WUTC DOCKET: UE-190334
EXHIBIT: LDK-1T (R)
ADMIT ☑ W/D ☐ REJECT ☐

Exhibit LDK-1T
Dockets UE-190334/UG-190335/UE-190222
Witness: Lance D. Kaufman
(REDACTED)

BEFORE THE

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION Complainant, v. AVISTA CORPORATION d/b/a AVISTA UTILITIES Respondent.	DOCKETS UE-190334, UG-190335 and UE-190222 *(Consolidated)*

RESPONSE TESTIMONY OF LANCE D. KAUFMAN

ON BEHALF OF THE

ALLIANCE OF WESTERN ENERGY CONSUMERS

(REDACTED VERSION)

October 3, 2019

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EXHIBIT LIST

I. INTRODUCTION AND SUMMARY OF TESTIMONY

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Lance D. Kaufman, and my business address is 4801 W. Yale Ave., Denver, CO 80219.

Q. PLEASE STATE YOUR OCCUPATION AND IDENTIFY THE PARTY ON WHOSE BEHALF YOU ARE TESTIFYING.

A. I am an independent economics consultant. I am appearing on behalf of the Alliance of Western Energy Consumers ("AWEC"), a non-profit trade association whose members are large energy users served by electric and gas utilities located throughout the West, including customers that receive gas and electrical services from Avista Corporation ("Avista" or the "Company").

Q. PLEASE SUMMARIZE YOUR EDUCATION AND WORK EXPERIENCE.

A. A summary of my education and work experience can be found at Exhibit LDK-2.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. I address issues related to labor benefits, labor escalation, allocations, revenue, AvistaUtilities.com, depreciation, rate spread, and rate design. I provide recommendations related to those issues and support these recommendations. Bradley G. Mullins and Michael P. Gorman are also submitting testimony on behalf of AWEC in this case. The revenue requirement impact of my recommendations is included with the testimony of Mr. Mullins.

Q. WHAT WAS THE SCOPE OF YOUR REVIEW?

A. I reviewed Avista's filing and its associated workpapers, conducted discovery, reviewed Avista's discovery responses and performed independent research on Avista's affiliate activities. Based on my review of this information, I have developed 11 recommendations. Specifically, I recommend the Commission:

1. *Update 2020 benefits to reflect 2020 Actuarial report and historic over-forecast.*
2. *Reduce 2020 union labor escalations from full year to partial year to reflect timing of wage increase.*
3. *Reject the Hydro One component of Avista's labor pro-forma adjustments 3.03 and 3.04.*
4. *Require Avista employees to record actual time spent on utility and non-utility projects and to allocate unspecified time proportional to specified time.*
5. *Require Avista to allocate or assign IT costs to affiliates and non-utility proportionately to use of IT resources.*
6. *Adjust pole attachment revenue to include $20,000 of additional small cellular related attachment and to defer revenues in excess of $20,000 per year.*
7. *Disallow a portion of the AvistaUtilities.com project costs.*
8. *Update depreciation expense to reflect final capital amounts.*
9. *Modify the rate spread to bring all schedules either at or closer to rate parity.*
10. *Limit Schedule 25 rate increases to demand charges and rate decreases to energy charges until revenue is collected proportional to the cost of service study.*
11. *Increase Schedule 25 transmission credit to prevent transmission customers' subsidization of distribution expenses.*

Q. WHAT IS THE IMPACT OF YOUR RECOMMENDATIONS?

A. The impact of each of these recommendations is detailed in Table 1, below.

TABLE 1
Impact of recommendations

	Recommendation	Electric	Gas	Type
1	AWEC P.F. Benefits (3.05.A10)	(2,080,992)	(631,405)	Expense
		(1,104,192)	(335,029)	Plant
2	AWEC Labor Esc. (3.04.A9)	(91,683)	(31,626)	Expense
3	Hydro One (2.12.A1)	(563,486)	(140,412)	Expense
4	Employee Time Tracking	None		
5	IT Allocations (2.12.A4)	(992,469)	(306,373)	Expense
6	Pole Attachment Revs. (3.01.A8)	20,000	None	Revenue
7	AvistaUtilities.com (3.10.A11)	(3,128,731)	(2,029,808)	Plant
		(625,746)	(405,962)	Expense
8	Update Depreciation Expense	Initial estimate included in adjustments		
9	Ratespread	None		
10	Sch. 25 Demand Charge	None		
11	Sch. 25 Transmission Credit	None		

I discuss each of these recommendations in the following sections of testimony.

II. LABOR BENEFITS

Q. PLEASE SUMMARIZE THIS ISSUE.

A. Avista proposes pro-forma adjustments to labor benefits to reflect expected benefit costs for 2020. However, Avista's adjustments over-forecast historical benefit costs by 7 percent. I recommend updating Avista's adjustment to account for 2020 budgets and Avista's historic over-forecast. This reduces system wide 2020 benefit costs by $7.5 million. This reduction is applied to both operation and maintenance expense. I propose a functionally similar adjustment for 2019 capitalized labor.

Q. PLEASE EXPLAIN YOUR UPDATE FOR 2020 BUDGETS.

A. The category of labor benefits includes health and medical benefits. Avista's filed case adopts the 2019 actuarial forecast of $73 million for the 2020 budget for these benefits.[1/] A more recent 2020 actuarial forecast produced in discovery shows the 2020 budget is $70.7 million.[2/] This represents a reduction of $2.4 million from Avista's filed case. I take the 2020 actuarial forecast as the baseline forecast for 2020 labor benefits as it is a more recent study and aligns more closely with the rate period.

Q. PLEASE EXPLAIN HOW AVISTA OVER-FORECASTS BENEFIT COSTS.

A. Table 2, below, identifies Avista's forecast and actual benefit costs from 2011 to present.[3/] Avista over-forecasted benefits in seven of the last eight years by an average of 7.2 percent.

