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March 29, 2000

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+++WASHINGTON & CALIFORNIA STATE BARS
*IDAHO STATE BAR
**IDAHO & WASHINGTON STATE BARS
***IDAHO & OREGON STATE BARS
ALL OTHERS WASHINGTON STATE BAR

Carole J. Washburn, Secretary
Washington Utility & Transportation Comm'n.
1300 S. Evergreen Park Drive, SW
P. O. Box 47250
Olympia, WA 98504-7250

RE: **Docket Nos. UE-9912455, UE-99-1262 and UE-991409**

Dear Ms. Washburn:

Please find enclosed for filing on behalf of Avista Corporation the original and nineteen (19) copies of AVISTA CORPORATION'S ANSWER TO PETITIONS FOR RECONSIDERATION.

Please conform and return the additional copy of the Answer in the enclosed self-addressed stamped envelope. Thank you for your assistance.

Very truly yours,

PAINE, HAMBLEN, COFFIN,
BROOKE & MILLER LLP


Gary A. Dahlke

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Enclosure

cc: Service List

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

RECEIVED
00 MAR 30 AM 9:48
STATE OF WASHINGTON
UTILITY BOARD

In the Matter of the Application of)
)
AVISTA CORPORATION)
)
for Authority to Sell its Interest in the)
Coal-Fired Centralia Power Plant)

DOCKET NO. UE-991255

In the Matter of the Application of)

PACIFICORP)
)
for an Order Approving the Sale of its)
Interest in (1) the Centralia Steam Electric)
Generating Plant, (2) the Rate Based)
Portion of the Centralia Coal Mine, and)
(3) Related Facilities; for a Determination)
of the Amount of and the Proper Rate)
Making Treatment of the Gain Associated)
with the Sale, and for an EWG)
Determination)

DOCKET NO. UE-991262

In the Matter of the Application of)

PUGET SOUND ENERGY, INC.)
)
for (1) Approval of the Proposed Sale of)
PSE's Share of the Centralia Power Plant)
and Associated Transmission Facilities,)
and (2) Authorization to Amortize Gain)
Over a Five-Year Period)

DOCKET NO. UE-991409

AVISTA CORPORATION'S
ANSWER TO PETITIONS
FOR RECONSIDERATION

I. INTRODUCTION

The Commission issued a Notice of Opportunity to File Answer, dated March 17, 2000, requiring that answers to petitions for reconsideration be filed no later than March 30, 2000 in

the above referenced dockets. Avista Corporation (“Avista” or “Company”) disagrees with the two points pertaining to income taxes offered by Public Counsel. Avista will be required to pay Montana, Oregon and California state income taxes on a portion of the gain on the sale of the Centralia Power Plant (“Centralia Plant”). These state income taxes are a cost associated with the sale and a proportionate share of the taxes should be deducted from both the ratepayer and shareholder portions of the gain applicable to Washington operations. As to Public Counsel's position on excess deferred taxes, Avista has applied all deferred federal income taxes, including excess deferred taxes, to the ratepayer portion of the gain. Avista does not believe that an IRS ruling on excess deferred income taxes is required as long as ratepayers receive the benefit of the excess deferred income taxes in the gain calculation.

Avista also concurs with Commission Staff that the issue of transaction costs should be clarified. However, rather than allocating transaction costs between ratepayers and shareholders as Commission Staff suggests, Avista believes that transaction costs should be deducted from the cash proceeds on the sale in determining the pre-tax book gain on the assets sold.

II. DISCUSSION

A. State Income Tax Issues

Public Counsel requests that the Commission clarify that Washington ratepayers will not be responsible for taxes imposed by other states, namely, state income taxes. (Public Counsel Petition for Clarification at 2.) Avista disagrees with Public Counsel's position. Mr. McKenzie indicated during cross-examination that Avista pays state income taxes in Idaho, Montana, Oregon and California. (Tr. 297.) All of these states use a 3-factor method of apportioning income for state income tax purposes that is based on the proportion of plant, revenues and labor within the respective state to total company amounts. (Tr. 298.) The gain from the sale of the

Centralia Plant will cause an increase in the amount of income allocated to each state for state income tax purposes. (Tr. 300.)

Idaho state income taxes are directly assigned to the Idaho jurisdiction. Washington electric customers currently pay a portion of Montana state income taxes in their rates, irrespective of the tax impacts of the Centralia gain. (Tr. 298-300.) Montana state income taxes are apportioned between Washington and Idaho electric operations using the production/transmission allocation, the same allocation that is being used to allocate the gain on the sale of the Centralia Plant to Washington and Idaho. Normally, Oregon and California state income taxes are directly assigned to the gas operations of each respective state. The gain on the sale of the Centralia Plant will cause an increase in the amount of Oregon and California state income taxes. Avista does not believe it is appropriate to recover Oregon and California state income taxes on the Centralia gain from its gas customers in those two states. (Tr. 301-02.)

