	186xxx.GD.WA	$ 50,000.00	
Regulatory Credits - Decoupling Deferred Revenue	4074xx.GD.WA		$ 50,000.00
Deferred Tax Expense	410100.GD.WA	$ 17,500.00	
Deferred Taxes - Decoupling Deferred Revenue	283xxx.GD.WA		$ 17,500.00

If the monthly calculation results in an overage or rebate direction, example -$25,000

		Debit	Credit
Regulatory Credits - Decoupling Deferred Revenue	4074xx.GD.WA	$ 25,000.00	
Misc Deferred Debits - Decoupling Deferred Revenue	186xxx.GD.WA		$ 25,000.00
Deferred Taxes - Decoupling Deferred Revenue	283xxx.GD.WA	$ 8,750.00	
Deferred Tax Expense	410100.GD.WA		$ 8,750.00

Enter Interest Income on Deferred Revenue balance, example $2,000

		Debit	Credit
Misc Deferred Debits - Decoupling Deferred Revenue	186xxx.GD.WA	$ 2,000.00	
Interest Income	419xxx.ZZ.ZZ		$ 2,000.00
Deferred Tax Expense	410200.ZZ.ZZ	$ 700.00	
Deferred Taxes - Decoupling Deferred Revenue	283xxx.GD.WA		$ 700.00

At the time a Deferred Revenue Balance is approved for collection through rates - transfer into Regulatory Asset acct, example $750,000 surcharge

		Debit	Credit
Regulatory Asset - Deferred Revenue Approved for Collection	1823xx.GD.WA	$ 750,000.00	
Misc Deferred Debits - Decoupling Deferred Revenue	186xxx.GD.WA		$ 750,000.00

As revenues are collected through customer rates, amortize balancing acct, example $10,000 surcharge

		Debit	Credit
Regulatory Debits - Decoupling Revenue Collected	4073xx.GD.WA	$ 10,000.00	
Regulatory Asset - Deferred Revenue Approved for Collection	1823xx.GD.WA		$ 10,000.00
Deferred Taxes - Decoupling Deferred Revenue	283xxx.GD.WA	$ 3,500.00	
Deferred Tax Expense	411100.GD.WA		$ 3,500.00