TABLE 2

Avista's Forecast and Actual Benefit Costs (2011 – Present)

Year	Forecast	Actual	Error	Percent Error
2011	$52,692,000	$47,236,757	($5,455,243)	-10.4%
2012	57,607,000	56,087,429	(1,519,571)	-2.6%
2013	60,879,000	58,249,028	(2,629,972)	-4.3%
2014	51,351,000	40,101,367	(11,249,633)	-21.9%
2015	56,218,000	54,610,015	(1,607,985)	-2.9%
2016	58,207,339	61,850,056	3,642,717	6.3%
2017	63,875,000	57,187,580	(6,687,420)	-10.5%
2018	60,055,000	53,229,096	(6,825,904)	-11.4%
Average	57,610,542	53,568,916	(4,041,626)	-7.2%

1/ See Avista Workpaper ("WP") "Andrews PF 3.05 WP '(WA 2019) FLB Retirement and Medical.xlsx'".

2/ Exh. LDK-3 at 2-3 (Avista Response to Staff Data Request ("DR") 80).

3/ See Exh. LDK-3 at 9-10 (Avista Response to AWEC DR 47). Avista states that budgeted amounts prior to 2011 are not available.

Q. IS THERE ANY EVIDENCE THAT AVISTA HAS CORRECTED THE ERROR AND THAT THE 2020 FORECAST IS NOT SUBJECT TO THE SAME ERROR?

A. There is no evidence that Avista has corrected for the error. There is no trend present in the error, and the most recent data show that both 2017 and 2018 were worse than average. Nor does the data indicate that Avista's benefit costs are increasing. This means that the 2020 forecast should be corrected to be an accurate representation of Avista's expected costs.

Q. HOW CAN THE COMMISSION CORRECT FOR THE FORECAST ERROR?

A. The Commission can correct this error by multiplying the average error by the 2020 forecast. This results a reduction of $5.1 million, from $70.7 million to $65.6 million.

Q. WHAT IS THE COMBINED IMPACT OF UPDATING FOR THE 2020 ACTUARIAL REPORT AND THE HISTORIC FORECAST ERROR?

A. The combined impact of this adjustment is a reduction of $7.4 million in system benefits. A large portion of Avista's benefit costs are capitalized. Table 3, below, shows the breakdown of this adjustment by capital and O&M, and by jurisdiction.

Table 3

Benefit Adjustment Affects O&M, Depreciation, and Ratebase

	System	WA Electric	WA Gas
Total 2020 adj	($7,469,195)		
Share O&M	56%		
2020 O&M Adj	($4,205,904)	($2,019,675)	($612,800)
2020 Depreciation Adj	($127,691)	($61,317)	($18,605)
Total 2019 Adj	($5,263,083)		
Share Capital	44%		
2019 Capital Adj	($2,299,441)	($1,104,192)	($335,029)

III. LABOR ESCALATIONS

Q. PLEASE SUMMARIZE HOW AVISTA ESCALATES UNION LABOR.

A. Avista begins with 2018 union labor expense, multiplies by 1.00714 to annualize a mid-year 2018 pay raise, multiplies by 1.03 to reflect a mid-year 2019 pay raise, and multiplies by 1.03 to reflect a final mid-year 2020 pay raise.[4/]

Q. WHAT CONCERN DO YOU HAVE WITH AVISTA'S CALCULATION?

A. Avista's final escalation is not correct because it reflects an annualized amount of labor, after the March 2020 pay raise. The first three months of 2020 labor expense will be at the pre-2020-raise salaries. Avista should only include 9 months of labor expense at the 2020 rates.

Q. WHAT IS YOUR RECOMMENDATION?

A. I recommend that 2020 labor expense only be escalated for 9 months from the 2019 annualized expense. This reduces labor expense for Washington Electric by $91,683 and for Washington Gas by $31,626.

IV. HYDRO ONE LABOR ADJUSTMENTS

Q. PLEASE SUMMARIZE THIS ISSUE.

A. Avista's 2018 results of operations reflect 2018 labor allocations to non-utility activities, including activity related to Hydro One. Avista proposes to eliminate the impact of Hydro One on non-utility labor allocations by allocating labor consistent with 2016 non-

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[4/] See Andrews PF 3.05 WP "(WA 2019) FLB Retirement and Medical.xlsx".

utility labor activity.[5] In 2018 about 78 percent of executive labor was assigned to utility operations. Avista increases the utility's allocation of executive labor from 78 to 90 percent.[6]

I recommend the Commission deny Avista's proposed adjustment, and make corrections for non-utility executive leave for the following reasons:

1. Avista's Hydro One activity was funded in part by ratepayers and Avista shareholders received a windfall from the termination payment associated with the failed merger.
2. Avista has demonstrated it can safely and effectively operate using 2017 and 2018 levels of utility-assigned labor.
3. A one-sided adjustment for Hydro-One type events will not result in accurate forward-looking rates.

The impact of my recommendations is a $563,486 reduction in Washington Electric labor expense and a $140,412 reduction to Washington Gas labor expense.

Q. HOW DID AVISTA SHAREHOLDERS RECEIVE A WINDFALL FROM THE FAILED MERGER?

A. Avista claims that all Hydro One expenses were assigned to non-utility. However, Avista fails to note that utility rates for 2017 and 2018 did not reflect the assignment of these expenses to non-utility. This means that utility customers paid for the labor that was used to support Hydro One. Avista spent $38 million on merger activities, not including

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[5] Exh. EMA-1T at 49:1-3.
[6] EMA 3.04 PF Workpaper "(WA 2019) FLB Forecast Labor Executive.xlsx".

income tax.[7/] Avista has not shown that the cash used to finance the merger was held separately from working cash included in utility customer rates.

Avista received a $103 million termination fee as part of the failed merger.[8/] This resulted in a $65 million windfall for Avista's shareholders that Avista does not intend to return to customers.[9/]

Q. WHY IS AVISTA NOT RETURNING THE MERGER WINDFALL TO CUSTOMERS?

A. Avista claims that "[t]he Termination Fee does not represent utility revenue, nor was the fee derived from rates collected from customers or from the sale of utility assets funded by customers."[10/] Contrary to Avista's claim, the Termination Fee was derived in part from rates collected from customers. $2 million of the $38 million spent on the Hydro One merger was from direct assignment of Avista labor. A large portion of this labor expense was included in customer rates in 2017 and 2018. Retail rates also include Avista's working capital, which appears to have been used to finance merger activities.[11/] Customer rates also provide Avista shareholders with the high return on equity that Hydro One was "desperate to get."[12/] Absent Avista's rate regulated utility business, Hydro One would not have sought a merger and shareholders would not have benefited from $65 million in "non-utility" earnings.

