



June 4, 2010

VIA: Electronic Mail

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

Re: Comments of Avista Utilities - Docket No. U-100522

Dear Mr. Danner,

On April 8, 2010, the Washington Utilities and Transportation Commission (Commission) issued a Notice of Opportunity to File Statement of Issues and Written Comments in the above referenced Docket. On April 23, 2010 Avista filed with the Commission its response and participated in the workshop on May 4, 2010. On May 13, 2010, the Commission issued a Notice of Opportunity to File Written Comments on a Consolidated Issues List, and on May 19, 2010, the Commission provided a Notice of Amendment to Consolidated Issues List. The Company appreciates the opportunity to provide comments on the amended issues list and looks forward to participating in the upcoming workshop on June 29, 2010. The following is the Company's response to the notice:

General

- 1) Definitions. What is decoupling? What is lost margin? How is it measured? What are fixed costs?

Avista's Response:

Decoupling - Decoupling is a ratemaking and regulatory approach designed to break the link between a utility's recovery of fixed costs and a consumer's energy consumption. The Company's current rate structures provide recovery of the majority of Avista's fixed costs on a sales volume

basis, and as such, energy efficiency and conservation objectives are directly at odds with the recovery of the fixed costs of providing service.

Lost Margin – Those fixed costs that have been approved for recovery in rates but are not recovered due to reduced use per customer resulting from “programmatic” and “non-programmatic” DSM¹. Typically the recovery of lost margin is cumulative until rates are reset in a general rate case.

How is Lost Margin Measured – see the Company’s response to # 4 and #6 below.

Fixed Costs – Those costs, previously approved for recovery by the Commission, that do not vary with customer consumption. These typically include all costs except commodity costs and perhaps some O&M expenses.

- 2) *Recovery of Conservation Program Costs.* Are the utilities’ conservation program costs recovered from ratepayers in a timely manner?
- a. If cost recovery is untimely, please describe how and why
 - b. Are there other methods of funding conservation programs that would be more efficient and effective at acquiring conservation resources?

Avista’s Response:

- a. Direct program expenses are currently expensed each year, and the combination of Tariff Rider revenues and deferred accounting provide recovery of those costs. This timely recovery does not extend to fixed cost recovery resulting from successful DSM efforts or a return component under current practices. To ensure timely recovery of costs, it is appropriate to continue to adjust the Tariff Rider rate annually², similar to the annual Purchased Gas Adjustment, so that the deferral balance does not grow (positive or negative) from year to year.

¹ Programmatic DSM are those demand side management programs offered by the Company where energy efficiency savings can be directly quantified as a result of the Company’s promotion and efforts. Non-programmatic DSM is essentially everything else, such as energy efficiency messaging, where there are assumed energy savings, however they are more difficult to directly quantify.

² See Docket UE-100176.

- b. Utilities earn a return on the acquisition of generating resources, but not on the acquisition of DSM “resources”. It would be appropriate to consider capitalizing a portion of the DSM acquisition to place it on more of a “level playing field” with other resource acquisitions.

Impact of Conservation Resource Development on Rate of Return

- 3) *Statement of the Issue.* Does the development of conservation resources deny the utility an opportunity to earn its allowed rate of return? Would an attrition study be the best way to determine this question? Are there alternative ways of making such a determination?

Avista’s Response:

This docket should provide for the clarification or determination of all recoverable costs. By doing so, recovery of fixed costs and an appropriate return—as defined and described in our response to questions #1 and #2—would provide cost recovery and, by definition, remove disincentives. The provision of incentives is separate and apart from cost recovery. Providing an appropriate return is not an “incentive”; rather it is part of the cost of doing business. Returns are universally accepted as necessary for sustainable provision of service. An incentive would be a bonus or incremental payment/reward for defined achievement beyond expected results.

Threshold issues should be considered by the Commission:

- a. A primary contextual item is that cost-effective energy efficiency is the least expensive new resource. The average cost of Avista’s energy efficiency programs (including administrative expenses) historically has been between \$20 and \$30 per megawatt hour (MWh). Power purchases are currently available at approximately \$48 to \$52 per MWh. (This is the current market rate for short-term—or less than 18 months—periods.) Long-term purchase or power plant construction costs, depending on the resource type, are in the \$70 to \$110 per MWh range per the Company’s 2009 Integrated Resource Plan.
- b. Providing for full cost recovery would maintain cost-effective energy efficiency as the lowest cost new resource. The inclusion of all costs, including “lost and found margins” and an appropriate return, would not change the cost relationship between energy

efficiency and the next resources in the power provision stack. For reasons to be elaborated on below, more energy efficiency may result which, in turn, would reduce the need for future higher cost resources.

