MEMORANDUM

January 27, 2009

TO: Chairman Sidran
Commissioner Jones
Commissioner Oshie
David Danner
Anne Solwick
Ann Rendahl (w/attachments)
Sally Brown (w/attachments)
Marilyn Meehan
Mike Parvinen

FROM: Lisa Wyse, Records Center

SUBJECT: The Washington State Attorney General's Office, Public Counsel Section, v. Washington Utilities and Transportation Commission (UE-080416/UG-080417 (consolidated))
Petition for Judicial Review
No. 09-2-00171-2

A petition for review has been filed in Superior Court of Washington for Thurston County, on January 27, 2009, by Simon J ffitch, Senior AAG, representing Petitioner listed above. The petition was received by the Commission on January 27, 2009.

Please contact the Records Center if you would like copies of the attachments.

Rob McKenna
ATTORNEY GENERAL OF WASHINGTON
800 Fifth Avenue #2000 • Seattle WA 98104-3188

January 27, 2009

DELIVERED VIA ABC/LMI ON 1/27/09
Betty J. Gould, County Clerk
Thurston County Superior Court
2000 Lakeridge Dr. S.W.
Building 2
Olympia, Washington 98502-6001

RE: The Washington State Attorney General's Office, Public Counsel Section, Petitioner v. Washington Utilities and Transportation Commission, Respondent

Dear Ms. Gould:

Enclosed for filing please find the original and one copy of a Petition for Judicial Review of Final Agency Order, Proof of Service and Thurston County Superior Court Case Information Cover Sheet.

Attached is the voucher in the amount of $200.00 for the filing fee and a self-addressed envelope to process payment.

Sincerely,

Simon J. ffitch
Senior Assistant Attorney General
Public Counsel Section
(206) 389-2055

SJf:cjw
Enclosures

cc: Washington Utilities and Transportation Commission, Chairman Mark Sidran
Gregory Trautman, Assistant Attorney General, WUTC Staff
David J. Meyer, Attorney for Avista Corporation
S. Bradley Van Cleve, Irion Sanger & Allen C. Chan, Attorneys for ICNU
Ronald L. Roseman, Attorney for The Energy Project
Chad M. Stokes, Tommy A. Brooks, Attorneys for NWIGU

CASE TYPE 2

THURSTON COUNTY SUPERIOR COURT

CASE INFORMATION COVER SHEET

Case Number _____ **Case Title** The Washington State Attorney General's Office, Public Counsel Section, Petitioner v. Washington Utilities and Transportation Commission, Respondent

Attorney Name Simon J. ffitch, Assistant Attorney General **Bar Membership Number** WSBA 25977

Please check one category that best describes this case for indexing purposes. Accurate case indexing not only saves time in docketing new cases, but helps in forecasting needed judicial resources. Cause of action definitions are listed on the back of this form. Thank you for your cooperation.

APPEAL/REVIEW
- _X_ Administrative Law Review (ALR 2)
- ___ Appeal of a Department of Licensing Revocation (DOL 2)
- ___ Civil, Non-Traffic (LCA 2)
- ___ Civil, Traffic (LCI 2)

CONTRACT/COMMERCIAL
- ___ Breach of Contract (COM 2)
- ___ Commercial Contract (COM 2)
- ___ Commercial Non-Contract (COL 2)
- ___ Third Party Collection (COL 2)

MERETRICIOUS RELATIONSHIP
- ___ Meretricious Relationship (MER 2)

PROTECTION ORDER
- ___ Civil Harassment (HAR 2)
- ___ Domestic Violence (DVP 2)
- ___ Foreign Protection Order (FPO 2)
- ___ Sexual Assault Protection (SXP 2)
- ___ Vulnerable Adult Protection (VAP 2)

JUDGMENT
- ___ Abstract Only (ABJ 2)
- ___ Foreign Judgment (FJU 2)
- ___ Judgment, Another County (ABJ 2)
- ___ Judgment, Another State (FJU 2)
- ___ Tax Warrant (TAX 2)
- ___ Transcript of Judgment (TRJ 2)

OTHER COMPLAINT/PETITION
- ___ Action to Compel/Confirm Private Binding Arbitration (MSC 2)
- ___ Change of Name (CHN 2)
- ___ Deposit of Surplus Funds (MSC 2)
- ___ Emancipation of Minor (EOM 2)
- ___ Injunction (INJ 2)
- ___ Interpleader (MSC 2)
- ___ Malicious Harassment (MHA 2)
- ___ Minor Settlement (No guardianship) (MST 2)
- ___ Petition for Civil Commitment (Sexual Predator)(PCC 2)
- ___ Seizure of Property from Commission of Crime (SPC 2)
- ___ Seizure of Property Resulting from a Crime (SPR 2)
- ___ Subpoenas (MSC 2)

PROPERTY RIGHTS
- ___ Condemnation (CON 2)
- ___ Foreclosure (FOR 2)
- ___ Land Use Petition (LUP 2)
- ___ Property Fairness (PFA 2)
- ___ Quiet Title (QTI 2)
- ___ Unlawful Detainer (UND 2)

TORT, MEDICAL MALPRACTICE
- ___ Hospital (MED 2)
- ___ Medical Doctor (MED 2)
- ___ Other Health Care Professional (MED 2)

TORT, MOTOR VEHICLE
- ___ Death (TMV 2)
- ___ Non-Death Injuries (TMV 2)
- ___ Property Damage Only (TMV 2)
- ___ Victims of Motor Vehicle Theft (VVT 2)

TORT, NON-MOTOR VEHICLE
- ___ Asbestos (PIN 2)
- ___ Other Malpractice (MAL 2)
- ___ Personal Injury (PIN 2)
- ___ Products Liability (TTO 2)
- ___ Property Damage (PRP 2)
- ___ Wrongful Death (WDE 2)

WRIT
- ___ Habeas Corpus (WHC 2)
- ___ Mandamus (WRM 2)
- ___ Restitution (WRR 2)
- ___ Review (WRV 2)
- ___ Miscellaneous Writs (WMW 2)

IF YOU CANNOT DETERMINE THE APPROPRIATE CATEGORY, PLEASE DESCRIBE THE CAUSE OF ACTION BELOW.

Petition for Judicial Review of Final Agency Order

☐ **EXPEDITE**
☑ **No Hearing Set**
☐ **Hearing is Set**
Date:
Time:

STATE OF WASHINGTON
THURSTON COUNTY SUPERIOR COURT

THE WASHINGTON STATE ATTORNEY GENERAL'S OFFICE, PUBLIC COUNSEL SECTION, Petitioner, v. WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Respondent.	NO. 09-2-00171-2 PETITION FOR JUDICIAL REVIEW OF FINAL AGENCY ORDER

COMES NOW the petitioner, the Public Counsel Section of the Washington State Attorney General's Office (Public Counsel), by and through Senior Assistant Attorney General (AAG), Simon J. ffitch, and petitions pursuant to chapter 34.05 RCW for judicial review of agency action by the respondent, the Washington Utilities and Transportation Commission (Commission). In support of this petition, the petitioner respectfully shows pursuant to RCW 34.05.546 as follows:

/ / /

/ / / /

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

(1) NAME AND MAILING ADDRESS OF PETITIONER:

Public Counsel Section
Washington State Office of the Attorney General
800 5th Avenue, Suite 2000
Seattle, WA 98104-3188

(2) NAME AND MAILING ADDRESS OF PETITIONER'S ATTORNEYS:

Simon J. ffitch, Senior AAG, Section Chief
Sarah A. Shifley, AAG
Public Counsel Section
Washington State Office of the Attorney General
800 5th Avenue, Suite 2000
Seattle, WA 98104-3188

(3) NAME AND MAILING ADDRESS OF AGENCY WHOSE ACTION IS AT ISSUE:

Washington Utilities and Transportation Commission
1300 S. Evergreen Park Dr. SW
P.O. Box 47250
Olympia, WA 98504-7250

(4) IDENTIFICATION OF THE AGENCY ACTION AT ISSUE:

At issue is the final order of the Commission in Avista's 2008 consolidated general rate adjudicative proceeding (general rate case), *Washington Utilities and Transportation Commission v. Avista Corporation d/b/a Avista Utilities*, Docket Nos. UE-080416 and UG-080417 (consolidated). The final order is titled "Order 08, Final Order Approving and Adopting Multi-party Settlement Stipulation And Requiring Compliance Filing." Order 08 was served on Public Counsel on December 29, 2008. A copy of the order is attached to this petition as Attachment A.

(5) IDENTIFICATION OF PARTIES IN ADJUDICATIVE PROCEEDINGS THAT LED TO AGENCY ACTION:

Washington Utilities and Transportation Commission (complainant below)

Avista Corporation, d/b/a Avista Utilities (Avista)(respondent below)

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

Washington Utilities and Transportation Commission Staff (Staff)[1]

Public Counsel

Industrial Customers of Northwest Utilities (ICNU)(intervenor)

Northwest Industrial Gas Users (NWIGU)(intervenor)

The Energy Project (intervenor)

(6) JURISDICTION AND VENUE:

(a) This is an action seeking judicial review of a final order of the Commission. This court has jurisdiction pursuant to Part V of the Washington Administrative Procedure Act, RCW 34.05.510-34.05.598.

(b) Venue is appropriate in Thurston County pursuant to RCW 34.05.514(1)(a).

(7) FACTS THAT DEMONSTRATE THAT THE PETITIONER IS ENTITLED TO OBTAIN JUDICIAL REVIEW:

(a) Petitioner Public Counsel is a section of the Washington State Attorney General's Office that represents the interests of the people of the state of Washington before the Commission. RCW 80.01.100; RCW 80.04.510. Pursuant to this statutory role, Public Counsel represents and advocates for the interests of ratepayers of Washington's regulated natural gas and electric utilities, including natural gas and electricity customers of Avista. As stated above, Public Counsel was a party to Avista's 2008 general rate case adjudicative proceeding which resulted in the final order from which this appeal is taken.

---

[1] In adjudicative proceedings such as this general rate case the Commission's regulatory staff functions as an independent party with the same rights, privileges, and responsibilities as other parties to the proceeding. There is an "*ex parte* wall" separating the Commissioners, the presiding Administrative Law Judge and the Commissioners' policy and accounting advisors from all parties, including regulatory staff. RCW 34.05.455.

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

(b) Respondent Commission is an administrative agency of the state of Washington, established under RCW 80.01.010. The Commission must regulate electric and natural gas companies in the public interest and ensure that the rates charged by such companies are fair, just, reasonable, sufficient, and otherwise consistent with the law. RCW 80.01.040; 80.28.010(1), RCW 80.28.020. In so doing, the Commission considers the consumers' interest in paying the lowest reasonable rate for utility service, sufficient to cover the utility's prudently incurred and lawful costs and to allow an opportunity for a reasonable return on investment.

(c) Avista Utilities, formerly known as Washington Water Power, is a "public service company," an "electrical company," and a "gas company," as those terms are defined in RCW 80.04.010 and used in Title 80 RCW. Avista is engaged in Washington State in the business of supplying electric and natural gas utility service to the public for compensation. Avista's principal place of business is in Spokane, Washington. Avista provides service to approximately 231,000 electricity and 144,000 natural gas customers primarily in Eastern Washington.

(d) Avista filed tariffs at the Commission on March 4, 2008, designed to increase electric and natural gas rates by $36.6 million (10.29 percent) and $6.6 million (3.33 percent), respectively. The Commission suspended the operation of these tariff revisions by Order 01 entered March 6, 2008, pending an investigation and hearing concerning the proposed changes and whether they were just and reasonable. The Commission conducted a prehearing conference on March 28, 2008, and on April 3, 2008, entered Order 02, Prehearing Conference Order, granting various pending petitions to intervene,

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

authorizing formal discovery, entering a protective order, and establishing a procedural schedule.

On July 28, 2008, Avista filed a Motion for Leave to File Supplemental Testimony, including supplemental testimony and exhibits based on updated financial data and power cost inputs which increased its asserted new electric revenue requirement from $36.6 million to $47.7 million. However, Avista did not revise its tariff filing to increase its "as-filed" revenue requirement. Public Counsel opposed the Motion for Leave to File Supplemental Testimony. On August 8, 2008, the Commission entered Order 04, Order Granting the Motion for Leave to File Supplemental Testimony. In Order 04, the Commission extended the date for non-Company parties to file testimony responding to Avista's general rate request from September 12 to September 19, 2008.

On September 16, 2008, prior to the date for filing responsive testimony, Avista, Commission Staff, NWIGU, and The Energy Project (collectively referred to as the "settling parties") filed a Settlement. The Settlement purported to resolve all issues in the rate case proceeding and allow Avista to recover in rates an increase in annual electric revenue of $32.5 million (9.1 percent) and an increase in annual natural gas revenue of $4.8 million (2.4 percent). ICNU supported in part, and opposed in part, the Settlement. Public Counsel did not join the Settlement.

On September 19, pursuant to the case schedule, Public Counsel and ICNU filed joint expert testimony responding to the Avista evidence in support of its general rate request. *Inter alia,* Public Counsel and ICNU proposed 11 adjustments, recommending an increase to electric revenue requirement of $20.1 million (5.6 percent); and a natural

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

gas revenue requirement of $630,000 (.32 percent).[2] On September 23, 2008, the settling parties, except ICNU, filed joint testimony in support of the Settlement.

On October 10, 2008, pursuant to Commission scheduling order, Public Counsel and ICNU filed joint testimony specifically in response to the Settlement. On October 22, 2008, Avista filed rebuttal and Staff filed cross-answering testimony opposing the Public Counsel/ICNU testimony.