7/ Exh. LDK-3 at 6 (Avista Supplemental Resp. to AWEC DR 34).
8/ Id. at 7 (Avista Resp. to AWEC DR 35).
9/ Id.
10/ Id.
11/ AWEC DR 34 Supplemental - Attachment A - Hydro One Transactions - 2017-2019.xlsx does not show any interest expense or other finance costs assigned to Hydro-One activities.
12/ https://www.utilitydive.com/news/merger-they-wrote-avista-and-hydro-one-ask-washington-regulators-to-recon/544713/

Q. ARE YOU PROPOSING ANY RATE TREATMENT OF THE MERGER PROCEEDS?

A. No. While I believe customers should have received at least some portion of the merger windfall, I do not propose specific rate treatment of the merger proceeds. The windfall illustrates how Avista shareholders can gain from allocating low levels of labor dollars to non-utility in rate cases while employing high levels of labor dollars in non-utility activities post rate-case. The practice of using historic numbers to allocate unregulated labor expense provides a reasonable check on the incentive to accomplish this type of expense-shifting.

Q. WHAT EVIDENCE IS THERE THAT AVISTA CAN OPERATE EFFECTIVELY AT 2018 LEVELS OF UTILITY LABOR?

A. Avista admits that it "provided safe and reliable service to our customers during the merger proceedings."[13/] In fact, Avista achieved its highest ever customer satisfaction rating and exceeded all six of its customer service benchmarks in 2018.[14/] Avista's testimony does not include any evidence that additional labor hours beyond 2018 or 2017 hours were necessary to achieve these results. Therefore, the Commission should approve a level of labor spending that reflects the amount of labor necessary for safe and effective operations. Barring any evidence that 2017 or 2018 levels of labor were imprudently low, there is no reason to deviate from the Commission's historic method of forecasting labor, which relies on historic labor levels.

13/ Exh. LDK-3 at 5 (Avista Response to AWEC DR 9).
14/ Id.

Q. WHY WILL AVISTA'S PROPOSAL RESULT IN INACCURATE RATES?

A. One-sided labor allocation adjustments, such as the one proposed by Avista, will not result in accurate rates because they do not reflect expected outcomes. Avista is proposing an after-the-fact change to its standard practice. This proposal is arbitrary and one-sided because it includes no ongoing adjustments for abnormally low levels of non-utility labor. Because this adjustment is one-sided and after-the-fact, utility rates will not reflect the average level of non-utility labor.

Q. DID AVISTA EXECUTIVES BENEFIT FROM THE FAILED MERGER?

A. Yes, Avista executives hold a large number of shares in Avista stock. In the six months leading up to the merger announcement, Avista executive stock holdings increased by 26 percent.[15/] Avista executives held 516,000 shares of Avista stock on July 1, 2017, just prior to the merger announcement.[16/] The Avista share price increased $10 in the two days after the merger, from $42.74 on July 19, 2017 to $52.50 on July 21, 2017 following the announcement of the merger.[17/] This represents a gain of over $5 million for Avista executives. As major shareholders, Avista executives also benefited from the shareholder retention of the $103 million termination fee.

Q. DOES AVISTA CONTINUE TO PURSUE UNREGULATED AND AFFILIATE ACTIVITIES?

A. Yes, Avista continues to pursue a broad number of unregulated and affiliate activities. For example, in 2019 the unregulated subsidiary Avista Development announced a

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15/ Exh. LDK-3 at 11 (Avista Response to AWEC DR 48).

16/ Id.

17/ Yahoo Finance https://finance.yahoo.com/quote/AVA?p=AVA&.tsrc=fin-srch

partnership with Duke Energy to develop energy software.[18/] Avista has invested $50.4 million since 2017 in 18 different ventures and plans to invest an additional $50.7 million in the near future.[19/] Therefore, it is likely that Avista executives will continue to spend significant time on non-utility projects, which further justifies rejecting Avista's pro forma labor adjustment.

Q. PLEASE EXLAIN HOW YOU CALCULATE THE ADJUSTMENT TO LABOR ALLOCATIONS.

A. The adjustment has two components, executive labor and non-executive labor. The executive labor adjustment is calculated by multiplying the projected executive salaries by the 2018 non-utility labor percentages and subtracting Avista's proposed non-utility labor expense. I calculate $1.04 million in non-utility executive labor. Avista calculates $0.4 million. The difference, $640,000, is the adjustment to Avista's system labor expense. This amount is split between Avista's jurisdictions.

The non-executive component is included in Avista's workpaper for pro-forma 3.03, which shows the system Hydro One reclassification equal to $255,749. My proposed adjustment is to reverse this component of 3.03, which returns $255,749 in labor expense to Avista's system labor expense.

Q. WHAT IS THE IMPACT OF YOUR ADJUSTMENT ON ELECTRIC AND GAS RATES?

A. The impact of my recommendations is a $563,486 reduction in Washington Electric labor expense and a $140,412 reduction to Washington Gas labor expense.

[18/] See https://news.duke-energy.com/releases/avista-duke-energy-invest-in-grid-edge-software-technology-to-deliver-benefits-to-customers

[19/] Exh. LDK-3 at 38-39 (Avista Response to AWEC DR 149).

V. NON-UTILITY COST ASSIGNMENT

Q. DO YOU HAVE ANY OTHER CONCERNS WITH AVISTA'S NON-UTILITY COST ASSIGNMENTS?

A. Yes, Avista does not fully allocate or assign costs to non-utility and affiliate activities. My concern falls into two general categories: labor tracking and administrative support.

a. Labor Tracking

Q. WHAT CONCERNS DO YOU HAVE WITH RESPECT TO LABOR TRACKING?

A. Avista records time on a prospective basis, rather than on a retrospective basis. This means assigned costs are based on time projections, not on actual time spent.