- c. Avista has been providing energy efficiency services under the current ratemaking methods since 1995. Avista's energy efficiency budget (on a system basis) averaged approximately \$10 million per year between 1995 and 2006. However, Avista spent \$27 million on energy efficiency in 2009. This two and a half fold increase in DSM expenditures has led to a further reduction in fixed cost recovery.
- d. RCW 19.285 (aka I-937 or the Energy Independence Act and codified by Commission rule as WAC 480-109) requires the acquisition of all cost-effective conservation. While RCW 19.285 requires that all cost-effective energy efficiency be acquired, it is silent on cost-recovery methods. This is the purview of the Commission. All costs, as defined in response to Question #1, can and should be defined and accepted by the Commission.
- e. Historically, Washington's investor-owned utilities have "over-performed" in their energy efficiency acquisition under current Commission policy. However, it seems that Commission policies may need to be reexamined. This Commission was the first Commission in the United States to approve a non-bypassable, or "system benefit," charge in 1994 to fund energy efficiency. The "tariff rider" concept then became the Country's predominant form of funding energy efficiency. This was the right ratemaking mechanism at that time, as many thought industry restructuring was inevitable; a pass-through surcharge on the distribution system to fund energy efficiency would deliver meaningful energy efficiency to customers. Times have changed. The magnitude and scale of energy efficiency budgets and achievement have fundamentally changed and this, in turn, brings into question whether current regulatory practices are sufficient to promote energy efficiency.

An attrition adjustment, by itself, would not be an appropriate mechanism. Past practice in Washington has linked, to some degree, an attrition adjustment to a utility experiencing financial

hardship. See excerpts from Commission orders in Attachment A. Therefore, if an attrition adjustment were to be employed, it would be important that it be designed specifically to achieve the intended outcome and not simply used as a means to alleviate undo financial hardship. In summary, recovery of all costs (including fixed costs and a return) are currently not provided in Washington.

- 4) *Magnitude of the Risk.* How much lost margin can be attributed to each utility’s conservation programs? How much lost margin can be attributed to the other types of conservation referenced in question 6 below?

Avista’s Response:

Based on the calculations shown below, for 2009, total lost margin for programmatic DSM and the Northwest Energy Efficiency Alliance (NEEA) was \$1,605,236.

WA Schedule 31 - E	\$	0.01597	25,794	\$	411.93
WA Schedule 101 - G	\$	0.25305	958,024	\$	242,427.97
WA Schedule 111 - G	\$	0.14176	474,552	\$	67,272.49
WA Schedule 121 - G	\$	0.09720	5,155	\$	501.07
Total				\$	1,454,884.91
Lost Margin - NEEA					
Rate Schedule		Margin per kWh	kWh Savings		Lost Margin
WA Schedule 1 - E*	\$	0.01987	6,990,480	\$	138,900.84
WA Schedule 11 - E**	\$	0.04741	171,338	\$	8,123.11
WA Schedule 21 - E**	\$	0.01942	171,338	\$	3,327.37
			7,333,155	\$	150,351.32
* Total NEEA Savings was 9,986,400 - 70% was attributed to WA for this analysis					
** Total Non Residential NEEA Savings were 342,675. One half was attributed to Schedule 11, the rest to Schedule 21					

Lost margins from non-programmatic efforts would add to these figures. These figures would also change with the increase in energy efficiency efforts in the future.

- 5) *Direct Conservation Incentives and Rate of Return.* What is the rationale for making incentive payments to utilities for acquiring conservation resources? Is it to encourage conservation? (See questions 14-17 below relating to conservation mandates.) Is it to ensure that the utility earns a sufficient rate of return? Does an incentive program act as an effective substitute for decoupling?

Avista's Response:

Avista would not be seeking "incentive payments...for acquiring conservation resources" but for clearly defined achievement beyond stated goals, as described in our response to Question #3. Utilities should first recover the costs of providing energy efficiency resources, including fixed-cost recovery or lost margins. This is to make a company whole for its energy efficiency activities. To do otherwise does not allow for a sustainable and growing commitment to energy efficiency.

