Exhibit _____ (TES-1T)
Docket No. UE-010395
Witness: Thomas E. Schooley

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Avista Corporation's) **Petition for Recovery of Expenditures)** **Related to Electric Deferral Mechanism)** **)** **___________________________________)**	**DOCKET NO. UE-010395**

TESTIMONY OF
THOMAS E. SCHOOLEY

STAFF OF
WASHINGTON
UTILITIES AND TRANSPORTATION COMMISSION

RE: AVISTA PETITION FOR A 37% EMERGENCY SURCHARGE

August 24, 2001

Q. PLEASE STATE YOUR NAME AND ADDRESS.

A. My name is Thomas E. Schooley. My business address is 1300 S. Evergreen Park Drive S.W., PO Box 47250, Olympia WA 98504-7250.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by the Washington Utilities and Transportation Commission as a Revenue Requirements Specialist.

Q. HOW LONG HAVE YOU BEEN EMPLOYED BY THE COMMISSION?

A. Since September 1991.

I. QUALIFICATIONS

Q. PLEASE BRIEFLY DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE AT THE COMMISSION.

A. I received a Bachelor of Science degree from Central Washington University in 1986. I met the requirements for a double major in Accounting and Business Administration-Finance. Additionally, I have a Bachelor of Science degree in geology from the University of Michigan. I passed the Certified Public Accountant exam in May 1989. Since joining the Commission I have attended several regulatory accounting courses, including the summer session of the Institute of Public Utilities.

Since joining the Staff of this Commission I have jointly investigated a large waste disposal company (Docket No. TG-911369); analyzed data and developed text which was incorporated into the testimony of senior Staff in PRAM 2 (Docket No. UE-920630); presented the Staff recommendation on environmental remediation (Docket No. UE-911476); prepared detailed statistical studies for use by Commissioners and others; and interpreted utility company reports to determine compliance with Commission regulations. I analyzed PacifiCorp's proposed accounting treatment of Clean Air Act allowances (Docket No.UE-940947), and participated in meetings of PacifiCorp's inter-jurisdictional task force on allocations. I also prepared and presented testimony in the merger between Washington Natural Gas and Puget Sound Power and Light Co., Docket No. UE-960195. Most recently I presented and defended testimony in the Avista general rate case, Docket No. UE-991606.

II. SCOPE OF TESTIMONY

Q. WHAT ISSUES DO YOU PRESENT IN YOUR TESTIMONY?

A. My testimony addresses the following subjects:

1. Whether Avista's petition to Amend the Settlement Stipulation is consistent with the Settlement Stipulation. I will describe Paragraph 4 of the Settlement Stipulation and discuss whether the justifications required by the Settlement Stipulation are satisfied by Avista.
2. Whether Avista's proposed Schedule 93, 37% emergency surcharge, is justified under the Commission's interim relief criteria.
3. Whether Avista's proposed amendments to the Settlement Stipulation are appropriate.

Q. DO YOU SPONSOR ANY EXHIBITS IN SUPPORT OF YOUR TESTIMONY?

A. Yes, I sponsor Exhibit ______(TES-2) and Exhibit ____(TES-3).

III. IS AVISTA'S FILING PERMITTED UNDER PARAGRAPH 4 OF THE SETTLEMENT STIPULATION?

Q. WHAT IS THE SETTLEMENT STIPULATION?

A. The Settlement Stipulation approved in May 2001 in this docket reflects the Company's plan to manage its power costs such that the accumulated deferred power costs would reach a zero balance by February 2003, without an increase in retail rates.

