BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

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THE WASHINGTON UTILITIES          )
AND TRANSPORTATION COMMISSION,    )
                                  )
               Complainant,       )
                                  )
     vs.                          ) DOCKET NO. UE-991606
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AVISTA CORPORATION                )
                                  )
               Respondent.        )
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THE WASHINGTON UTILITIES          )
AND TRANSPORTATION COMMISSION,    )
                                  )
               Complainant,       )
                                  )
     vs.                          ) DOCKET NO. UG-991607
                                  )
AVISTA CORPORATION,               ) VOLUME V
                                  ) Pages  537 - 650
               Respondent.        )
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A hearing in the above matter was held on March 29, 2000 at 1:08 p.m., at 1300 South Evergreen Park Drive Southwest, Olympia, Washington, before Administrative Law Judge KAREN M. CAILLE, Chairwoman MARILYN SHOWALTER, Commissioners RICHARD HEMSTAD and WILLIAM R. GILLIS.

The parties were present as follows:

THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, by GREGORY J. TRAUTMAN and MARY M. TENNYSON, Assistant Attorneys General, 1400 South Evergreen Park Drive Southwest, Post Office Box 40128, Olympia, Washington 98504.

AVISTA CORPORATION, by DAVID MEYER, General Counsel, East 1411 Mission, Spokane, Washington 99202.

THE PUBLIC, by SIMON J. FFITCH, Assistant Attorney General, 900 Fourth Avenue, Suite 2000, Seattle, Washington 98164-1012.

Kathryn T. Wilson, CCR
Court Reporter

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P R O C E E D I N G S

JUDGE CAILLE: This is the third day of hearings in the cross-examination of Avista's rate case filings in Dockets UE-991606 and UG-991607. The parties have previously entered their appearances. Mr. DeFelice was sworn in yesterday and his exhibits are admitted, and we are ready to begin his cross-examination.

MR. TRAUTMAN: Thank you, Your Honor.

CROSS-EXAMINATION

BY MR. TRAUTMAN:

Q. Good afternoon, Mr. DeFelice, I'm Greg Trautman, assistant attorney general for the Commission staff. If you could turn first to your prefiled testimony, Exhibit T-290. Do you have that?

A. Yes, I do.

Q. Looking at Page 1, Lines 15 through 18, do you there describe your job responsibilities as including financial analysis, tariff administration, and other regulatory processes?

A. Yes, I do.

Q. Would it be correct then that depreciation analysis is not one of your responsibilities?

A. Not on a day-to-day basis.

Q. What do you mean by that?
A. I typically will sit down with our depreciation analyst from time to time to go over depreciation issues as need be, and prior to that, I worked on the depreciation desk for two years in the late '80's and have been involved with the depreciation study with Deloitte and Touche at that time.
Q. Lines 20 to 22 of that page, you indicate that the scope of your testimony covers the Company's proposed changes in depreciation rates; is that correct?
A. That's correct.
Q. Are you testifying as a depreciation expert in this case?
A. Yes, I am.
Q. Have you testified as a depreciation expert before?
A. No, I have not.
Q. Have you ever conducted a depreciation study?
A. I've been involved with a depreciation study that Deloitte and Touche has conducted.
Q. Deloitte and Touche conducted the study; is that correct?
A. That's correct.
Q. You did not conduct the study; is that

correct?
A. Yes.
Q. Is it correct that in September of 1999, Avista provided Staff with a copy of a document from Deloitte and Touche titled, "The Washington Water Power Company Book Depreciation Study"?
A. That is correct.
Q. Does Exhibit 291, which was your Exhibit No. 33, does that show the depreciation rates resulting from the study?
A. Yes, it does.
Q. Was the study prepared by you or under your direction?
A. The study was prepared by Deloitte and Touche along with folks from the finance department.
Q. Does the finance department prepare the data?
A. Yes, they do.
Q. Back to your testimony on Page 1, Lines 12 and 13, you indicate that you were involved in the Company's 1990 depreciation study; is that correct?
A. Specifically, the study was conducted in 1998 that I was involved with, and then in 1989, I was involved in a study of additional plant that had not been studied the year before, and then I changed jobs during the middle of the study process.

Q. Is it correct that with the 1990 depreciation study that the Staff and Company were able to resolve depreciation issues informally?

A. Yes, that's correct.

Q. Is it correct that the 1990 depreciation study was not filed as part of a general rate proceeding?

A. That is correct.

Q. Do you know why the Company decided to file a current depreciation study as part of the general rate case in this proceeding?

A. Basically, you might say the cycle for analyzing our fixed assets was due to be analyzed with the depreciation study, and given that there is a change being recommended, it was included in the rate case for that matter.

Q. Would you agree that a depreciation study should be done every five years?

A. I don't know that there is any set number, but they should be done. They need to be done periodically.

Q. Is it correct that the Commission staff reviewed the Deloitte and Touche study and provided you with its recommendations regarding depreciation parameters?

A. Yes, that is correct.
Q. And is it correct that you informed the Staff that the Company would not agree with the Staff recommendations?
A. That is correct.
Q. At this point; is it the Company's position that the Commission should decide the unresolved depreciation issues?
A. Yes.
Q. In your view, what are the outstanding depreciation issues that the Commission should decide?
A. Specifically, the service lives on certain general plants accounts pertaining to high-tech equipment, net salvage factors for distribution and transmission plant, the change in the interest rate on the sinking fund, depreciation method for hydroplant, and net salvage issues on steam production plant.
Q. Did the high-tech accounts that you refer to include computer and communications?
A. Yes.
Q. The Deloitte and Touche depreciation study has not been filed as an exhibit in this case; is that correct?
A. That is correct.
Q. Does the Company intend to provide testimony

in this case regarding the depreciation issues that it has not been able to resolve with Staff?

A. Yes.

Q. When?

MR. MEYER: Your Honor, if I may, part of the confusion is we are sponsoring a depreciation analysis. Until Staff and Intervenors file their case, the issues haven't been joined. When the issues are joined, if matters are not otherwise settled in the mean time, then our rebuttal will respond to the issues raised by Staff and other parties, so I'm troubled by the question.

MR. TRAUTMAN: I don't know what the trouble is. This is the Company's depreciation case. We have asked whether they filed a study, and they said they did not, and we asked whether they filed testimony to resolve the issues outstanding and they said they had not, so I think it's entirely appropriate to ask when the Company intends to file testimony to support its case.

MR. MEYER: Your Honor, we have. Mr. DeFelice's testimony, as well as Exhibit 33, are the results of the depreciation study and form the basis for the depreciation adjustment. That is our direct case. If Staff chooses to take issues with two, three, four, however many components -- it's their prerogative -- then we will respond to those issues once they have been joined. We have a case in on this.

MR. FFITCH: Your Honor, may I be heard on this point as well?

JUDGE CAILLE: Yes, Mr. ffitch.

MR. FFITCH: I move to respond in addition to Staff because of the representation that the Company's main case with respect to these contested issues may not be presented until rebuttal, so for the record, I would like to make a formal request that Public Counsel and other parties as well be provided an opportunity to file surrebuttal testimony in response to, essentially, what sounds like will be the chief testimony on these issues from the Company.

JUDGE CAILLE: Any response, Mr. Meyer?

MR. MEYER: Yes. I don't know where Public Counsel inferred that we haven't filed our case with respect to depreciation. Our case is set forth. Mr. DeFelice's Exhibit T-290, as well as in his Exhibit 291, that is the direct case upon which we have proformed depreciation. That is our case. It is not up to us then to anticipate the issues that other parties may have with what we are proposing. That's their job. When they respond, we will, as the schedule

contemplates, file our rebuttal testimony. We have a case. It's already in.
MR. TRAUTMAN: May I respond?
JUDGE CAILLE: Just a moment, please. I specifically would like a response to Mr. ffitch's proposal that they file surrebuttal testimony in the event that your case -- what we don't want to have happen here is that in the Company's surrebuttal case we get all these new issues that haven't been addressed, so if you could respond to Mr. ffitch's proposal about other parties filing surrebuttal to whatever this testimony may be.
MR. MEYER: If we go that route, think of where that leads us. In every piece of direct testimony that we file that seeks to make its case, are we to anticipate with perfect foresight every issue that Staff and Public Counsel may raise with regard to an adjustment? In this case it happens to be depreciation. Obviously, no.
Our responsibility is to present the direct case, providing material support for any adjustments we've made. We've done that. It is up to Staff and Intervenors to identify issues they may have and challenge our direct case with their case. Once that's done, we'll file our rebuttal. It would be highly

unusual for us to have to anticipate each and every issue and then provide, not only for this witness but for any other witness, surrebuttal opportunities. That turns the hearing on its head.

MR. TRAUTMAN: The difficulty is that this is this Company's depreciation case. They are asking for changes in depreciation rates. There is no study that's been filed. That study would be the basis of what Staff would base its analysis on, as I imagine the Commission would as well. That study has not been filed. For Staff to be required to essentially wait until July or June and not have any testimony by the Company until then, it seems entirely unfair, and Staff will join the request for surrebuttal, and we would add that we've addressed this issue in previous cases.

MR. MEYER: Your Honor, we've had --

JUDGE CAILLE: I've had enough argument, thank you.

(Discussion off the record.)

JUDGE CAILLE: I'll just make the point that, as Mr. Meyers said, you do have to support your depreciation study, and at this point, I do think it's a bit premature to rule on whether there should be surrebuttal testimony. We would entertain a motion for surrebuttal, but at this point, we will just take it under advisement, and let's move on.

Q. (By Mr. Trautman) Turning to Exhibit 291 again, Page 1 of this exhibit shows a proforma adjustment increasing electric plant depreciation expense by approximately 6.7 million dollars; is that correct?

A. On a system basis, that's correct.

Q. Turning to Page 2, does that show a proforma adjustment increasing the gas plant depreciation expense by about $796,000?

A. On a system basis, that's correct.

Q. Is the bulk of the increase due to the Company's proposal to increase the cost of removal component of net salvage and to use a lower service life in the computer equipment account?

A. Yes, it is.

Q. Could you now refer to what's been marked as Exhibit 302. This is a portion of the Washington Water Power Company Book Depreciation Study of Electric Properties as of December 31st, 1997, and it includes pages discussing salvage and cost of removal analysis; do you have that?

A. Yes, I do.

Q. Directing your attention to Page 13, in the middle of the page, there is a sentence that reads,

"Cost of removal factors are understated because the amount of inflation reflected in the cost to remove young property is much less than the amount that will be reflected to remove the surviving property." Do you see that?
A. Yes, I do.
Q. What evidence in the study or in this case has been provided to support that statement?
A. In the work papers of the study, in the consultant's analysis of various accounts, the retirements that took place in some of those accounts were at an age that is less than the average service life for the account, and from that, this statement was derived.
Q. Does the cost of removal adjustment reflect the theory that labor costs are increasing over time and that cost of removal estimate should reflect those anticipated increases?
A. Indirectly, it does.
Q. If you could now turn to what's been marked as Exhibit 303. This is a page in the upper right-hand corner it says, "Depreciation System DSALVGO1, The Washington Water Power Company." Do you see that?
A. Yes, I do.
Q. Do you recognize this sheet as part of the

salvage analysis work papers for the gas mains account from the Deloitte and Touche study?
A. Yes, I do.
Q. Does the sheet show the historic salvage data for the gas mains account?
A. Yes, it does.
Q. Looking at the first column of the sheet under the word "year," the column shows successive bands of years of data showing all the data and then decreasing each year; is that correct?
A. That's correct.
Q. Is this called a shrinking band analysis?
A. Yes.
Q. Looking over to the column labeled cost of removal, in particular the ratio percentage, is it correct that the cost of removal has been trending down since 1993?
A. By a very small amount.
Q. Do I not see it trending down from 65 percent to 35 percent? Is that a small amount?
A. I feel like it is, yes.
Q. How does this data support the premise for the cost of removal adjustment proposed in the depreciation study that the cost of removal is increasing over time?