Decoupling is not an incentive. Decoupling is a means for recovery of costs already deemed prudently incurred. Capitalizing is not an incentive; it is a means to recover a cost to finance the investment. An "incentive" therefore is not a substitute for decoupling, fixed cost recovery, or capitalizing. An incentive is a financial bonus for achievement in excess of a stated goal.

Details of a Conservation Incentive Mechanism

6) *Categories of Lost Margin Due to Conservation Eligible for Recovery.* Identify which, if any, of the following declines in customer use should be subject to recovery by the utility and how each could be calculated or measured:

- a) Margin decline from company-sponsored conservation programs that provide a rebate or that provide direct assistance with conservation-measure deployment (such as a site visit evaluation)
- b) Information provided by the utility to the customer, such as educational programs, bill inserts, or information on the utility's website
- c) A Company's share of Northwest Energy Efficiency Alliance (NEEA) regional conservation savings including market transformation that is not counted in the utility's programmatic or informational efforts. If yes, how can NEEA savings be separated from other conservation savings that occur for the purposes of a cost recovery mechanism -
- d) Independent customer conservation efforts (no rebate or direct utility assistance documented)
- e) Conservation due to codes and standards
- f) Elasticity (i.e. heating fewer rooms, lowering thermostat, et cetera).
- g) Other (describe)

Avista's Response:

- a) Programmatic participation is highly measurable and represents the most documentable representation of the direct impact of utility conservation programs. Recovery of lost margins is appropriate. There are a number of ways that could be used to address recovery, such as decoupling, per-kWh or per-therm margin recovery, or reduction of test-period loads by planned savings, among others.
- b) To the extent utility educational efforts yield a measurable change in customers energy use, independent of all other influences, lost margin recovery should be allowed.
- c) NEEA's calculation of energy savings attributed to their market transformation ventures is based upon the adoption of efficiency measures above an estimate of baseline adoption. It also specifically excludes the savings claimed through local utility programs. Thus the claimed regional savings are both "net" of natural adoption and incorporate an adjustment to the regional claim to avoid "double-counting" the energy savings. Individual utilities can and do have significant influence upon the success of the regional NEEA portfolio both through their participation in the management of the organization as well as the management of local efforts to leverage the benefits of regional activities. Therefore, the allocation of NEEA savings should be incorporated into lost margin calculations and any incentive calculations.
- d) Excluding demonstrable influence by the utility as outlined in b. above, efficiency measures or behaviors adopted by the customer without the documented participation in a utility program are inherently difficult to measure. It would be difficult to develop a metric of success that is sufficiently precise to warrant inclusion for cost recovery.
- e) Energy savings derived from higher codes and standards are reasonably measurable and therefore lost margin recovery would be appropriate. Successful local utility programs can both accelerate the adoption of cost-effective codes and standards as well as increase code

compliance. For those reasons there should be an accommodation of utility success in this area to the extent possible.

f) To the extent related to education, communications, and energy efficiency efforts promoted by the utility, lost margin recovery would be appropriate. Customer response to changes in retail rates, except as they overlap with participation in utility conservation programs or behavioral measures promoted by the utility, are separate and distinct from the efficiency efforts driven by utility-sponsored programs and should not be included in lost margin recovery.

7) *Impact of Conservation Incentive Mechanism on Utility Incentives to Encourage Consumption.* If a utility recovers lost margin as calculated by installed conservation measures, does it still have an incentive to encourage customers to use more energy in some other application? Are any utilities promoting the use of more energy by its customers?

Avista's Response:

A fixed cost recovery adjustment would recover lost margins of installed conservation measures. Avista does not encourage customers to use more electricity. A fixed cost recovery adjustment would not change this practice. Avista does promote the direct use of natural gas for multiple reasons. The direct use of natural gas is the best use. The direct use of natural gas at the customer level, rather than the use of electricity, is the most efficient use of this resource as it would otherwise be used as the fuel for a combustion turbine to produce electricity at a much lower level of efficiency.

8) *Offsets.* To what extent should any recovery of lost margin be offset by revenues associated with new load (sometimes referred to as "found margin"), including:

- a) New customers,
- b) Additional load for existing customers,
- c) Other?