Q. WHAT ARE THE TERMS OF PARAGRAPH 4 OF THE STIPULATION?

A. Paragraph 4 of the Settlement Stipulation states as follows: "The Company shall petition the Commission to alter, amend, or terminate the Settlement Stipulation (or propose other appropriate action) should the deferral balance increase or be reasonably anticipated to increase substantially due to unanticipated or uncontrollable events, such as an unplanned outage of a large Company-owned thermal unit, or worsening drought conditions. Nothing in this Settlement is intended to predetermine any issue in that proceeding or to preclude the Company from proposing any particular remedy in its Petition, including the need for rate relief. Nothing in this Settlement is intended to preclude any Party from taking a position on any of the issues presented by such petition, and any Party may support or oppose any such petition. The petition shall address the propriety of the

Company's proposed treatment of a deferral balance, if any, that might exist as of February 28, 2003, as a result of such unanticipated or uncontrollable events. Only upon such petition may the deferral balance be greater than zero for regulatory purposes by February 28, 2003."

Q. WHAT DOES AVISTA RELY ON AS "UNANTICIPATED OR UNCONTROLLABLE EVENTS?"

A. Avista lists as unanticipated or uncontrollable events "the worst hydroelectric conditions in 73 years of record together with unprecedented high wholesale market electric prices occurring at the same time." Exhibit T- ____(GGE-T), page 1, lines 23-25.

Q. HAS THERE BEEN WORSENING DROUGHT CONDITIONS SINCE THE SETTLEMENT STIPULATION WAS SIGNED?

A. Yes.

Q. BY WAY OF BACKGROUND, WHAT HYDRO-GENERATION LEVEL CONSTITUTES “CRITICAL” HYDRO-GENERATION LEVELS FOR AVISTA?

A. For Avista’s owned resources and its Mid-Columbia contracts, a critical year provides for approximately 402 aMWs of hydro-generation or about 157 aMWs less than the average hydro-generation for these resources.

Q. WHAT WAS AVISTA'S PROJECTION OF HYDRO-GENERATION THAT WAS USED TO SUPPORT THE SETTLEMENT STIPULATION?

A. About 135 aMWs below normal, for the period through 2001.

Q. WHAT LEVEL OF HYDRO-GENERATION DOES AVISTA USE TO SUPPORT ITS 37% RATE SURCHARGE?

A. About 194 aMWs below normal, for the period through 2001, or a 59 aMW deterioration in expected hydro-production compared to the earlier 135 aMW estimate.

Q. DID AVISTA KNOW THAT HYDRO WAS DETERIORATING FROM THE 135 AMW AT THE TIME OF THE STIPULATION AGREEMENT?

A. Yes. Workpapers provided as support for Mr. Norwood's testimony show that, at the time the Stipulation was being signed by the parties and brought forward to the Commission, the Company was presenting internal documents which indicated that the deferral balance could be managed to zero, even with assumptions that hydro-generation for the period would be 172 aMWs below normal. If this 172 aMW level was the focus, rather than the 135 aMW, the further deterioration of hydro-generation from levels Avista projected at the time of the Settlement Stipulation would be only 22 aMWs (194 aMW less 172 aMWs) rather than the 59 aMWs Avista claims.

Q. HAVE HYDRO CONDITIONS IN FACT BEEN WORSENING?

A. Yes. Staff understands that the current hydro conditions being experienced in the region are unusual and may result in new critical year figures. Staff also understands that hydro-generation projections have deteriorated somewhat in the period subsequent to the Settlement Stipulation being approved, and that these lower water conditions were not expressly anticipated by the plan. The 37% surcharge is also based on projections that are not only worse than earlier projections, but also significantly worse than critical water year levels.

Q. HAS STAFF MADE A DETAILED ANALYSIS OF THE STREAMFLOW STUDIES THAT WOULD SUPPORT THE HYDRO-GENERATION PROJECTIONS USED BY THE COMPANY?

A. No. Staff has utilized projections of hydro-generation that are incorporated in the Company's testimony and supporting workpapers. The schedule in this docket has not allowed for a detailed review of any studies supporting the projections. It is anticipated that this review will occur in the next phase of this docket, to the extent that actual data is not available.