A. I think what this analysis shows is that the cost of removal that is in the current rates is less than what this particular analysis shows, and then the resulting recommended removal rate was derived from this.
Q. So you believe this data does support that?
A. Yes.
Q. If wages are increasing over time but the cost of removal is decreasing, wouldn't you agree that there are factors affecting the level of removal cost other than inflation?
A. Possibly.
Q. Do you know?
A. I don't know for sure what those may be.
Q. So the Company did no study of this?
A. No, we did not.
Q. Regarding the computer equipment account, is it correct that the Company is asking for a change in the service life of this account from eight years to five years?
A. That is correct.
Q. Turning to Page 8 of your testimony T-290 on Lines 17 to 18, is it correct that the Company is saying that the computer equipment lives were reduced from eight to five years to more appropriately reflect

asset turnover?
A. Yes.
Q. Is the term "asset turnover" the same as retiring asset or otherwise removing it from service?
A. Yes.
Q. Does the analysis of the retirement experience of this account support your request for a five-year life?
A. The decision to go from eight to five years was based upon our forecasted estimates of turnover in that account. The historical experience in Account 391 Sub 1 was not utilized for that estimate due to the fact that that account is under a fixed amortization accounting process.
Q. Is that a yes or a no to my question?
A. Could you rephrase the question?
Q. Does the analysis of the retirement experience of this account support your request for a five-year life?
A. The retirement experience was not the basis for the recommended change.
Q. Is it correct that there is about 10 million dollars of investment in the computer account?
A. That is correct.
Q. Can you explain the basis for the Company's

request to use a five-year life for this account? Has Staff audited the account to confirm the nature of equipment in this account?
A. Commission Staff?
Q. Yes.
A. Not to my knowledge.
MR. TRAUTMAN: As our next record requisition, we would request the Company to provide an inventory listing for the computer equipment account.
JUDGE CAILLE: Can the Company provide that?
MR. MEYER: Is that doable?
THE WITNESS: I believe so.
MR. MEYER: Then we can.
JUDGE CAILLE: That would be Record Request No. 18.
Q. (By Mr. Trautman) And that would be for Account 391.1?
A. Yes, that's correct.
Q. How much of that investment is related to equipment on a three-year lease?
A. The equipment that will be leased actually was began to be leased in '98 and '99 is roughly about one-and-a-half to two million dollars.
Q. If you were to calculate a weighted average service life for the computer account investment using

a three-year life for two million dollars of the investment, the least portion, and an eight-year life for the remaining eight million dollars of computer investment, would you agree or accept subject to check that the weighted service life would be seven years?
A. Subject to check, I would accept that.
Q. Is it correct that Commission Staff proposed that the Company use a six-and-a-half year life for the computer account?
A. That's correct.
Q. Did the Company reject that offer?
A. Yes, we did.
MR. TRAUTMAN: I have no further questions.
JUDGE CAILLE: Mr. ffitch?
MR. FFITCH: I do have some questions, Your Honor, if I might have just a moment to set up my materials.

CROSS-EXAMINATION

BY MR. FFITCH:
Q. Good afternoon, Mr. DeFelice. I'm Simon ffitch, the assistant attorney general with the Public Counsel's office, and my first question is, do you have in front of you the cross-exam exhibits that have been identified for Public Counsel? They are numbers 292

through 301, and the first one on top is the response to Data Request 74.
A. Yes, I have those.
Q. I'd like to start out by briefly discussing your use of sinking fund depreciation with hydraulic production plant. I've drawn the enviable mid afternoon slot for cross-examining on depreciation matters, so I'm going to try and speak quickly and energetically and use gestures and so on.
CHAIRWOMAN SHOWALTER: Mr. ffitch, just your opening phrase of sinking fund depreciation on hydraulic something or other was enough to --
MR. FFITCH: Create a sinking feeling, perhaps?
CHAIRWOMAN SHOWALTER: I was trying to write it down.
MR. FFITCH: Sinking fund depreciation with hydraulic production plant; in other words, dams.
Q. (By Mr. ffitch) First I'll just ask you to look at your direct testimony on Page 2 beginning at Line 21, a quick reference there. There you say that it should be noted that the Company continues to employ the sinking fund methodology for determining the depreciation expense of its hydroelectric generating facilities; is that correct?

A. That's correct.

Q. Your calculation of depreciation for hydroplant appears on your Exhibit 33, which we have marked as 291, and specifically, on Pages 5 and 6; is that right?

A. That's right.

Q. Are the rates that you show on Exhibit 33 or what we've now marked as 290, Page 5, Column 9 --

MR. MEYER: Do you mean 291, Page 5?

MR. FFITCH: I stand corrected. It is 291. The direct is 290.

Q. I'm looking at Page 5 of 291. I'm looking at Column 9 with the heading "study rate percent." My question is, are these the actual proposed rates, the actual proposed rates for the test period, or are they the composite of the rates that are actually to be applied to each individual account for the test period?

A. They are the composite rates of the annuity factor and interest rate factor.

Q. Now I'd like to refer you to what has been marked for identification as Exhibit 292, which you should recognize, I hope, as the Company's response to Public Counsel Request No. 74.

A. That's correct. I have those.

Q. Is the response to this request true and

correct to the best of your knowledge?
A. Yes, it is.
Q. And the sinking fund methodology was adopted by the Company for hydroelectric plant in 1950 or possibly even earlier; is that correct?
A. That's correct.
Q. And you've indicated in this response, specifically in Part B, that the Company does not actually maintain a sinking fund or replacement fund where it accumulates funds from this depreciation source; is that correct?
A. That's correct.
Q. So the funds collected from depreciation hydroelectric plants are used for the current needs of the Company; is that true?
A. They just go into the general fund of the Company.
Q. When one is depreciating a single asset, is it true with sinking fund depreciation -- I'm sorry. I think I wanted to follow up a bit more before I got onto that so I'll withdraw that question for the moment.
There are variations of the sinking fund depreciation method; correct?
A. I believe so.

Q. The sinking fund or compound interest method can be applied with either depreciated or undepreciated rate base for depreciable rate base; correct?
A. I'll have to think about the question that you asked.
Q. Would you like me to restate it?
A. Yes.
Q. I'm asking you whether the sinking fund method can be applied with either a depreciated rate base or an undepreciated rate base?
A. A depreciated rate base was your term?
Q. Yes. Would you like an explanation of that term; do you need one?
A. The question is fairly unclear to me.
Q. You are not familiar with the term "depreciated rate base" versus "undepreciated rate base"?
A. Yes, I'm familiar with that.
Q. Would you like me to rephrase the question?
MR. MEYER: If you don't understand the question -- you need to understand the question first.
THE WITNESS: I'll have to have you rephrase the question.
Q. (By Mr. ffitch) When I refer to depreciated rate base, I'm referring to net rate base and plant,

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and when I'm referring to undepreciated, I'm referring to gross plant before the subtraction of accumulated interest.

A. Okay.

Q. Accumulated depreciation, excuse me.

A. The way our sinking fund calculation works is the annuity factor is applied to the average ghost plant balance, and the interest rate factor is applied to the beginning depreciation reserve account.

Q. Is that before deduction of accumulated depreciation?

A. On the annuity factor?

Q. Yes.

A. No, it's not.

Q. Let me go back to the topic I started to ask you about a moment ago. When one is depreciating a single asset, is it true with sinking fund depreciation that the annual depreciation charge becomes larger as the plant ages?

A. Yes, that is true.

Q. So in theory, at least, with the sinking fund depreciation methodology, in the first year of the plant's life, the annual depreciation charge is the smallest, and I'll use gestures here, and in the last year of its life, the annual depreciation charge is the

largest; is that true?
A. That's true.
Q. So the sinking fund methodology is sort of the reverse of an accelerated depreciation methodology, would you say?
A. Yes, it is.
Q. To state it another way, with sinking fund, the annual charges for depreciation would be lower than average in the first half of the plant life and higher than average in the last half of the plant's life; wouldn't that generally be true?
A. Generally, yes.
Q. Is it true that the Commission, if it approves your proposal, will not be approving a specific set of rates for hydroelectric plant because the sinking funds rates are recalculated and change each year?
A. The composite rates change. The nominal rates would stay the same.
Q. Could you define "nominal rates," please?
A. The annuity factor and the interest rate factor that I spoke of earlier would stay the same each year, and given that the beginning depreciation reserve balance increases each year, that would increase the composite rate minus any other retirements or addition

activity.
Q. So in general, if you know, in the composite, is the remaining service life of the Company's hydraulic production plant, such as hydroelectric dams, is it approximately two-thirds to one half of the overall average service life at this time? I'm trying to get some idea of where we are with the age of the hydroelectric plants in the composite.
A. I would have to check on that specifically because it would be different for each plant, given that some plants have been refurbished here in the last several years.
Q. I understand that you apparently feel the need to check on this, but what I'm asking you is for a composite number, a weighted number for all of the plant together rather than specific individual plants. Do you have an ability to answer that question with regard to all the plant?
A. Only in generality.
Q. In generality, what would your answer be?
A. I would say they are around 50 percent.
Q. So for hydroelectric plant with no new additions, no new dams, we're rapidly approaching the period in which the average depreciation charges will be larger than average in the last half of the plants'

lives; is that true?
A. Generally.
Q. Could I ask you to look at Page 8 of your testimony, which is Exhibit 290, at Lines 9 through 11. There you state that a primary cause of the increase in hydraulic production plant was the recommendation to update the interest rate included in the sinking fund calculation from the old rate of six percent to nine percent to better reflect the Company's current cost of capital; that is correct?
A. That is correct.
Q. My question is, if you increase the sinking fund interest rate, that will also, of course, increase the annual depreciation expense for hydroelectric plant, will it not?
A. Yes, it will.
Q. Do you understand what I mean when I say, "present worth depreciation"?
A. I've heard that term synonymously with sinking fund.
Q. So is what the Company really using here sinking fund depreciation, or is it present worth depreciation?
A. My understanding is those two methodologies are maybe subtly different in their mechanics, which

I'm not familiar with specifically, but substantively, they are pretty much the same.

Q. Can you agree with the statement that sinking fund and present worth depreciation methods produce the same result if the same interest rate is used?

A. I could agree to that.

Q. If you know, isn't it the case with present worth depreciation that the interest rate is set at what is considered a fair return or the Company's cost of capital; is that correct?

A. I believe so.

Q. And you have indicated that your objective is to move the sinking fund rate closer to the Company's cost of capital; correct?

A. Right.

Q. You agreed earlier that the sinking fund depreciation methodology produces annual depreciation charges that increase with the age of the plant. I'll refer you back to the response to our Data Request 74, which is Exhibit 292. There you state in answer to Subpart A -- the question in A is, "Why does the Company feel that sinking fund is appropriate for hydroelectric generating facilities?"

Your answer is, in part, the last sentence of your answer: "In addition, the Company believes that the sinking fund method results in a systematic allocation of costs that continues to be equitable with customers." Is that correct?

A. That's correct.

Q. By "allocation of costs," do you mean the annual depreciation charges associated with the overall cost of the plant?

A. Yes.

Q. Under the sinking fund methodology, since the depreciation charges increase with age, essentially what happens is that the charges become larger as the Company's customer base grows and the load factor of the plant increases; isn't that true?

A. The amount of depreciation expense increases with time.

Q. Also, concurrently the expense increases along with the growth of the customer base and the load factor; isn't that the case?

A. Yes.

Q. I guess my question is, is this why you consider the methodology equitable to consider customers because, in essence, it weights and allocates the cost to the larger customer base?