The Commission convened an evidentiary hearing in the consolidated proceeding at Olympia, Washington on November 6, 2008, before Chairman Mark H. Sidran, Commissioners Patrick J. Oshie and Philip B. Jones and Administrative Law Judge Patricia Clark. At the hearing, Public Counsel objected to the admission into the record of Avista's supplemental testimony increasing its revenue requirement (the subject of Order 04 referenced above). The objection was overruled.

Avista, Staff, Public Counsel, and ICNU filed simultaneous post-hearing briefs on November 24, 2008.

On December 29, 2008, the Commission issued its final order (Order 08, Attachment A) approving the Settlement Stipulation and authorizing Avista to file compliance tariffs implementing settlement rates, effective January 1, 2009, as requested in the Settlement. Avista made the required compliance tariff filings and the new gas and electric rates went into effect on January 1, 2009, increasing Avista's electric rates by $32.5 million (approximately 9.1 percent) and its gas rates by $4.8 million

[2] At the evidentiary hearing, Public Counsel and ICNU corrected some computational errors. The corrections increased their proposed electric revenue requirement to $24.8 million and the gas revenue requirement to $3.47 million.

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

(approximately 2.4 percent). These rates are now being charged to customers for all electric and gas service provided after January 1, 2009.

(e) Avista's Washington ratepayers are irreparably harmed by the Commission's Order for which judicial review is hereby sought. They must now pay electricity and natural gas rates which the Petitioner believes are unlawful and which are in excess of fair, just, reasonable, and sufficient rates. Avista's customers are entitled to refund of these improper rates. A decision of the court setting aside or reversing the Commission's Order 08, ordering refunds, and remanding the case for further proceedings will substantially redress this harm.

(8) PETITIONER'S REASONS FOR BELIEVING THAT RELIEF SHOULD BE GRANTED:

Public Counsel and the Avista ratepayers it represents are and will continue to be adversely affected by the Commission's Order.

Order 08 violates the procedural and substantive requirements of the Washington Administrative Procedure Act, RCW 34.05.570(3), and of Title 80 RCW in the following respects:

ASSIGNMENTS OF ERROR

A. The Commission Erroneously Interpreted and Applied the Law. RCW 34.05.570(3)(d).

The Commission's final order, Order 08, erroneously interpreted and applied the law in the following respects:

(1) By authorizing recovery from current and future ratepayers for payments to the Coeur d'Alene tribe for costs attributable to past periods, and thus

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

properly recoverable in rates, if at all, only in past periods. This decision is unlawful and in violation of the rule against retroactive ratemaking.

(2) By authorizing recovery from current and future ratepayers for payments to the Coeur d'Alene tribe for costs attributable to claims for past unlawful trespass. Penalties or other payments attributable to unlawful or imprudent conduct are not recoverable from ratepayers.

(3) By allowing Avista to present evidence of and recover electric revenue amounts included in a supplemental increased power cost request several months after its initial rate request without filing a new tariff for the higher requested amount as required by, *inter alia*, RCW 80.28.050, 060, 080 and RCW 80.04.130.

(4) By allowing recovery in rates for unlawful Administrative and General expenses, including charitable and advertising expenses.

(5) By allowing recovery from ratepayers of tax amounts not in fact paid by Avista, in violation of the requirement that ratepayers only be charged in rates for costs actually incurred by the utility in providing service.

B. The Commission's Decision Did Not Decide All Issues Requiring Resolution By the Agency (All Material Issues). RCW 34.05.570(3)(f).

The Commission's final order did not decide all material issues presented in the case. *Inter alia,* the Commission failed to address or decide the following:

(1) The question of whether settlement payments attributable to alleged unlawful conduct (trespass on Coeur d'Alene tribal property) are recoverable in rates.

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

(2) Whether Avista was required to file new tariffs in connection with its supplemental request for additional power costs.

(3) The lawfulness of recovery in rates for seven categories of Administrative and General Expenses, challenged by Public Counsel evidence, totaling over $1.6 million in revenue impact (advertising, charitable donations, dues and membership fees, sporting events, executive base salaries, directors' compensation and shareholder expenses, and Directors and Officers (D&O) insurance).

(4) Whether allowing additional power costs to be included by supplemental testimony circumvents the cost sharing requirements of the Avista ERM (Energy Recovery Mechanism) which requires Avista to share part of the burden of power cost recovery.

C. The Commission's Decision Is Not Supported by Substantial Evidence. RCW 34.05.570(3)(e).

(1) The Commission determination regarding Public Counsel's proposed adjustments to the Administrative and General expenses is not supported by substantial evidence in the record.

(2) The Commission's overall finding that the electric and natural gas rates resulting from the Settlement are fair, just, reasonable and sufficient for service provided by Avista is not supported by substantial evidence in the record.

/ / /

/ / / /

/ / / / /

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

D. Inconsistent With Agency Rule. RCW 34.05.570(3)(h).

(1) The Commission's decision regarding Administrative and General expenses is inconsistent with WAC 480-90-223 and 480-100-223 (advertising or marketing expenses);

(2) The Commission decision allowing supplementary evidence that increased Avista's revenue request is inconsistent with the Commission's Order 01 in this proceeding which does not permit Avista to change or alter its tariffs filed in this docket during the suspension period unless authorized by the Commission.

(9) PETITIONER'S REQUEST FOR RELIEF:

Pursuant to RCW 34.05.570 and 34.05.574, Public Counsel respectfully requests relief as follows:

1. For an entry of judgment vacating or setting aside Order No. 08;
2. Identifying the errors contained in the order;
3. Finding that the current rates are unlawful;
4. Remanding this matter to the Commission for further proceedings consistent with these rulings and rejecting Avista's new tariffs;
5. Finding that ratepayers are entitled to refund; and,

/ / /

/ / / /

/ / / / /

/ / / / / /

/ / / / / / /

/ / / / / / / /

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

6. For such other relief as the Court deems just and appropriate.

RESPECTFULLY SUBMITTED this 27th day of January, 2009.

ROBERT M. McKENNA
ATTORNEY GENERAL

By: _____

Simon J. ffitch
WSBA 25977
Senior Assistant Attorney General
Public Counsel

Sarah Shifley
WSBA 39394
Assistant Attorney General
Public Counsel

ATTORNEY GENERAL OF WASHINGTON
Public Counsel
800 Fifth Avenue, Suite 2000
Seattle, WA 98104-3188
(206) 464-7744

PROOF OF SERVICE

I certify that I served a copy of this document on all parties or their counsel of record on the date below as follows:

☒ Delivered documents via ABC/Legal Messenger to:

Chairman Mark Sidran
Washington Utilities and Transportation Commission
Records Center
1300 S. Evergeen Park Dr. SW
P.O. Box 47250
Olympia, WA 98504-0128

Office of The Attorney General
Gregory J. Trautman
Assistant Attorney General, Attorneys for WUTC Staff
1400 S. Evergreen Park Dr. SW
P.O. Box 40128
Olympia, WA 98504-0128

☒ Sent copies via US Mail Postage Prepaid via Consolidated Mail Service to:

Avista Corporation
David J. Meyer
P.O. Box 3727
1411 E. Mission Ave., MSC-13
Spokane, WA 99220-3727

ICNU
S. Bradley Van Cleve, Irion Sanger, and
Allen C. Chan
Davison Van Cleve, P.C.
333 S.W. Taylor, Suite 400
Portland, OR 97204

The Energy Project
Ronald L. Roseman
Attorney At Law
2011 14th Avenue East
Seattle, Washington 98112

Northwest Industrial Gas Users
Chad M. Stokes and Tommy A. Brooks
Cable Huston Benedict Haagensen & Lloyd LLP
1001 SW Fifth Avenue, Suite 2000
Portland, OR 97204-1136

☒ Sent courtesy copy electronically to all parties above on January 27, 2009.

I certify under penalty of perjury under the laws of the state of Washington that the foregoing is true and correct.

DATED this 27th day of January, 2009, at Seattle, WA.

Carol Williams
Legal Assistant for Public Counsel
(206) 464-6215

ATTACHMENT A

ORDER 08 - FINAL ORDER APPROVING AND ADOPTING MULTI-PARTY SETTLEMENT STIPULATION AND REQUIRING COMPLIANCE FILING (DOCKET NOS. UE-080416 AND UG-080417 (CONSOLIDATED)

BEFORE THE WASHINGTON STATE UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,	)	DOCKETS UE-080416 and UG-080417 *(consolidated)*
Complainant,	)	
	)	ORDER 08
v.	)	
AVISTA CORPORATION, d/b/a AVISTA UTILITIES,	)	FINAL ORDER APPROVING AND ADOPTING MULTI-PARTY SETTLEMENT STIPULATION AND REQUIRING COMPLIANCE FILING
Respondent.	)	

Synopsis: *The Commission approves and adopts the Multi-party Settlement Stipulation entered into among Avista, the Commission's Staff, Northwest Industrial Gas Users, and The Energy Project, and, in part, the Industrial Customers of Northwest Utilities as a reasonable resolution of Avista's request for increases in electric and natural gas rates.*

The Settlement resolves the issue of what rates consumers will pay commencing January 1, 2009, for electric and natural gas service provided by Avista. The Commission finds reasonable the parties' agreed $32.5 million, or 9.1 percent rate increase, in annual electric revenues, and a $4.8 million, or 2.4 percent, rate increase in annual natural gas revenues. The Commission requires Avista to file electric service and natural gas service tariff sheets in compliance with the terms and conditions of the Settlement.

TABLE OF CONTENTS

SUMMARY

1 **NATURE OF PROCEEDING.** On March 4, 2008, Avista Corporation d/b/a Avista Utilities (Avista or Company) filed with the Washington Utilities and Transportation Commission (Commission) revisions to its currently effective Tariff WN U-28, Electric Service, in Docket UE-080416, and revisions to its currently effective Tariff WN U-29, Gas Service, in Docket UG-080417. The proposed revisions would implement a general rate increase of $36.6 million, or 10.3 percent, for electric service and $6.6 million, or 3.3 percent, for gas service. The Commission suspended the filings on March 6, 2008, consolidated the two dockets, and set the dockets for hearing.

2 **MULTI-PARTY SETTLEMENT.** On September 16, 2008, Avista, the Commission's regulatory staff (Commission Staff or Staff) [1] Northwest Industrial Gas Users (NWIGU), and The Energy Project filed a Multi-party Settlement Stipulation (Settlement) resolving all disputed issues between those parties. The Settlement, if approved and adopted by the Commission, would resolve all issues in the proceeding and allow Avista to recover in rates an increase in annual electric revenue of $32.5 million (9.1 percent) and an increase in annual natural gas revenue of $4.8 million (2.4 percent). Industrial Customers of Northwest Utilities (ICNU) joins in part, and opposes in part, the Settlement's terms and conditions. Public Counsel opposes the Settlement.

---

[1] In formal proceedings, such as this, the Commission's regulatory staff functions as an independent party with the same rights, privileges, and responsibilities as other parties to the proceeding. There is an "*ex parte* wall" separating the Commissioners, the presiding Administrative Law Judge, and the Commissioners' policy and accounting advisors from all parties, including regulatory staff. *RCW 34.05.455.*

3 **APPEARANCES.** David Meyer, attorney, Spokane, Washington, represents Avista. Greg Trautman and Michael Fassio, Assistant Attorneys General, Olympia, Washington, represent Staff. Ron Roseman, attorney, Seattle, Washington, represents The Energy Project. Chad Stokes, attorney, Portland, Oregon, represents NWIGU. Irion Sanger, attorney, Portland, Oregon, represents ICNU. Simon ffitch, Assistant Attorney General, Seattle, Washington, represents Public Counsel.

4 **COMMISSION DETERMINATION.** The Commission finds on the basis of the evidence presented that Avista requires rate relief for its electric and natural gas service operations and determines that the Settlement results in a reasonable resolution of the issues in this proceeding and is in the public interest. The rates that will result from adoption and approval of the Settlement are fair, just, reasonable, and sufficient.

MEMORANDUM

I. Background and Procedural History

5 Avista provides electric and natural gas service within a 26,000 square mile area of eastern Washington and northern Idaho including approximately 231,000 electric customers and 143,561 natural gas customers in Washington.

6 Avista filed tariffs on March 4, 2008, designed to increase electric and natural gas rates by $36.6 million (10.29 percent) and $6.6 million (3.33 percent), respectively. The Commission suspended the operation of these tariff revisions by Order 01 entered March 6, 2008, pending an investigation and hearing concerning the proposed changes and whether they are just and reasonable. Avista's initial request was based on:

- A test year ending December 31, 2007.
- An overall rate of return of 8.43 percent.
- A rate of return on common equity of 10.8 percent.
- A capital structure with 46.3 percent common equity.

- Total *pro forma* electric operating revenues of $448 million; a $36.6 million (10.3 percent) increase.
- Total electric rate base of $951 million.
- Total *pro forma* natural gas operating revenues of $206 million; a $6.6 million (3.3 percent) increase
- Total natural gas rate base of $173 million.

7 The Commission conducted a prehearing conference on March 28, 2008, and on April 3, 2008, entered Order 02, Prehearing Conference Order, granting various pending petitions to intervene, authorizing formal discovery, entering a protective order, and establishing a procedural schedule. On June 16, 2008, the Commission entered a Notice of Hearing scheduling public comment hearings in Pullman and Spokane, Washington, on September 18, 2008.