Q. IN YOUR ANALYSIS OF AVISTA'S FILING IN SUPPORT OF THE 37% SURCHARGE, DID YOU ANALYZE WHETHER ANY OF THE COSTS INCURRED AND/OR DEFERRED BY AVISTA WERE PRUDENT, OR OTHERWISE RECOVERABLE CONSISTENT WITH THE CONDITIONS STATED BY THE COMMISSION IN DOCKET NO. UE-000972?

A. No. I understand those issues are reserved for the next phase of this docket.

Q. IN STAFF'S VIEW, DOES THIS EVIDENCE OF WORSENING DROUGHT CONDITIONS PERMIT AVISTA TO PETITION TO AMEND THE SETTLEMENT STIPULATION PER PARAGRAPH 4?

A. Yes.

IV. EVALUATION OF THE AMENDMENTS TO THE SETTLEMENT STIPULATION SOUGHT BY AVISTA

Q. PLEASE DESCRIBE THE AMENDMENTS TO THE SETTLEMENT STIPULATION SOUGHT BY AVISTA.

A. Avista seeks to amend the Settlement Stipulation in five ways:

1. Avista seeks a 27 month surcharge of 36.9%, subject to refund;
2. Avista seeks immediate application of the surcharge revenues to the balance of the deferred power costs,
3. Avista seeks to extend the deferral accounting through December 2003,
4. Avista seeks to apply credits from the PGE monetization credit to the deferral balance,
5. Avista seeks to include in deferral balances operation and maintenance costs, depreciation, and a return on its investment in certain Company-owned projects, including Coyote Springs II.

These items listed above are not called amendments by Avista witnesses. Mr. Falkner describes the effects of items 1-4 above in his testimony. Exhibit T-____ (DMF-T), p. 2-7. Item 5 above is only found in Exhibit ___ (DMF-1) and in Company workpapers.

Q. WHAT IS THE ANNUAL DOLLAR IMPACT OF THE REQUESTED SURCHARGE?

A. The 36.9% surcharge represents an increase in revenue requirements of $87,387,337 annually. Ex.____ (DMF-1), page 1. If the surcharge lasts for 27 months as proposed by Avista, this means the ratepayers could pay nearly $200 million or more in additional revenues compared to current rates, depending on usage.

Q. HOW DOES AVISTA ARRIVE AT THE FIGURES OF $87.4 MILLION AND 36.9%?

A. The $87 Million represents the annual level of revenue requirement which, under Avista's assumptions, will reduce the power cost deferral balance to approximately zero by December 31, 2003. The accumulated deferral balance consists of the actual deferred amount at June 30, 2001 and Avista's projection of deferrals from July 2001 through the end of 2003.

Along with these deferred power costs, the Company is proposing to amortize, over a 15 month period ending December 2002, the deferred credit related to the monetization of the PGE sale agreement plus capital and O&M costs on certain Company-owned projects.

The 36.9 percent figure is the $87.4 million amount divided by normalized utility revenues from the last general rate case of $236,966,000 which serves as the basis of applying the increase to the different customer classes. Specifically, the requested annual surcharge represents:

Annual level of surcharge before revenue sensitive items	$ 80,409,105
Gross-up of equity return on certain Company-owned projects	$ 3,569,860
Gross-up of misc. revenue sensitive items	$ 3,408,372
Total Surcharge Revenue Requested	$ 87,387,337

Q. REFERRING FIRST TO THE AMOUNT OF MONEY AVISTA IS SEEKING, ON WHAT BASIS HAS AVISTA SOUGHT TO JUSTIFY ITS REQUEST FOR A 37% RATE SURCHARGE?

A. Mr. Eliassen states that Avista Corp. is undergoing significant financial stress because the cost of obtaining power to serve its customers is much more than the amount included in rates and that Avista is unable to obtain construction financing for the Coyote Springs II project through normal financing channels. According to Mr. Eliassen, Avista's bankers and lenders show concern about the size of the deferral balances and the lack of rate relief to deal with the deferred costs. Mr. Eliassen claims that without rate relief, Avista may violate certain debt covenants by the end of the year. Exhibit T- ____ (JEE-T), page 1, lines 18-20; page 2, lines 13-14; page 3, lines 10-16.