A. That's one perspective. I think the other is that over time on a constant dollar basis, the argument

would be that with the interest rate set at a level close to or equal to the Company's allowed rate of return, it tends to levelize the revenue requirements associated with operating those plants.
Q. I'm going to ask you now to turn to Page 6 of your Exhibit No. 33. That's Exhibit 291. Nearly at the bottom of the page right above the heading, "northeast turbine plant," on the far right-hand column, this shows the net increase in depreciation expense associated with hydraulic production plant as a $1,003,943; is that correct?
A. That's correct, on a system basis.
Q. The far right column reflects the increase or decrease for each of the categories shown on that page, does it not?
A. Yes, it does.
Q. Subject to check, this is approximately 15 percent of your total depreciation proforma expense increase; is that right?
A. That's correct.
Q. I'd like now to turn to some questions about computer equipment, following up on the area that was touched on by Staff, and refer you to Page 8 of your direct testimony, first of all, beginning at Line 16. Starting at Line 16, and I think you may have already

answered this in response to Staff, but you state that the computer equipment lives were reduced from eight to five years to more appropriately reflect asset turnover, don't you?
A. Yes, that's correct.
Q. And then if we go to Exhibit 291, your tables, you go to Page 8, we see that the amount associated with that is $2,690,000; is that correct? That's an increased amount?
A. That's correct.
Q. And that's shown, the account number on the left side of the page is 391.1, computer equipment, and then the figure we've just mentioned is on the far right-hand side of the page.
A. That's correct.
Q. At the bottom of the page, the second line from the bottom in the category "total common plant," you show a total increase of $3,345,204, and again, that's in the far right-hand column; correct?
A. That's correct.
Q. So the proposed increase in the rate for computer equipment is a fair piece of the increase in general or common plant total; right?
A. That's right.
Q. Would you accept subject to check that it's

just a tad bit over 80 percent of the increase?
A. I'll accept that subject to check.
Q. The proposed increase in this one single account for computer equipment is over two-and-a-half times larger than the impact of all the Company adjustments in the hydroelectric plant; is that correct?
A. That's correct, on a system basis, right.
Q. I'm going to refer you to what has been marked for identification as Exhibit 293, and that is the Company's response to Public Counsel Data Request 78, and was that prepared by you or under your direction?
A. Yes, it was.
Q. And it's true and correct to the best of your knowledge?
A. Yes.
Q. And the response to this request confirms that you are proposing to increase the computer equipment depreciation rate by 34 percent; is that correct?
A. That's correct.
Q. Now I'm going to refer you to Exhibit 294, and do you recognize this as a sheet from the Company's depreciation study relating to this account 391.1

computer equipment?
A. Yes, I do.
Q. And the exhibit shows that you are using any remaining life of 1.66 years in the calculation of the rate, doesn't it?
A. Yes, it does.
Q. And that's shown in the right-hand column under the heading "current study."
A. That's right.
Q. And obviously, on the third line opposite the term remaining life.
A. Uh-huh.
Q. And the salvage value, likewise, is shown in that column directly underneath as zero. That's right for salvage value?
A. That's right.
Q. And the existing rate that the Company is currently using is based upon an assumed remaining life 3.69 years; is that correct?
A. That's correct.
Q. With an assumed salvage value of 10 percent?
A. That's correct.
Q. To mathematically calculate the proposed depreciation rate, we subtract the reserve ratio and the net salvage ratio from one and then divide that

result by the remaining life period; is that correct?
A. That sounds correct, subject to check.
Q. So in this instance, we would divide by a remaining life of 1.66 years.
A. That's right.
Q. And can you accept, subject to your check, that using the appropriate reserve ratio from this case and subtracting that from one and subtracting a net salvage of zero from one, dividing by 1.66 as the remaining life, yields a proposed rate of 36.08, which is the number you are proposing for this account?
A. That's correct.
Q. So in the mathematical calculation of the rate, it's the remaining life of 1.66 years that directly affects the level of the rates; is that true?
A. That's true.
Q. So although you testified at Page 8 of your testimony, which we referred to earlier, that you reduced the lives from the eight to five years, it's not the five-year life that directly affects the calculation; isn't that true?
A. Actually, the five-year life does affect the calculation because it does affect the remaining life as well. The remaining life calculation is a true-up of the theoretical reserve to the actual reserve.

Q. But if we substituted five years in the calculation for 1.66 years, would you accept, subject to check, that mathematically, at least, that would yield a depreciation rate of 12.01 percent as contrasted with 36.08 percent?
A. Subject to check, I'll accept that.
Q. I'd like to ask you to just turn back one exhibit to Exhibit 293, which is, again, our question and your response to Data Request No. 78, and there you say in your answer, third sentence, "It is the Company's expectation that minimal new assets will be added to this account after 1998, and beginning in '99, the Company is utilizing a three-year lease agreement for all PC's and related software"; is that correct?
A. That's correct.
Q. So if there are no new additions to the computer equipment account after 1998, then the remaining plant, which had a remaining life of 1.6 years in 1998, on average, at least, would now in the year 2000 have a remaining life of nearly zero; isn't that right?
A. That's right.
Q. So if we assume no new additions by the conclusion of this proceeding, the remaining life on average would be zero for this account.

A. It would not be technically at the end of this proceeding because the new rates would have to go into effect in order to create the result that you just described.

Q. Looking still at this Exhibit 293, the request asks in a regulatory setting, "Is it the Company's position --" this is in the final sentence of the request. "Is it the Company's position that a depreciation rate of 36.08 percent will prospectively reflect a five-year average service life as indicated in Mr. DeFelice's testimony," and your answer is no; is that correct?

A. That's right.

Q. At Page 9 of your testimony, which is Exhibit 290, and I'll give you a minute to go back to that, at Lines 7 and 8 -- do you have that?

A. Yes, I do.

Q. -- there you indicate that an average of five years is a better reflection of the overall assets in this account. That is the case even with the three-year lease program; is that correct?

A. That's correct.

Q. When the Company replaces a computer, a personal computer, does the Company also generally replace the monitor?

A. Generally, yes. That's my understanding.
Q. You indicate that the increase in the computer equipment depreciation rate is driven by technological obsolescence; is that correct?
A. That's correct.
Q. So is it your opinion that every employee, no matter what function they are performing within the Company, even if they are only doing word processing, need to have their entire computer equipment replaced every three years?
A. That's the current plan under the refresh lease program.
Q. Advanced Micro Devices, Incorporated, recently announced it had the first gigahertz computer chip ready for market, and Intel made a similar announcement about a day or so later. I think this was in the news early in March. Did you hear this news?
A. No, I did not.
Q. We're now at the point where personal computers have very significant amounts of storage and memory. Do you still see a future where the Company will, on average, have to replace its computers every three years in order for each and every employee to serve the needs of its customers?
A. I'm not qualified to answer that. You would

have to direct that question to experts in that field at our company.

Q. Is there someone who has not yet testified from the Company that I could direct that to?

A. No.

Q. Anybody that has testified so far in the hearing that I should have asked that question?

A. Not that I know of, no.

Q. Are you familiar with the Financial Accounting Standard Boards Statement No. 13 -- that's initial caps, FASB -- regarding accounting for leases?

A. Not particularly, no.

Q. Are you aware that that standard requires under certain conditions that leases be capitalized?

A. Yes.

Q. Do you know if the lease arrangements the Company has entered into regarding computer equipment will require a capitalized lease accounting treatment?

A. I've been told by the finance department personnel that those leases will be expensed.

Q. Those operating leases will be expensed?

A. Yes.

Q. Do you know the annual lease expense for computer equipment in 1999?

A. We have provided that to you in -- let me back up. We have prepared that information for you in Data Request No. 100, which I don't believe has been submitted to you yet.

Q. You are correct that we did have an outstanding DR, and at last check, we didn't have the answer yet. Do you have before you now the answer to that question?

A. Yes, I do. In 1999 was your question; is that correct?

Q. Correct.

A. For Washington electric operations, the annual lease expense in 1999 was $257,851.52.

Q. What was the depreciation charge for account 391.1 in 1999?

A. For Washington electric operations, it was $447,895.

Q. I'll refer you now to your testimony once again to Page 8, Line 18. There you state, "Account 397, communications equipment, lives were reduced from 18 to 10 years to better reflect the type of asset --" I'm sorry. I'm maybe getting ahead of you. Have you found that place?

A. Yes.

Q. "Communication equipment lives were reduced from 18 to 10 years to better reflect the type of asset

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being installed"; is that right?
A. That's right.
Q. We'll find reference to that account also in Exhibit 291, again, your Attachment 33, and that's on the bottom of Page 7, three lines up from the bottom. The general heading near the bottom is "general plant utility." This is the third line up, Account 397.0, communications equipment, and on the far right-hand side of the page, we see that the increase in this account is $583,900; is that right?
A. That's right.
Q. And if we look over at Page 8, again in the general plant category, two-thirds of the way down the page, 397.0, communications equipment, we look over in the far right-hand column, we see an increase of $248,138; is that right?
A. That's correct.
Q. So there is a total increase in Account 397.0 of $832,062; is that correct?
A. Actually, no it's not correct. There is another line item in "utility," Code 7 on Page 8.
Q. Okay. So can you direct me to the correction that I need to make in that calculation?
A. Sure. On Page 8 of Exhibit 291, from the line that you just identified a moment ago, 397 Sub 0

under "general plant utility 9", if you look up to the next grouping of accounts under "general plant utility 7," there is Account 397 Sub 0 as well.
Q. I see that. So total of those is actually approximately $1,065,000?
A. On a system basis reallocated, that's correct.
Q. If you look at any one of those lines that we've referred to, each of them indicates in Column 4 the existing rate, and in Column 9, study rate, and we are moving -- in each case, they reflect that in this account we are moving from seven percent to 11.9 percent?
A. That's correct.
Q. And again, subject to employment of a calculator, that amounts to an increase of 59.86 percent, does it not?
A. Generally, that's correct.
Q. And if we add that amount, that $1,065,000, add that to the increase of $2,690,000 for the computer equipment account, which is 391.1, that pretty much explains the total increase in common plant of 3.3 million dollars, does it not?
A. Yes, it does.
Q. Let me ask you to go to Page 1 of the same

exhibit, again, Exhibit 291. If you look at the column labeled "proforma adjustment," which is the third column in the right, at the bottom of the column, the amount shown for total electric plant, the total adjustment to depreciation expense is $6,762,000 before allocation to Washington and Idaho; correct?
A. That's correct.
Q. So the proposed increases in computer equipment and the communications equipment account represent roughly half of your proforma adjustment to electric depreciation expense; is that correct?
A. That's correct.
Q. I'd like to now turn to the most exciting part of my cross-examination as we have pictures now. Going to Exhibit 295, these are a series of graphs. These are 11 pages of graphs from the depreciation study, are they not?
A. Yes, they are.
Q. This study is actually 1,800 pages in size, is it not?
A. I'll take your word for it.
Q. Unfortunately, I believe we had it produced to us so I have some sense of the scale. Now that we have these in hand, I'm going to ask you just to check back to your testimony at Page 4. At Line 18 you

state: "From this, actual survivor curves were visually fitted to Iowa type standard curves."

In Public Counsel Request No. 75, we asked you to provide copies of these visual comparisons. Your response was: "The only recorded visual Iowa curve fits are those included in the depreciation study work papers." That was your response; right?

A. That's correct.

Q. So do these graphs in Exhibit 295 represent that described analysis and the visual comparison which you mention in your testimony?

A. Yes. Those were the curves that the consultants supplied to us. What we referred to in the response, in the data request, was the fact that the curves that were, in essence, thrown out through the interdivisional process were not provided to us.

Q. The first page of this exhibit, really the first graph, is a summary of the results of the analysis for computer equipment for various lengths of time or bands, the last five years, the last 10 years, so on; is that correct?

A. That is correct.

Q. The shapes or the markings on the various curves are explained by a legend at the bottom of the page, are they not?

A. Yes, that's right.

Q. If we turn to Page 2, we see an analysis for the period of 1968 through 1997; isn't that right?

A. That's right.

Q. There are two lines plotted on the graph on Page 2. One line has little boxes along the way. The other does not. Can you tell us what these two lines represent?

A. The line with the little boxes is the depiction of the actual retirement history, the survivor curve resulting from the actual retirement history, excuse me, and the curve on the left that is unmarked is a five-year R-3 curve.

Q. An Iowa curve.

A. Yes.

Q. Then at the bottom of the graph, there is a marking which states, "5-R 3.0." Can you tell us what the 5 represents there?

A. Five-year average service life.

Q. The actual line, which is the line with the boxes to the right of the Iowa curve, crosses the 50 percent line on this graph at about eight or nine years; isn't that correct?

