

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-080416

DOCKET NO. UG-080417

REBUTTAL TESTIMONY OF

KELLY O. NORWOOD

REPRESENTING AVISTA CORPORATION

I. INTRODUCTION

Q. Please state your name, employer and business address.

A. My name is Kelly O. Norwood. I am employed by Avista Corporation as the Vice-President of State and Federal Regulation. My business address is 1411 E. Mission Avenue, Spokane, Washington.

Q. What is the scope of your rebuttal testimony in this proceeding?

A. I will provide an overview of the Company's reply to the direct and response testimony of the Public Counsel Section of the Washington State Attorney General's Office (Public Counsel) and the Industrial Customers of Northwest Utilities (ICNU). Together with other Company witnesses, I will show that, by correcting simple computational errors in their proposed Federal Income Tax (FIT) adjustment, adding back the uncontested power supply adjustments, and reaffirming the traditional use of straight-line depreciation, the electric revenue requirement of Public Counsel/ICNU would actually exceed that which is contained within the Multiparty Settlement Stipulation. Finally, I will introduce the Company's rebuttal witnesses and discuss why the Multiparty Settlement Stipulation is in the public interest and should be approved by the Commission.

Q. Do you have any initial observations related to the testimony presented by Public Counsel/ICNU?

A. Yes. Public Counsel/ICNU present two witnesses. Mr. Charles W. King addresses alternative depreciation rates and expenses compared to those proposed by the Company. Mr. Michael J. Majoros addresses the Company's revenue requirement, arguing for an electric revenue requirement increase of \$20.118 million as compared to our original request of \$36.617 million, and a natural gas revenue requirement increase of \$0.627 million versus the original request of

1 \$6.587 million. By way of comparison, the Multiparty Settlement Stipulation would increase
2 electric revenues by \$32.5 million, and natural gas revenues by \$4.8 million.

3 The Company will show in its rebuttal testimony that the adjustments proposed by Public
4 Counsel/ICNU that serve to further reduce the revenue requirement are not supported by sound
5 evidence and analysis. For example, the FIT adjustment proposed by Public Counsel/ICNU
6 witness Mr. Majoros reduced the Company's electric revenue requirement by \$5.563 million,
7 comprised of the FIT adjustment of \$3.44 million and the corresponding net conversion factor
8 impact of \$2.12 million, as a result of using a reduced FIT rate. Mr. Majoros' FIT adjustment was
9 not only based on faulty reasoning, but was largely driven by simple computational errors. As will
10 be described further below, even if one were to accept the theory behind this FIT adjustment
11 proposed by Mr. Majoros – which the Company does not – the calculation of this adjustment was
12 done incorrectly, serving to overstate the electric revenue requirement reduction by approximately
13 \$4.358 million. The remaining portion of this adjustment, which approximates \$1.21 million
14 (\$5.563 million – \$4.358 million = \$1.21 million), unrelated to the computational error, is also not
15 supportable for reasons explained in Company witness Mr. Falkner's testimony.

16 These errors with respect to the Public Counsel/ICNU FIT adjustment also apply to the gas
17 revenue requirement. The computational error alone, if corrected, would increase the gas revenue
18 requirement by \$2.714 million, and the remaining portion of the gas FIT adjustment of \$0.777
19 million is not supportable as explained by Mr. Falkner.

20 **Q. Did ICNU or Public Counsel otherwise contest the Power Supply Adjustments**
21 **in the Settlement?**

22 A. No. In fact, ICNU expressly supported the net Power Supply adjustments included
23 in the Multiparty Settlement totaling \$7.433 million (see Section III, Part A), and no issues have

1 otherwise been raised with respect to these Power Supply adjustments in the testimony of Public
2 Counsel/ICNU witnesses.

3 **Q. By eliminating the error caused by Mr. Majoros' incorrect calculation of the**
4 **FIT adjustment, and including the uncontested net Power Supply Adjustments contained**
5 **within the Multiparty Settlement, what effect would that have on Public Counsel/ICNU's**
6 **electric revenue increase recommendation of \$20.118 million?**

7 A. As further described below, these two adjustments alone, i.e., the removal of the
8 FIT error and inclusion of the net Power Supply Adjustments, would total \$11.791 million, and
9 would increase Public Counsel/ICNU's recommended electric revenue increase level from
10 \$20.118 million to \$31.891 million, as compared to the proposed Settlement Agreement increase
11 of \$32.538 million – for a difference of only \$647,000. This is before consideration of extensive
12 rebuttal provided by Avista on a whole host of other adjustments proposed by Public
13 Counsel/ICNU that are, themselves, not reasonable. Acceptance of even a portion of the
14 Company's rebuttal of these issues would result in a revenue increase to Avista that is well above
15 the \$32.538 million that the Company has agreed to accept in the Multiparty Settlement
16 Agreement.