Q. HAS AVISTA RELIED ON ANY SPECIFIC CRITERIA TO JUSTIFY ITS 37% SURCHARGE REQUEST?

A. Avista references only "prior Commission orders regarding such a request." Exhibit T-____ (GGE-T), p. 9. The Company's response to Staff Data Request No. 136 indicates this reference is intended to refer to the criteria listed in the Commission's 1975 order in Cause No. U-75-40, involving Pacific Northwest Bell Telephone Company ("PNB"). As Staff witness Mr. Elgin points out, these criteria were first adopted in 1972 in Cause No. U-72-30 tr. In any event, Avista's testimony provides neither a list of the Commission's criteria, nor an explicit, systematic analysis of those criteria.

Q. PLEASE REITERATE THE SIX INTERIM RATE RELIEF STANDARDS.

A.
1. This commission has authority in proper circumstances to grant interim rate relief to a utility, but this should be done only after an opportunity for adequate hearing.
2. An interim rate increase is an extraordinary remedy and should be granted only where an actual emergency exists or where necessary to prevent gross hardship or gross inequity.
3. The mere failure of the currently realized rate of return to equal that approved as adequate is not sufficient standing alone to justify the granting of interim relief.

4. The Commission should review all financial indices as they concern the applicant, including rate of return, interest coverage, earnings coverage and the growth, stability or deterioration of each, together with the immediate and short term demands for new financing and whether the grant or failure to grant interim relief will have such an effect on financing demands as to substantially affect the public interest.

5. In the current economic climate the financial health of a utility may decline very swiftly and interim relief stands as a useful tool in an appropriate case to stave off impending disaster. However, this tool must be used with caution and applied only in a case where not to grant would cause clear jeopardy to the utility and detriment to its ratepayers and stockholders. That is not to say that interim relief should be granted only after disaster has struck or is imminent, but neither should it be granted in any case where full hearing can be had and the general case resolved without clear detriment to the utility.

6. Finally, as in all matters, we must reach our conclusion with the statutory charge to the Commission in mind, that is to "Regulate in the public interest." This is our ultimate responsibility and a reasoned judgment must give appropriate weight to all salient factors.

Q. PLEASE PROVIDE YOUR ANALYSIS OF AVISTA'S REQUEST FOR A 37% RATE INCREASE UNDER THE COMMISSION'S INTERIM RELIEF STANDARDS, ASSUMING THEY APPLY.

A. The first criterion is "This commission has authority in proper circumstances to grant interim rate relief to a utility but this should be done only after an opportunity for adequate hearing." The Commission will hear testimony and cross-examination on September 5-6, 2001. The Staff has done the best it can to respond to the issues in this compressed time frame.

Q. WHAT IS REQUIRED BY THE SECOND CRITERION?

A. The second criterion states, "An interim rate increase is an extraordinary remedy and should be granted only where an actual emergency exists or where necessary to prevent gross hardship or gross inequity." In this case, Avista claims an emergency largely due to the growing deferred power costs on its balance sheet without a determination of the prudence of those power costs or a Commission-approved means to recover them. Without recovery, Avista's alleges it may potentially violate certain covenants of the notes issued in April 2001 and may be unable to finance existing capital projects.

Q. IS THERE EVIDENCE OF AN EMERGENCY ON AN HISTORICAL BASIS?

A. The most recent information available indicates the Company did not appear to be experiencing an actual emergency at June 30, 2001. Exhibit _____(RRP-1), p. 1 coverage ratios as of June 30, 2001 that comply with applicable financial ratio covenants. However, in Avista's response to Staff Data Request No. 171, Avista indicates it did not comply with one liquidity condition as of June 30, 2001.