A. That is correct.

Q. If we look through the graphs on Pages 3, 4,

5, and 6, the next four pages, we would see a very similar result; would you agree?
A. Yes, that's correct.
Q. These are all comparisons with the Iowa R-3.0 curve again, are they not?
A. That's correct.
Q. We are up to Pages 7 through 11. This is a similar analysis except that the comparison is with the Iowa type survivor curve S-2.0; is that right?
A. Yes, that's correct.
Q. And all of these graphs show the plotted lines crossing the 50 percent line from eight to nine years; isn't that right?
A. On Pages 7 and 8 and 9?
Q. Actually, 7 through 11.
A. That is correct.
Q. Does that mean that 50 percent of the computer equipment is retired before eight or nine years, and 50 percent is retired after eight or nine years?
A. In this case in this account, that's not true.
Q. Is that because the S curve is not a symmetrical curve?
A. No. The reason that is is that account I

referred to earlier is under a fixed amortization method of recordkeeping whereby there is not specific asset identification for retirement in that we don't have a dispersion of retirements across all years.

Basically, the way the accounting works, and I'm referring back to a memo the Company provided to the Commission back in 1993 whereby the dollars, the vintage dollars, are tracked, and when those vintages reach eight years old, that entire vintage is retired from that property account.

Q. So are you testifying that these graphs do not reflect an average service life of eight or nine years?

A. The recorded history indicates that we have been experiencing an eight-year life on that account.

Q. Thank you. Just doing a visual comparison, it appears that the S-2.0 curve comparisons on Pages 7 through 11, the second group that we looked at, produce a tighter fit with the S-2.0 curve than the first set of graphs fit the 3.0 curve; isn't that right?

A. Right.

Q. Let me ask you a couple of questions about the R-3 curves that we've been talking about here. An R curve means the mode was located to the right of the curve's average life; isn't that right?

A. That's correct.
Q. By "mode," I mean the highest point of the retirement frequency curve where essentially the largest number of the studied populations retirements occur; is that right?
A. That's correct.
Q. And on the other hand, with an L curve, the mode is to the left; is that right?
A. That's right.
Q. And an S curve means that it is symmetrical with the average life; correct?
A. Right.
Q. The R-3 curve in the exhibit means -- again, those were the first six pages of the graphs. The R-3 curve means that it would have less dispersion or standard deviation than an R-0, R-1, or R-2 curve; is that right?
A. I believe that's right.
Q. And the S curve means that the mode or highest point of the retirement frequency curve is symmetrical to the curve's average life?
A. That's correct.
Q. Let me refer you to Exhibit 296. Do you recognize that as an excerpt from depreciation work papers regarding the 391.1 account?

A. Yes, I do.

Q. On this exhibit in the right-hand column, this shows the conclusion was that the S-2 curve with eight to nine years of average service life, or ASL, was a better fit than the curves used in the prior study; is that correct?

A. That's correct.

Q. Curves used in the prior study are shown under the heading "prior curve," are they not?

A. Yes, that's right.

Q. However, on Exhibit 294, which we referred to earlier, that shows that the Company adopted a five-year average service life with an SQ curve. That's Q as in quick rather than S-2. That's what the Company did; is that right?

A. That's right.

Q. As shown on Exhibit 294, the Company is proposing a depreciation rate of 36.08 percent as you've stated; isn't that right?

A. Right.

Q. That rate of 36.08 would recover the Company's investment in less than three years; right?

A. As of the balance at the end of the test year when the rate gets put into effect, that's correct.

Q. I'll ask you now to turn to Exhibit 297,

which is our second set of graphs. Do you recognize these as graphs from the depreciation study regarding Account 397?
     A.   Yes, I do.
     Q.   And that's the account for communications equipment?
     A.   That's correct.
     Q.   This represents the same type of analysis we just reviewed for computer equipment; correct?
     A.   That's correct.
     Q.   In this case, the depreciation study compared historical experience with an L-1, L-2, L-3, and S-2 Iowa type survivor curve; is that true?
     A.   Yes, that is correct.
     Q.   Those curves are actually indicated at the bottom of each page after the time period reference; isn't that right?
     A.   That's right.
     Q.   As indicated at the bottom of Pages 2 through 6, the indicated average service life was from 20 to 22 years, and there, I'm looking at the number that's right in the front of the curve designation for each graph.
     A.   That's correct.
     Q.   Now if I could ask you to turn to Exhibit

298, and again, do you recognize this as two pages from the Company's depreciation study work papers?

A. Yes, I do.

Q. And these relate to Account 397 for communications equipment; right?

A. That's correct.

Q. If you look at Page 2 of this exhibit, it shows for the current study an average service life of 20 to 22 years, and that's under the column headed "current ASL"; isn't that right?

A. That's right.

Q. However, on the line marked "selection," which is right above the dollar amounts there, it shows 10 years for curve L-2; do you see that?

A. Yes, I do.

Q. And also on Page 2 at the bottom under the notes, it says, does it not, "longer ASL --" average service life -- "longer ASL indicated by technology advances and limits ASL changes"; do you see that?

A. Yes, I do.

Q. And if you turn back to Page 1 of this exhibit, it shows that the Company adopted an average service life of 15 years. That's shown on the top line under "current study" on the right-hand column.

A. Right.

Q. Referring back to your testimony where we started this discussion back on Page 8, again, Lines 18 through 19, you indicated there that the communications equipment lives were reduced from 18 to 10 years to better reflect the type of asset being installed. I'm sorry; you are behind me a bit there. Do you have that?
A. Yes.
Q. Again, you indicated that the lives for communications equipment were being reduced from 18 to 10 years to better reflect the type of asset.
A. That's correct.
Q. What specific changes in the type of assets installed have caused the lives to drop from the 20, 22-year range indicated in Exhibit 298 to the 10 years selected by the Company?
A. That was as a result, again, of recommendations from the people that run these departments and their plans and budgets for equipment change-outs in the communication area due to technological changes and other changes regarding radio frequency wave access, you might say, and their budgeting for extensive replacements of those systems in the near term.
Q. Staying with Exhibit 298, these two pages of

work papers for communications equipment, the Company reduced remaining life from 13.65 years in the center column under "existing" to 5.24 years; correct?
A. That's correct.
Q. So the remaining life was cut to less than half of what it was; is that right?
A. That's right.
Q. As we discussed earlier when we were talking about 1.66 remaining life, it's the remaining life that's used to calculate the depreciation rate; is that right?
A. That's right.
Q. So this change would result in an increase in the rate, would it not?
A. Yes, it would.
Q. I would like now to go to Page 8 again of your testimony, Exhibit 290, and Lines 4 and 5, and there you state that net salvage changes were mostly decreases due to decreased salvage and increased costs of removal, and that would have the effect of increasing the depreciation rates; correct?
A. That's correct.
Q. With the increased interest in recycling, why would net salvage values decline; do you know?
A. Basically, as the service life of an asset is

greater or as it increases, the salvage value is going to tend to decrease in the cost of removal given that the effort to remove assets remains the same and that the cost if labor generally increases, we would see an increase in the relationship that we stated here in the testimony.
Q. Would you please turn to Exhibit 299. Do you recognize this as the Company's response to Public Counsel Data Request No. 87?
A. Yes, I do.
Q. Again, this was prepared by you or under your direction?
A. That's correct.
Q. And it's true and correct to the best of your knowledge?
A. Yes.
Q. The request points at three accounts found in transmission and distribution plant and indicates that the Company is proposing increases from 20 percent to 59 percent for these accounts; although, the underlying depreciation study had comments like "no strong basis for change." I'm just paraphrasing our request so far, and your response was that the change was driven by changes in net salvage; correct?
A. That's correct.

Q. If we go back to Exhibit 291, which is your Attachment 33 to Page 7, if we look about two thirds of the way down the page, Account 364.0, poles, towers and fixtures, and the category "distribution plant," this account shows an increase in depreciation expense of $1,027,000; is that correct?
A. That's correct, on a system basis.
Q. This is one of the accounts we just discussed in the Exhibit 299 that responds to Request 87, isn't it?
A. Yes, it is.
Q. The proposed change in the rate, which is shown on Exhibit 291 there and again on that same line for 364, the change in rate is 1.45 up to 2.3, and that's an increase of 58-odd percent, is it not?
A. Yes, that's correct.
Q. Now I refer you to what has been marked for identification at Exhibit 300. Do you recognize this as a page from the Company's depreciation study for Account 364, poles, towers and fixtures?
A. Yes.
Q. This sheet shows on the left-hand side of the page bands for five, ten, and full years. On the right-hand side on the far right column, it shows the net salvage percents for those bands, does it not?

A. Yes, that's correct.
Q. And the net salvage shown for those bands respectively is plus 17 percent plus 14 percent plus 14 percent; correct?
A. That's correct.
Q. In the notes section on the right-hand side, the language, "suggest no change to net salvage based solely on history" appears; isn't that right?
A. That's right.
Q. However, as shown on the exhibit in the selection line, the Company selected a negative net salvage of 10 percent; isn't that correct?
A. That's correct.
Q. I'd like you to go back now to Exhibit 291. Again, this is your Attachment 33, and I'm referring you to Page 9 of the exhibit, and the Page 9 is a summary of your proposed rates in calculations for gas and gas common plant and equipment; correct?
A. Correct.
Q. And the proposed increase in Account 1376 remains, and that is the middle of the page, gas distribution plant grouping, second entry in the far right-hand column we see a proposed increase of $563,900,000; is that right?
A. That's right.

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Q. And the total increase in gas depreciation expense or grand total at the very bottom of the page, far right-hand column, is only $348,071; is that correct?

A. That is correct.

Q. So some of the proposed increase in mains, the mains account is offset by declines, the most prominent being the decline in depreciation for Account 1380 for services; is that right?

A. That is right.

Q. And that is shown also in gas distribution plant grouping right in the middle, fifth line down. On the far right-hand column, it shows a negative $362,500 amount.

A. That's right.

Q. If you could turn to Exhibit 301, or what has been marked for identification as such, do you recognize that as three pages from the Company's depreciation study regarding Account 1376 for mains?

A. Yes.

Q. If you go to Page 3 of that exhibit, please, on Page 3, it shows for the current study a selection of 15 percent salvage, 45 percent cost of removal, and a net salvage of 30 percent; is that correct?

A. Negative 30 percent, that's correct.

Q. In the notes section on the right-hand side of the page, it states, "based on full experience initial selections, salvage, 15 percent, cost of removal--" or COR "--45 percent"; is that right?
A. That's right.
Q. Now, if you would turn back to Page 1 of the exhibit, if you look there on that first page of the exhibit, we see that the Company adopted a cost of removal of 60 percent rather than 40 percent; is that correct?
A. That is correct.
Q. That's on the far right-hand column.
A. Uh-huh.
Q. Can you accept subject to your check that mathematically if we used all the same parameters shown on Page 1 of this exhibit, but we used a cost of removal factor of 40 percent rather than 60 percent, then the net salvage would be a negative 25 rather than negative 45, and this would result in a depreciation rate of 2.26 percent, which would still be an increase, but it would be an increase of 2.01 percent rather than the proposed increase of 23.1 percent?
A. I'll accept that subject to check.
Q. One final question, Mr. DeFelice, have you been asked as part of your assigned duties to prepare

rebuttal testimony on the depreciation issues in this case?
A. I have not been asked as of yet.
Q. Do you know if Avista will be using any other witnesses on depreciation in rebuttal in this case?
A. I don't know at this time.
MR. FFITCH: Your Honor, I have no further questions. I would like to offer Exhibit 292 through 301 at this time.
JUDGE CAILLE: Any objection?
MR. MEYER: No objection.
JUDGE CAILLE: Exhibits 292 through 301 are admitted.
MR. FFITCH: Let me make sure those are all of the exhibits I had intended to address. Thank you, they are, Your Honor. Thank you, Mr. DeFelice.
THE WITNESS: You are welcome.
JUDGE CAILLE: Did the Commissioners have any questions of this witness?
CHAIRWOMAN SHOWALTER: I have a few.