Oregon and California state income taxes on the Centralia gain, as well as Montana state income taxes, need to be considered as a cost of the sale and a proportionate share of these taxes needs to be deducted from the ratepayer portion of the gain applicable to Washington operations. It is estimated that approximately \$300,000 of Montana, Oregon and California state income taxes will apply to the Washington portion of the gain assigned to ratepayers. If the Commission were to adopt the position suggested by Public Counsel, the result would be to reduce the shareholder portion of the after-tax gain by approximately \$300,000 (from \$2,292,000 to approximately \$1,992,000). Assigning state income taxes associated with the ratepayer share of the gain to shareholders is totally inappropriate. State income taxes are a cost of the sale. State income taxes associated with the ratepayer share of the gain should be assigned to ratepayers.

Likewise, state income taxes associated with the shareholder portion of the gain should be assigned to shareholders.

B. Excess Deferred Taxes Issues

Public Counsel suggests that there is an incentive for the companies to submit a request to the IRS that the IRS would reject, which would allow the companies to keep excess deferred taxes for shareholders. (Public Counsel's Petition for Clarification at 2.) First, Avista has applied all deferred federal income taxes, including excess deferred taxes, to the ratepayer portion of the gain. (See Avista Corporation's Consolidated Motions for Reconsideration and for Correction of Order, Attachment A, line 32). Second, Avista does not believe that an IRS ruling on excess deferred income taxes is required as long as ratepayers receive the benefit of the excess deferred income taxes in the gain calculation. In addition to being unnecessary, Avista believes that obtaining an IRS ruling will be costly and time consuming. A more effective approach would be to reverse the excess deferred taxes, to the benefit of ratepayers in the gain calculation, and wait to see if the IRS takes exception to the handling of excess deferred taxes on audit. If so, the Company could then request an exception letter. Avista does not believe that excess deferred taxes would be an issue with an IRS auditor, since, in effect, from the seller's point of view the depreciable life of Centralia ends when the plant is sold. There is no depreciable life remaining over which to amortize any deferred taxes, excess or otherwise.

C. Transaction Costs Issues

Avista concurs with Commission Staff that the issue of transaction costs should be clarified. Transaction costs are a cost of the sale. (Petition of Commission Staff for Reconsideration of Second Suppl. Order at 4.) Transaction costs include attorney and investment banker fees, miscellaneous closing costs including real estate taxes and other cost overruns. Commission Staff

suggests allocating transaction costs equally between ratepayers and shareholders. Avista believes that a more appropriate approach is for transaction costs to be deducted from the cash proceeds on the sale in determining the pre-tax book gain on the assets sold. The gain, net of transaction costs, is then shared equally between ratepayers and shareholders. The end result of the Company and Staff approaches is the same, but the Company believes that it is more appropriate to allocate the gain rather than allocating individual items that increase or reduce the gain.

III. CONCLUSION

Public Counsel's positions on state income taxes and excess deferred income taxes should be rejected. A portion of state income taxes should be assigned to the ratepayer share of the gain. Avista should not be required to file for an exemption from the IRS on excess deferred income taxes as long as such deferred taxes are credited to the benefit of ratepayers. Transaction costs should be deducted from the sales proceeds in determining the net gain to share equally between ratepayers and shareholders.

DATED this 29th day of March, 2000.

Respectfully submitted,

PAINE, HAMBLÉN, COFFIN,
BROOKE & MILLER LLP

By: 
Gary A. Dahlke
Attorneys for Avista Corporation

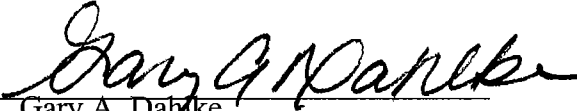
CERTIFICATE OF SERVICE
 UE-991255, UE-991262 and UE-991409

I HEREBY CERTIFY that I served a copy of the foregoing AVISTA CORPORATION'S ANSWER TO PETITIONS FOR RECONSIDERATION upon the parties on the official service list in this proceedings by depositing same in the United States Mail at Spokane, Washington, a true and correct copy thereof, contained in a sealed envelope, with postage prepaid:

WUTC	Honorable Marjorie R. Schaer Administrative Law Judge Washington Utilities & Transportation Comm'n 1300 S. Evergreen Park Drive, SW Olympia, WA 98504-7250
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DATED this 29th day of March, 2000.

By: 
 Gary A. Dahlke