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***VIA: Electronic Mail***

September 14, 2012

David Danner

Executive Director and Secretary

Washington Utilities & Transportation Commission

1300 S. Evergreen Park Drive S. W.

P.O. Box 47250

Olympia, Washington 98504-7250

**Re: Comments of Avista Utilities - Docket No. UG-120715**

Dear Mr. Danner,

On May 18, 2012, the Washington Utilities and Transportation Commission (Commission) filed with the Code Reviser a Preproposal Statement of Inquiry (CR-101) to examine whether companies subject to the Commission’s jurisdiction should do more to enhance the safety of their natural gas distribution systems and, if so, to develop appropriate requirements or incentives to accomplish that goal. The Commission issued a notice and is seeking written comments from interested persons on issues related to enhancing pipeline safety. The Commission received comments from interested parties and conducted workshops on June 21, 2012, and July 1, 2012.

On August 24, 2012, The Commission issued a Notice of Request for Pipeline Safety Plans and a Notice of Opportunity to Comment on Proposed Interim Cost Recovery Mechanisms. The Commission stated that they needed additional information before taking further action on pipeline integrity issues. Specifically, the Commission requested that (1) the natural gas utilities provide pipeline replacement plans; and (2) interested parties provide additional comment on two mechanisms that Staff has proposed for interim recovery of costs incurred to accelerate replacement of higher risk pipe.

The Company appreciates the opportunity to provide comments on the two mechanisms that Staff has proposed for interim recovery of costs incurred to accelerate replacement of higher risk pipe. The Company’s response is provided below:

Commission Staff has set forth two proposals for interim recovery of pipeline replacement costs. The first proposal is referred to as the Capital Cost Deferral and Recovery Mechanism (CCDR), and the second proposal is referred to as the Interim Pipeline Replacement Cost Recovery Mechanism (IPL-CRM). Both proposals, as originally drafted, fall short of compensating the Company, on an interim basis, for costs associated with pipeline integrity replacements. This Docket was established to address, in part, “interim cost recovery mechanisms.” The Company does not understand why both cost recovery proposals are clearly designed to be ineffective at truly providing interim cost recovery. Avista’s comments on each proposal are provided below, as well as a proposal that Avista believes should be adopted.

**A. Capital Cost Deferral and Recovery Mechanism (CCDR)**

This proposal would allow the Company to defer a net-of-tax return on eligible projects for later recovery. The deferral would not begin until the first day of the calendar year following the replacement year. No other project costs would be allowed for deferral.

Under Staff’s proposal, there is a lag between the completion date of a project and the date that the deferred return is allowed to be recorded. For example, assume a project was completed in January 2012. Under Staff’s proposal, no return would begin to be deferred until January 1, 2013, with the Company not being allowed to defer a return on its invested capital for a full eleven months. If a project was completed in June 2012, there would be a six-month lag. Also, there is no provision for a carrying cost on the deferred return between the time of the deferrals and the time that the deferrals are included as a component of rate base in a general rate case.

In addition to not allowing for the sufficient recovery of a return on invested capital, the mechanism would not allow for the recovery of the other project costs such as incremental O&M costs, income taxes, property taxes, or depreciation between rate cases. As Avista has stated in the past, timely recovery of costs associated with all prudent utility investments is appropriate and necessary if the utility is to be afforded an opportunity to actually earn the return determined by the Commission to be reasonable. The proposal falls short by not allowing for the recovery of incurred costs and should not be approved.

**B. Interim Pipeline Replacement Cost Recovery Mechanism (IPL-CRM)**

This proposal would allow the Company to recover costs associated with some incremental pipeline replacements between general rate cases. The costs eligible for recovery are rate year depreciation and amortization, income taxes, property taxes, and return on investment, for investments over-and-above the “normal” investment that would otherwise occur without an interim recovery mechanism. Rates would be adjusted with the effective date of the Company’s purchased gas adjustment mechanism for the expected costs during the rate year. There is a true-up mechanism to the extent that actual costs for the rate year are more or less than projected costs.

Avista has no problem with the concept of this recovery mechanism, except that the proposal:

“…would reduce the total investment in pipeline investment by the amount of normalized investment. For example, if a company normally invests $3 million in pipeline infrastructure replacement annually, the amount eligible for recovery outside a rate proceeding would be reduced by $3 million.”

This means that the Company would not be allowed to recover costs associated with those replacements that would normally be budgeted. Only replacements that exceed the “normal” level of replacements would be eligible for cost recovery. This proposal would do nothing to compensate the Company for replacements that it would normally make until those replacements are reflected in a general rate case. It might, however, incent a company to make replacements faster than it normally would, until that level of replacements becomes the new “normal” level. The proposal invites gamesmanship and contention over the “normal” level of replacements, and does nothing to compensate the Company for its normal level of replacements.

Avista does not believe that there should be any cap on the level of replacement eligible for recovery.

**C. Avista Proposal**

Avista has no problem with the IPL-CRM proposal if the proposal is amended to include all eligible pipeline replacements without a reduction for the normal level of replacements. Such a mechanism would allow for the timely recovery of costs.

As Avista has previously stated, replacements are being made because it is the right thing to do, and have not been dependent, conditioned or contingent upon timely recovery of costs, or the presence or absence of a financial incentive. Avista is not receiving timely recovery of new capital investment, including new investment in natural gas pipe. With the use of “historical test-year” ratemaking in Washington there can be a two-year lag, or longer, from the time the new investment is made, and the time the new investment is reflected in rate base in retail rates. Avista believes the timely recovery of prudently-incurred investments should not be viewed as a ‘reward or incentive’ for proper management of its business, but as a basic, equitable principle of regulated cost recovery.

That being said, Avista welcomes a mechanism that allows for the timely recovery of costs and believes the IPL-CRM proposal without a reduction for the normal level of replacements allows for the timely recovery of costs, at least for pipeline replacements, and should be adopted.

Avista appreciates the opportunity to submit these additional comments, if you have any questions regarding this information, please contact Patrick Ehrbar at 509-495-8620 or by email at [pat.ehrbar@avistacorp.com](mailto:pat.ehrbar@avistacorp.com).

Sincerely,



Kelly Norwood

Vice President, State & Federal Regulation

Avista Utilities