CROSS-EXAMINATION

BY CHAIRWOMAN SHOWALTER:
Q. I just wanted to ask you a little bit about the computers. First of all, what kinds of computers

are these? Are these desk tops and laptops primarily?
A. Yes. Desk tops and laptops and network equipment associated with the PC.
Q. So this is not larger, other types of computers?
A. No. We don't own mainframe equipment.
Q. With regard to the ones that are leased, if that were your only group of computers, would those computers have an actual life under your operations of three years, or is there some carryover? When you turn them back, do you financially get a break on the next one? I'm trying to get a sense of when you turn one in, is that the end of that computer, or is there a benefit on the next one?
A. I don't know the specific terms of the lease, if there are rollover options or not. My understanding is it's a three-year term.
Q. If you assume those are a three-year term, and you are achieving a proposed average of five years, then I assume that must mean that some of these computers have an actual life of longer than five years to make it come out right, or is this simply an accounting mechanism not related to the computers?
A. A couple of points of clarification, if I might. I understand your point. At the time that the

study was conducted, it was assumed that there would not be any additional dollars added in Account 391 and that all equipment would be on this lease. Subsequent to that time and in preparation for the Data Response 100 for Public Counsel that we have not submitted yet, we have found out that, in fact, there will be dollars being charged to Account 391 Sub 1 relating to the network equipment for these computers.

The computers themselves will be on the lease. The network equipment will be capitalized, and given that the technology of the computers and the software systems will affect the compatibility of the networking equipment, it's at the advice of the people managing that department that the networking equipment will most likely be turned over every three to four years. That remains to be seen, obviously, as time goes forward.

Q. Is it fair to characterize your proposal as a transition to a point at which everything is on a three-year cycle, the computers at least? I don't know about the network parts. Is the five year really a transition figure at the end of which -- and maybe the end is just the end of this year; I'm not sure, but your intent is to get onto a three-year cycle not five.

A. Not specifically right now. I think that what may lead you to think that is the 36 percent rate which was a result of the five-year average service life with a remaining life true-up, as I call it, calculating the truing-up theoretical reserve to the actual reserve, under the assumption that the account activity would cease after 1998 was to fully exhaust that account in 1.6 or roughly two years.

Given that equipment is still going to be charged to that account, what would happen on a subsequent depreciation study under the current methodology is that depending on when the study is conducted, a true-up would reflect more of what you would think of intuitively as a five-year life rate for the remaining equipment, the network equipment.

Q. If we can project forward to 2003, do you expect there to be any equipment that is more than three-year cycle?

A. It wouldn't be the vast majority of what's in the account, from what I'm told.

Q. Then with respect to the graphs -- I guess this would be Exhibit 295, and I'll just say in particular, Pages 7 through 11 of Exhibit 295. I just want to be clear what it is I'm looking at. I thought I heard you say, but I'm not sure, that this compares a given curve with not the actual retirement of actual

computers, but with an accounting methodology in which there is a fixed amortization; is that right?
A. That's right. Under normal circumstances, retirements would be recorded as they physically occur, so if you had equipment that was being retired in year one, year two, year three, et cetera, that would be reflected in an actual life curve.
In these accounts, all the general plant accounts except for the transportation accounts and communication, the equipment is not specifically identified, if you will, when it's physically removed. It's just assumed from an accounting methodology standpoint is taken off the books every eight years. The eight-year-old vintage is removed, so that's going to cause a historical survivor curve to follow the symmetry that you see here, and the reason that Company went to that method of, quote, "fixed amortization," was to reduce man hours for identification what we will call small assets. This keeps the books cleaner in that respect, that all the dollars are retired systematically, and furthermore, the historical survivor curves, if you will, would not give you an indication of future expected service lives. They are just basically a snapshot of that accounting methodology.

Under normal circumstances, your historical survivor curves may reflect some trend that you may expect to see in the future but not necessarily, and I think in the high-tech accounts, it's even more important we get a perspective of what we expect to see in the future because of the technological advances that we see today, we'll continue to see in the future.

CHAIRWOMAN SHOWALTER: I think we are all lucky that Avista is not run by teenagers because it would be a lot less than three years if it were. I don't have any more questions.

JUDGE CAILLE: I do have a question.

EXAMINATION

BY JUDGE CAILLE:

Q. Do you know if the leased computers will have service contracts?

A. I don't know that. We can find that out for you.

Q. Please look at Exhibit 293, the last sentence on that page, beginning in 1999, could you explain the nature of the renewable options as described in your response?

A. I don't know the specifics of those renewable options right at this point.

JUDGE CAILLE: Mr. Meyer, do you have extended redirect?

MR. MEYER: No, I wouldn't dare, but I do have limited redirect.

JUDGE CAILLE: Let's try to finish up this witness then before we break.

REDIRECT EXAMINATION

BY MR. MEYER:

Q. Pursuing the line of questioning of Chairwoman Showalter, your comment to the Chair was that the historical survivor curves, whether they are shown for computer equipment in the one exhibit or for telecommunications for the other exhibit -- I believe the latter was 297. The former was 295 -- those historic survival curves, if I understood your testimony, do not provide a satisfactory indication of future service lives. Was that your testimony?

A. That's correct.

Q. In arriving at that particular conclusion, did you have an opportunity to inquire within the Company of those who might have knowledge of future planned change-outs for telecommunication or for computers?

A. Yes, we did.

Q. What did you learn from that survey process?
A. Basically, what we learned is what I referred to earlier in my discussion was that the technology advances that are being made and with the requirements around telecommunication equipment and computer equipment that the service lives will be significantly less than what is currently in the Company's depreciation rates.
Q. So your decision to adjust service lives was not based on theoretical accounting notions but rather on actual investigation of near-term planning.
A. That's right.
Q. Do you happen to recall offhand how long a sinking fund depreciation has been used for hydro facilities?
A. We believe it's been in effect since the 1950's.
Q. When it was put in effect, I believe one of your data responses introduced into this case explained part of the rationale for that.
A. That's correct.
Q. Would you explain what that said?
A. Back in the '50's, because of some significant competitive pressures the Company was facing from PUD's, the Company's approach was to

minimize the initial rate impact to customers related to the construction of the Noxon and Cabinet Gorge hydroelectric projects.

Q. Has that sinking fund methodology been the subject of ongoing review periodically by staffs of both Commissions?

A. Yes, it has.

Q. And it has remained in place until as we speak?

A. That's correct.

Q. Would you comment then as to the appropriateness of retaining that methodology going forward, given its intended purpose?

A. It's appropriate for a couple of perspectives. One, that we feel it's a reasonable systematic allocation of costs related to the consumption of those assets. Additionally, if there was a switch to a different methodology, the Company would be faced with a material accounting adjustment ranging anywhere from a 37-million-dollar write-off to a 37-million-dollar regulatory asset, and that's the result of talking to our external auditors.

We don't feel that's appropriate because the plants are economical; they are efficient, and as the next witness, Mr. Anderson, will tell you, we have received new licenses for the operation of Noxon and Cabinet Gorge from the FDRC, so we don't see the justification of creating, I guess, effects on the Company's financial records that may lead people to think that there are negative contingencies pertaining to the hydroelectric plants.

MR. MEYER: Thank you. That concludes my redirect.

JUDGE CAILLE: Is there any recross?

MR. TRAUTMAN: Just a couple from Staff. First, I believe I neglected to move for the admission of Exhibits 302 and 303 and would like to do that at this time.

JUDGE CAILLE: Is there any objection?

MR. MEYER: No objection.

JUDGE CAILLE: Those exhibits are admitted.

FURTHER CROSS-EXAMINATION

BY MR. TRAUTMAN:

Q. Mr. DeFelice, in the discussion of the computer account, I believe you indicated that the account is being amortized?

A. That is correct.

Q. When did the amortization practice begin?

A. 1993.

Q. Was the computer account data that was used for the depreciation study actuarial data, or was it simply overall plant balances or retirements?

A. I will have to check on that with the consultant to identify.

MR. TRAUTMAN: Could we make a records requisition for that information?

JUDGE CAILLE: Mr. Trautman, would you please state again what that requisition is?

MR. TRAUTMAN: The requisition was to determine whether the computer account data that was used for the depreciation study was actuarial data or whether it was simply overall plant balances or retirements.

JUDGE CAILLE: That will be Record Request No. 19.

Q. (By Mr. Trautman) Is it correct that the Company recently replaced its SCADA system, which is the signaling system for sending impulses to power stations and transformers?

A. I'm not familiar whether it was changed out or not.

Q. So you are not aware of that?

A. Not specifically, no.

MR. TRAUTMAN: That's all I have.

JUDGE CAILLE: Anything from you, Mr. ffitch?

MR. FFITCH: Yes, Your Honor.

FURTHER CROSS-EXAMINATION

BY MR. FFITCH:

Q. Mr. DeFelice, you mentioned that you had conducted an inquiry inside the Company regarding your retirement of computer and communications equipment; is that right?

A. That's right.

Q. To whom did you speak in conducting that inquiry?

A. The managers of the two respective departments.

Q. So those were two conversations, essentially, with two individuals?

A. Actually, it was more than two conversations, but yes.

Q. Are those individuals still with the Company?

A. Yes, they are.

Q. What are the respective departments you are referring to?

A. The IS department, information services, and telecommunications.

Q. Is telecommunications a department within Avista Utilities, or is that somehow related to Avista Telecommunications?
A. It's Avista Utilities.
Q. You had, you testified, a number of conversations with those two individuals?
A. That's right.
Q. Were there any documents or surveys of equipment generated by these conversations?
A. Yes, there were.
Q. Have those been produced in this proceeding to date?
A. Not to date, no.
MR. FFITCH: Your Honor, we are going to make a record requisition of those surveys, assuming that Avista is able to provide those.
THE WITNESS: I believe so.
JUDGE CAILLE: That will be designated as Record Request No. 20.
MR. FFITCH: The request will be for all documents or surveys generated as a result of Mr. DeFelice's internal inquiry regarding depreciation of computer and communications equipment.
JUDGE CAILLE: Mr. Meyer?
MR. MEYER: Just a housekeeping matter I

wanted to inquire of counsel. We had provided the lengthy Deloitte and Touche study regarding book depreciation as of '97 upon which Mr. DeFelice replied to ICNU, and copies were to have been provided to Staff. Staff presumably has a copy of this study?

MR. TRAUTMAN: The 1997 one, yes.

MR. MEYER: Thank you. That's all I had.

JUDGE CAILLE: Then the witness is excused. Thank you, Mr. DeFelice.

THE WITNESS: Thank you.

JUDGE CAILLE: We will take a 15-minute break and come back at 3:15.

(Recess.)

MR. MEYER: We call our next witness, Mr. Robert Anderson.

(Witness sworn.)

EXHIBITS MARKED FOR ROBERT D. ANDERSON:

Exhibit T-345, Direct Testimony RDA-37T; Exhibit 346, Hydro Relicensing Expense Analysis RDA-38; Exhibit 347, NARUC Bulletin No. 5-2000 (Staff Cross Exhibit); Exhibit 348, Appendix U to Clark Fork Settlement Agreement: Funding Summary Table (Final Draft 10/23/98) (Staff Cross Exhibit.)

JUDGE CAILLE: You may proceed, Mr. Meyer.

DIRECT EXAMINATION

BY MR. MEYER:

Q. For the record, would you please state your full name and your employer.

A. My name is Robert Anderson. My employer is Avista Corporation.

Q. Have you prepared direct testimony marked for identification as Exhibit T-345?

A. Yes, I have.

Q. With the errata sheet containing the changes having been distributed as well and given those revisions, if I were to ask you the questions that appear in that prefiled testimony, would your answers be the same?

A. Yes, they would.

Q. Are you also sponsoring what has been marked for identification as Exhibit 346?

A. Yes.

Q. Was that prepared by you or under your direction and supervision?

A. Yes, by me.

MR. MEYER: With that, Your Honor, I move for the admission of Exhibits T-345 as well as 346.

JUDGE CAILLE: Is there any objection?
MR. TRAUTMAN: No.
JUDGE CAILLE: Those exhibits are admitted, and we will pause for just a moment while we get the Commissioners, Mr. Trautman.