Q. PLEASE EXPLAIN WHY PROSPECTIVE TIME TRACKING IS PROBLEMATIC.

A. Prospective time tracking is problematic because it is prone to judgement errors and it cannot be audited or validated. For example, AWEC inquired about time allocations of executives for a day where executives and the Avista board toured affiliate operations.[20/] Because Avista's time records are prospective, the hours recorded for this day did not reflect non-utility time for many executives on the days requested.[21/] If Avista recorded time on a retrospective basis, it would be possible to audit time-keeping records to confirm that Avista correctly assigned costs to non-utility operations.

20/ Exh. LDK-3 at 40 (Avista Response to AWEC DR 150).

21/ Id.

Q. WHAT DO YOU RECOMMEND WITH RESPECT TO TIME TRACKING?

A. I recommend that Avista ask employees to track hours spent retrospectively, and to assign labor costs retrospectively. I also recommend that Avista track time with at least three categories: Utility, Non-utility, and General. General time represents time that is not directly associated with specific utility or non-utility projects and the cost associated with general time should be allocated between utility and non-utility proportionately to the directly assigned hours. For example, time associated with staff training not associated with specific regulated utility projects should be considered general, and the associated dollars should be allocated to both utility and non-utility operations.

b. Administrative Support

Q. WHAT CONCERN DO YOU HAVE WITH AVISTA'S ALLOCATION OR ASSIGNMENT OF ADMINISTRATIVE COSTS?

A. Avista does not assign IT costs associated with administrative support to affiliates or non-utility activity. For example, Avista Capital, Avista Development, Avista Energy, Avista NW Resources and Salix have no employees, and Avista maintains financial records for these affiliates using regulated IT resources.[22/] However, the costs for these resources, specifically accounting, financial, and other general administrative software and server costs, do not appear to be assigned to affiliates.[23/]

22/ Exh. LDK-3 at 37 (Avista Response to AWEC DR 148)

23/ Id.

Q. WHAT IS YOUR RECOMMENDATION FOR THE ASSIGNMENT OF ADMINISTRATIVE COSTS?

A. I recommend that IT costs be assigned to affiliates and non-utility in proportion to the labor that utilizes those IT resources. Approximately 8 percent of non-executive administrative labor is assigned to non-utility operations[24/]. Avista's common intangible IT amortization expense is $27 million [Avista results of operations]. I allocate eight percent ($2 million) of common intangible IT amortization expense to non-utility. This equates to a $1 million reduction in amortization expense for Washington Electric and a $306,000 reduction for Washington Gas.

VI. OTHER REVENUE: POLE ATTACHMENTS

Q. PLEASE EXPLAIN WHAT "OTHER REVENUE" IS AND HOW IT RELATES TO THIS CASE.

A. Other revenue is all utility revenue other than retail utility revenue that offsets revenue requirement. One type of other revenue is from pole attachments. Utility poles often include attachments serving third parties, such as communication attachments. Third parties are charged for the use of utility pole attachments.

Q. WHAT IS YOUR CONCERN WITH AVISTA'S POLE ATTACHMENT REVENUE?

A. Avista has invested in developing part of downtown Spokane into the "five smartest blocks in the world."[25/] Public Utilities Fortnightly states Spokane is one of the five

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24/ Calculated from AWEC DR 37, Attachment A and Avista PF 3.03 WP.

25/ Former Avista CEO Scott Morris, https://www.inlander.com/spokane/how-do-you-build-with-a-clean-energy-future-in-mind-avista-and-mckinstry-hope-to-find-out/Content?oid=17894547.

smartest communities in the US. According to Public Utilities Fortnightly, "A smart city uses … 5G everywhere."[26/] Avista has partnered with Version through Urbanova to continue developing Spokane as a smart city.[27/] However, Avista has not accounted for growth in pole attachment revenue related to 5G deployment in this filing.[28/] Under Avista's two-year rate plan, this means Avista forecasts no 5G pole attachment revenue until 2022, even though 5G is currently being deployed across the US.[29/]

Q. WHY DID AVISTA NOT INCLUDE 5G REVENUE IN ITS FILING?

A. Avista states that "the Company does not have any documentation to provide that would make these estimates 'known and measurable'."[30/]

Q. WHAT IS THE POTENTIAL REVENUE FROM 5G DEPLOYMENT?

A. About 48,000 antennae are needed to cover all of Spokane and Spokane Valley at 250-foot intervals. At $46 per attachment,[31/] this equates to $2.2 million per year in additional pole attachment revenue, as shown in Table 4, below.

26/ https://urbanova.org/wp-content/uploads/2019/07/July2019PUFSmartestCommunities.pdf at page 6.

27 https://www.globenewswire.com/news-release/2018/10/18/1623712/0/en/Verizon-and-Urbanova-work-with-the-City-of-Spokane-to-create-a-smarter-more-sustainable-and-more-connected-place-to-live.html

28/ Exh. LDK-3 at 8 (Avista Response to AWEC DR 40).

29/ Id.

30/ Id.

31/ Id. at 35 (Avista Response to AWEC DR 144, Attachment B).

TABLE 4

Potential 5G Revenue Exceeds $2.2 Million

	Square Miles	Antennae
Spokane	69.5	31001
Spokane Valley	38.01	16955
Total	107.51	47956
Rate per attachment		$46
Potential Revenue		$2,205,976

Q. GIVEN THE UNCERTAINTY ABOUT WHEN 5G WILL BE DEPLOYED IN SPOKANE, WHAT DO YOU RECOMMEND FOR THE RELATED REVENUE?

A. Avista's current expectation for 2020 5G revenue growth is $20,000.[32/] I suggest that Avista include $20,000 in revenue in base rates, and that Avista file for a deferral of any revenue in excess of $20,000 on an annual basis until its next general rate case is effective.

Q. CAN AVISTA BE RELIED ON TO VOLUNTARILY DEFER THESE REVENUES?

A. No. Avista received over $100 million in revenue as part of its recent merger activity and failed to file for a deferral of these revenues or to return any of these revenues to customers, even though at least some of this revenue was directly due to regulated activity. The Commission, therefore, should explicitly order Avista to defer 5G revenues above the $20,000 I recommend be included in rates.

[32/] Id. at 8 (Avista Response to AWEC DR 40).