17 **Q. By way of further example, what would be the impact of rejecting Public**
18 **Counsel/ICNU's position with respect to the cost of removal for depreciation purposes.**

19 A. For reasons explained by Company witnesses Mr. Spanos and Mr. Felsenthal on
20 behalf of the Company, what Public Counsel/ICNU propose by way of a sinking fund-type
21 methodology for net salvage represents a significant departure from the long-standing depreciation
22 practices in this and nearly every other jurisdiction. By rejecting their proposal in this regard, and
23 reaffirming existing practice, their recommended revenue requirement would increase by an

1 additional \$3.3 million for electric service and \$1.3 million for natural gas service.

2 **Q. Have you prepared a simplified table that brings together just these elements**
 3 **that have been discussed thus far – i.e. FIT, Power Supply, and Depreciation?**

4 A. Yes. For ease of illustration, I have prepared the following table that isolates the
 5 impact on the revenue requirement of simply adjusting for these three issues, even before addressing
 6 the several remaining revenue requirement issues raised by Public Counsel/ICNU:

7 **Table 1: Impact on Revenue Requirement of Certain Adjustments**

| (Dollars are in thousands) | Impact on Revenue Requirement | |
|---|-------------------------------|-----------------|
| | Electric | Natural Gas |
| Correct for FIT Computational Error (& resulting conversion factor flow through impact) | \$ 4,358 | \$ 2,714 |
| Net Power Supply Adjustments Agreed to in Multiparty Settlement (and endorsed by ICNU) | 7,433 | - |
| Reaffirm Straight-line Depreciation (Re: cost of removal) | 3,057 | 1,197 |
| Total | \$ 14,848 | \$ 3,911 |
| Public Counsel/ICNU Recommended Revenue Requirement | 20,118 | 627 |
| Addition of above 3 items to Recommended Rev. Req. of PC/ICNU | \$ 34,966 | \$ 4,538 |
| Revenue Requirement agreed to in Multiparty Settlement | \$ 32,538 | \$ 4,768 |

8
 9 What this demonstrates is that if we:

- 10 1) simply correct for a computational error in the FIT adjustment (and without ever arguing
 11 the merits of Public Counsel/ICNU's adjustment);
- 12 2) remove Public Counsel/ICNU's Depreciation adjustment for "cost of removal" – a
 13 proposal that flies in the face of Commission precedent here and elsewhere in the country;
 14 and

1 Mr. Don M. Falkner, Assistant Treasurer and Tax Director, addresses the Federal Income
2 Tax adjustment proposed by Mr. Majoros. Mr. Falkner demonstrates the following regarding that
3 FIT proposed adjustment:

- 4 • Mr. Majoros' calculation is simply inaccurate and significantly overstates the
5 proposed adjustment.
- 6 • The proposed adjustments violate jurisdictional cost allocation principles.
- 7 • The proposed adjustments may violate the Internal Revenue Code's normalization
8 provisions.
- 9 • Regulatory bodies such as the WUTC and FERC have previously rejected this type
10 of an adjustment.

11
12 Ms. Elizabeth M. Andrews, Manager of Revenue Requirements, will address the individual
13 revenue requirement adjustments proposed by Public Counsel/ICNU witnesses Mr. Majoros and
14 Mr. King, which materially impact the Company's proposed electric and natural gas revenue
15 requirement.

16 Mr. John J. Spanos, Vice President of the Valuation and Rate Division of Gannett Fleming,
17 Inc., addresses specific accounting adjustments proposed by Public Counsel/ICNU. In summary, he
18 concludes that their net salvage proposals should be rejected because:

- 19 • Their attempt to substitute financial accounting standards for sound and tested
20 ratemaking policies is unreasonable.
- 21 • The depreciation rates and their parameters have already been recently addressed.
- 22 • Public Counsel/ICNU's methodology has not been embraced by this Commission.
- 23 • The traditional net salvage accrual, as presented by Avista, properly matches
24 recovery of service value across generations of ratepayers.
- 25 • Financial Accounting Standard ("FAS") No. 143 does not govern the development
26 of regulatory depreciation rates.

27
28 Mr. Alan D. Felsenthal, Managing Director of Huron Consulting Group, also responds to
29 the direct testimony of Public Counsel/ICNU's witnesses Mr. King and Mr. Majoros on several
30 issues. Mr. Felsenthal concludes that the historical methodology used to include an estimate of

1 “cost of removal” as a component of annual depreciation rates is appropriate and should continue.