CROSS-EXAMINATION

BY MR. TRAUTMAN:
Q. Good afternoon, Mr. Anderson.
A. Good afternoon.
Q. I'm Greg Trautman, assistant attorney general for the Commission Staff. How long have you been involved with the project to relicense the dams on the Clark Fork River?
A. Since the inception of our planning process on through the consultation and the filing of an application and the receipt of a license order, which encompassed the period 1992 through the present.
Q. When did the project to relicense these two dams begin?
A. The notice of intent, the formal application to relicense, was in 1996, and our completed application following the consultation process was in February of 1999.
Q. FERC issued the new license for the Cabinet

Gorge and Noxon Rapids hydroelectric projects just recently; is that right?
A. Yes, February 23rd.
Q. Is this the first time that FERC has relicensed a dam prior to the expiration of an existing license?
A. This is the first time that a project of this size has been relicensed by FERC since the amendments to the Federal Power Act in '86.
Q. Was this under an alternative process codified by FERC in October of '97?
A. Yes, it was.
Q. Was the quick action from FERC primarily due to the fact that Washington Water Power approached the relicensing project with a goal of reaching a settlement with all the interested parties?
A. Yes, it was.
Q. Is it correct that many parties participated and a settlement agreement was reached?
A. Yes.
Q. If you could turn to what's been marked as Exhibit 348. At the top of the page, it says, "funding summary table," and in the upper right-hand corner it says, "Appendix U, Clark Fork Settlement Agreement," and it has Pages U-1 through U-5.

A. Yes.
Q. This is the settlement agreement from the Cabinet Gorge hydroelectric project, Volume 3. Do you recognize that?
A. Yes. Both Cabinet Gorge and Noxon Rapids.
Q. Now, if you would also turn to what has been marked as Exhibit 346, and that would be your Exhibit No. 38, originally marked.
A. Yes.
Q. At the top it says, Clark Fork Settlement Agreement Expense Costs for Protection Mitigation and Enhancement PME measures, with an expense component; do you see that?
A. Yes.
Q. Comparing the table in Exhibit 348 to your Exhibit 346, there are far more dollars in the settlement agreement than are presented in your exhibit; is that correct?
A. Yes.
Q. Does the requested adjustment include dollars for land acquisitions or plant improvements which can be capitalized?
A. No.
Q. Is it correct that the amounts in Exhibit 346 represent ongoing annual expenses only?

A. The dollars represented in 346 represent expense dollars that are a component of the settlement agreement.
Q. Looking at Exhibit 346, of the annual expenses, is it correct that by far the largest one is administration, which is at the bottom of the table?
A. Yes.
Q. Is it correct that the requested recovery is for the incremental amount over the existing administrative costs since an amount of $736,000 has been deducted?
A. Yes.
Q. Nevertheless, the additional or remaining administrative costs are $650,000; is that correct, that being 1390 minus the 736?
A. Yes.
Q. That's more than any one of the listed mitigation measures; is that correct?
A. Yes.
Q. Are the current administrative costs, that is, the $736,000, considered part of the operating cost of the power produced at the dams?
A. Yes, I believe they are.
Q. Are the administrative costs that you request in your adjustment required payments in the FERC

license?
     A.   No, they are not.
     Q.   Turning to Exhibit 348, and this is the funding summary table --
     A.   Could I go back just for a second? The required payments, from the standpoint they are a part of the settlement agreement, which is a part of the license order, from that standpoint, they are a part of the settlement agreement and then required of the Company to implement the programs of the license order.
     Q.   Would it be correct to say that they are not a license requirement?
     A.   They are a license requirement.
     Q.   On Exhibit 348, and this is the funding summary table, there are several columns at the top of the page. You have fund, estimated, budgeted, periodic. Which of the amounts listed in this table, and it continues for five pages, which of these amounts listed are firmly known annual payments that Avista must make?
     A.   The category fund, if you look at that category, those are annual obligation of the Company that will be available for that specific PM and E measure.
     Q.   The budgeted amount, what does that

represent?
A. The budgeted amount represents dollars for specific PM and E's that are used to implement on the ground measures for that specific PM and E, and they are not to exceed amount on an annual basis.
Q. Would it be correct that the estimated column is just what it appears to be, that some amount will be spent but just how much is unknown?
A. Right.
Q. The periodic column, what does that represent?
A. Those are one time or periodic costs that would occur over the license period that are forecasted for specific impacts or analysis that might occur in the future.
Q. But those are not annual payments.
A. They are not annual payments.
Q. Are any of the periodic payments included in your Exhibit 346?
A. No, they are not.
Q. Are the known annual payments exactly the dollar amounts indicated?
A. The known annual payments specifically in the fund category are a set amount. The budgeted dollars are not to exceed. The periodic costs are relatively

fixed. The various funds do rollover into the next year if they are not utilized in that specific year.
Q.   Let me ask it this way then: Are the known annual payments adjusted for inflation over time?
A.   Yes, they are.
Q.   Are they adjusted by the GDP of implicit price deflator?
A.   Yes.
Q.   For payments beginning in future years, the first payment made in a future year, is that increased by the inflation since the beginning of the settlement plant?
A.   It varies for the different categories.
MR. TRAUTMAN: As a record requisition, we would ask to have the Company produce a year-by-year schedule of the payments for each of the items that are listed in Exhibit 346, and for that, we would like the amounts that are agreed funding levels, budgeted amounts, estimated and so forth.
JUDGE CAILLE: Will the Company be able to provide that?
MR. MEYER: Is that doable?
THE WITNESS: Sure. We can run those out. I think you are asking over the licensed term of 45 years, produce a table that would show these costs on

an annual basis?
MR. TRAUTMAN: Yes.
JUDGE CAILLE: That would be Record Request No. 21.
Q. (By Mr. Trautman) Going back to the 1.39 million dollars in administrative costs, I believe you indicated that was required by the license.
A. Yes.
Q. Are all of those costs required by the license, including, for example, the amounts for Avista personnel labor and expenses?
A. The exact amount of 1.39 million dollars is not, as such, a requirement. The requirement is for the personnel and the equipment to implement the protection and mitigation enhancement measures. That 1.39 million is controlled by the Company, and in some years, it may reach that amount. Some years it may be less, and some years, it could possibly go over that amount.
MR. TRAUTMAN: I would move for admission of Exhibit 348 at this time, and we need not move for admission of 347.
JUDGE CAILLE: Is there any objection to the admission of 348?
MR. MEYER: None, Your Honor.

JUDGE CAILLE: Then it is admitted, and 347 will not be offered. Does that conclude your cross-examination, Mr. Trautman?

MR. TRAUTMAN: Yes.

MR. FFITCH: No questions for Public Counsel, Your Honor.

JUDGE CAILLE: Commissioners, do you have any questions for this witness?

COMMISSIONER HEMSTAD: No.

JUDGE CAILLE: Any redirect?

MR. MEYER: Just one or two.

REDIRECT EXAMINATION

BY MR. MEYER:

Q. The discussions surrounding the $1,390,000 reflected in your exhibit for administration programs --

A. Yes.

Q. -- you indicate personnel. Would you provide a sense for the type of personnel and responsibilities of those personnel as they implement programs?

A. Yes. The Avista Staff that's required to implement the provisions of the license order consists of a staff of biologists, program manager, technicians, clerical assistants at our Noxon field office in Noxon,

Montana. It also consists of support personnel from the Spokane office.
It also consists of contracts that we have with the State of Idaho, the State of Montana and the U.S. Fish and Wildlife Service for what's called "aquatic program leads" who will be responsible for implementation of the aquatic measures within the State of Montana, within the State of Idaho, and within the Fish and Wildlife Service for fish passage program. There is also funds in there for some legal fees, real estate support, and other contingencies.
Q. Mr. Anderson, do you feel those categories of costs are, in fact, the nature of costs that are required to be incurred in order to implement the settlement agreement?
A. Yes, I do.
Q. With respect to the Staff Exhibit 348, consisting of funded as well as budgeted expenditures -- do you have that in front of you?
A. Yes.
Q. -- how reasonably confident are you that those budgeted items adequately fairly reflect the level of expense that will be incurred as we move into the future?
A. We are relatively confident of these

forecasted costs because these expenditures have been developed by the signatories to the settlement agreement. This took place over a three-year period during consultation where the technical issues were carefully scoped and the costs for each one of those technical areas was arrived at by consensus as well as the technical area itself so that we came up with plans for each one of the protection mitigation enhancement measures from which these costs are based.

MR. MEYER: Thank you. That completes my redirect.

JUDGE CAILLE: Is there any recross?

MR. TRAUTMAN: Just one question.

FURTHER CROSS-EXAMINATION

BY MR. TRAUTMAN:

Q. Are the Avista personnel to which you referred, are they new staff members needed to implement the plan, or are there some ongoing staff?

A. There are some ongoing staff. I've also hired four additional staff at Noxon and one additional staff in Spokane.

Q. So then how many are new and how many are ongoing?

A. My staff now consists of 17 individuals. We had added, I think, five because of the settlement agreement and the license order. Also, we are doing some other things in the department with relicensing on other projects and additional staff has been hired, but some of this crosses over.

MR. TRAUTMAN: That's all I have.

JUDGE CAILLE: Anything further, Mr. Meyer?

MR. MEYER: Just to make sure the record is clear.

FURTHER REDIRECT EXAMINATION

BY MR. MEYER:

Q. Does the administration of program costs of the $1,390,000 net less existing administrative costs, does that net figure represent the incremental cost of additional employees or FTE's necessary to implement?

A. Yes, it does.

MR. MEYER: That's all.

JUDGE CAILLE: Anything further? Thank you, Mr. Anderson, for your testimony. Let's go off the record and get ready for the next witness.

(Discussion off the record.)

JUDGE CAILLE: Mr. Meyer, would you please call your next witness.

MR. MEYER: I call to the stand Ms. Katherine

Mitchell, please.

(Witness sworn)

EXHIBITS MARKED FOR KATHERINE E. MITCHELL:

Exhibit T-365, Direct Testimony KEM-39-T; Exhibit 366, Proforma Electric Labor/Benefit Summary KEM-40; Exhibit 367, Proforma Gas Labor/Benefit Summary KEM-41; Exhibit 368, Proforma Officer Compensation Adjustment KEM-42; Exhibit 369, Workpapers in support of Exhibit Nos. 40, 41, and 42 (Staff Cross Exhibit); Exhibit 370, 98 Pacesetter Electric Expensed & Paid in 98 (Staff Cross Exhibit); Exhibit 371, Team Incentive Rewards paid in 1995 (Staff Cross Exhibit); Exhibit 372, E-mail and attached summary of incentives (Staff Cross Exhibit); Exhibit 373, General Ledger Journal Entry of Adjust Wholesale Incentive Account (Staff Cross Exhibit); Exhibit 374, 1998 Annual Report, Proxy Statement and Financial Report (Staff Cross Exhibit); Exhibit C-375, Confidential: Response to Staff Data Request No. 18 (Staff Cross Exhibit); Exhibit 376, Response to Staff Data Request No. 219 (Staff Cross Exhibit); Exhibit 377, Washington Water Power SEC Form 10-K for 1996 (Staff Cross Exhibit); Exhibit 378, Response to Staff Data Request No. 20 (Staff Cross Exhibit); Exhibit 379, Response to Staff Data Request No. 21 (Staff Cross

Exhibit; Exhibit 380, Response to Staff Data Request No. 171 (Staff Cross Exhibit); Exhibit C-381, Confidential: Response to Staff Data Request No. 171 (C) (Staff Cross Exhibit); Exhibit 382, Response to Staff Data Request No. 172 (Staff Cross Exhibit); Exhibit 383, Response to Staff Data Request NO. 173 (Staff Cross Exhibit); Exhibit 384, Response to Staff Data Request No. 174 (Staff Cross Exhibit); Exhibit C-385, Confidential: Response to Staff Data Request No. 175 (C)(Staff Cross Exhibit); Exhibit 386, Response to Staff Data Request No. 176 (Staff Cross Exhibit); Exhibit No. 387, Response to Staff Data Request No. 177 (Staff Cross Exhibit); Exhibit C-388, Confidential: Response to Staff Data Request No. 178 (C) (Staff Cross Exhibit); Exhibit 389, Washington Water Power General Ledger Journal Entry dated 6/30/98 (Staff Cross Exhibit); Exhibit 390, E-mail from Kathy Mitchell to Joanna Huang dated 2/24/2000 re: Questions and Incentives (Staff Cross Exhibit); Exhibit C-391, Confidential: Salary History Profile (Staff Cross Exhibit); Exhibit 392, Avista Utilities, WWP Division, Electric System Labor Dollars Average Monthly Average Basis for Twelve Months Ended 12/31/98 (Staff Cross Exhibit)

JUDGE CAILLE: Mr. Meyer, you may proceed.