VII. NEW CUSTOMER REVENUE

Q. WHAT LEVEL OF RETAIL ENERGY SALES DOES AVISTA ASSUME IN THIS CASE?

A. Avista assumes weather normalized 2018 energy sales when calculating revenue.[33/]

Q. IS THERE EVIDENCE THAT AVISTA'S 2020 AND 2021 ENERGY SALES WILL DIFFER FROM 2018 SALES?

A. Yes, Avista has added new customers since 2017. For example, Avista has added service to a new 270,000 square foot manufacturing facility in Spokane Valley,[34/] and to its own new 190,000 square foot development in downtown Spokane.[35/] Amazon will soon open a new fulfillment center in Spokane that will employ 1,500 workers.[36/] The annual energy requirements of all new customers from 2018 are only partially reflected in 2018 energy use. None of the annual energy requirements of 2019 new customers are reflected in proposed rates.

Q. HAS AVISTA MADE CAPITAL ADDITIONS IN 2018 AND 2019 RELATED TO NEW CUSTOMERS?

A. Yes. Avista provides a line extension allowance to new customers to offset the cost of a customer connecting to Avista's distribution system. This allowance is a ratebased investment.

33/ Exh. EMA-1T at 36:20-37:9.

34/ See https://www.katerra.com/2019/09/23/katerra-opens-state-of-the-art-mass-timber-factory-in-spokane-valley-wa/

35/ Exh. LDK-3 at 41 (Avista Response to AWEC DR 154).

36/ See https://www.spokanejournal.com/local-news/amazon-maintains-aggressive-place-on-spokane-project/

Q. DOES AVISTA'S FILING INCLUDE CAPITAL ADDITIONS FOR NEW CUSTOMERS?

A. Avista's filing includes capital additions for 2018 and 2019 for new customers. 2018 capital additions are included in the base results of operations and 2019 forecasted additions are included through Avista's pro-forma adjustment 3.10. Accordingly, it is one-sided and unfair for Avista to include the costs of these new customers in rates, but not the associated revenue.

Q. HOW DO YOU RECOMMEND THE COMMISSION ADDRESS CUSTOMER ADDITIONS IN 2018 AND 2019?

A. I recommend the Commission adopt the recommendation made by Mr. Mullins in his response testimony.

VIII. AVISTAUTILITIES.COM REDESIGN

Q. WHAT COSTS HAS AVISTA INCLUDED IN THIS CASE RELATED TO ITS REDESIGN OF THE AVISTAUTILITIES.COM WEBSITE?

A. Avista has requested recovery of $11.9 million incurred to redesign its website.[37/]

Q. WHAT DO YOU RECOMMEND WITH REGARD TO THESE COSTS?

A. I recommend that the Commission disallow $9.1 million of these costs, as Avista has failed to demonstrate the prudence of this level of investment. This adjustment limits the cost of the redesign to [redacted]

37/ Exh. JMK-1T at 7:21.

Q. PLEASE EXPLAIN THE AVISTAUTILITIES.COM REDESIGN PROJECT.

A. This project was to update the old avistautilities.com website to the new myavista.com website. The project was performed in two phases, the first to create the design blueprint and the second to implement the website[38/]. Avista bid each phase out separately, and awarded the first phase to IBM and the second phase to ConnectiveDX.[39/]

The website redesign was initially estimated to cost approximately $1.5 million, but the final cost ballooned to nearly $12 million.[40/] While Avista states that the $1.5 million estimate was "an early 'very rough order of magnitude' (VROM) estimate based on limited scope,"[41/] after Avista bid the project out and selected the winning vendors, it signed contracts with IBM and ConnectiveDX for $[redacted] and $[redacted], respectively.[42/] While the latter was a "not to exceed price," Avista nevertheless increased ConnectiveDX's total compensation to $[redacted] through a series of contract amendments, a 2,200% increase.[43/] Further, even with these increases, the total amount Avista spent on contractors for its website redesign was still only $[redacted]. Notably, this is in line with the approximately $2 million Avista spent developing the original avistautilities.com website in 2008, adjusted for inflation.[44/] It is also only a small fraction of the $12 million total Avista requests recovery for in this case. While unclear

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38/ Exh. LDK-3 at 13 (Avista Response to AWEC DR 73).

39/ Exh. LDK-3 at 42 (Avista Response to AWEC DR 161).

40/ In Re Avista Corporation, dba Avista Utilities, Request for a General Rate Revision, OPUC Docket No. UG 325, Exh. Avista/602 at 86 (Nov. 30, 2016).

41/ Exh. LDK-3 at 21 (Avista Response to AWEC DR 90).

42/ Exh. LDK-3C at 43-46 (Excerpts of Avista Response to AWEC DR 161, Confidential Attachment A and Confidential Attachment B).

43/ Exh LDK-3C at 47 (Excerpt of Avista Response to AWEC DR 161, Confidential Attachment B).

44/ Id. at 20 (Avista Response to AWEC DR 89).

from the discovery responses in this case, it appears that Avista itself incurred the remainder of the cost for "[b]ack-end development," though what the specific projects associated with this activity were are unclear.[45]

Q. WHAT WERE THE GOALS OF THE WEBSITE REDESIGN?

A. The primary drivers of the website upgrade were: "improving navigation, updating the look and feel of the overall site, creating a new homepage layout, and improving self-service and search functionality."[46] These are issues common to any website and do not seem to warrant the uncommon costs Avista incurred. Indeed, the new website's functionality is typical of other utility websites. Customers can pay their bill online, view outages, and start or stop service.[47]

Q. DID AVISTA EXPLAIN WHY ITS WEBSITE REDESIGN COST SO MUCH MORE THAN INITIALLY ESTIMATED?

A. No. When asked, Avista simply stated that the website redesign was needed based on industry benchmarking and customer preferences. It did not provide any reasons for the cost increase.[48]

Q. DOES THE INDUSTRY BENCHMARKING AVISTA RELIED ON SUPPORT THE BUSINESS CASE FOR A FULL WEBSITE REDESIGN?

A. No. In fact, the benchmarking surveys Avista retained and stated it relied on as a basis for its website redesign project show that Avista's website and customer experience were above the industry average prior to its overhaul. An E-Source study, for instance, shows

