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Sent Electronically and via Overnight Mail

Mr. David Danner, Executive Director and Secretary
Washington Utilities and Transportation Commission
1300 S. Evergreen Park Drive SW
P. O. Box 47250
Olympia, Washington 98504-7250

Re: Notification to Defer Costs Associated with the Palouse Wind Power Purchase Agreement
and Thornton 230 kV Switching Station

Dear Mr. Danner:

Pursuant to WAC 480-100-435 (see "Attachment A") Avista hereby notifies the Commission of its intent to defer costs in connection with the Palouse Wind Power Purchase Agreement (Palouse Wind PPA) and the Thornton 230 kV Switching Station.

Project Description

The Palouse Wind PPA is a 30-year agreement for Avista to purchase all of the generation output and all environmental benefits associated with the Palouse Wind, LLC power project. The Agreement also includes a purchase option after year ten. The Palouse Wind Project will consist of 58 Vestas 1.8 MW wind turbines that will be located 30 miles South of Spokane with a total capacity of approximately 105 MWs (39 aMW energy). The project will be directly connected to the Avista electric system via the Thornton 230 kV Switching Station, and is expected to begin commercial operation by the end of 2012. Test power is expected to be received in mid-September 2012.

Avista's 2009 Integrated Resource Plan (IRP) indicated an approximate need for 50 aMW of qualifying renewable energy credits prior to 2016, in order to meet Washington's renewable portfolio standard (RPS). In early 2011, the 2011 IRP was well into development and identified a slightly lower need level of 42 aMW of qualifying renewable energy credits. In February 2011, Avista decided to issue a request for proposals (RFP) that would meet the Company's 2016 need for qualifying renewable energy credits prior to the December 31, 2012 expiration of renewable energy federal and state tax incentives and other benefits, and also take advantage of the low equipment and construction costs that appeared to be available at the time. The Palouse Wind PPA was selected as a result of the RFP. The Palouse Wind PPA meets Washington's renewable portfolio standard (RPS) under the Energy Independence Act (19.285 RCW).

Notification of Avista's Intent to Defer Costs

Pursuant to Section (3)(a) of WAC 480-100-435 Avista must notify the commission within ten business days of its intent to defer costs associated with an eligible renewable resource as defined in RCW 19.285.030 that the electrical company owns or has entered a power purchase agreement for a term of five or more years. Avista hereby makes such notification to defer costs

associated with the Palouse Wind PPA and the Thornton 230 kV Switching Station that will connect the project to Avista's transmission system.

Section (4) of WAC 480-100-435 states that the deferral begins with the date on which the power plant begins commercial operation or the effective date of the power purchase agreement. Avista proposes that deferrals begin effective with the month that Avista begins to receive test power from the Palouse Wind PPA, potentially anticipated to be on or about September 10, 2012. The Thornton 230 kV Switching Station will be in service when the test power is received.

Avista's pending general rate case filing (Dockets UE-120436 & UG-120437, and UE-110876 & UG-110877 (consolidated)) reflects inclusion of the Palouse Wind PPA and the Thornton 230 kV Switching Station. The Company's pro forma power supply adjustment reflected by Company witness Mr. Johnson includes the expenses and generation related to the purchase from the Palouse Wind PPA. The Company's 2012 Capital Additions adjustment included in Company witness Ms. Andrews testimony and exhibit reflects the capital addition and related costs associated with the Thornton 230 kV Switching Station. Company witness Mr. Lafferty's testimony and exhibits reflect the process of selecting the Palouse Wind PPA. Avista is proposing to defer costs associated with the Palouse Wind PPA and the Thornton 230 kV Switching Station until those costs are recovered through its pending general rate case filing.

The costs that Avista intends to defer are the cost associated with the purchase of test power, the cost of power purchased under the Palouse Wind PPA after test power purchases are concluded, and costs associated with the Thornton 230 kV Switching Station. The price of test power is to be at 80% of the market price of energy when the test power is delivered. When testing is concluded, purchases will be at prices reflected in the Palouse Wind PPA.