DIRECT EXAMINATION

BY MR. MEYER:

Q. For the record, would you please state your name and employer?

A. My name is Katherine Mitchell. I'm employed by Avista Corporation.

Q. Have you prepared the direct testimony marked for identification as Exhibit T-365?

A. Yes, I have.

Q. With the errata sheet having been distributed, if I were to ask you the questions that appear in that testimony, would your answers be the same?

A. Yes, they would. I do have one correction on Page 2.

Q. Go ahead. I'm sorry, which page?

A. Page 2, Line 16, I would change 1999 to 1998.

Q. Do those complete your changes to your direct testimony?

A. Yes, it does.

Q. Have you also sponsored Exhibits 366, 367, and 368?

A. Yes, I have.

Q. Were those prepared by you or under your direction and supervision?

A. Yes.

MR. MEYER: With that, Your Honor, I move the admission of T-365 and 366, 67 and 68.

JUDGE CAILLE: Is there any objection?

MR. TRAUTMAN: No.

JUDGE CAILLE: Then those exhibits are admitted.

MR. MEYER: Thank you, and the witness is available for cross.

CROSS-EXAMINATION

BY MR. TRAUTMAN:

Q. I'm Greg Trautman, assistant attorney general for the Commission Staff. If you could turn first to what's been marked as Exhibit 369, and these are labeled "Workpapers in Support of Exhibit Nos. 40, 41 and 42."

A. I'm there.

Q. If you could turn to after the cover page, the second page, I think it might say Page 1 at the bottom.

A. It does.

Q. Mine is scratched out. This is a page at the top entitled "Avista Utilities adjusted electric labor dollars, Washington"; do you see that?

A. Yes, I do.

Q. Looking to the first column, which says, "total Washington," does that column include bonuses?

A. It includes pacesetter bonuses. It includes any bonus that was both paid and expensed in 1998.

Q. Would it include both the team incentive awards and the pacesetter awards?

A. Not the bulk of the team incentive award.

Q. Which portion of the team incentive awards are not included?

A. I know that there is an exhibit that Staff intends to show. It would be on 372. The two incentives that are included in that column, when you look in the 1998 recorded column, moving down, it includes the 726 less the capital component of $5,400, and then the $374,000 number less the $137,000 number.

Q. It includes those two items.

A. It includes the 726, the 374, but then you have to back out the components that were capitalized, because Page 2 that you were looking at in that column is just O and M and A and G, not capital, so you would want to tally up just the expense portion.

Both of those categories, team recorded in 1998 and paid in 1998, and pacesetter recorded and paid in '98 are the components that would be included in

that column. The other ones would not be.
    Q. Going back to Exhibit 369, the second column is entitled, "remove officers"; do you see that?
    A. Yes.
    Q. Does that column remove the officer compensation for purposes of computing the proforma salary increases?
    A. It removes officer compensation that was run through the payroll system. There were other elements of officer compensation that did not hit expense through the payroll system. This is only compensation that was recorded through payroll system.
    Q. What other types of expenses would you be referring to?
    A. Anything that is recorded on a journal entry is not included in here. This report comes from charges that were processed through the payroll system. The payroll system feeds into the general ledger system, and the journal entry system feeds into the general ledger, so payroll system is one feeder source into the general ledger.
    Q. Moving to the column, "adjusted total Washington," would that be the total Washington less the officers compensation?
    A. Yes.

Q. Is it correct also that the officer salaries are removed from Accounts 920 and 930? That would be on the third page of this table.

A. Yes.

Q. Is the "adjusted total Washington" column, the basis, used to calculate the 1998 proforma wage adjustment?

A. The 1262 at the bottom of Page 4?

Q. No. The "adjusted total Washington," not the "remove officer." Is the "adjusted total Washington" column the basis for calculating the 1998 proforma wage adjustment?

A. Yes, for the non officer.

CHAIRWOMAN SHOWALTER: What page are we on?

MR. TRAUTMAN: Right now, I'm on Page 1 at the bottom.

CHAIRWOMAN SHOWALTER: Is this Exhibit 369?

MR. TRAUTMAN: Yes. Cover paper is work papers. There is then a short table, and then there is a page with a lengthwise table that has columns moving across there.

Q. (By Mr. Trautman) Staying on this table on Exhibit 369, is it correct this column entitled, "1998 increase and 1999 increase" calculate the annual effect of the wage increases granted in March 1998 and March

1999?
A. Yes, it is.
Q. In your exhibit, is it correct that the 1998 and 1999 wage increases are applied to the entire adjusted total Washington amount?
A. Yes, it is.
Q. And that includes certain bonuses; is that correct?
A. That's true.
Q. Is it correct that the 1998 bonuses that were actually paid by the Company to the administration and union employees were not calculated by taking the 1997 figures and multiplying them by a fixed percentage, for example, 0.737 or 0.04, to obtain the 1998 figures?
A. Can you ask that one more time?
Q. The bonuses that were actually paid in 1998, is it correct that the Company did not calculate that bonus by taking a 1997 bonus, for example, for an administrative employee, and saying, we'll multiply that by 0.737 percent -- well, add on 0.737 percent? Is that correct that the bonus was not calculated that way?
A. No. Those bonuses would have been calculated to an amount that was appropriate to reward that particular employee or employees for their performance

on a particular project.
Q. Is it correct that the bonuses paid each year to administration and union employees are paid at the management's discretion?
A. This is true.
Q. Could you turn to what's been marked as Exhibit 371. This is a two-page exhibit. At the top, the first page it says, "the Washington Water Power Company team incentive rewards paid in 1995."
A. This is true.
Q. Looking at Page 1, would you agree that the 1995 bonuses include team incentive awards totaling approximately 1.75 million dollars?
A. I think the number reads 1.57 million, if we are looking at the same page.
Q. The actual page I'm looking at has $1,575,550.85.
A. I'm sorry. I must have heard 1.75.
Q. So you agree on that?
A. Yes, it's 1.57.
Q. And the next page of that exhibit, Page 2, which deals with the pacesetter rewards is approximately $47,000; correct?
A. Yes.
Q. So the total for 1995 with bonuses is

approximately 1.62 million dollars?
A. That sounds reasonable.
Q. Staying on the same exhibit in the middle of the two pages are handwritten notes from the 1996 bonuses. Is it correct that those bonuses are about 1.895 million dollars for 1996 team incentives and $281,000 for pacesetter rewards for '96?
A. Yes.
Q. So the total would be about 2.17 million dollars.
A. That sounds reasonable.
Q. If you could turn now to Exhibit 372, and in particular, Page 2 of this exhibit, which is the table to which you referred earlier. Do you have that?
A. Yes, I'm there.
Q. Do you agree that the 1997 bonuses include pacesetter rewards of $248,000 and team incentive rewards of a million dollars for a total of approximately 1.287 million dollars in '97 bonuses?
A. Yes.
Q. Would you agree that the 1998 bonuses include the pacesetter rewards of about $374,000 and team incentive rewards totaling 4.4 million dollars for a total of 1998 bonuses of 4.7 million dollars?
A. Yes.

Q. So reviewing the figures, the bonuses in 1995, I think we agreed, total about 1.6 million dollars; in 1996, 2.1 million; 1997, 1.2 million, and 1998, 4.7 million. Is that correct?
A. Yes.
Q. Subject to check, you would agree that the 1998 bonuses are approximately four times the amount of the 1997 bonuses; is that correct?
A. That's close.
Q. Could you turn to -- this is an exhibit previously marked Exhibit 5. I believe it was admitted with Mr. Matthews. It's a 10-K for 1998.
MR. MEYER: Do you have a copy of that?
THE WITNESS: I think it's one of the exhibits here.
MR. TRAUTMAN: We have the proxy statement, but that's different.
MR. MEYER: We'll provide a copy to the witness.
Q. (By Mr. Trautman) Do you have that exhibit?
A. I'm there.
Q. Could you turn to Page 25.
A. Okay.
Q. At the top of the page is entitled "Avista Corporation." It says, "Item 6, selected financial

data," and beneath that is a table of dollar figures.
Do you see that?
A. Yes.
Q. Exhibit 5 is the 1998 form 10-K report to the SEC; correct?
A. Yes, it is.
Q. And the table shows selected financial data. Do you agree looking under "operating revenues," that the line "national energy trading and marketing" contains operating revenues for nonregulated operations?
A. I believe that that would be where it would be included.
Q. Are these operating revenues from subsidiaries other than Avista Utilities?
A. Yes.
Q. Do you agree, likewise, that the nonenergy line contains operating revenues from nonregulated operations, that is, from subsidiaries other than Avista Utilities?
A. Yes, it would.
Q. Under the operating revenues figures, would you agree that approximately in 1997 that the nonregulated operating revenues of the total of 1.3 million, that the nonoperating revenues are

approximately only 32 percent of the total; that being about $411,000 out of 1.3 million?
A. I'm sorry. Can do you that one more time for me, please?
Q. In 1997, the total operating revenue was about 1.3 million dollars?
A. Yes.
Q. The nonregulated portion would be approximately $411,000; correct?
A. Yes.
Q. Would you agree subject to check that that's about 32 percent of the total?
A. Subject to check.
Q. Looking to 1998, the total is 3.6 million dollars in total revenues, but would you agree now that the nonregulated operating revenue accounts for over 2.6 million, which is approximately 72 percent of the total, subject to check?
A. Subject to check, yes.
Q. Looking also at the increase in the total operating revenues from 1997 to '98, that goes from 1.3 million to 3.6 million. Would you agree that the increase in the total operating revenue between '97 and '98 is almost entirely accounted for by nonregulated revenues; that is, all but $150,000 of the increase?

A. Yes. It looks as though the bulk of it was in the nonregulated.
Q. Is it correct that the operating income, the regulated operations in 1998, and that's the box below "operating revenues," is it correct that the operating income for regulated operations in 1998 is actually lower than that of 1997? It goes from $178,000 to $143,000?
A. I'm sorry. I'm thinking I'm looking at the wrong table. I'm looking at "operating revenues"?
Q. I'm in "operating income" now, and I'm looking at energy delivery and generation resources, which is the regulated side.
A. I'm on that.
Q. So you agree that the operating income for regulated operations in 1998 is actually lower than that of 1997?
A. Yes, it is.
Q. Turning back to Exhibit 372 for a minute, this is the table of the pacesetter awards and the team incentives. Would you agree that the increase in the 1998 bonuses compared to the 1997 bonuses is due almost overwhelmingly to the increase in the team incentives rewards as opposed to the pacesetter awards?
A. I would agree the bulk of it is definitely in

the team incentive awards.
Q. Turn now to what's been marked as Exhibit 374. This is Avista's 1998 proxy statement.
A. I'm ready.
Q. If you could turn to Page 12 of that statement, this is under the heading "annual incentive compensation"; do you see that?
A. Yes, I do.
Q. Looking down to the second paragraph, looking to the last sentence in that paragraph, am I correct that that sentence reads: "As a result of various factors, including a significant shift in corporate strategy as discussed below, the targets established in early 1998 were not met, and therefore, no awards were made to executive officers under the 1998 executive incentive plan." Do you see that?
A. Yes.
Q. Is it correct that Avista's compensation and benefit committee did give cash bonuses to Officers Eliassen, Ely, and Fukai in 1998, and I believe you will find that on the summary table on Page 13 of the proxy statement?
A. Yes.
Q. Is it correct that those amounts were $40,000 for Mr. Eliassen, $40,000 for Mr. Ely, and $30,000 for

Mr. Fukai?