Q. WHAT IS YOUR ANALYSIS UNDER THE THIRD CRITERION?

A. The third criterion states: "The mere failure of the currently realized rate of return to equal that approved as adequate is not sufficient standing alone to justify the granting of interim relief." Avista's latest Commission basis report (Docket No. UE-010690 for the period ending December 31, 2000) shows an actual return on rate base of minus 0.3% and a normalized return on rate base of 4.8%. These amounts are well below the return of 9.03% allowed in the latest rate case, Docket No. UE-991606. The above results reflect the deferral of power costs per the UE-000972 order. If those deferred power costs were included in the results of operations, the returns on rate base would be even lower.

Q. WHAT IS YOUR ANALYSIS UNDER THE FOURTH CRITERIA?

A. The fourth criteria states the Commission will "review all financial indices as they concern the applicant, including rate of return, interest coverage, earnings coverage and the growth, stability or deterioration of each, together with the immediate and short term demands for new financing and whether the grant or failure to grant interim relief will have such an effect on financing demands as to substantially affect the public interest."

Q. WHAT ARE AVISTA'S IMMEDIATE AND SHORT TERM DEMANDS FOR NEW FINANCING?

A. Avista shows maturing debts of $64,000,000 during the rest of 2001. (Avista's Response to Staff Data Request No. 165). According to Avista, to meet the projected completion date of June 2002, the Coyote Springs II project requires funding totaling $47,178,000 during the second half of 2001, and $31,800,000 during the first six months of 2002. Avista states that other capital investments in the second half of 2001 require funds totaling $86,631,000. (Avista's Response to Staff Data Request No. 164). Taken together, Avista appears to require upwards of $200 million in financing during the remainder of 2001.

Q. HAS AVISTA PROVIDED EVIDENCE DEMONSTRATING THESE PROJECTS ARE STILL VIABLE AND COST EFFECTIVE?

A. No.

Q. WHICH FINANCIAL INDICES ARE OF CONCERN TO AVISTA IN THIS CASE?

A. The covenants in an April 2001 bond issuance required Avista to meet certain fixed charge coverages and debt to total capitalization.

Q. WHAT IS THE NATURE OF THE COVENANTS AVISTA MUST SATISFY IN ORDER TO FINANCE AS IT PROPOSES?

A. Avista Corporation is required to comply with covenants under its Corporate Credit Agreement. The following covenants could be impacted by Avista's requested surcharge, and the accounting for that surcharge:

- Consolidated Fixed Charge Coverage Ratio:

This ratio is calculated as the ratio of total Company cash flow to total Company fixed charges for the current and three prospective quarters. The total Company cash flow is calculated from consolidated net income, plus and minus various adjustments. The adjustments include the changes in after-tax gas and electric deferrals, plus all cash on the balance sheet as of the last day of the period. A similar consolidated fixed charge coverage ratio applies for Avista Utilities, as well as Avista Corporation. By telephone on Thursday August 23, 2001 Avista said that within one week, Avista would be required to, and would, request a waiver from its banks on this fixed charge coverage ratio requirement.

- Consolidated Total Debt to Consolidated Total Capitalization Ratio:

This ratio is required to be at or below 0.60 (60%) at the end of any fiscal quarter.

- Investments:

Under this covenant, Avista may not loan, advance or guarantee any obligation in any subsidiary if the aggregate of all such obligations exceeds $100 million in 2001 or $75 million in 2002. This covenant should not affect the Coyote Springs II project, since that project is owned by Avista Utilities.

Avista's 9.75% Senior Notes require Avista to comply with two conditions in order for a number of “suspended covenants” to remain suspended. The two conditions are the absence of any default and: “During any period of time that (i) Moody’s and S&P have issued credit ratings of Avista’s senior unsecured debt of at least Baa2 and BBB, respectively, in each case with a stable or improving outlook….”