8 On July 28, 2008, Avista filed a Motion for Leave to File Supplemental Testimony, including supplemental testimony and exhibits based on updated financial data and power cost inputs which increased its revised electric revenue requirement to $47.7 million. However, Avista did not revise its tariff filing to increase its "as-filed" revenue requirement. Public Counsel opposed the Motion for Leave to File Supplemental Testimony. On August 8, 2008, the Commission entered Order 04, Order Granting the Motion for Leave to File Supplemental Testimony.

9 On September 16, 2008, Avista, Commission Staff, NWIGU, and The Energy Project (collectively referred to as the "settling parties") filed a Settlement. The Settlement, if approved and adopted by the Commission, would resolve all issues in this proceeding and allow Avista to recover in rates an increase in annual electric revenue of $32.5 million (9.1 percent) and an increase in annual natural gas revenue of $4.8 million (2.4 percent).

10 ICNU supports, in part, and opposes, in part, the Settlement. Public Counsel opposes the Settlement. ICNU and Public Counsel (collectively referred to as the "joint parties") filed joint responsive testimony on September 19, 2008. The joint parties

proposed 11 adjustments, including some to Avista's original filing that purported to support an electric revenue requirement of $20.1 million, or a 5.6 percent increase, and a natural gas revenue requirement of $.63 million or a .32 percent rate increase.[2] Their proposed adjustments included: adopting a consolidated tax adjustment that reduces Avista's federal income tax rate; modifying depreciation expense; sharing the cost of Director's and Officer's (D&O) insurance between shareholders and ratepayers; disapproving the costs of the confidential litigation; reclassifying non-legal asset removal obligations (AROs), removing certain advertising, administrative and general (A&G), and charitable contribution expenses; removing half of Avista's claim for directors' compensation and all claims for shareholder services expenses; disallowing certain dues and membership fees; and, reducing executive compensation.

11 On September 23, 2008, the settling parties, except ICNU, filed joint testimony in support of the Settlement. On September 26, 2008, the Commission convened a second prehearing conference to consider revising the procedural schedule in light of the settling parties' request that the Settlement be approved effective January 1, 2009. By Order 06, Prehearing Conference Order, entered October 8, 2008, the Commission established a revised procedural schedule and scheduled this matter for hearing November 6, and 7, 2008.

12 On October 10, 2008, the joint parties filed testimony in response to the Settlement adhering to the recommendations in their responsive testimony. On October 22, 2008, Avista filed rebuttal and Staff filed cross-answering testimony opposing the joint parties' testimony. On November 5, 2008, the joint parties filed a corrected exhibit on behalf of their witness, Michael Majoros. On November 6, 2008, and again on November 10, the joint parties filed a second and third corrected exhibit on behalf of Mr. Majoros. On November 19, 2008, the joint parties filed a revised exhibit on behalf of witness Charles King. On November 21, 2008, the joint parties filed a fourth corrected exhibit on behalf of Mr. Majoros.

---

[2] At hearing, Public Counsel and ICNU corrected some computational errors that increased the proposed electric revenue requirement to $24.8 million and the gas revenue requirement to $3.47 million. The joint parties' revised revenue requirement is fully discussed later in this Order.

13 The Commission conducted public comment hearings in Pullman and Spokane, Washington, on September 18, 2008. One consumer presented testimony in Pullman, ten consumers presented testimony in Spokane, and more than 1,700 consumers filed written comments largely in opposition to the proposed rate increase.[3]

14 The parties prefiled extensive testimony and exhibits sponsored by 25 witness, including 19 for Avista, two for Staff, one for NWIGU, one for The Energy Project, and two by the joint parties. The Commission convened an evidentiary hearing in this consolidated proceeding at Olympia, Washington on November 6, 2008, before Chairman Mark H. Sidran, Commissioners Patrick J. Oshie and Philip B. Jones and Administrative Law Judge Patricia Clark. Altogether, the record includes more than 192 exhibits entered during the evidentiary hearing. Avista, Staff, Public Counsel, and ICNU filed simultaneous post-hearing briefs on November 24, 2008.

II. Proposed Multi-party Settlement

15 A copy of the Settlement is attached to this Order as Appendix A and, by this reference, incorporated herein. If there is any discrepancy between our summary and the terms and conditions in the Settlement, the latter controls. We summarize here the primary provisions of the Settlement:

- An increase of $32.5 million in Avista's annual revenue requirement for electric service and $4.8 million for natural gas service. Both of these figures include the effect of the agreed-upon return on equity and overall rate of return.

- An overall rate of return of 8.22 percent including a return on equity of 10.2 percent and a capital structure equity share of 46.3 percent.

- Power Supply-Related Adjustments. These adjustments include a hydro filtering adjustment that lowers the *pro forma* power costs by $1.6 million, lowers net power costs of $136,000 reflecting an adjustment to the WNP-3

[3] Absent objection, the Commission admits into evidence two exhibits received after the evidentiary hearing; Exhibit No. 6 which is a compilation of public comments filed by Public Counsel on November 14, 2008, and Public Counsel and ICNU's response to Bench Request No. 4, filed November 19, 2008.

contract, adjusts natural gas fuel costs upward by $8.5 million, corrects a mathematical error in Colstrip fuel cost lowering fuel costs by $877,000, and adjusts rate base upward by $8.7 million to reflect an upgrade at the Noxon hydroelectric generation plant. Altogether, these five adjustments to power supply costs increase revenue requirement $7.4 million.

- Accounting Treatment for Spokane River Project Relicensing and certain Litigation Expenses. The settling parties agree that the expenses filed in this case were prudently incurred, but should not be collected in rates until Avista receives the final license for the Spokane River Project from the Federal Energy Regulatory Commission (FERC). They further agree, once Avista receives the license, to defer as a regulatory asset Washington's share of the depreciation/amortization associated with relicensing costs and related expenditures, together with a carrying charge on the deferral, as well as a carrying charge on the amount of relicensing costs not yet included in rate base. Any costs that exceed the *pro formed* costs filed in this case would be considered in a separate filing.

- Treatment of Montana Riverbed Litigation Expenses. The settling parties agree to Avista's requested amortization of costs, together with recovery of accrued interest on Washington's share of the deferral and the weighted cost of debt, net of the related deferred tax benefit.

- Modify the Energy Recovery Mechanism (ERM). This adjustment incorporates a level of asymmetry in the ERM by giving customers a greater share of benefits when power expenses are lower than the authorized level and retaining the current sharing proportion when power expenses exceed the authorized level.

- Increase the Low Income Rate Assistance Program (LIRAP) and Demand Side Management (DSM) funding. LIRAP annual funding is increased by $500,000 to an annual funding level for electric low- income customers of $2,864,000 and $1,580,000for natural gas customers. DSM funding increases by $350,000 over the existing level of $1,132,000.

- Consolidate all Line Item Adjustments to a stipulated amount.

- The proposed change in rates would go into effect of January 1, 2009.

III. Standard for Review

A. Settlements.

16 Our standard for reviewing proposed settlements is found in WAC 480-07-750(1): "The commission will approve settlements when doing so is lawful, the settlement terms are supported by an appropriate record, and when the result is consistent with the public interest in light of all the information available to the commission."

17 In reviewing the settlement we ask:

(1) Whether any aspect of the proposal is contrary to law.

(2) Whether any aspect of the proposal offends public policy.

(3) Whether the evidence supports the proposed elements of the settlement as reasonable resolution of the issues at hand.

18 We may decide to:

- Approve the proposed settlement without condition.
- Approve the proposed settlement subject to condition(s).
- Reject the proposed settlement.

19 If we approve the proposed settlement without condition, it is adopted as the Commission's resolution of the proceeding. If we approve the proposed settlement subject to one or more conditions, the settling parties will have an opportunity to give notice, within seven days, that they find the condition(s) unacceptable and withdraw from the Settlement. If that occurs, or if we reject the proposed settlement, our rules provide that the proceeding will return to its posture as of the day before the settlement was filed. If this occurs, then we will conduct such further process as is

required to allow fully adjudicated results considering the parties' respective litigation positions and due process rights.

20 In reaching a decision, we emphasize that our purpose is to determine whether the settlement terms are lawful and in the public interest. We do not consider the settlement's terms and conditions to be a "baseline" subject to further litigation. If opponents of a settlement demonstrate that its terms are not in the public interest, we may modify the terms in question, or reject the settlement in its entirety. Should we modify a settlement, the settling parties may withdraw from the agreement, which has the same practical effect as our rejecting a settlement; the case goes to hearing.

B. Ratemaking Principles.

21 The Commission is charged by statute with the responsibility to regulate public utilities in the public interest. In the context of establishing rates for electric and natural gas companies, this responsibility is reflected by the Commission's determination that proposed rates are fair, just, reasonable, and sufficient. This standard balances consumers' interests in paying the lowest reasonable rates for utility service, while providing the utility with rates sufficient to recover prudently incurred costs and an opportunity to earn a return on its investment. The allowed return on investment must be adequate to allow the utility to attract required capital at reasonable rates and on reasonable terms.

IV. Discussion and Decision

22 Avista bears the burden of proof in this proceeding and supports adoption and approval of the Settlement. Our focus here is to determine whether the Settlement is lawful and in the public interest. Ordinarily we would address the terms and conditions of the Settlement first. However, two adjustments proposed by the joint parties form the basis for a significant portion of the difference between the revenue requirements proposed by the settling parties and the joint parties. Accordingly, in the interest of judicial economy we address those adjustments first as our ruling on those issues substantially affects the outcome of our final determination.

A. Joint Parties' Adjustments to Original Filing.

1. Federal Income Tax (FIT) Adjustment.

23 In responsive testimony, the joint parties proposed that Avista Utilities' federal income tax rate be lowered from the 35 percent statutory rate to an "effective tax rate" of 31 percent based on a Consolidated Tax Adjustment (CTA) which offsets Avista Utilities' projected tax liability with the tax liabilities of some, but not all, of Avista Corporation's subsidiaries.[4] According to the joint parties', the CTA recognizes that Avista Corporation has several subsidiary companies that incurred tax losses during the 2005 and 2006 tax years. Thus, they argue that Avista's parent paid less in total federal income taxes than the sum of the tax liabilities of each company.[5] They conclude that the Commission should recognize the unregulated subsidiaries' tax losses as a benefit that should flow through to ratepayers of the regulated utility.

24 In preparing the CTA, the joint parties also adjust Avista Utilities' taxable income to remove the benefits of accelerated depreciation and income tax credits based on a private letter ruling from the Internal Revenue Service (IRS).[6] The joint parties contend that Avista will not lose its accelerated depreciation tax benefits as result of this adjustment. With these benefits removed, the CTA reduces the revenue requirement by $3.4 million for electric service and $3.1 million for gas service.

25 In rebuttal, Avista explains that while all Avista companies file a consolidated tax return, the IRS requires that actual taxable income be computed for each separate legal entity.[7] The statutory tax rate for the consolidated companies and for Avista is the same, 35 percent.[8] In addition, Avista corrects a computational error in the joint parties' CTA calculation that incorrectly applied the full pre-tax impact of subsidiary losses as a reduction to Avista's tax expense rather than the tax effect of the losses.[9] While not supporting a CTA, Avista calculates the corrected effective tax rate to be

---

[4] Majoros, Exh. No. MJM-1TC at 11-14 and Exh. No. MJM-6.
[5] Majoros, Exh. No. MJM-4TC at 12.
[6] Majoros, Exh. No, MJM-4TC at 13.
[7] Fallkner, Exh. No. DMF-1T at 4.
[8] *Id.*
[9] *Id.* at 5.

34 percent rather than 31 percent, and points out that the CTA does not properly allocate between the jurisdictions in which it operates. Correcting for the proper allocation between jurisdictions and calculating Washington's jurisdictional share of the loss, the combined electric and natural gas tax savings associated with subsidiary company losses would reduce the joint parties' proposed $4.324 million adjustment to $910,717.[10]

26 After correcting the computational and jurisdictional allocation errors, Avista confronts the CTA's premise by noting that the joint parties selected only subsidiaries with tax losses and excluded those with taxable gains.[11] Avista argues that legal entities under the same parent should not necessarily share taxable gains and losses.[12] Rather, tax liabilities should be segregated based on whether the taxable event resulting in a gain or loss occurred because of regulated or unregulated activities.[13] Finally, Avista asserts that the theory of a CTA may violate IRS normalization principles.[14]

27 At hearing, the joint parties acknowledged a computational error in the calculation of the CTA and revised their exhibits to reflect a proposed increase to electric revenue requirement from $20,118,000 to $24,477,000 and a proposed increase to gas revenue requirement from $627,000 to $3,441,000.[15]

Commission Determination.