Avista's Response:

- a) New Customers - To the extent that the incremental costs to serve new customers are lower than the embedded fixed costs, then that margin could be used to offset other lost margin. However, the Company demonstrated in UG-060518 that certain incremental costs are higher than embedded costs because of inflation and depreciation, and as such, there was no found margin from new customers.³
- b) Additional Load – The goal of the Company is to have the conditions in place which would allow it to recover its fixed costs. This would provide alignment of state policy to promote energy efficiency and rate making practice to provide recovery of costs associated with it. If the savings from DSM are offset to some degree by increased use per customer, that increased use can be used to offset the lost margin from DSM savings.

- 9) *Application to Industrial Customers.* Should large customers be treated differently than residential or commercial customers with regard to lost revenue recovery or incentives? If so, please explain the rationale for excluding large customers.

Avista's Response:

For programmatic DSM lost margin, if the industrial customer class pays into in the Company's Energy Efficiency Tariff Rider, then they should be subject to lost margin recovery. However, when it comes to other mechanisms such as decoupling, the Company believes that these customers are much more prone to changes in the general economic and business climate, and that any decrease in use per customer is often not related to conservation programs and messaging.

- 10) *Other Characteristics of an Incentive Mechanism.* What characteristics should an incentive mechanism include?
- a) Should it allow the utility to recover an absolute dollar amount? If so, how should the amount be calculated? Should recovery be based on all conservation that occurs over a given period, or

³ Page 3, line 19 Rebuttal Testimony of Brian J. Hirschorn, Docket Nos. UE-090134, UG-090135, and UG-060518 (consolidated)

- be proportional to the conservation that occurs as a result of a utility's actions?
- b) For electric utilities, should the incentive targets be different and greater than the Energy Independence Act (EIA or I-937) targets?
 - c) Should there be penalties for failing to achieve the incentive mechanism's target or rewards for achieving only a percentage of the target?
 - d) Should there be an earnings test to determine if the utility is over earning?
 - e) Should the incentive include all customer classes in the target and in the collection of the incentive payments?
 - f) Are there other complementary rate making policies that should be matched with an incentive mechanism such as a pro forma adjustment to account for lower loads? Please provide details of any such proposals.

Avista's Response:

- a. An incentive mechanism—separate and distinct from fixed cost recovery and return—should be based on achieving energy efficiency results in excess of stated targets. The mechanism could take the form of an additional rate of return (say, 2% or 200 basis points) as is provided by RCW 80.28.260. Alternatively, a shared savings plan could be considered in which a portion of the net benefits (for example, 10% of a generally accepted metric such as the Total Resource Cost test) could be provided to shareholders. Another option would be a defined bonus which could be provided based on achievement of stated goals. The simplest mechanism would be symmetry with RCW 19.285 (or I-937) in which the \$50/MWh penalty for not achieving targets would be balanced by a \$50/MWh reward for exceeding targets.
- b. Incentives should be defined to be in excess of a stated target, e.g., I-937 targets. Incentives should not be defined to include fixed cost recovery or return components.
- c. Such penalties exist from RCW 19.285 (or I-937) which provides for a penalty of \$50/MWh for not meeting targets.
- d. No, the incentive should be independent of other cost-recovery.

- e. To the extent that the customer classes fund programmatic DSM, the incentive should include all customer classes in the target and in the collection of the incentive payments.
- f. Yes. One example is an adjustment to reduce test-period loads to reflect the planned reduction in loads related to energy efficiency. This would be a direct way to address lost margin recovery.

Impact on Rates

- 11) *Impact on Various Classes of Customers.* How should the costs of an incentive mechanism be spread among the various rate classes? Are transport customers appropriately protected from a recovery mechanism's costs?

Avista's Response:

This could be accomplished in a number of ways, depending on the mechanism. By far the simplest way would be to spread the costs of the incentive mechanism proportionately to those rate schedules causing the savings. If, for instance, 75% of conservation savings came from Rate Schedule 1 (residential), then 75% of the cost of the incentive should come from that rate schedule. Another way that the costs can be spread is by adding those costs to the DSM programmatic costs, and seek recovery using the same methodologies used for the existing energy efficiency tariff riders. As it relates to natural gas transportation customers, for Avista, this customer class does not contribute to the Energy Efficiency Tariff Rider. As such, they would not be subject to an incentive mechanism as they are not subject to the surcharge, and therefore are appropriately protected.