These "suspended covenants" include "Restricted Payments." The Restricted Payments covenant with which Avista must comply states that "Unless the rating condition is satisfied, Avista Corp. will not, and will not permit any of its Restricted Subsidiaries to, directly or indirectly = (i) declare or pay any dividends…" The document provides that Avista may nonetheless declare or pay dividends if, among other conditions, its fixed charge coverage ratio satisfies the conditions of the indenture, after giving pro forma effect to restricted payments.

Other covenants which are not suspended, with which Avista must comply, address the following topics:

- Asset Sales
- Incurrence of Indebtedness and Issuance of Preferred Stock
- Dividend and Other Payment Restrictions Affecting Subsidiaries
- Transactions with Affiliates
- Sale and Leaseback Transactions

There are cross-default provisions between Avista's Corporate Credit Agreement and Avista's 9.75% Senior Notes.

Q. WHAT IS AVISTA'S CURRENT CREDIT RATING?

A. On August 2, 2001 Standard & Poors downgraded Avista Corporation's senior unsecured debt to BBB- with a negative outlook. On July 27, 2000, Moody's downgraded Avista Corporation's senior unsecured debt to Baa2, with a continued negative outlook.

Q. HAS STAFF HAD TIME TO RESEARCH HOW NON-REGULATED OPERATIONS AFFECTED AVISTA UTILITIES' FINANCIAL SITUATION?

A. No.

Q. WHAT IS THE TREND IN THE ACTUAL COVERAGES OR RATIOS FOR AVISTA'S RECENT PAST?

A. Table 1 of my Exhibit ____ (TES-2), Part 1 shows the fixed charge coverages from 1996 through June of 2001. The trend for the utility goes from a high of 4.2 in 1997 to a low of 0.8 in 2000. (Avista Response to Staff Data Request 163). The actual fixed charge coverage for utility operations is reported as 2.23 as of June 2001. Ex. ____(RRP-1). The required coverage ratio is 1.25 for utility operations and 1.00 for the total company under Avista’s corporate credit agreement.

Q. HOW HAS THE CAPITALIZATION RATIO CHANGED OVER THE RECENT PAST?

A. The debt as a percent of total capital has increased to 51.9% at the end of 2000 from 43.2% in 1998, this is also a negative trend. Ex. ____(RRP-1), page 5. At June 30, 2001, the debt to capital ratio is 55.7%, and by the end of 2001, Avista projects the debt to total capital ratio as 59.8%. This is very close to the 60% limit in the covenants.

Q. DO THE COVENANTS OF THE RECENT FINANCINGS REQUIRE FORWARD LOOKING COVERAGE ESTIMATES?

A. Yes.

Q. WHAT DATA DOES AVISTA PRESENT TO MEET THOSE COVENANTS?

A. Mr. Peterson's Exhibit ___(RRP-1), page 1, shows the estimated fixed charge coverage ratios for the last half of 2001 to the end of 2002. Avista's evidence shows a serious decline by the third quarter of this year with negative cash flow and an inability to cover its fixed interest charges. The trend improves over the next several quarters, but not to the point of meeting the fixed charge coverages required.

Q. WHY DOES THIS TREND SHOW SUCH A DRAMATIC DECLINE THIS YEAR?

A. The main reason is the use of Avista's revolving credit line to finance the Coyote Springs II project.

Q. HOW DOES A CHANGE IN THE ASSUMPTION ON HYDRO-GENERATION AFFECT THE PROJECTED DEFERRAL BALANCES AND CONSEQUENTLY THE FINANCIAL RATIOS?

A. If the hydro-generation assumption is revised to reflect critical water from Avista's assumption of far less than critical, the deferral is reduced by $11 million to $187 million from $198 million. Under normal hydro conditions, the deferred balance by the end of 2001 would decline by $24 million to $174 million from $198 million.