28 In establishing rates for regulated utilities, we have followed well-established principles regarding the segregation of regulated and non-regulated operations, as they are fundamentally different in nature and purpose.[16] Regulated operations serve

---

[10] *Id.*
[11] *Id.* at 10.
[12] *Id.* at 9.
[13] *Id.*
[14] *Id.* at 2.
[15] Majoros, Exh. No. MJM-9C at 1-2.
[16] *WUTC v. Washington Natural Gas Company,* Docket UG-920840, 4th Supplemental Order, (September 27, 1993) at 14-16; *In the Matter of the Application of Puget Sound Energy, Inc. For an Order Approving a Corporate Reorganization to Create a Holding Company, Puget Energy, Inc.,* Docket UE-991779, Order Accepting Stipulation (August 15, 2000) at 2; *WUTC v. Avista Corporation d/b/a Avista Utilities,* Docket UG-021584 (February 13, 2004) at 3; *In the Matter of*

the public with rates and conditions of service established by the Commission according to regulatory principles embodied in statutes and rules that protect the public from monopoly rents and unreasonable terms and conditions. On the other hand, non-regulated operations are competitive enterprises offering services and products unnecessary to, and many times wholly unrelated to, the utility service offered to the public.[17]

29 Consistent with our regulatory principles, if a utility's costs are prudently incurred and if property is used and useful in providing utility service, it is entitled to recover those costs and to place such property in its rate base, where it may recover and have an opportunity to earn a reasonable return on its original investment.[18] Conversely, a utility is not allowed to recover in customer rates costs or expenses related to activities that do not provide service to its ratepayers.[19] For this reason, we strive to isolate ratepayers from the impacts of a utility's non-regulated activities, concluding that ratepayers should not be required to subsidize or be exposed to the risks of the non-regulated operations of a utility. Should a compelling reason be shown to commingle regulated and non-regulated operations, the costs and benefits must go hand in hand. We must ensure that the costs and burdens do not flow disproportionately to regulated operations, while the beneficial aspects flow disproportionately to non-regulated activities.

30 The principle of segregating regulated and non-regulated operations has been emphasized in several recent proceedings involving the acquisition of utility companies or the formation of holding companies following enactment of the federal

---

the Application of Avista Corporation d/b/a Avista Utilities, for an Order Approving a Corporate Reorganization To Create a Holding Company, AVA Formation Corp,, Docket U-060273, Order 03(February 28, 2007) at 5-7.

[17] The prices and quality of services or products offered by such competitive enterprises are governed by the actions of the consumer, who is expected to act according to the principles of a free market.

[18] Calculation of the rate base and the reasonableness of return on investment are fundamental elements of a utility's revenue requirement.

[19] *See* n.16; Docket U-060273, Order 03 (February 28, 2007) at 6. In fact, we have required "ring-fencing" provisions in acquisition cases in order to isolate utility operations from any negative financial impacts that could flow from unregulated operations. *See* Order 03 in Docket U-060273 cited above and *WUTC v. PacifiCorp d/b/a Pacific Power & Light Company, Docket UE-050684, Order 04 (April 17, 2006) at 59.*

Energy Policy Act of 2005, including repeal of the Public Utility Holding Company Act of 1935, effective February 8, 2006.[20] These acquisitions were approved with specific "ring-fencing" provisions intended to isolate utility operations from any negative financial impacts flowing from unregulated units.[21] The isolation aspects of ring-fencing provisions are intended: "(1) to ensure that the utility maintains a strong credit rating and can attract capital; (2) to prevent cross-subsidization of non-regulated ventures; and (3) to ensure regulators' access to timely and accurate information."[22] In our approval of the Avista Corporation's reorganization, we specifically found that after reorganization there would be "no link between the non-regulated businesses and Avista [Utilities]" and that several measures were in place to ensure that "there are appropriate cost allocation principles and standards in effect to ensure that Avista [Utilities] will not be subject to cross-subsidization."[23] Our recent reinforcement of the principle of segregating regulated and non-regulated operations means the proponent of consolidation should present a compelling reason for us to stray from these principles.[24] The joint parties do not offer one here.

31 Rather, the CTA proposes a simple, though unbalanced adjustment that would offset Avista Utilities' tax liability with the tax benefits associated with some, but not all, of Avista Corporation's non-regulated subsidiaries. Specifically, it isolates, for ratemaking consideration, only those operations of non-regulated enterprises that had

---

[20] In the Matter of the Joint Application of MidAmerican Energy Holdings Company and PacifiCorp, d/b/a Pacific Power & Light Company For an Order Authorizing Proposed Transaction, Docket UE-005190, Order 07 (February 22, 2006); Docket U-060273, Order 03 (February 28, 2007); In re Application of MDU Resources Group, Inc. & Cascade Natural Gas Corp. Docket UG-061721, Order 06 (June 27, 2007).

[21] Order 03 in Docket U-060273 at 6. For a full citation, see n. 16.

[22] Order 03 in Docket U-060273 at 6 quoting *Mergers and Ring-Fencing Issues: An Oregon Perspective,* Oregon Public Utility Commissioner Ray Baum presentation at the Technical Conference on Public Utility Holding Company Act of 2005, December 7, 2006.

[23] Order 03 in Docket U-060273 at 7. We note that AVA Holdings will not be formed until the commissions in all jurisdictions in which Avista operates approves the transaction.

[24] While we recently found moot a CTA proposed by ICNU, we concluded that should parties recommend similar adjustments in future proceedings, we expected a full airing of the appropriate accounting for deferred taxes arising from the parent company's payment of taxes on a consolidated basis as well as the principles of the benefit-burden test in this context. *WUTC v. PacifiCorp d/b/a Pacific Power & Light Company,* Docket UE-050684, Order 04 (April 17, 2006) at 59. The benefit-burden test was not adequately addressed by the joint parties in the proposed CTA.

taxable losses and does not include those that had taxable income in the 2005 and 2006 tax years.[25] In other words, the joint parties "cherry pick" those subsidiaries with a tax impact that is favorable to a CTA without including those that had tax liabilities. Focusing solely on those entities with tax losses is inconsistent, unbalanced and unfair; reasons enough to reject the concept. Even if we "corrected" the CTA to base the adjustment on the performance of all non-regulated operations, we would be placed in the untenable position of requiring ratepayers to subsidize those operations with taxable gains. Finally, under either circumstance, the CTA violates the principle, if not the letter, of our recent decisions establishing "ring-fences" that protect ratepayers from non-regulated activities by declining to pull benefits or burdens from activities "outside the ring-fence" into the regulated business. Not only are we provided no reason to act contrary to our recent precedent in this regard, doing so here could jeopardize the integrity of the rationale for "ring-fencing" and undermine its defensibility if it were attacked.

32 Even ignoring our concerns for the CTA's adherence to our established regulatory framework, we find it has little impact on the revenue requirement proposed by the Settlement. First, we note that the CTA was replete with computational errors that were corrected by Avista on rebuttal and acknowledged by the joint parties at hearing.[26] The joint parties initially applied the entire pre-tax loss, not the tax impact of the loss and failed to allocate it between the jurisdictions in which Avista operates.[27] After correcting these errors, the difference between the statutory rate of 35 percent and the corrected "effective tax rate" of 34 percent is *de minimis*; a difference that would not warrant adoption of the CTA or rejection of the Settlement.

33 Finally, we are concerned that the isolation aspect of the CTA may violate provisions of the Internal Revenue Code (IRC). Avista must apply consistent treatment to its tax expense, depreciation expense, reserve for deferred taxes, and rate base or it may violate the normalization provisions of the IRC. The joint parties propose an

---

[25] Falkner, Exh. No. DMF-1 at 4 and 7. As noted by Falkner, only one subsidiary of the Avista consolidated group had a loss in 2007.

[26] In its uncorrected form, we give this testimony little, if any, weight given the number of errors embodied in the CTA.

[27] Falkner, Exh. No. DMF-1T at 5.

adjustment only to tax expense. This creates a classic Hobson's choice:[28] if Avista consistently includes non-regulated property in tax expense and rate base in order to comply with the normalization provisions of the IRC, then it will run afoul of the basic ratemaking principle that non-regulated property cannot be placed in rate base.

34 In sum, we reject the joint parties' CTA for the reasons expressed above, finding the weaknesses of its theory and application in this case to overwhelm any alleged benefits.

2. Depreciation.

35 In its original filing, Avista makes *pro forma* adjustments to reduce electric depreciation expense by $326,000 and gas depreciation expense by $330,000 pursuant to the depreciation study approved by the Commission in the last general rate case.[29] The joint parties propose to further decrease depreciation expense by modifying Avista's calculation of removal costs for certain categories of electric and natural gas plant in service. Their proposal would reduce the Company's depreciation expense for electric transmission and distribution plant downward by $3,733,975 and for natural gas distribution plant downward by $1,808,729.[30]

36 In response to Bench Request No. 4, the joint parties corrected an error in their depreciation adjustment thereby increasing their proposed depreciation expense by $513,268 for the electric utility and by $195,422 for the natural gas utility.[31] As a result, the joint parties' further revised their exhibits to reflect increases in their proposed recommended electric revenue requirement from $24,477,000 to

---

[28] An apparently free choice that offers no real alternative. [After Thomas Hobson (1544-1630), English keeper of a livery stable, from his requirement that customers take either the horse nearest the stable door or none.]

[29] Andrews, Exh. No. EMA-1T at 14 and 33. Andrews, Exh. No. EMA-2 at 5. Andrews, Exh. No. EMA-3 at 4. *WUTC v. Avista Utilities,* Dockets UE-070804/UG-070805, Order 05 (December 19, 2007). In Order 05, the Commission approved and adopted an uncontested settlement stipulation.

[30] King, Exh. No. CWK-1T at 2.

[31] *See* n. 3 and King, Exh. No. CWK-4 (revised November 19, 2008) at 1.

$24,841,000 and the proposed gas revenue requirement from $3,341,000 to $3,471,000.[32]

37 The joint parties contend that Avista's depreciation study is flawed because it uses an inappropriate method to estimate and recover "removal costs" for plant that is treated in aggregate, or as "mass property."[33] They assert that the conventional procedure for accruing removal costs increases the depreciation rate in an amount sufficient to collect these costs over the life of the plant.[34] By using a ratio that compares current dollars of removal expense to past dollars of original plant cost, they argue that Avista's method "grossly overestimates removal cost."[35]

38 They argue further that the proper method for accruing removal costs should be based on the accounting standards in Financial Accounting Standard (FAS) 143, applicable to removal costs required by law, regulation, or contract.[36] They point out that the FAS 143 method recognizes the change in the value of dollars (due to inflation) during the life of an asset and allocates that value to each of the years in which removal costs are accrued.[37] Using the FAS 143 method, the joint parties recalculate and reduce Avista's depreciation expense in the amounts expressed above.[38] The joint parties contend such a reduction would remedy the "intergenerational inequity" created by Avista's depreciation methodology."[39]

---

[32] Majoros, Exh. No. MJM-9C (revised November 21, 2008) at 1-2. This exhibit further revises the joint parties' revenue requirement to account for the corrected King, Exh. No. CWK-4.
[33] King, Exh. No. CWK-1T at 7. Removal costs reflect the cost of removing plant at the end of its useful life, net of any salvage value.
[34] King, Exh. No. CWK-1T at 3.
[35] *Id.* at 6. The joint parties refer to this method as the "Traditional Inflated Future Cost Approach or TIFCA" and assert that TIFCA is unfair to customers because it: (1) projects the rate of historical inflation that occurred between the times of the original plant investment and removal of that plant into the future to estimate net removal cost at asset retirement; and 2) charges current customers future removal costs in inflated dollars.
[36] King, Exh. No. CWK-1T at 11.
[37] *Id.*
[38] *See* ¶ 35.
[39] King, Exh. No. CWK-1T at 16. "Intergenerational equity" is a regulatory principle designed to ensure that ratepayers are charged only for the costs to serve them, at the time the service is rendered and the costs are incurred.

39 In cross-answering testimony, Staff opposes the joint parties' depreciation adjustment, arguing their proposed treatment of removal costs would create a "mismatch in timing of the actual dollars collected . . . because . . . fewer dollars are collected in the early years and more dollars will have to be collected in the later years."[40] Staff contends the remaining life depreciation method used by Avista and all other regulated electric companies in Washington will not over-charge customers for removal costs because it allows for adjustment of the depreciation rate to adjust balances over the asset's remaining life. Staff argues further that customers are compensated for the removal costs collected in depreciation because accumulated depreciation is deducted from rate base under original cost regulation.[41]

40 In its rebuttal to the joint parties' proposal, Avista also argues that the depreciation adjustment should be rejected as it is based upon a depreciation method that fails to properly match the accrual of funds to cover the costs of removal with the "service value" received by customers.[42] Avista characterizes the joint parties' approach as a "sinking fund" that requires collection of a progressively higher amount to cover removal costs instead of the equal, annual accrual collected under the traditional, straight-line method. Avista contends that the "sinking fund" method requires two steps: 1) the ratable depreciation of the present value of future removal cost; and 2) an annual accretion to the ratable depreciation to account for each year's inflation.[43] They point out that this method would require an annual adjustment to depreciation rates to accomplish the inflation adjustment. As to effect, Avista argues that this method charges future customers greater net removal costs which both violates the matching principle (offending intergenerational equity) and makes it probable that Avista will never fully recover net removal costs if rates are not adjusted annually.[44]

41 In addition, Avista argues that the straight-line remaining-life depreciation method, including the accrual of net removal costs, was proposed in the Company's last general rate case, settled by all parties, and approved by the Commission.[45] It points out that the depreciation study received careful attention from the parties including

---

[40] Parvinen, Exh. No. MPP-1T at 7.
[41] *Id.*
[42] Spanos, Exh. No. JJS-1T at 4.
[43] *Id.*
[44] *Id.* at 5. See also Felsenthal, ADF-1T at 9.
[45] Order 05, Docket UE-070804/UG-070805.