- 12) *Impact on Low Income Households.* Should the design of an incentive mechanism consider its impact on low-income customers? Would a lost margin recovery mechanism cause low-income households to bear a higher percentage of system costs? Are existing utility conservation programs for the residential class accessible to low-income customers? If not, is the relationship between bill impacts and access to programs for low-income equitable?

Avista's Response:

The design of any mechanism or program should consider the impact on all affected customer groups, including low-income. What should be recognized, though, is that it is somewhat difficult to determine which customers in the Company's residential rate schedules are considered limited income, as the Company does not collect income data.

On the whole, the low-income population may be net beneficiaries of such programs. For example, during the pilot phase of the Company's Decoupling Mechanism, the Company showed that limited income customers were net beneficiaries when comparing the benefit from DSM versus the decoupling surcharge. The Company demonstrated that the average limited income customer would save \$42.34 versus their billed surcharges of \$14.79, for a net benefit of \$27.55. These investments in energy efficiency create long term net savings to customers. Therefore, as a customer group, the savings from energy efficiency more than offsets the cost of the DSM and decoupling surcharge.

Finally, all of the Company's existing conservation programs for residential customers are available for limited income customers.

- 13) *Impact on Utility Incentives.* Does the recovery of lost margin from conservation provide an incentive for the utility to control costs? What is the incentive to minimize purchased gas adjustment (PGA) costs (within some risk level) if the utility is compensated for any decline in sales from conservation?

Avista's Response:

Incentives, lost margin recovery, or other mechanisms play no role in the Company's responsibility to control costs. It is our responsibility to provide safe and reliable service to our customers in a prudent and efficient manner.

The Company does not financially benefit from changes in the cost of the natural gas commodity. (Avista provides natural gas commodity to customers at cost). The Company only benefits from its investment in facilities used to deliver natural gas to its customers. Avista would be seeking lost

margin recovery, not lost revenue recovery. In regards to the purchase of the natural gas commodity, Avista actively works to keep natural gas prices as low as possible for our customers by mitigating volatility through diversification. This is completed through the use of storage, hedging (short-term and long-term), and index purchases. Further, these transactions are completed over various delivery periods and at several supply basins.

Relationship of Incentives to Conservation Mandates

- 14) *Impact of Conservation Mandate in I-937.* In light of the legal requirement for an electric utility to pursue all available conservation that is cost-effective, reliable and feasible under I-937, is it appropriate to provide an incentive to electric utilities for conservation?

Avista's Response:

It is appropriate to provide for recovery of all costs, including fixed cost recovery and a return component. These are not incentives. These should be provided with or without the mandate specified in I-937. Any incentive should be calculated based on savings in excess of that required by law.

- 14.5) *State greenhouse gas emission reduction goal (70.235.020).* How would removing the linkage between the number of kilowatt hours sold and financial returns for utilities impact the state's ability to meet its statutory greenhouse (GHG) emission reduction limits (RCW 70.235.020)?

Avista's Response:

Conservation is a key element to any strategy for reducing greenhouse gas emissions. Removing the linkage between the number of kilowatt hours sold from the financial returns for utilities would remove the disincentive for the promotion of conservation. With more conservation resulting, the State would be better able to meet its statutory requirements due to the delay or elimination of new generating resources.

- 15) *Incentives to Exceed I-937 Targets.* Under the EIA, the Commission may consider providing positive incentives for an investor-owned utility to exceed the conservation targets established in

RCW 19.285.040. Do ratepayers benefit from encouraging the utility to pursue conservation that is not cost-effective and therefore beyond its target?

Avista's Response:

Avista does not support acquiring non-cost-effective energy efficiency but for special situations. The special situations include testing pilot programs or acquisition of what would otherwise be a "lost opportunity" to gain other savings for a net benefit. Avista does support the consideration of incentives for cost-effective resource acquisition beyond that required by I-937. The achievement of exceeding targets with an inclusion of an incentive (in addition to full cost recovery) would benefit customers if the total cost is lower than alternative resources.

- 16) *Impact of Disincentive.* As investor-owned electric utilities currently acquire more than their share of the Northwest Power and Conservation Council's assessment of conservation potential, does a disincentive to encourage conservation actually exist?