Avista has not been able to provide a recast of the estimated fixed charge coverages for the near future with the assumptions of critical or normal hydro conditions. My analysis of the impact on the fixed charge coverage ratio uses a simplified approach. In the critical water scenario, my calculation moves the fixed charge ratio change to a negative 2.33 from Avista's figure of negative 2.42. If the planned financings are included, the ratio improves to negative 0.07 compared with Avista's negative 0.15.

If normal hydro conditions returned, the fixed charge ratio again improves to negative 2.23 without the new financing, and to a slightly positive 0.03 with the financings.

Q. ARE THESE CHANGES SIGNIFICANT COMPARED TO THE REQUIRED FIXED CHARGE COVERAGE RATIO OF 1.25?

A. No. All the scenarios produce a shortfall in this covenant requirement.

Q. BASED ON THE ONE FACTOR, FIXED CHARGE COVERAGE, WHAT LEVEL OF CASH IS NEEDED TO BRING THE RATIO TO THE REQUIRED 1.25 FROM THE PROJECTED DECEMBER LEVEL OF NEGATIVE 2.42?

A. My Exhibit ___(TES-3) presents a calculation of this amount. In the calculation, I assume Avista is able to finance the Coyote Springs II plant and that Avista successfully issues $67,600,000 of common stock in the remainder of 2001. (Avista Response to Staff Data Request No. 166). With those adjustments, my calculation indicates a need for $19,483,000 in the fourth quarter of 2001. This is an increase of 32.6% over current revenues. This amount is comparable to Avista's surcharge request which provides $20,292,000 in 2001.

Q. HOW DOES THIS CHANGE IMPACT THE CENTS PER KILOWATT-HOUR CHARGE PROPOSED BY STAFF?

A. This reduces the emergency rate to 1.5 cents per kilowatt-hour from 1.7 cents.

Q. GIVEN THE ABOVE ANALYSIS, DOES AVISTA SHOW A NEED FOR INTERIM RATE RELIEF?

A. Yes. In my opinion, Avista needs cash from its utility operations in the very near future.

Q. HAVE YOU HAD TIME TO INVESTIGATE WAYS FOR AVISTA TO RAISE CASH THROUGH MEANS OTHER THAN COLLECTING MORE MONEY FROM ITS RATEPAYERS?

A. No.

Q. WHAT IS THE FIFTH COMMISSION CRITERION?

A. The fifth criterion states "In the current economic climate the financial health of a utility may decline very swiftly and interim relief stands as a useful tool in an appropriate case to stave off impending disaster. However, this tool must be used with caution and applied only in a case where not to grant would cause clear jeopardy to the utility and detriment to its ratepayers and stockholders. That is not to say that interim relief should be granted only after disaster has struck or is imminent, but neither should it be granted in any case where full hearing can be had and the general case resolved without clear detriment to the utility."

Q. IN YOUR OPINION, IS AVISTA ACTUALLY FACING AN IMPENDING DISASTER?

A. Avista's Exhibit ____ (RRP-1), page 1, shows that Avista meets required fixed charge coverage ratios as of June 2001. Avista claims it faces serious financial hardship if the increasing deferral balance is not offset with cash revenues, in the form of rate increases. I conclude earlier that without significant additional revenue, Avista would not meet certain financial covenants.

Q. WHAT IS THE COMMISSION'S SIXTH CRITERION?

A. The sixth, and last, criterion states: "Finally, as in all matters, we must reach our conclusion with the statutory charge to the Commission in mind, that is to 'regulate in the public interest.' This is our ultimate responsibility and a reasoned judgment must give appropriate weight to all salient factors."

Q. WHAT IS YOUR EVALUATION UNDER THIS STANDARD?

A. The first threshold of those salient factors in the present case is whether or not the interim rate relief standards do apply. Staff witness Mr. Elgin addresses this question. Assuming they do, the salient issues become whether failure to grant immediate rate relief would cause gross hardship or gross inequity, and whether the financial indices indicate the need for immediate rate relief.