Public Counsel, who voiced no objection to the study's net removal cost method, which has now been approved by commissions in all states served by Avista.[46]

42 Next, Avista contends that it is inconsistent to modify depreciation rates to reflect present value costs for net removal, but not all other costs, including original asset cost. It argues that, to be consistent, the method proposed by the joint parties should apply removal cost ratios to the current (not original) cost of the asset.[47]

43 Turning to its approved method, Avista claims that method is conservative because it may actually underestimate the ultimate cost of removal. Avista explains that under the approved method the removal cost ratio is based on the current cost of removal compared to the original cost of the asset. This method captures inflation between the date of original investment and the date of removal from the statistical data base but fails to account for any future inflation. Therefore, if technological improvements fail to offset inflation, the accruals will fail to fully cover the net cost of future removals. Should costs be over-recovered, Avista agrees with Staff that any over-recovery is compensated by the commensurate reduction in rate base and can be mitigated in the next depreciation study.[48]

44 In conclusion, Avista contends that FAS 143 is not relevant to regulatory accounting.[49] It argues the standard is focused on ensuring that financial accounting makes clear to investors what removal costs are company liabilities based on legal obligations, and that it has no application to removal obligations that are not specifically required by law.[50] Finally, the Company argues that FAS 143 does not address the ratemaking principles of deferral accounting and matching, which ensure intergenerational equity in ratemaking.

Commission Determination.

45 The depreciation study under scrutiny in this proceeding was conducted only three years ago. The depreciation rates developed from that study were an issue in the last

---

[46] Spanos, Exh. No. JJS-1T at 11.
[47] *Id.* at 6.
[48] *Id.* at 16.
[49] *Id.* at 14 and Felsenthal, Exh. No. ADF-1T at 3.
[50] Spanos, Exh. No. JJS-1T at 15.

general rate case and were modified on the basis of recommendations from parties in that proceeding. Ultimately, the parties reached an uncontested settlement which we accepted and adopted. While settlement agreements do not serve as precedent, having recently resolved this issue to the satisfaction of all parties, including Public Counsel, we are not inclined to reconsider Avista's depreciation methodology absent a change in circumstances, which has not been shown. [51]

46 This Commission has long favored use of the straight-line depreciation methodology for determining depreciation expense.[52] Our goal is to allocate the cost of an asset over its useful life in a manner that matches the benefits utility customers receive from an asset with its cost burdens. Avista's depreciation methodology accomplishes this goal while preserving "intergenerational equity" over the asset's useful life. Finally, we favor a methodology that requires few changes or adjustments to accomplish its objectives. With this background, we turn to the merits of the joint parties' proposal.

47 First, the joint parties' proposal would require Avista to annually adjust depreciation rates to conform to changes in the rate of inflation. In turn, rates would have to change to give the adjustment effect. As regulating in the public interest includes promoting rate stability, we are reluctant to adopt a depreciation methodology that would result in even more rate changes than those faced by ratepayers in the current regulatory environment. Absent annual consideration of the Company's depreciation rates, Avista would likely under-collect net removal costs and be forced to turn to future ratepayers to compensate for these under-collections. In this circumstance, the joint parties' proposal neither observes the "matching" principle nor preserves "intergenerational equity".

48 As to the joint parties' contention that Avista's accrual of removal costs should be based on FAS 143, we conclude that the Financial Accounting Standards Board (FASB) standards are applicable to financial reporting, not the regulatory processes

---

[51] Litigating the company's depreciation methodology on an annual basis is not an efficient use of the time and resources of the parties to these proceedings or the Commission.

[52] Parvinen, Exh. No. MPP-1T at 6. Spanos, JJS-1T, at 19 noting that 47 commissions, including the Washington commission, primarily or exclusively use the traditional straight-line depreciation method. *See* also our recent order in *WUTC v. Puget Sound Energy, Inc.*, Dockets U-072300 and UG-072301, Order 12 (October 8, 2008) at 20.

used to formulate utility rates.[53] In fact, FAS 143 acknowledges that regulated utilities can recover removal costs over the life of assets through depreciation rates:

> The amounts charged to customers for the costs related to the retirement of long-lived assets may differ from the period costs recognized in accordance with this Statement, and therefore, may result in a difference in the timing of recognition for financial reporting and rate-making purposes.[54]

49 Therefore, we find that FAS 143 does not control Avista's treatment of removal costs in its depreciation methodology. Finally, we turn to the quality of the evidence the joint parties have provided on this matter. We have examined Mr. King's testimony closely, and particularly his Exhibit No. CWK-4, which purports to calculate the depreciation expense that would result from implementing his proposed methodology. The joint parties rely on this exhibit as an accurate calculation applying Mr. King's theory to net removal costs for mass property accounts derived from Avista's depreciation study. Indeed, Exhibit No. CWK-4 is the sole source for the magnitude of their proposed depreciation adjustments. In response to our bench inquiry about a formula used in two of the spreadsheets included in Exhibit No. CWK-4, Mr. King acknowledged an error and provided a revised set of spreadsheets. However, his revised spreadsheets may have introduced a second error or, at the very least, a reason to question the reliability of the spreadsheet. Mr. King's revised spreadsheet not only corrects an error in the form of the calculation used in Schedule 4 of Exhibit No. CWK-4 to produce the "Present Value of Removal Costs at 3%," it also modifies the period of years used in this formula. Mr. King's revised calculation is based on the average service life of the assets. His original calculation was based on the expired service life of the assets. Mr. King does not provide an explanation of why he made this additional change. Moreover, the revised calculation is arguably inconsistent with testimony where he describes his method as calculating "removal costs discounted back to the beginning of the account."[55] In the end, we find Exhibit No. CWK-4 not reliable.

---

[53] Felsenthal, Exh. No. ADF-1T at 21.
[54] *Id.* at 24. (Emphasis added).
[55] King, Exh. No. CWK-1T at 14.

50 In conclusion, we reject the joint parties' proposed depreciation adjustment, finding it neither conforms to the removal cost methodology approved in our most recent rate case, nor promotes rate stability for ratepayers. Nor do we accept the joint parties' assertion that FAS 143 necessitates use of their methodology. We find the FAS 143 permissive as applied to regulated utilities; allowing regulators discretion in applying its terms to removal costs. We see no reason to do so on the record before us. Finally, we find the errors in the joint parties' testimony significant enough to affect its weight and thus the evidence insufficient to support their proposed adjustment.

51 We turn now to the terms and conditions of the Settlement and address the largest adjustment first.

B. Settlement Provisions.

1. Power Supply-Related Adjustments:

52 The settling parties propose the following power supply-related adjustments :

- *Hydro-filtering.* Remove the power supply expense from the 50-year average for months when hydro generation was either higher or lower by more than one standard deviation from the average generation for that month.[56]

- *WNP-3 Contract.* Increase the amount of energy purchased under the contract by including 2007 energy purchases in the five-year average, which lowers power supply expense because the contract price is lower than market power prices in the AURORA model.[57]

- *Natural Gas Fuel Costs.* Reflect a *pro forma* period natural gas price of $8.30/Dth[58] for gas-fired generation for the unhedged portion of 2009 generation.

- *Colstrip Coal Cost.* Correct a mathematical error to properly reflect the 2009 *pro forma* period fuel price.

---

[56] Settlement, Exh. No. 5 at 5.
[57] *Id.* at 6.
[58] Decatherm (Dth) is a unit of energy equal to 10 therms or one million British thermal units (MMBtu).

- *Noxon Generation Upgrade.* Properly match the capital investment in a plant upgrade with the resulting increase in generation.

- *Energy Recovery Mechanism (ERM) Adjustment.* Incorporate an element of asymmetry in the ERM by giving customers a greater share of the benefits when power expenses are lower than the authorized level. The sharing level in the second ERM band ($4 million to $10 million) is changed to 75 percent customer/25 percent Company when power supply expenses are lower (rebate direction), while maintaining the current 50 /50 sharing in the second band when power supply expenses are higher (surcharge direction).[59]

53 ICNU joined in the section of the Settlement regarding power supply-related adjustments. Public Counsel did not address any power cost-related issues in its testimony. However, in its post-hearing brief, Public Counsel opposes acceptance of these adjustments because it disagrees with our decision to accept the Supplemental Testimony filed by Avista arguing that power supply costs are based on that testimony.

Commission Determination.

54 Public Counsel's opposition is legal argument rather than evidence. In its post-hearing brief, filed simultaneously with Public Counsel's, Avista characterizes its position on this issue as "unopposed."[60] As a practical matter, Avista is correct. We must base our decisions on the weight of evidence in the record. As there is none in opposition to these power supply-related adjustments, we consider them unopposed.

55 We find that the settlement terms respecting power supply-related costs are supported by an appropriate record and are consistent with the public interest in light of all the information in the record.

---

[59] Settlement, Exh. No. 5 at 5-7; Joint Testimony in Support of Settlement, Exh. No. 4T at 4-6, 12-21.

[60] Avista Brief at ¶ 55.

2. Other Revenue Requirement Adjustments.

56 The joint parties propose a number of other adjustments to the operating costs that support the revenue requirement proposed in the Settlement.[61] We have examined each of the proposed adjustments in light of the evidence presented and the parties' arguments.[62] We considered, among other things, whether the evidence discloses any errors on the part of the settling parties in the data that underlies the Settlement. We find no errors in the evidence that supports the Settlement's terms and conditions regarding these adjustments. Accordingly, we find that the settlement terms respecting these revenue requirements are consistent with the public interest.

3. Uncontested Settlement Provisions.

57 The remainder of the settlement provisions including, but not limited to, the overall rate of return of 8.22 percent, the rate of return on common equity of 10.2 percent, a capital structure with 46.3 percent common equity, the Spokane River Relicensing costs, the Montana Riverbed litigation adjustment, the customer deposit adjustment, the incentives adjustment, the correction to the error in officers' salaries, the adjustment to union and non-executive salaries, the Colstrip generation and operation and maintenance expense, the administrative and general expense adjustment, the production property adjustment, the adjustment to restate debt, the modification of customer service charge, and increases to the LIRAP, DSM funding levels, are not in dispute.[63] We accept these provisions as supported by substantial evidence in the record and in the public interest.

4. Revenue Requirement.

58 As we noted earlier, we addressed the joint parties' proposed adjustments to the initial filing before considering the Settlement's terms and conditions because they have a

---

[61] These include adjustments to D&O insurance, advertising, sports sponsorship, charitable contributions, director's compensation, other shareholder-related expenses, dues and memberships, and executive compensation.

[62] This evidence includes: Majoros, Exh. No. MJM-4TC, Majoros, Exh. No. MJM-8T, Andrews, Exh. No. EMA- 7T, and Norwood, Exh. No. KON-1T.

[63] Settlement, Exh. No. 5 at 4-5, 7-14; Joint Testimony in Support of Settlement, Exh. No. 4T at 4-5, 9, 11-19, 24-29, and Majoros, Exh. No. 8T at 2.

significant impact on the outcome of our final determination.[64] As reflected in the following table, our rejection of the joint parties' proposed CTA and depreciation adjustments together with our acceptance of the Settlement's power supply-related adjustments has a dramatic effect on the joint parties' proposed gas and electric revenue requirements:

Dollars in thousands	Electric Service	Natural Gas Service
Correct for FIT Computational Error (& resulting conversion factor flow through impact)	$ 4,358	$ 2,714
Net Power Supply-Related Adjustments in Settlement	7,433	
Affirm Straight-line Depreciation (Re: cost of removal	3,057	1,197
Total	14,848	3,911
Joint Parties' Initial Recommended Revenue Requirement	20,118	627
Addition of above 3 items to Joint Parties' Recommended Revenue Requirement	**34,966**	**4,538**
Multi-party Settlement Recommended Revenue Requirement	**$ 32,538**	**$ 4,768**

[64] Norwood, Exh. No. KON-1T at 1.

59 The joint parties' electric revenue requirement increases to $35 million compared to the Settlement's $32.5 million, or $2.5 million higher than the Settlement Their gas revenue requirement increases from $627,000 to $4,538,000 compared to the Settlement's $4,768,000, or $230,000 lower than the Settlement. [65]

60 We are not bound to follow a specific formula or method when calculating rates. Rather, we are to establish rates that balance both investor and consumer interests to arrive at rates that are fair, just, reasonable, and sufficient.[66] In light of all the evidence in the record, we find the Settlement's electric and gas revenue requirements result in rates that meet this criteria. The fact that the Settlement's electric revenue requirement is substantially lower than that produced by the joint parties after our rejection of their principal adjustments supports our conclusion. Similarly, the $230,000 reduction in gas revenue requirement that follows from our rejection of the joint parties' adjustments is a reduction of less than five percent from the Settlement's proposed gas revenue requirement. In the context of public policy which favors settlements, this is not a reduction of sufficient magnitude to warrant rejection of the Settlement.[67]

5. Reclassification of Non-Legal Asset Removal Obligations (AROs).[68]

61 A portion of depreciation expense, including depreciation expense in the proposed Settlement, is for AROs or the future asset removal costs of long-lived plant net of any salvage value. For ratemaking purposes, Avista classifies a portion of the depreciation expense collected for AROs as accumulated depreciation and separately accounts for it in sub-accounts.

---

[65] Norwood, Exh. No. KON-1T at 4.
[66] *Federal Power Comm'n v. Hope Natural Gas Co.,* 320 U.S. 591,603 (1944), RCW 80.28.010 and 80.28.020.
[67] RCW 34.05.060.
[68] The term "non-legal asset removal obligations" refers to net removal costs for general plant assets that are not required to be incurred by law or regulation – so called "legal removal costs." Examples of legal removal costs include the cost of required site restoration or environmental remediation.