2 Further, Mr. Felsenthal concludes:

- 3 • The traditional and widely-accepted regulatory approach to recover cost of removal
4 on a straight-line basis through depreciation charges is the appropriate methodology
5 for such costs.
- 6 • That Avista is not permitted to remove amounts previously accrued for removal
7 costs from accumulated depreciation and record them in income or apply them to
8 some other account without regulatory approval.
- 9 • The accumulated cost of removal obligation is required to fund the future cost of
10 removal activities and is not available to offset other costs, such as the confidential
11 litigation settlement costs.

12
13
14 Ms. Toni E. Pessemier, Advisor to the Office of the President, will provide testimony
15 regarding the Confidential Litigation adjustment.

16

17 **III. CONCLUSION: WHY THE SETTLEMENT IS IN THE PUBLIC INTEREST**

18

19 **Q. What is the Commission being asked to do?**

20 A. The Commission is being asked to approve the Multiparty Settlement Stipulation
21 submitted by the Stipulating Parties, consisting of the Company, the Commission Staff, the
22 Northwest Industrial Gas Users, and the Energy Project. WAC 480-07-750 provides for the
23 Commission to accept—with or without conditions—or reject settlements. Section (1) of this rule
24 states the Commission “will approve settlements when doing so is lawful, the settlement terms are
25 supported by an appropriate record, and when the result is consistent with the public interest in
26 light of all the information available to the commission.” The testimony in support of the
27 Settlement demonstrates this to be the case. The Commission, under the rules, is not being asked
28 to approve an alternative revenue requirement at this time, should the Settlement be rejected. That
29 would be the subject of subsequent proceedings.

1 **Q. Please describe how the Settlement Stipulation is lawful and “supported by an**
2 **appropriate record.”**

3 A. The direct testimony of the Company provides evidence in support of a
4 much-needed revenue requirement. The Company had filed for \$36.6 million in increased electric
5 revenue and for a \$6.6 million increase in natural gas revenues, and its evidence would still support
6 that revenue requirement were this matter to be fully litigated. Indeed, supplemental testimony
7 filed by the Company would suggest an even higher electric revenue requirement would be
8 warranted – i.e., \$47.4 million. The Joint Testimony of the Stipulating Parties supports the
9 Settlement Stipulation and explains its rationale. Further, the Company's rebuttal testimony in
10 response to Public Counsel/ICNU further demonstrates that the Multiparty Settlement Agreement
11 is reasonable and its “end result” falls well within the zone of reasonableness.

12 **Q. What is the effect of the Multiparty Settlement Stipulation?**

13 A. The Multiparty Settlement Stipulation represents a negotiated compromise among
14 the Stipulating Parties. Thus, the Stipulating Parties have agreed that no particular party shall be
15 deemed to have approved the facts, principles, methods, or theories employed by any other in
16 arriving at these stipulated provisions, and that the terms incorporated should not be viewed as
17 precedent setting in subsequent proceedings except as expressly provided. In addition, the
18 Stipulating Parties have the right to withdraw from the Multiparty Settlement Stipulation if the
19 Commission adds any additional material conditions or rejects any material part of the Multiparty
20 Settlement Stipulation.

21 **Q. Why is the Settlement in the public interest?**

22 A. As was explained in the joint testimony in support of the Stipulation, the Settlement
23 strikes a reasonable balance between the interests of Avista’s customers, including limited income

1 customers, and the Company. This Stipulation, if approved, would provide a measure of certainty
2 regarding future cost recovery, which is an important element in improving the Company's
3 financial health and improving its credit standing. The Stipulation was a compromise among
4 differing interests and represents a give-and-take. For example, from Avista's point of view, it
5 does not reflect any adjustment for union wage increases that we know will occur in 2009. Nor
6 does the agreed-upon revenue increase cover the significant capital additions that will occur in
7 2009. As such, the Settlement, even if approved, will not fully address increasing costs during the
8 2009 rate year and represents, if anything, a conservative portrayal of Avista's need for rate relief.

9 The Stipulating Parties have agreed that the Company has demonstrated the need for a
10 revenue requirement increase for both its electric and natural gas customers. It provides not only
11 for the recovery of additional costs, but also for a substantial increase in funding for low-income
12 DSM and LIRAP. It also incorporates agreed-upon changes to the structure of the ERM.

13 The Stipulation was entered into following extensive discovery, audit and review of the
14 Company's filing and its books and records. Staff's comprehensive review of Avista's filing
15 included a review of the Company's per books numbers, test-year results of operations, cost of
16 service model, the proposed rate spread/rate design, capital structure and rate of return.

17 The Settlement represents a negotiated package that appropriately balances the interests of
18 all stakeholders, and the Company and other signing parties request that it be approved by the
19 Commission

20 **Q. Does this conclude your rebuttal testimony?**

21 **A. Yes.**