Costs associated with the Thornton 230 kV Switching Station include return on investment, depreciation expense, and property taxes. "Attachment B" shows an example calculation as to how the deferral amounts are to be determined. The first and last month of the Thornton 230 kV Switching Station deferrals would be prorated based, in the first month, on when test power begins to be received, and, in the last month, based on the effective date of the general rate increase. Costs would be deferred by debiting a 186 Account and crediting a 407 Account for the Thornton 230 kV Switching Station costs, and crediting or debiting, as appropriate, a 557 Account for the power purchases. Once a prudence determination is made in the rate case, the costs would be transferred from the 186 Account to the ERM Account 182.350 that reflects amounts approved for recovery or rebate.

Please direct any questions related to these filings to Patrick Ehrbar at (509) 495-8620.

Sincerely,



Kelly Norwood
Vice President State and Federal Regulation
RM

WAC 480-100-435

Electrical company deferral of costs associated with long-term financial commitments — Notice and reporting.

(1) An electrical company may account for and defer for later consideration by the commission costs incurred in connection with a long-term financial commitment for:

(a) Baseload electric generation; or

(b) An eligible renewable resource as defined in RCW 19.285.030 that the electrical company owns or has entered a power purchase agreement for a term of five or more years.

(2) Deferred costs may include operating and maintenance costs, depreciation, taxes, and cost of invested capital.

(3) An electrical company deferring costs under subsection (1) of this section must:

(a) Notify the commission within ten business days of its intent to defer such costs; and

(b) File quarterly with the commission a report documenting the balances of costs deferred in a form specified by the commission.

(4) The deferral begins with the date on which the power plant begins commercial operation or the effective date of the power purchase agreement and continues for a period not to exceed twenty-four months; provided that if during such period the company files a general rate case or other proceeding for the recovery of such costs, deferral ends on the effective date of the final decision by the commission in such proceeding. Creation of such a deferral account does not by itself determine the actual costs of the long-term financial commitment, whether recovery of any or all of these costs is appropriate, or other issues to be decided by the commission in a general rate case or other proceeding authorized by the commission for recovery of these costs.

Avista Utilities
 Thornton 230kV Switching Station
 Projected Revenue Requirement
For the First Twelve Months in Service

Line No.	<u>Washington Authorized Rate of Return in UE-100467 & UG-100468</u>			
		Capital		Weighted
	<u>Component</u>	<u>Structure</u>	<u>Cost</u>	<u>Cost</u>
1	Debt	53.50%	5.93%	3.17%
2	Equity	46.50%	10.20%	4.74%
3	Total	100.00%		7.91%
	Effective 12/1/2010. This is the most recent case that specified a rate of return and debt and equity components.			
4	Gross plant - assumed in service mid-September 2012			\$4,350,000
5	Accumulated depreciation			-89,610
6	Accumulated deferred income tax			-103,583 (1)
7	Rate base 12 months after being placed in service			<u>\$4,156,807</u>
8	Average rate base			\$4,253,404
9	Rate of return			<u>7.91%</u>
10	Return requirement			\$336,444
11	Depreciation expense		0.0206	89,610
12	Property tax		0.015	65,250
13	FIT benefit of depreciation and property tax			-54,201
14	FIT benefit of interest			<u>-47,192</u>
15	Total net operating income requirement			\$389,911
16	Net to gross conversion factor - WA			<u>0.620815</u>
17	Total revenue requirement - first twelve months			\$628,063
18	Washington allocation			<u>65.24%</u>
19	Washington portion of revenue requirement			\$409,748
20	Monthly Washington revenue requirement			\$34,146

(1) Calculation of accumulated deferred income tax after twelve months

21	2012 tax depreciation - 3.5 months	0.0375	\$163,125
22	2013 tax depreciation - 8.5 months	0.07219	\$222,435
23	Less book depreciation for 12 months		<u>-89,610</u>
24	Tax depreciation in excess of book depreciation		\$295,950
25	Federal income tax rate		<u>0.35</u>
26	Accumulated deferred income tax at end of 12 months		-\$103,583