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45/ Id. at 42 (Avista Response to AWEC DR 161).
46/ Exh. JMK-3 at 15.
47/ Exh. LDK-3 at 14 (Avista Response to AWEC DR 83).
48/ Id. at 21 (Avista Response to AWEC DR 90).

that Avista's customer service ratings were substantially above its peer group and even improved between 2013 and 2014.[49/] Similarly, a JD Power survey shows satisfaction with Avista's website and mobile application above the industry average.[50/]

Q. DID AVISTA CONSIDER ALTERNATIVES TO THE WEBSITE UPGRADE?

A. Not really. Exhibit JMK-3 includes a business case for the web redesign project in which the only alternative presented to a complete refresh of the website at $12.6 million was to do nothing. This is particularly surprising given the business case's statement that "our website still ranks well among industry standards and with our own metrics," reflecting the conclusions of the benchmarking surveys discussed above. Given this fact, a $12 million complete overhaul of the website appears excessive; a middle-ground approach may have been warranted. Such a middle-ground approach, however, does not appear to have been considered.

Further, there is no indication that Avista executives questioned the cost of the website upgrade or undertook any serious due diligence of the project. The six-page business case included in Exhibit JMK-3 represents the only written analysis of the web redesign, the need for it, and examination of other alternatives. When asked for any additional documents or information other than this business case that Avista management reviewed before approving the requested funding for the web redesign,

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49/ Exh. LDK-3C at 26-27 (Avista Supplemental Response to AWEC DR 99, Confidential attachment O at 63-64).

50/ Id. at 28 (Avista Supplemental Response to AWEC DR 99, Confidential attachment P at 1).

Avista provided none and only referred to a narrative about how projects are discussed and approved within its various business groups.[51]

Q. DO AVISTA'S SHAREHOLDERS BENEFIT FROM ITS WEBSITE?

A. Most likely. The number of unique visits to the website since it went live in June 2017 has been well over 3 million per year.[52] Since Avista only serves approximately 700,000 customers (gas and electric), customers are clearly not the only ones that use the website. The website has a detailed page dedicated exclusively to investors where they can view earnings reports and presentations, dividend payments, and other benefits. Avista's website prominently promotes "Avista Marketplace" and processed enrollment for an appliance sweepstakes.[53]

Q. IS A $9.1 MILLION DISALLOWANCE PUNITIVE TO THE COMPANY?

A. No, in fact it is arguably conservative because Avista includes costs from other information technology programs in this case that appear to be duplicative of the benefits customers were supposed to see from the website redesign.

Q. PLEASE EXPLAIN.

A. Avista's includes over $20 million in capital in this case for its Technology Expansion program. The business case supporting this project states that it will help address "consumer demand for swift and easy access to their utility service provider to pay their bills, order new services, monitor outage maps, learn of new offerings that relate to their

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[51] Exh. LDK-3 at 15, 17 (Avista Response to AWEC DRs 84 and 87).
[52] Exh. LDK-3 at 33 (Avista Response to AWEC DR 141).
[53] https://www.myavista.com/-/media/myavista/content-documents/your-account/bill-inserts/2019/may-19/marketplace-bill-insert.pdf?la=en

particular needs or lifestyles, and more."[54/] Many of these benefits are strikingly similar to the benefits customers supposedly realized through the AvistaUtilities Redesign project. Mr. Kensock, for instance, testifies that "one of our first initiatives under the [AvistaUtilities Redesign] business case, delivered a web outage map."[55/] He also notes that "the first iteration of the new website design … allowed customers the ability to make payments seamlessly and securely through the new payment processor service integrated in the new website."[56/] If these were some of the benefits customers paid over $12 million for with respect to the website redesign project, it is unclear why they appear to be paying even more for the same benefits under a different information technology program. Further, when asked what "new services" and "new offerings" customers enjoyed through Avista's investments in the Technology Expansion project, the Company identified the ability to "start new electric or natural gas service via a self-service channel" and "finding an HVAC contractor; signing up for billing and/or outage alerts; researching energy efficient appliances … or researching renewable energy options."[57/] Again, these all appear to be services and offerings available through Avista's website, and it is unclear why this functionality was not included in the cost of the website redesign.

54/ Exh. JMK-3 at 8-9.
55/ Exh. JMK-1T at 14:6-7.
56/ Id. at 15:1-3.
57/ Exh. LDK-3 at 16 (Avista Response to AWEC DR 86).

Q. DO ANY OTHER INFORMATION TECHNOLOGY PROGRAMS APPEAR TO OVERLAP WITH THE WEBSITE REDESIGN?

A. Yes. Avista includes $11.3 million as a pro forma adjustment in this case associated with its Customer Facing Technology program.[58/] The total authorized capital investment for this project through 2023 is $48.5 million.[59/] This project appears primarily dedicated to creating mobile app functionality, including bill payments, outage tracking, and appointment notifications.[60/] In other words, much of this project can be viewed as an extension and outgrowth of the Company's website redesign. From this perspective, it is concerning that a $12 million website upgrade would not itself include mobile web app functionality. Instead, to provide a fully web-based experience for customers, Avista has requested recovery of over $23 million in this case, and projects over $37 million more over the next several years.

Q. HAS THE AVISTAUTILITIES.COM REDESIGN PROJECT REDUCED COSTS FOR CUSTOMERS?

A. No, at least not that Avista can quantify. The only quantification of cost savings Avista identified from any of its IT investments was $100,000 for resolving one out of every four unsuccessful web transactions that the AvistaUtilities Redesign project was supposed to enable.[61/] Avista confirmed, however, that this estimated savings was not included in the Company's filing, and was instead "redeployed" to other areas of the business.[62/]

58/ Exh. JMK-1T at 17:9.
59/ Exh. JMK-3 at 28.
60/ Exh. JMK-1T at 24:14-22.
61/ Exh. JMK-3 at 14.
62/ Exh. LDK-3 at 18 (Avista Response to AWEC DR 88).