62 The joint parties' recommend reclassifying a portion of the depreciation expense collected for non-legal AROs to Account 254 – Other Regulatory Liabilities and creating a new account for these funds.[69] The joint parties assert that Avista has over-collected $209.4 million for future removal costs.[70] The joint parties contend that it is appropriate to treat these funds in accordance with FAS 143 and recognize these AROs as a regulatory liability.[71]

63 The joint parties contend that, regardless of being included in accumulated depreciation, these monies have already been collected from ratepayers for the future cost of removal.[72] The joint parties argue that unless the Commission requires it, there is no provision to refund ratepayers these amounts if Avista fails to use these funds for removal costs.[73] The joint parties' proposed reclassification does not have an impact on the revenue requirement.[74]

64 In rebuttal, Avista states that FAS 143 is not applicable to ratemaking, in general.[75] Moreover, Avista considers the reclassification unnecessary and inappropriate and points out that Avista maintains sub-accounts within the accumulated depreciation account to track removal costs.[76] Avista contends that there is no need to place these funds in a separate account to ensure that the funds will be spent for their intended purpose (costs of removal) and notes that the Federal Energy Regulatory Commission (FERC) has the authority to prohibit a utility from making other use of these funds.[77]

65 In cross-answering testimony, Staff argues that reclassification is unnecessary because there is no Commission or FERC requirement to do so and there is no revenue requirement impact.[78] Staff contends that collections over actual removal

---

[69] Majoros, Exh. No. MJM-4TC at 5.
[70] *Id.*
[71] *Id.*
[72] *Id.* at 9.
[73] *Id.* at 10.
[74] *Id.* at 11.
[75] Spanos, Exh. No. JJS-1T at 15.
[76] Felsenthal, ADF-1T at 4.
[77] Felsenthal, ADF-1 at 12.
[78] Parvinen, Exh. No. MPP-1T at 3.

costs are returned under current methods and customers would "receive no greater safeguard" with the proposed reclassification.[79]

Commission Decision.

66 We conclude that the joint parties have failed to demonstrate the need for reclassifying AROs as regulatory liabilities and accordingly deny their request. There is no evidence that Avista has failed to properly use these funds for their intended purpose. Moreover, the joint parties failed to demonstrate that reclassification of these funds would afford ratepayers any greater protection should that contingency arise.

6. Settlement with the Coeur d'Alene Tribe.[80]

67 Avista requests recovery of costs associated with the settlement of the Coeur d'Alene Tribe's (Tribe) claim for damages related to the operation of Avista's Spokane River Hydroelectric Project (Project), including its Post Falls hydroelectric facility located on the Spokane River downstream of Lake Coeur d'Alene.[81] As designed, the Project uses Lake Coeur d'Alene as a water storage facility – manipulating water levels as necessary to optimize system efficiency.

68 From 1907 to 1972, Avista operated the Project under authority granted by the State of Idaho.[82] In 1972, Avista filed a petition with the FERC seeking a federal license to operate the Project. In 1973, the Tribe intervened in the proceeding, claiming a portion of Lake Coeur d'Alene was on its reservation and under its exclusive use and control.[83] In response, Avista argued that ownership of the lake was held by the State of Idaho, which had issued all relevant permits necessary for the Project's operation. After years of litigation in a number of forums, the United States Supreme Court ultimately determined in 2001 that the United States holds, in trust for the Coeur

---

[79] *Id.* at 3-4.
[80] This issue addresses information that was protected from public disclosure by the terms and conditions of Order 03, Protective Order, entered April 3, 2008, until Avista relinquished its claim of confidentiality to most information on December 19, 2008.
[81] Pessemier, Exh. No. TEP-1T at 1.
[82] *Id.* at 3.
[83] *Id.*

d'Alene Tribe, those portions of the lake within the boundaries of the Coeur d'Alene Reservation.[84] The Court's ruling did not, however, settle the Tribe's dispute with Avista related to the historic and future use of the lake to benefit Project operations, including compensatory claims founded in §10(e) of the Federal Power Act for inundating reservation lands.[85]

69 In 2008, Avista and the Tribe reached a comprehensive settlement whereby Avista agrees to compensate the Tribe for past damages and future use of the lake to serve the Project. Additional settlement terms include the issuance of a tribal water rights permit for the Project's benefit, and new or renewed rights-of-way to maintain "existing transmission lines across Tribal Trust Lands."[86] As compensation for past trespass and §10(e) water storage claims, Avista will pay the Tribe $25 million in 2008, $10 million in 2009, and $4 million in 2010.[87] Future §10(e) compensation consists of flat annual payments of $400,000 for the first 20 years of the license and $700,000 flat annual payments for the remaining 30 years of the license.[88] The settling parties would allow recovery of Avista's immediate settlement payments and offer a ratemaking treatment set forth below.

70 The Settlement would defer Washington's share of Avista's 2008 and 2009 payments to the Tribe, totaling $35.4 million, as a regulatory asset.[89] The deferral would include depreciation/amortization associated with said payments together with a carrying charge of five percent.[90] In addition, Avista would be allowed to defer a carrying charge on the costs not yet included in rate base for subsequent recovery in rates.[91] Finally, the deferral's recovery in rates would be spread over the remaining life of the Project.

---

[84] *Id.*
[85] *Id.* at 4-5.
[86] Pessemier, Exh. No. TEP-1T at 5-6, and Exh. No. TEP-4TC at 19.
[87] Andrews, Exh. No. EMA-1T at 24.
[88] *Id.*
[89] The deferral would commence when Avista makes its first payment to the Tribe. Avista Brief at 10.
[90] Andrews, Exh. No. EMA-1T at 24.
[91] *Id.*

71 The proposed ratemaking treatment would result in a *pro forma* adjustment that decreases Washington net operating income by $499,000 and increases rate base by $15,084,000.[92] The settling parties agree that the *pro forma* costs associated with the settlement with the Tribe are prudent[93] and that any costs that exceed the *pro formed* costs in this case would be addressed in a separate proceeding.[94]

72 The joint parties argue that Avista's payments to the Tribe should be disallowed as imprudent because Avista "admitted to past trespass."[95] They assert that the settlement with the Tribe would require current customers to pay for past misconduct and usage charges resulting in retroactive ratemaking in violation of RCW 80.28.020, which requires the Commission to set rates prospectively.[96] The joint parties argue that the past §10(e) usage costs and past trespass damages are costs that should have been included in ratemaking for previous periods.[97] If the Commission approves these expenses, the joint parties propose that these funds be offset by monies collected under non-legal asset removal obligations (AROs).[98]

73 In rebuttal, Avista denies that its settlement expenses were imprudently incurred and asserts that it has not admitted to trespass.[99] Avista contends that ownership of Lake Coeur d'Alene was not conclusively determined until the Supreme Court ruling and that, even then, it reasonably believed that its rights were protected by an earlier assignment of rights to operate the Post Falls dam site and the issuance of a permit in 1909 to use the lake to store water.[100] Avista further contends that the settlement does not constitute retroactive ratemaking because there were no "past management mistakes."[101] It argues that settlement payments to the Tribe could not have been anticipated or previously recovered through rates; there was no obligation until an

---

[92] *Id.*
[93] Settlement, Exh. No. 5 at 4 and 11; Joint Testimony in Support of Settlement, Exh. Nos. 4TC at 27; Pessemier, Exh. No. TEP-1TC at 1-7, TEP-3C at 1-12, and TEP-4TC at 2-21.
[94] Settlement, Exh. No. 5 at 4 and 11, Joint Testimony in Support of Settlement, Exh. No. 4TC at 27.
[95] Majoros, Exh. No. MJM-4TC at 16.
[96] *Id.*
[97] Public Counsel's Brief at 24.
[98] Majoros, Exh. No. MJM-4TC at 18.
[99] Pessemier, Exh. No. TEP-4TC at 4-6 and Exh. No. TEP-5.
[100] Pessimier, Exh. No. TEP-4TC at 2-3.
[101] *Id.* at 6; Avista's Brief at 54.

agreement was reached with the Tribe in 2008.[102] Avista argues further that the settlement resolves all disputed issues, settles historic claims over use of the lake for hydroelectric generation and, for the next 50 years, preserves a valuable, low cost energy resource for the benefit of its customers.[103] Staff joins in its arguments.

74 Finally, Avista and Staff oppose the use of ARO funds to offset any settlement expenses arguing to do so would be inappropriate.[104] In cross-answering testimony, Staff contends that it is inappropriate to use the non-legal ARO's for any purpose other than the cost of asset removal.[105] Staff contends that the joint parties ignore the fact that these funds were collected specifically for future removal costs.[106]

Commission Decision.

75 The evidence demonstrates that Avista began operating the Project under authority granted by the State of Idaho to control the level of Lake Coeur d'Alene. The joint parties do not explain why Avista knew or should have known that the Tribe shared jurisdiction over Lake Coeur d'Alene with the State of Idaho prior to the Supreme Court's 2001 ruling. Indeed, the long, complex legal history of this issue belies the joint parties' assertion.

76 The controversy over the lake's ownership arose approximately 35 years ago when the Tribe first asserted its claim of ownership of those portions of the lake within its reservation. Litigation ensued before the FERC, which ruled initially that the lake was owned by Idaho.[107] FERC's decision was appealed and eventually remanded for review, where it decided that it lacked jurisdiction to resolve this issue in 1988.[108] Finally, the United States, acting in its capacity as trustee for the Tribe, brought suit against Idaho to settle the question. In 2001, the Court ruled 5-4 in favor of the

---

[102] Avista's Brief at 54.
[103] Pessemier, Exh. No. TEP-4TC at 3.
[104] Felsenthal, Exh. No. ADF-1T at 16.
[105] Parvinen, Exh. No. MPP-1T at 5.
[106] *Id.* at 6.
[107] Pessemier, Exh. No. TEP-4TC at 15.
[108] *Id.* at 7.

United States, finally resolving the Tribe's ownership claim.[109] Throughout this dispute's long legal history, Avista either pursued all legal remedies at its disposal or had no choice but to await the litigation's outcome. The matter now decided, Avista pursued an opportunity to settle all claims raised by the Tribe, including those affecting the relicensing of the Project. We believe Avista's actions were both reasonable and prudent.

77 In sum, we reject the joint parties' argument that Avista's operation of the Project or its actions in response to the Tribe's claim were imprudent. Avista operated the Project with authority from the entity it reasonably believed was the lawful owner, the State of Idaho, and, when challenged, it defended its right to operate it pursuant to the authority granted. Without further legal recourse, Avista acted prudently to settle its dispute with the Tribe and wrap the Project's relicensing issues into a comprehensive agreement ensuring long-term availability of valuable hydroelectric resources for the benefit of Avista's current and future ratepayers.[110]

78 Finally, we find that the settling parties' treatment of the costs related to the settlement with the Tribe is reasonable and well supported by the evidence in the record.[111] The costs associated with the settlement will be recouped over time and with reasonable carrying charges. Contrary to the joint parties' assertion, the settlement does not constitute retroactive ratemaking. Retroactive ratemaking involves the *current* collection, through rates, of *past* obligations.[112] Until Avista reached a settlement earlier this year, it had no obligation to the Tribe. This case presents Avista's first opportunity to recover the charges associated with that obligation.[113] We also reject the joint parties' alternative proposal to use ARO's to

---

[109] *Idaho v. United States,* 533 U.S. 262 (2001). In that case, the Court held that the post-Idaho statehood ratification of treaties with the Tribe demonstrated Congressional intent to reserve certain submerged lands of the lake for the benefit of the Tribe.

[110] The Tribe's original claims potentially exposed Avista to much higher damages. (Pessemier, Exh. No. TEP-4TC at 17). If successful, these claims could threaten the Project's future economic viability.

[111] *See* n. 93.

[112] *In the Matter of the Application of Puget Sound Energy For Authorization Regarding the Deferral of the Net Impact of the Conservation Incentive Credit Program, Schedule 125, and Subsequent Recovery Thereof Through Schedule 120, Conservation Rider,* Docket UE-010410, Order Denying Petition to Amend Accounting Order (November 9, 2001).

[113] Pessemier, Exh. No. TEP-4TC at 6.

offset any settlement expenses; it is inappropriate to use ARO's for any purpose other than the cost of asset removal. We conclude that the Settlement's terms dealing with payments made to the Tribe are reasonable and supported by the record.

V. Conclusion.

79 We favor the resolution of contested issues through settlement when a settlement's terms and conditions comply with the law and are consistent with the public interest. After thorough consideration, we find the Settlement to be lawful and in the public interest and that the resulting rates are fair, just, reasonable, and sufficient. We adopt the Settlement as the Commission's resolution of all matters in this proceeding.

FINDINGS OF FACT

80 Having discussed above in detail the evidence received in this proceeding concerning all material matters, and having stated above our findings and conclusions upon issues in dispute among the parties and the reasons supporting the findings and conclusions, the Commission now makes and enters the following summary findings of fact, incorporating by reference pertinent portions of the preceding detailed findings:

81 (1) The Washington Utilities and Transportation Commission is an agency of the State of Washington, vested by statute with authority to regulate rates, rules, regulations, practices, and accounts of public service companies, including electric and gas companies.

82 (2) Avista Utilities is a "public service company," an "electrical company," and a "gas company," as those terms are defined in RCW 80.04.010, and as those terms are used in RCW Title 80. Avista is engaged in Washington State in the business of supplying utility services and natural gas to the public for compensation.

83 (3) The existing rates for electric and natural gas service provided by Avista in Washington are insufficient to yield reasonable compensation for the services rendered. Avista requires prospective rate relief for its electric and natural gas services in Washington.