Q. WOULD FAILURE TO GRANT IMMEDIATE RATE RELIEF CAUSE GROSS HARDSHIP OR GROSS INEQUITY?

A. One might ask "Gross hardship to whom?" Certainly customers will face significantly larger electric bills which will cause some of them hardship. If investors are unwilling to provide funds, Avista may not be able to adequately invest in the infrastructure needed to serve those same customers. Or Avista may only be able to issue debt at a higher interest level. Avista has not shown that higher cost debt is more or less cost effective than the 37%, 27 month surcharge it has requested.

Q. DO THE FINANCIAL INDICIES SHOW A NEED FOR IMMEDIATE RATE RELIEF?

A. The one factor I was able to analyze in the time available, the fixed charge coverage ratio, shows Avista needs cash in the very near future.

Q. WHAT IS YOUR RECOMMENDATION CONCERING EMERGENCY RATE RELIEF REQUEST BASED ON THE COMMISSION'S INTERIM RELIEF STANDARDS?

A. Based on my analysis under the interim rate relief standards, Avista shows an immediate need for rate relief. I recommend a rate increase of 32.6%, subject to the other staff recommendations.

Q. ASSUMING THE COMMISSION GRANTS EMERGENCY RATE RELIEF, SHOULD THE PROCEEDS BE USED TO OFFSET DEFERRED POWER COSTS NOW, AS AVISTA PROPOSES?

A. No. The Commission's orders in Docket No. UE-000972 state several conditions that must be met before any deferral power costs are recovered in rates. Before any revenues are used to offset deferred power costs, these conditions must be satisfied.

Q. TURNING NOW TO THE OTHER AMENDMENTS TO THE SETTLEMENT STIPULATION PROPOSED BY AVISTA, SHOULD THE SETTLEMENT STIPULATION BE AMENDED TO PERMIT AVISTA TO CONTINUE THE DEFERRAL COST MECHANISM UNTIL THE END OF 2003?

A. No. Staff recommends the deferrals terminate June 30, 2001. This subject is addressed by Mr. Elgin.

Q. SHOULD THE SETTLEMENT STIPULATION BE AMENDED TO APPLY THE REGULATORY LIABILITY FROM THE PGE MONETIZATION CREDIT TO THE DEFERRAL BALANCE?

A. No. The disposition or use of the PGE monetization credit is an issue which should be determined in a general rate case when we will have a complete picture of the Company's circumstances. In addition, as I indicated above, no offset of deferrals should occur absent findings that Avista has satisfied the conditions in the Commission's orders in Docket No. UE-000972.

Q. SHOULD THE SETTLEMENT STIPULATION BE AMENDED TO INCLUDE IN THE DEFERRAL BALANCE OPERATION AND MAINTENANCE COSTS, AS WELL AS A RETURN OF, AND A RETURN ON THE CAPITAL COST OF CERTAIN COMPANY-OWNED PROJECTS, INCLUDING COYOTE SPRINGS II?

A. No. Operation and maintenance expenses are ongoing period costs inherent in a utility's daily business. These are appropriately included in calculating the revenue requirements in a general rate case, and should not be deferred. Capital costs necessary to build a power plant or to meet distribution plant extensions are part of the investments a utility makes to meet its service obligations. These are provided for in a general rate case. O&M, depreciation, and the new capital expenditures should not be included in the existing or projected deferral balances.

Q. WAS AVISTA ALLOWED TO INCLUDE SUCH COSTS IN THE DEFERRAL UNDER THE LANGUAGE IN PARAGRAPH 2 OF THE SETTLEMENT STIPULATION, WHICH REFERS TO "EXTRODINARY COSTS INCURRED DURING THE DEFERRAL PERIODS TO ACHIEVE POWER COST SAVINGS?"

A. No. This language was intended to cover such extraordinary events as flying generators from overseas, which Avista had actually contemplated at that time. Everyday costs like O&M costs were never intended to be recovered in the deferral.

Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes, it does.