Q. PLEASE SUMMARIZE YOUR RECOMMENDATION REGARDING THE AVISTAUTILITIES.COM REDESIGN PROJECT.

A. I recommend the Commission disallow $9.1 million of the costs of this project, allowing Avista to recover only the amount it spent on [redacted] for the project and bringing the costs in line with the cost to develop the original avistautilities.com website. The project was vastly over-budget; the basis for the project was questionable given the old website's benchmark ratings; the Company has been unable to demonstrate any financial benefits to customers from the project, which also likely benefits the Company's shareholders; and the Company appears to have included even higher costs associated with the website redesign that are being recovered through other information technology programs.

IX. DEPRECIATION

Q. PLEASE SUMMARIZE YOUR CONCERNS WITH RESPECT TO DEPRECIATION AND PROVIDE YOUR RECOMMENDATION.

A. I have recommended reductions to the amount of capital included in Avista's rate base. These reductions have corresponding reductions associated with accumulated depreciation and depreciation expense. I expect other parties in this case will also propose adjustments to Avista's capital. I recommend that Avista recalculate accumulated depreciation and depreciation expense included in rates to be consistent with the Commission's final determination of Avista's rate base. The adjustments in my testimony include estimates of the impact on depreciation expense.

X. RATE SPREAD

Q. WHAT CONCERN DO YOU HAVE WITH THE COMPANY'S PROPOSED RATE SPREAD?

A. My primary concern with the Company's proposal is that it is not consistent with the Company's own cost of service study. The Company proposes to spread rates in a manner that increases cross-subsidization for two of six electric rate categories and maintains substantial cross subsidizations for the remaining four categories.[63/]

I am concerned that the minor adjustments proposed by Avista are not sufficient to match escalating costs of service. Avista has requested a two-year rate plan. If this rate plan is approved, rates will diverge even further from costs than they presently are. This means both an extended period of inequitable rates and an even harder correction will be necessary when Avista files its next rate case and the ongoing cost of service rulemaking is concluded.

I recommend Avista make larger progress towards cost-based rates now, in order to soften the impact of any changes needed in the future. Rate schedules that are close to parity should move to parity. Rate schedules that are more distant to parity should make at least 50% movement toward rate parity.[64/] My proposed rate spread is included in Tables 5 and 6, below.

63/ Exh. JDM-1T, Table 5.

64/ Under my proposal, Residential Schedules absorb the additional net impact of the schedules that move to rate parity because the residential class is the farthest below parity.

Table 5

Proposed Electric Rate Spread

Type of Service (a)	Present Relative ROR (b)	Proposed Relative ROR (c)	% Move Towards Parity (d)
Residential 1/2	**0.43**	**0.72**	51%
General Service 11/12	**2.24**	**1.62**	50%
Large General Service 21/22	**1.55**	**1.27**	50%
Extra Large General Svc. 25	**1.08**	**1.00**	100%
Pumping Service 30/31/32	**0.85**	**1.00**	100%
Street & Area Lights 41-48	**1.14**	**1.00**	100%

Table 6

Proposed Gas Rate Spread

Type of Service (a)	Present Relative ROR (b)	Proposed Relative ROR (c)	% Move Towards Parity (d)
General Service 101	**0.68**	**0.84**	51.2%
Large General Service 111	**2.68**	**1.84**	50.0%
Interruptible Service 131	**2.19**	**1.59**	50.0%
Transportation Service 146	**1.14**	**1.00**	100.0%

Q. WHAT IS RELATIVE RATE OF RETURN?

A. Relative rate of return is a measure of how far a schedule’s rates are from cost-based rates. If a schedule’s relative rate of return (“ROR”) is lower than one, the schedule is being subsidized by other classes. If the relative ROR is greater than one, the schedule is subsidizing (i.e., paying costs of service caused by) other classes. If the relative ROR is equal to one (rate parity or rate unity), the schedule is experiencing no cross-subsidies.

Q. WHY DO YOU PROPOSE BRINGING SOME TYPES OF SERVICE ALL THE WAY TO PARITY IN ONE STEP?

A. By bringing schedules to rate parity I am proposing rates consistent with cost-causation. Several groups of schedules are already close to rate parity and do not require gradual steps.

Q. AVISTA'S PROPOSED RATE SPREAD PUSHED SCHEDULE 25 AND SCHEDULES 30/31/32 FURTHER FROM PARITY. DOES AVISTA OPPOSE BRINGING SCHEDULE 25 CLOSER TO PARITY?

A. No. In response to AWEC DR 56, Avista stated that it had no opposition to bringing Schedule 25 closer to parity.[65/] This is a reasonable position that is in line with the concept of cost-based rates.

Q. WHY DO YOU PROPOSE LIMITING THE CHANGE FOR THREE GROUPS TO 50 PERCENT OF THE DISTANCE TO RATE PARITY?

A. Some schedules are a substantial distance to rate parity. I recommend smoothing the transition to cost-based rates by limiting the change for these schedules. This helps promote the principle of gradualism and avoids rate shock for these customers.

Q. UNDER YOUR PROPOSAL DO YOU EXPECT CUSTOMERS TO REACH UNITY WITHIN TWO YEARS?

A. No. Even though I propose making 50 percent movement towards parity, my proposal should still be viewed as a gradual proposal. The cost of serving residential customers is growing more rapidly than Avista's overall cost. Given Avista's forecasted capital investments in its distribution system and in technology, I expect this growth rate to continue. This means that in Avista's next general rate case, much of the progress

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65/ Exh. LDK-3 at 12 (Avista Response to AWEC DR 56).

towards unity made by my proposal will be eroded by the growth of residential service costs.

Q. YOU APPEAR TO BE ACCEPTING AVISTA'S COST OF SERVICE STUDY AS ACCURATE. IS THAT THE CASE?

A. No, my testimony should not be interpreted as acceptance of Avista's cost of service model. I understand that there is an ongoing rulemaking addressing cost of service issues more broadly. In view of the ongoing process, and in the interest of minimizing the disputed items in this case, I have not proposed an alternate cost of service study. However, I have some concerns with Avista's current model, and I agree that there is reason to continue the ongoing cost-of-service process.

Q. AVISTA PROPOSED ALLOCATING NONE OF ITS REQUESTED RATE INCREASE TO THE LIGHTING SCHEDULES. WHAT IS YOUR RESPONSE?

A. Avista is concerned about the financial position of lighting customers and the risk that Avista will lose lighting customers if they are charged their full cost of service. This is a risk that Avista faces with all customers and does not justify preferential treatment for lighting customers. Avista's proposal does not result in fair and reasonable rates.