CONCLUSIONS OF LAW

84 Having discussed above all matters material to this decision, and having stated detailed findings, conclusions, and the reasons therefore, the Commission now makes the following summary conclusions of law incorporating by reference pertinent portions of the preceding detailed conclusions:

85 (1) The Washington Utilities and Transportation Commission has jurisdiction over the subject matter of, and parties to, this proceeding. *RCW Title 80.*

86 (2) The rates proposed by tariff revisions filed by Avista Utilities on March 4, 2008, and suspended by prior Commission order, were not shown to be fair, just or reasonable and should be rejected.

87 (3) Avista Utilities' existing rates for electric and natural gas service provided in Washington are insufficient to yield reasonable compensation for the service rendered. Avista Utilities requires relief with respect to the rates it charges for electric and natural gas service provided in Washington.

88 (4) Informal settlements in administrative proceedings are encouraged. *RCW 34.05.060.* The Commission may approve settlements "when doing so is lawful, when the settlement terms are supported by an appropriate record, and when the result is consistent with the public interest in light of all the information available to the commission." *WAC 480-07-750(1).*

89 (5) The Settlement is supported by the record, and is consistent with the law and the public interest.

90 (6) The electric and natural gas rates resulting from adoption of the Settlement are fair, just, reasonable, and sufficient for services Avista Utilities provides to customers in Washington.

91 (7) Avista should have the opportunity to earn an overall rate of return of 8.22 percent based on the capital structure and costs of capital set forth in the body of this Order, including a return on equity of 10.2 percent on an equity share of 46.3 percent.

92 (8) Avista should be authorized and required to make a compliance filing to recover its revenue deficiency of $32.5 million for electric service and $4.8 million for natural gas service, consistent with the terms of this Order.

93 (9) The Commission Secretary should be authorized to accept by letter, with copies to all parties to this proceeding, a filing that complies with the requirements of this Order.

94 (10) The Commission should retain jurisdiction over the subject matter of and the parties to this proceeding to effectuate the terms of this Order. *RCW Title 80.*

ORDER

THE COMMISSION ORDERS THAT:

95 (1) The proposed tariff revisions filed by Avista Utilities on March 4, 2008, and suspended by prior Commission order, are rejected.

96 (2) The Settlement attached as Appendix A and incorporated into this Order by prior reference is approved and adopted.

97 (3) Avista Utilities is authorized and required to file tariff sheets following the effective date of this Order that are necessary and sufficient to effectuate its terms. The required tariff sheets must be filed by 5:00 p.m. on December 30, 2008.

98 (4) The Commission Secretary is authorized to accept by letter, with copies to all parties to this proceeding, a filing that complies with the requirements of this Order.

Dated at Olympia, Washington, and effective December 29, 2008.

WASHINGTON STATE UTILITIES AND TRANSPORTATION COMMISSION

MARK H. SIDRAN, Chairman

PATRICK J. OSHIE, Commissioner

PHILIP B. JONES, Commissioner

NOTICE TO PARTIES: This is a final order of the Commission. In addition to judicial review, administrative relief may be available through a petition for reconsideration, filed within 10 days of the service of this order pursuant to RCW 34.05.470 and WAC 480-07-850, or a petition for rehearing pursuant to RCW 80.04.200 or RCW 81.04.200 and WAC 480-07-870.

APPENDIX A

MULTI-PARTY SETTLEMENT STIPULATION

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION Complainant, v. AVISTA CORPORATION d/b/a AVISTA UTILITIES Respondent.	)	DOCKET UE-080416 and DOCKET UG-080417 MULTIPARTY SETTLEMENT STIPULATION

I. PARTIES

1. This Multiparty Settlement Stipulation is entered into by Avista Corporation ("Avista" or the "Company"), the Staff of the Washington Utilities and Transportation Commission ("Staff"), Northwest Industrial Gas Users ("NWIGU"), and The Energy Project, jointly referred to herein as the "Stipulating Parties." The Industrial Customers of Northwest Utilities ("ICNU"), while a signatory, only joins in those portions of the Stipulation identified below. The Public Counsel Section of the Washington Office of Attorney General ("Public Counsel") does not join in. The Stipulating Parties agree that this Multiparty Settlement Stipulation is in the public interest and should be accepted as a full resolution of all issues in these Dockets. ICNU agrees to resolve the issues identified below, but opposes the position that this Multiparty Settlement should resolve all

issues in these Dockets. The Stipulating Parties understand this Multiparty Settlement Stipulation is subject to Commission approval.

II. INTRODUCTION

2. On March 4, 2008, Avista filed with the Commission certain tariff revisions designed to effect general rate increases for electric service (Docket UE-080416) and natural gas service (Docket UG-080417) in the State of Washington. Avista requests an increase in electric rates of $36.6 million, or 10.3 percent, and an increase in natural gas rates of $6.6 million or 3.3 percent. On March 6, 2008, the Commission entered Order 01 suspending the tariff revisions and consolidating Dockets UE-080416 and UG-080417 for hearing and determination pursuant to WAC 480-07-320. A Prehearing Conference Order (Order 02) issued on April 3, 2008, which, inter alia, established a procedural schedule. On July 25, 2008, the Company filed supplemental pre-filed direct testimony and exhibits to reflect a revised electric service revenue requirement of $47.4 million; the Company, however, did not otherwise revise its tariff filing to reflect these changes. Representatives of all parties appeared at the August 20, 2008 Settlement Conference, which was held for the purpose of narrowing the contested issues in this proceeding. Subsequently, the parties participated in telephonic Settlement Conferences on August 29, 2008, September 4, 2008, September 8, 2008, and September 9, 2008.

3. The Stipulating Parties have reached a Multiparty Settlement Stipulation on all issues in this proceeding and wish to present their agreement for the Commission's consideration. The Stipulating Parties therefore adopt the following Multiparty Settlement Stipulation in the interest of expediting the disposition of this proceeding.

4. ICNU joins with the following identified portions of the Stipulation: Power Supply-Related Adjustments (Section III. A. (a.)); Cost of Capital (Section III. A. (m.)); Rate Spread/Rate Design (Section III. B.); Low Income Bill Assistance Funding (Section III. C.); Demand Side Management (DSM) Expenditures (Section III. D.); and Prudency of Energy Efficiency Expenditures (Section III. E.). ICNU expressly reserves the right to contest other issues that have been resolved among the Stipulating Parties and shall not be foreclosed from raising such additional issues as may be properly within the scope of this proceeding.

III. AGREEMENT

A. Revised Revenue Requirement

5. The Stipulating Parties have agreed to a number of revenue requirement adjustments to both the filed electric and natural gas cases. These are described in the tables set forth immediately below:

SUMMARY TABLE OF ADJUSTMENTS TO ELECTRIC REVENUE REQUIREMENT

000s of Dollars

		Revenue Requirement	Rate Base
Amount As Filed		**$ 36,617**	**$ 950,944**
Adjustments:			
* Power Supply-Related Adjustments			
	Hydro filtering	(1,597)	0
	WNP-3 Contract (Use of 5-year average availability)	(136)	0
	Fuel (Natural Gas) (Use of $8.30/Dth and include actual short-term transaction through August 25, 2008)	8,486	0
	Colstrip (Correct Colstrip fuel price)	(877)	0
	Noxon Generation Upgrade (Pro Form 2009 capital upgrade project)	1,557	8,714
* Cost of Capital			
	Adjust return on equity to 10.20%	(4,229)	0
	Adjust cost of debt to 6.51%	1,017	0
Relicensing/Litigation[1]			
	Relicensing and confidential litigation costs deferred for later recovery, with carrying charge (5.0%); Include amortization of Montana riverbed litigation costs with accrued interest	(8,053)	(37,044)
Capital Additions			
	Pro form in the capital cost and expenses associated with the major generation and transmission project upgrades	60	14,299
Customer Deposits			
	Remove customer deposits from Rate Base; include interest as operating expense	(189)	(2,155)
Federal/Deferred Income Tax Expense			
	Adjust federal and deferred federal income tax expense	405	0
Incentives			
	Adjust incentives to actual	(415)	0
Officers' Salaries			
	Adjust officers' salaries for correction of error	(140)	0
Union and Non-Executives' Salaries			
	Remove union and non-executive 2009 wage increase	(1,188)	0
Colstrip Generation O&M Expenses			
	Reduce mercury emissions O&M costs	(699)	0
Administrative and General Expenses			
	Remove sponsorship costs	(109)	0
Production Property			
	Flow through impact of Production & Transmission adjustments	2,174	4,549
Restate Debt Interest			
	Flow through impact of Rate Base adjustments	(146)	0
Total Adjustments		**(4,079)**	**(11,637)**
Adjusted Amounts		**$ 32,538**	**$ 939,307**

[1] Please see Andrews' (EMA-1T) unredacted testimony at Pages 23-24.

[*] Denotes concurrence of ICNU

SUMMARY TABLE OF ADJUSTMENTS TO NATURAL GAS REVENUE REQUIREMENT 000s of Dollars		Revenue Requirement	Rate Base
Amount As Filed		$ 6,587	$ 172,957
Adjustments:			
Cost of Capital			
	Adjust return on equity to 10.20%	(778)	0
	Adjust cost of debt to 6.51%	194	0
Natural Gas Inventory			
	Natural gas inventory included in Rate Base as originally filed	0	0
Capital Additions			
	Remove pro forma capital additions	(666)	(2,506)
Customer Deposits			
	Remove customer deposits from Rate Base; include interest as operating expense	(109)	(1,248)
Federal Income Tax Expense			
	Remove tax deduction	48	0
Incentives			
	Adjust incentives to actual	(109)	0
Officers' Salaries			
	Adjust officers' salaries for correction of error	(37)	0
Union and Non-Executives' Salaries			
	Remove union and non-executive 2009 wage increase	(320)	0
Restate Debt Interest			
	Flow through impact of Rate Base adjustments	(42)	0
Total Adjustments		(1,819)	(3,754)
Adjusted Amounts		$ 4,768	$ 169,203

Attached as Appendix 1 are the electric and natural gas Summary of Revenue Requirement Adjustments schedules showing adjusted pro forma results incorporating these agreed-upon adjustments.

a.) **Power Supply-Related Adjustments:**

(i) Hydro filtering – This adjustment removes the power supply expense from the 50-year average for months when the hydro generation was either higher or lower by more than one standard deviation from the average generation for that month.

(ii) WNP-3 Contract – This adjustment increases the amount of energy purchased under the WNP-3 contract by including 2007 energy purchased in the 5-year average. Increasing the amount of WNP-3 power purchased lowers power supply expense because the WNP-3 price is lower than market power prices in the AURORA model.

(iii) Adjust (Natural Gas) Fuel Costs – This adjustment reflects a pro forma period natural gas price of $8.30/Dth for natural gas-fired generation for the unhedged portion of the 2009 generation. This adjustment also includes the actual 2009 calendar-year wholesale electric and natural gas transactions entered into through August 25, 2008.

(iv) Correct Colstrip Fuel Cost Error – This adjustment corrects a mathematical error in the calculation of the Colstrip coal cost. The correction is designed to properly reflect the 2009 pro forma period fuel price.

(v) Noxon Generation Upgrade – The Noxon upgrade, scheduled for completion in March of 2009, is designed to increase that unit's efficiency by 5%, and provide additional capacity of 7.5 MW. The Company's original filing included the additional generation expected from the upgrade (2.33 average megawatts of additional energy in an average water year) within the Company's Dispatch Model for the rate year, but inadvertently excluded the capital investment for this project from its revenue requirement. The Stipulating Parties agree, for settlement purposes, to include the capital investment and increased generation for ratemaking purposes.

(vi) Modification to Energy Recovery Mechanism (ERM) – This adjustment

incorporates an element of asymmetry in the ERM by giving customers a greater share of the benefits when power expenses are lower than the authorized level. The adjustment changes the sharing level in the second ERM band ($4 million to $10 million) to 75% customer/25% Company when power supply expenses are lower (rebate direction), while maintaining the 50%/50% sharing in the second band when power supply expenses are higher (surcharge direction). This adjustment does not affect the pro forma power supply expense.

b.) **Capital Additions:**

Capital additions for electric operations shall include capital costs and expenses associated with the major generation and transmission project upgrades. Capital additions for natural gas operations shall include capital costs and expenses associated with the Jackson Prairie expansion project. These capital additions include projects completed during 2007, and projects expected to be completed and transferred to plant-in-service by December 31, 2008, in time for new rates to be in effect. The capital costs have been averaged for their appropriate pro forma period with the associated depreciation expense and property tax, as well as the appropriate accumulated depreciation and deferred income tax rate base offsets.

c.) **Customer Deposits:**

Customer deposits shall be removed from rate base, and interest on the customer deposits will be included as an operating expense for electric and natural gas operations.

d.) **Federal/Deferred Income Tax Expense:**

The Company's Schedule M tax computation deduction that was incorrectly included in the Company's calculation of taxable income in determining federal income tax expense shall be removed. Also, the proper level of deferred tax expense (DFIT) based on the proper allocation percentage used to calculate allocated DFIT for the test period has been reflected.

e.) **Incentives:**

The incentive calculation shall reflect the actual expenses for the test period instead of the six-year average proposed by the Company.

f.) **Officers' Salaries:**

This adjustment corrects the Company's pro forma adjustment of officers' salaries for an error identified by the Company.

g.) **Union and Non-Executives' Salaries:**

The pro formed 2009 wage increase for union and non-executives shall be removed.

h.) **Colstrip Mercury Emission O&M:**

This adjustment reduces the pro formed 2009 O&M costs associated with the mercury control abatement project at Colstrip. The original system expense amount of the mercury control O&M costs was estimated to be approximately $3 million annually or $250,000 monthly, and this process had been anticipated to start in July 2009. The plan was revised to start this mercury abatement process in November 2009, for a total cost of approximately $465,000 for two months.

i.) **Administrative and General Expenses:**

This adjustment removes non-utility expenses that should have been excluded from utility results within the Company's test period, in its original filing. These expenses are related to costs expended by the Company for sponsorship agreements in support of community affairs.

j.) **Production Property:**

This adjustment corrects an erroneous value in the calculation of the production property adjustment contained within the Company's original filing, representing approximately $2.1 million of this adjustment. The remaining portion of the adjustment is directly linked to all other adjustments in this Multiparty Settlement Stipulation that affect production and transmission related revenues, expenses, and rate base.

k.) Weather Normalization:

The Stipulating Parties agree that the use of a rolling 25-year average of normal heating and cooling degree days in the calculation of the weather adjustment is for settlement purposes only, and shall not be deemed as precedent for any other proceeding.

l.) Natural Gas Inventory:

The pro formed Jackson Prairie working gas inventory (AMA balance for 2009 pro forma period) shall be included in rate base.

m.) **Cost of Capital:**

The Stipulating Parties agree to a 10.2% return on equity, and adopt the capital structure as filed by the Company. The cost of debt has been adjusted from 6.38% to 6.51% to reflect actual cost of debt through July 2008 with pro forma adjustments to update the debt cost through December 31, 2008.