A. Yes.

Q. Those were booked to the utility side; correct?

A. Yes. Originally, they were booked to the utility side.

Q. Were they then changed?

A. In our proforma adjustment on officers compensation, for those officers that spend a portion of their time towards subsidiary activities, we adjusted this in the proforma.

Q. So you adjusted only a portion out.

A. We removed -- say, for example, Mr. Ely, I believe, maybe split his time fifty-fifty, then we would have removed 20 out of the utility, $20,000 out of the utility.

Q. Going back to Page 12 of this exhibit, of the proxy statement, in the third paragraph, and I'm reading near the end of the paragraph, is it correct that this statement reads: "In order to carry forth the board's strategic vision and implementation of specific initiatives, the total support and focused intention of the executive officers was required." Is that correct?

A. Yes.

Q. Then it refers to cash awards that were made to certain executive officers in the table on the next page, and the basis for those rewards were, would you agree, for the reasons stated in that prior sentence?
A. Yes.
Q. Did officers also receive team incentive bonuses in 1998?
A. No. Those incentives that you are talking about that appear in the proxy statement for those particular officers, those incentives are included in that 3.45 million dollar number on the team incentive page, so it's not in addition to what's discussed here in the proxy statement is also included in that 3.45 million dollars number on the team incentive exhibit that you are referring to, so it's not in addition to. It's just a break out of.
Q. Turning to Page 10 of the proxy statement, and we are still on Exhibit 374, this is beneath the heading that says, "to our shareholders," and I'm looking at the second paragraph, the first sentence.
A. Yes.
Q. Would you agree that this reads: "The primary objective in establishing compensation opportunities for executive officers is to support the Company's goal of maximizing the value of shareholders'

interests." Is that a correct reading?
A. Yes, it does say that. I'd like to add that that can't be done by disregarding customer interests.
Q. Well, I didn't ask you about that. I asked you what was in the proxy statement. Do you agree that's what in the proxy statement?
A. Right, and I added my understanding, yes.
Q. Your understanding is not stated in the proxy statement, is it?
A. That's true.
Q. Turning back to Exhibit 372 --
JUDGE CAILLE: Excuse me, Mr. Trautman. Commissioners have informed me that they have to be at a meeting, so I'm wondering, is this a convenient place for us to....
MR. TRAUTMAN: I only have about five minutes or 10.
Q. (By Mr. Trautman) On 372 again, this is the table, I believe it's a two-page exhibit, the second page of which is a table of bonuses in 1997 and 1998; do you see that?
A. This is the same one we've been looking at; correct?
Q. I believe so. Is it correct that the total amount of bonuses given in 1998 was about 4.7 million

dollars?

A. The total amount of bonuses expensed was 4.7 million dollars, and then you have to take out the $137,000 and the $5,000 that was capitalized, so paid. I should say paid.

Q. Is it correct that $231,000, approximately, of the total amount of 4.7 million was a reward from the 1997 team incentive plan?

A. Did you say 241?

Q. 231.

A. Yes.

Q. Is it correct that that $231,000 should have been booked in 1997?

A. Yes. It related to the 1997 plan.

Q. Is it correct that officers' salary is allocated between regulated and nonregulated operations?

A. Yes, it is true.

Q. Is it correct that the allocation of officers' salary to regulated operations is determined for each officer individually?

A. That would be the case.

Q. As I believe Mr. Matthews testified on Monday, is it correct that the allocations salary to regulated and nonregulated operations is based upon

subjective determinations or, in his words, he said thoughts and feels or gut reactions?
A. The various officers sit down with their executive assistants, and they look at what they've done the previous year and then they look at what their objectives are for the coming year, and from that -- it's a qualitative analysis in that respect, but from that, they determine, Do I need to change my allocation going forward.
Q. But you would agree, would you not, that Mr. Matthews' description of the process was accurate?
A. Yes, it was reasonably accurate.
Q. Is it correct that there are no work papers to support the basis of the allocations of salary to the regulated and nonregulated operations?
A. I think we have responded to that in a data request. In that data request, there were a couple of attached memos laying out what the various percentages are and what is done to determine those percentages, but it is not a calculated figure if you are looking for a calculation in a work paper.
Q. Was any study done to determine that allocation?
A. I believe that is discussed in my response to the data request. This study is the officers and their

executive assistants sit down and talk about where they've been and where they are going to go. In that respect, a qualitative study is performed.
Q. Do you recall what data request that was?
A. 172, I believe.
Q. Staff Data Request No. 172?
A. Staff Data Request No. 172, and I believe that's Exhibit 382.
Q. Would that be the extent of the work papers?
A. This data request is a discussion of the process, and two memos, one from 1996 from the manager of internal audit, and then a memo describing the established percentages for 1998.
Q. Would the response to that DR be the extent of the work papers to support the basis of the allocations?
A. With the body of my discussion as to how the process works.
Q. There were no time sheets to support them; is that correct?
A. Basically, time sheets are -- no, because basically, time sheets would follow these allocations and would follow the methodology that I've described in my response to the data request in that the officers are free to -- throughout the year if they feel that

the focus of their work has changed, they are free to step outside those allocations, and for a couple of officers over the last few years have modified their percentage mid course during the year.
Q. But again, there were no time sheets. You did say that; correct?
A. Right, because the time sheets in general would follow these allocations.
Q. Rather than the allocations following the time sheets.
A. Correct.
Q. I think we previously established that from 1997 to '98, whereas in '97 the nonoperating revenue was about 32 percent of the total operating revenues, in '98 constituted about 72 percent; do you recall that?
A. I do.
Q. Based on that, did Avista's executive officer salary allocations to nonregulated operations change accordingly?
A. Officer salary allocations are not based on operating versus nonoperating revenues. You need to remember that Avista Energy, because of its trading activities, is a high revenue and then conversely high expense activity with narrow margins.

Q. So there was not a change in the allocations.
A. Right, there was not a change.
Q. I just have one more question. Turning to Exhibit 374, on Page 11, again this is a proxy statement, and this is under the heading, "components of compensation." Do you see in the second paragraph the first sentence reads: "The committee considers but does not target executive officer compensation at the median of similarly situated executives of the Company's competitors." Do you see that?
A. I see that sentence.
Q. Is that a correct description of Avista's practices?
A. That's my understanding.

MR. TRAUTMAN: At this point, I would like to move for admission of Exhibit 369 through 392, and that includes several confidential exhibits.

JUDGE CAILLE: Is there any objection?

MR. MEYER: There is no objection.

JUDGE CAILLE: Those exhibits are admitted. Mr. ffitch?

MR. FFITCH: Your Honor, just for the record, I don't have any questions for Ms. Mitchell. We have been directed to her earlier in the hearing on one matter regarding Exhibit 261. I've conferred with

Mr. Meyer, and we are going to pursue our questions regarding that exhibit through a Data Request because of its confidential nature.

JUDGE CAILLE: Thank you, Mr. ffitch. Are there any questions from the Commissioners? Any redirect?

MR. MEYER: Very limited redirect.

REDIRECT EXAMINATION

BY MR. MEYER:

Q. You were asked by Staff counsel a question concerning allocation of officer salaries to regulated as opposed to unregulated operations. Do you recall that?

A. Yes, I do.

Q. Ms. Mitchell, if the process of allocating executive compensation for all officers of the Company for the test period were done by way of allocations to, first of all, regulated versus unregulated, then to jurisdiction and then to service, what would the Washington electric and gas share for all executive compensation be?

A. For all 12 officers, the Washington electric allocated piece was 1.2 million. The Washington gas allocated piece was three million, and that includes the CEO's signing bonus, which we split over five years, which is the term of the agreement, so we took the million-dollar signing bonus and basically said it needs to be treated $200,000 a year, and then from there, we would have taken a bonus like that, and we would have allocated 40 percent of it to the subsidiaries and then taken it further and broken it out between WP and G, Oregon, California, and Washington and Idaho.

Q. I believe you may have misspoke yourself or I may have misheard you. The Washington gas share for all 12 officers was what again?

A. Was $300,000, approximately.

Q. Do those totals in your proforma adjustment reflect an upward or downward adjustment for officer compensation for the test period?

A. Officer compensation for the test period resulted in a reduction to Washington electric of some $400,000, and for gas another $100,000 when we took all of the proforma items together and compared it to the 1998 expense levels, so annualizing everything and smoothing everything out actually resulted in a reduction for both Washington electric and Washington gas.

Q. Just to clarify, there was some discussion during Mr. Matthews' testimony about $150,000 entry in a proxy statement that for the '98 proxy, I believe, that appears in Exhibit 371 at Page 13. I know you had earlier examination by Staff, and there was an entry there for $150,000; correct?

A. Yes, there was.

Q. Does that show up under the utility column?

A. Yes, it does, in the proxy statement.

Q. Was that allocated?

A. That was allocated in the Company's proforma adjustment. Just as the example I used with Mr. Ely, that $150,000 was actually allocated in the proforma. We would have allocated 40 percent of it to the subsidiaries, leaving the remaining $90,000 to be split out among the various jurisdictions, and what that resulted in to the State of Washington, electric would have been $42,000 and $11,000 on the gas side of that original $150,000 that you see in the utility column on the proxy statement.

Q. I wanted to clarify that. There may have been a misimpression left on the record on Monday. Lastly, Staff counsel asked you a series of questions relating to '96, '97, and '98 levels of bonuses paid through pacesetter awards and team incentives. Do you recall that exchange?

A. Yes, I do.
Q. By '98, I believe the total had reached just approximately 4.7 million. Was that the testimony?
A. That's what I recall.
Q. That was inclusive of some officer bonus compensation?
A. Yes. The officer bonus compensation was included there.
Q. Do you believe that that level of team incentives represents a reasonable level of total bonus compensation for test period purposes to reflect the situation going forward?
A. Yes, I do, and I should also note that in 1998, that was the first year where the team incentives were available to all employees, including bargaining unit employees; whereas previous years, the team incentives were not available company wide and were not available, to my knowledge, to bargaining-unit employees.
Q. So that reflects a change in philosophy of sorts?
A. Yes, that did.
MR. MEYER: Thank you. That's all I have.
JUDGE CAILLE: Anything further, Mr. Trautman?

MR. TRAUTMAN: No.

JUDGE CAILLE: Thank you, Ms. Mitchell. You are excused, and we'll go off the record now,

(Discussion off the record.)

JUDGE CAILLE: Before we conclude this afternoon, I have a question regarding the subject of the depreciation studies by Deloitte and Touche. Mr. Meyer, during, I believe, it was your re-redirect of Mr. DeFelice, you mentioned a 1997 study that was, I think, a response of a data request.

MR. MEYER: It was a response to a data request, yes.

JUDGE CAILLE: So my question of Staff is, is that the study that you were referring to in your --

MR. TRAUTMAN: I think Mr. DeFelice had indicated in response to an earlier question. We had asked whether a study had been provided in September of 1999 informally to Staff, and I believe it was the 1997 study.

JUDGE CAILLE: So it was provided informally?

MR. TRAUTMAN: I believe so. It might be good to have Mr. Spinks confirm it. If that's not the case --

JUDGE CAILLE: You can let us know.

MR. MEYER: I'm advised that it was provided, again, because in connection with responding to the ICNU data request which asked for it, our practice was to provide copies of those responses to all parties, so I think Staff may have received another copy.

JUDGE CAILLE: I just want to make sure. There is just one study?

MR. MEYER: Same study, two copies.

MR. TRAUTMAN: I'd like to confirm that with Mr. Spinks tomorrow.

MR. FFITCH: We have certainly received an 1,800 page depreciation study. I assume that's the same one we are discussing here. To be honest, I'm not sure that it's 1997 versus '98.

MR. MEYER: Those are actually the work papers supporting that '97 study.

JUDGE CAILLE: Thank you everybody. And we will see you tomorrow at 9:30.

(Hearing recessed at 4:30 p.m.)