Q. WHY DOES AVISTA DIFFERENTIATE LIGHTING CUSTOMERS FROM OTHER TYPES OF CUSTOMERS?

A. Lighting customers are not metered. This means that lighting customers cannot reduce their bills by reducing electric usage. Avista claims this is the reason that lighting customers should be subsidized but not other customer classes that may want rate relief.

Q. DOES AVISTA HAVE ALTERNATIVE OPTIONS TO GIVE LIGHTING CUSTOMERS MORE FLEXIBILITY?

A. Avista could allow lighting customers more flexibility in energy use. For example, Avista is a partner in Urbanova, which is studying the use of smart and connected street lights. Avista could leverage this partnership to allow customers to reduce lighting use when it is not needed, such as after-hours lighting or turning off streetlights when there is no traffic. This is more advantageous than providing lighting customers with free energy because it aligns customer incentives with Avista's energy efficiency goals.

Q. UNDER YOUR PROPOSAL ARE LIGHTING CUSTOMERS TREATED FAVORABLY?

A. Yes. I propose a relatively small increase for lighting customers. This results in a substantial decrease in their relative rate of return, from 1.14 to 1, or rate parity.

XI. RATE DESIGN

Q. PLEASE SUMMARIZE YOUR CONCERNS WITH AVISTA'S PROPOSED RATE DESIGN.

A. I have two primary concerns with Avista's proposed rate design: excessive energy charges and insufficient credit for transmission service.

First, Avista's proposed rate design collects substantially more revenue through energy charges than warranted by Avista's cost of service study. As a result, Avista sends the wrong price signals to Avista's customers. The demand charge should reflect demand costs so that customers can make economic decisions about energy use. By aligning demand rates with demand cost Avista can slow or reverse Avista's future capacity deficiencies, which will reduce future rate increases for all customers.

Second, Avista's proposed rate design has insufficient credit for transmission service. This is a problem because it results in distribution customers paying a rate that is too low and not reflective of the distribution costs that these customers place on the system.

Q. WHAT EVIDENCE IS THERE THAT AVISTA COLLECTS MORE REVENUE THROUGH ENERGY CHARGES THAN WARRANTED?

A. Avista's cost of service and rate spread workpapers as filed by Avista show that only 60 percent of Schedule 25's revenue requirement is attributable to energy use,[66/] but 80 percent of Schedule 25 revenue is collected through energy charges.[67/]

Q. HOW DO YOU PROPOSE ADDRESSING THIS ISSUE?

A. I suggest that Schedule 25 rate increases be limited to demand charges until the ratio of demand to energy charges reflects the cost of service. The current demand charge is split into two blocks. I propose an equal percent increase to both blocks to meet the incremental revenue requirement. I also recommend that any Schedule 25 rate decreases be limited to energy charges until the ratio of demand to energy charges reflect the cost of service.[68/]

Q. WHY ARE YOU CONCERNED ABOUT THE SCHEDULE 25 TRANSMISSION CREDIT?

A. The base demand charge for Schedule 25 includes distribution costs. Transmission customers, however, do not use distribution services. To reflect this, Avista includes a credit for primary and transmission level customers to ensure that distribution customers

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66/ See Knox WP "WAElec COS Base Case UE-19____.xlsm" sheet "SUMCOST" rows 635 to 643.
67/ See Miller WP "Miller Electric RS-RD Workpapers.pdf" at JDM-E-4.
68/ If a reduction is necessary, I recommend an equal percent change in rates for all three energy blocks.

pay for distribution costs. However, the credit is currently too small and does not fully offset distribution expenses embedded in transmission customers' rates.

Q. WHAT EVIDENCE IS THERE THAT THE SCHEDULE 25 TRANSMISSION CREDIT IS TOO SMALL?

A. Avista's cost of service model shows $4.3 million in demand-related distribution expense for Schedule 25.[69/] Transmission customers pay 32% of the demand charges on Schedule 25 and contribute $1.4 million toward distribution expense. However, transmission customers only receive $1 million in credit under the current transmission credit rate.[70/]

Q. WHAT IS YOUR RECOMMENDATION FOR THE TRANSMISSION CREDIT RATE?

A. I recommend increasing the rates so that the transmission credit fully offsets the distribution expenses embedded in transmission customers' rates. This is a 38 percent increase, from $1.10 to $1.52 per kVA for greater than 60 kV service, and from $1.40 to $1.93 for greater than 115 kVA service. Table 7, below, summarizes these calculations.

69/ See Knox WP "WAElec COS Base Case UE-19____.xlsm" sheet "SUMCOST," rows 635 to 643.

70/ Calculated from Miller WP "Miller Electric RS-RD Workpapers.xlsm.

TABLE 7

Proposed Increase in Transmission Credit

Distribution Demand Expense	$4,264,145		
Schedule 25 Demand Charges	$14,940,064		
Transmission Cust. Demand Charges	$4,844,950		
Transmission Share of Demand Charges	32%		
Distribution Exp. Paid by Transmission Cust.	$1,382,830		
	>60 and <115 kV	**>115 kV**	**Total Credit**
Transmission KVA	118,788	622,947	
Current Transmission Credit	($1.10)	($1.40)	
Transmission Credit at Current Rate	($130,667)	($872,125)	($1,002,792)
Proposed Rate	($1.52)	($1.93)	
Transmission Credit at Proposed Rate	($180,558)	($1,202,287)	($1,382,845)

Q. WHAT RATES RESULT FROM THE COMBINED RECOMMENDATIONS OF AWEC WITNESSES?

A. Exhibit LDK-4 summarizes the rates that result from combined recommendations of Mr. Mullins, Mr. Gorman, and myself. Residential and pumping electric schedules receive a rate increase while remaining electric schedules receive a rate decrease. General service gas schedules receive a rate increase while the remaining gas schedules receive a rate decrease. My recommendation for a rate increase for some schedules and a decrease for others is a result of the relatively small change in total revenue requirement resulting from AWEC's recommendations combined with my recommendation to bring each rate schedule either closer to or at parity with their cost of service.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.