Agreed-upon Cost of Capital	Percent of Total Capital	Cost	Component
Total Debt	53.70%	6.51%	3.50%
Common Equity	46.30%	10.20%	4.72%
TOTAL	100.00%		8.22%

n.) **Accounting Treatment for Certain Costs:**

(i.) Spokane River Relicensing – The Company included in its filing the processing costs associated with its Spokane River relicensing efforts, which expenditures included actual life-to-date costs from April 2001 through December 31, 2007, and 2008 pro forma expenditures through December 31, 2008. (See Andrews' Direct Testimony at page 23.) Although the Company anticipates receiving a final license from the Federal Energy Regulatory Commission ("FERC") in the near future, that has yet to occur. The relicensing costs will remain in CWIP (Construction Work in Progress), and the Company will continue to accrue AFUDC until issuance of the license, at which time the relicensing costs will be transferred to

plant in service and depreciation will begin to be recorded. The Stipulating Parties have agreed that the costs were prudently incurred and have agreed, that once the Company receives the license, to defer as a regulatory asset (in Account 182.3 – Other Regulatory Assets) Washington's share of the depreciation/amortization associated with the aforementioned relicensing costs and related protection, mitigation, or enhancement expenditures, together with a carrying charge on the deferral, as well as a carrying charge on the amount of relicensing costs not yet included in rate base. The annual carrying charge for deferrals and rate base not yet included in establishing rates shall be 5.0%. Any costs that exceed the pro formed costs in this case would be addressed in a separate filing.

(ii.) Confidential Litigation – Company witness Andrews describes the confidential litigation at pages 23 and 24 of her pre-filed direct testimony (unredacted). Although the matter is still pending and has yet to be finally resolved, it is expected to reach resolution in the near future. The Stipulating Parties have agreed that the pro forma costs in this case are prudent and have agreed to defer as a regulatory asset (in Account 182.3 – Other Regulatory Assets) Washington's share of the depreciation/amortization associated with the aforementioned costs with a carrying charge on the deferral as well as a carrying charge on the amount of costs not yet included in rate base for subsequent recovery in rates. The annual carrying charge shall be 5.0%. Any costs that exceed the pro formed costs in this case would be addressed in a separate filing.

(iii.) Montana Riverbed Litigation – On November 11, 2007, Avista filed an Application with the Commission (Docket No.UE-072131) requesting an accounting order authorizing deferral of settlement lease payments and interest accruals relating to the recent settlement of a lawsuit in the State of Montana over the use of the riverbed related to the Company's ownership of the Noxon Rapids and Cabinet Gorge hydroelectric projects located on the Clark Fork River. The Commission, in its Order No. 01, authorized the deferral of settlement lease payments together with interest, at the weighted cost of debt, until the matter was addressed in this general rate filing. The Stipulating Parties have agreed to the Company's requested amortization of costs, together with recovery of accrued interest on the Washington share of deferrals at the weighted cost of debt, net of related deferred tax benefit.

6. ERM Authorized Level of Expense. Appendix 2 sets forth the agreed-upon level of power supply expense, retail load and revenue credit resulting from this Stipulation, that will be used in the monthly Energy Recovery Mechanism ("ERM") calculations.

7. Decoupling Baseline. Pursuant to the Commission's order adopting the Avista decoupling pilot, In Re Petition of Avista Corp., Order 04, Docket UG-060518, para. 49, the baseline for the decoupling mechanism has been updated so as to use the test year employed in this rate case proceeding. (See Settlement Agreement, Docket UG-060518, supra, section III. C. (6.)). The update of the baseline is reflected in Appendix 3.

B. Rate Spread/Rate Design:

8. The Stipulating Parties agree to apply a uniform percentage increase across the electric

service schedules for purposes of recovering Avista's revenue requirement. Appendix 4 shows the impact on each electric and natural gas service schedule of the spread of the proposed increase. The residential basic charge for electric and natural gas residential customers would be increased from $5.50 to $5.75 per month.

9. For Extra Large General Service Schedule 25 Rate Design, the Stipulating Parties agree with the following rate design recommendations for Schedule 25: The Company's proposed Schedule 25 demand charges should be adopted. The first and second energy block rates shall be increased by a uniform percentage. The increase applied to the third energy block rate shall be 2.0 percent less than the percentage increase applied to the first and second block rates as shown on Page 2 of Appendix 4. This Schedule 25 rate design formula shall apply to the final revenue requirement in this case, regardless of whether it is different from the revenue requirement in Appendix 4.

10. For natural gas, the Stipulating Parties agree that the final revenue requirement shall be spread across natural gas service schedules in the same proportion to the Company's filed rate spread proposal as set forth in column (d), Page 1 of 3, Exhibit (BJH-7). (See Appendix 4, Page 3)

C. **Low Income Bill Assistance Funding:**

11. The Stipulating Parties agree to adjust the LIRAP portion of the tariff riders (Schedules 91 and 191) to provide an increase in annual funding of $500,000. With this increase, the annual funding level for electric low income customers will be $2,864,000, and for natural gas customers will be $1,580,000. Appendix 5 identifies the tariff rider adjustments to schedule 91 and 191 (in ¢/kwh or ¢/therm) to reflect increased levels of funding for LIRAP and DSM (as discussed below).

D. **Demand Side Management (DSM) Expenditures:**

12. The Stipulating Parties agree to increase low income DSM by $350,000 over and above existing funding level of $1,132,000, and to adjust the Tariff Rider Adjustment Schedules (91 and 191) accordingly. For purposes of program administration, the total funding level of $1,482,000 for low income DSM includes amounts that may be dedicated to energy-related health and safety measures, the expenditures for which shall not exceed fifteen (15%) percent of overall actual low-income DSM expenditures. The Company and The Energy Project agree to work with participating low income agencies on the development of contract provisions to assure that the combined portfolio of electric and natural gas low-income DSM expenditures remain cost-effective. The Company will provide the External Energy Efficiency ("Triple-E") board with enhanced reporting on the status of the limited income portfolio on a quarterly basis and as part of the biannual meetings of the board.

E. **Prudency of Energy Efficiency Expenditures:**

13. The Stipulating Parties agree that Avista's expenditures for electric and natural gas efficiency programs for the period January 1, 2007 through December 31, 2007 have been prudently incurred.

F. **Effective Date:**

14. As an integral part of this settlement, the Stipulating Parties have agreed that the new rates shall be implemented on January 1, 2009, and will support a modification of the procedural schedule to accommodate such a date. ICNU is not in agreement with the proposed effective date for new rates.

IV. EFFECT OF THE MULTIPARTY SETTLEMENT STIPULATION

15. Binding on Parties. The Stipulating Parties agree to support the terms of the Multiparty

Settlement Stipulation throughout this proceeding, including any appeal, and recommend that the Commission issue an order adopting the Multiparty Settlement Stipulation contained herein. The Stipulating Parties understand that this Multiparty Settlement Stipulation is subject to Commission approval. The Stipulating Parties agree that this Multiparty Settlement Stipulation represents a compromise in the positions of the Stipulating Parties.. As such, conduct, statements and documents disclosed in the negotiation of this Multiparty Settlement Stipulation shall not be admissible evidence in this or any other proceeding.

16. Integrated Terms of Multiparty Settlement. The Stipulating Parties have negotiated this Multiparty Settlement Stipulation as an integrated document. Accordingly, the Stipulating Parties recommend that the Commission adopt this Multiparty Settlement Stipulation in its entirety. Each Stipulating Party has participated in the drafting of this Multiparty Settlement Stipulation, so it should not be construed in favor of, or against, any particular Party.

17. Procedure. The Stipulating Parties shall cooperate in submitting this Multiparty Settlement Stipulation promptly to the Commission for acceptance. The Stipulating Parties shall make available a witness or representative in support of this Multiparty Settlement Stipulation. The Stipulating Parties agree to cooperate, in good faith, in the development of such other information as may be necessary to support and explain the basis of this Multiparty Settlement Stipulation and to supplement the record accordingly.

The Stipulating Parties agree to stipulate into evidence the prefiled direct testimony and exhibits of the Company as they relate to the stipulated issues, together with such evidence in support of the Stipulation as may be offered at the time of the hearing on the Multiparty Settlement.

If the Commission rejects all or any material portion of this Multiparty Settlement Stipulation, or adds additional material conditions, each Stipulating Party reserves the right, upon written notice to the Commission and all parties to this proceeding within seven (7) days of the date of the Commission's Order, to withdraw from the Multiparty Settlement Stipulation. If any Stipulating Party exercises its right of withdrawal, this Multiparty Settlement Stipulation shall be void and of no effect, and the Stipulating Parties will support a joint motion for an expedited procedural schedule to address the issues that would otherwise have been settled herein.

18. Advance Review of News Releases. All Stipulating Parties agree:

(i.) to provide all other Stipulating Parties the right to review in advance of publication any and all announcements or news releases that any other Stipulating Party intends to make about the Multiparty Settlement Stipulation. This right of advance review includes a reasonable opportunity for a Stipulating Party to request changes to the text of such announcements. However, no Stipulating Party is required to make any change requested by another Stipulating Party; and

(ii.) to include in any news release or announcement a statement that Staff's recommendation to approve the settlement is not binding on the Commission itself. This subsection does not apply to any news release or announcement that otherwise makes no reference to Staff.

19. No Precedent. The Stipulating Parties enter into this Multiparty Settlement Stipulation to avoid further expense, uncertainty, and delay. By executing this Multiparty Settlement Stipulation, no Stipulating Party shall be deemed to have accepted or consented to the facts, principles, methods

or theories employed in arriving at the Multiparty Settlement Stipulation, and, except to the extent expressly set forth in the Multiparty Settlement Stipulation, no Stipulating Party shall be deemed to have agreed that such a Multiparty Settlement Stipulation is appropriate for resolving any issues in any other proceeding.

20. Public Interest. The Stipulating Parties agree that this Multiparty Settlement Stipulation is in the public interest.

21. Execution. This Multiparty Settlement Stipulation may be executed by the Stipulating Parties in several counterparts and as executed shall constitute one Multiparty Settlement Stipulation.

Entered into this 15th day of September, 2008.

Company: By: _____

David J. Meyer
VP, Chief Counsel for Regulatory and
Governmental Affairs

Staff: By: _____

Gregory J. Trautman
Assistant Attorney General

or theories employed in arriving at the Multiparty Settlement Stipulation, and, except to the extent expressly set forth in the Multiparty Settlement Stipulation, no Stipulating Party shall be deemed to have agreed that such a Multiparty Settlement Stipulation is appropriate for resolving any issues in any other proceeding.

20. Public Interest. The Stipulating Parties agree that this Multiparty Settlement Stipulation is in the public interest.

21. Execution. This Multiparty Settlement Stipulation may be executed by the Stipulating Parties in several counterparts and as executed shall constitute one Multiparty Settlement Stipulation.

Entered into this 15th day of September, 2008

Company: By: _____

David J. Meyer
VP, Chief Counsel for Regulatory and
Governmental Affairs

Staff: By: _____

Gregory J. Trautman
Assistant Attorney General

NWIGU: By: _____

Chad M. Stokes
Cable Huston Benedict
Haagensen & Lloyd LLP

ICNU: By: _____

S. Bradley Van Cleve
Davison Van Cleve, P.C.

The Energy Project: By: _____

Ronald Roseman
Attorney at Law

NWIGU: By: _____

Chad M. Stokes
Cable Huston Benedict
Haagensen & Lloyd LLP

ICNU: By: S. Bradley Van Cleve

S. Bradley Van Cleve
Davison Van Cleve, P.C.

The Energy Project: By: _____

Ronald Roseman
Attorney at Law

NWIGU: By: _____

Chad M. Stokes
Cable Huston Benedict
Haagensen & Lloyd LLP

ICNU: By: _____

S. Bradley Van Cleve
Davison Van Cleve, P.C.

The Energy Project: By: _____

Ronald Roseman
Attorney at Law