Avista's Response:

The potential exists for a disincentive to over-achieve a Company's two-year target. This is a "potential" disincentive because it is not clear how this will play out. A hypothetical example will best illustrate this. If a utility acquires 150% of its first two year target, no incentive or benefit results. But in the next two year period, if the utility achieves only 75% of its two year goal, then the utility could be penalized \$50/MWh for not meeting its current period goals. This is because there is no "carry-over" of the prior period's excess achievement.

However, reducing the second two-year period goal is, by definition, very difficult if not impossible due to timing. The Commission has required Avista to file future two year targets in November, or two months prior to the beginning of the next two year period. Meanwhile, disproportionate energy efficiency savings occur in the last two months of the year are not available for reporting for one or two more months. Thus there is a timing issue about appropriately calculating the next two year period's targets to properly account for over/under achievement of prior periods.

- 17) *Natural Gas Planning.* Does the lowest cost mix of resources described in WAC 480-90-238(2)(a)-(b) (natural gas integrated resource planning) require a gas utility to pursue all cost-effective conservation, i.e., conservation that has costs equal to or less than supply side resources?

Avista's Response:

Yes, the referenced WAC does require that the utility pursue all cost-effective conservation. However, it is recognized that the efficiency measures being pursued are not within the full and complete control of the utility but are rather owned by the customer whom the utility has the obligation to serve. Acquisition of 100% of the cost-effective resource potential is realistically impossible given the tools and authority available to the utility. A successful utility program can and generally will result in achieving a higher proportion of this potential than less-aggressive or less-innovative programs. Conservation incentives, not to be confused with fixed-cost recovery, are one effective approach to rewarding and encouraging this success.

Evaluation, Measurement and Verification

- 18) *Use Per Customer as a Metric.* Is use-per-customer for individual rate classes a useful metric for identifying conservation effects?

Avista's Response:

Yes. Applying use-per-customer as a metric for measuring energy efficiency results would provide the opportunity to capture energy efficiency related to programmatic and non-programmatic efforts. However, it is important to bear in mind that factors other than energy efficiency can affect use per customer.

- 19) *Load Forecasting.* Load forecasting is a key input for calculating conservation effects. How can load forecasting become more reliable? How does conservation get accurately incorporated into a company's load forecast?

Avista's Response:

While the Company believes that its load forecasting is reliable, it should be noted that its reliability can be affected largely by uncontrollable factors such as monthly weather fluctuations, the general economic cycle and other factors such as vehicle electrification projections. In our load forecast, the Company makes estimates of the weather impacts and adjusts historical sales to all weather sensitive customer groups to determine a weather adjusted trend in loads. Because Avista's Integrated Resource Plan (IRP) is updated every two years, the Company has a natural true-up cycle regarding load forecasting built into the computations.

In addition, each year Avista updates its economic forecasts which are purchased from Global Insight, the national economic consulting firm used by the State of Washington for revenue forecasting. In the last two years, Global Insight has been one of the top economic forecasting firms predicting the impact and duration of the present recession.

As for how conservation is accurately incorporated into the Company's load forecast, conservation is always included in the Company's load forecast. Existing conservation program impacts are included as load reductions.

- 20) *Methods for EM&V.* Should the Commission establish a method, or general guidelines for an evaluation, measurement and verification (EM&V) methodology?
- a) What role should a third party evaluator of EM&V play?
 - b) Are EM&V methods accurate enough to use the history of individual customer usage as the basis for determining the payments in an incentive mechanism?
 - c) What role should the Regional Technical Forum play in EM&V issues?

Avista's Response:

- a. Sufficient third party evaluation should occur such that a utility's EM&V results be reviewed for affirmation.
- b. Bill verification is one tool for determining energy efficiency savings but should not be the primary and/or only tool. Avista will have an EM&V plan filed with the Commission this fall

that should provide the basis for additional “comfort” that its claimed savings are reasonably accurate. Sufficient third party review will be provided.

- c. Peer-recognized industry standards are important. The fact that the RTF provides standards and measurements is valuable. Avista hopes that the RTF will be front and center with EM&V issues and supports its processes, findings and results.

- 21) *Impact on Cost-Effectiveness of Conservation Measures.* If lost margin is recovered in rates, should the cost be included in the cost-effectiveness test? How much would the inclusion of those costs decrease the amount of conservation achievable under the cost-effective threshold?

Avista’s Response:

Inasmuch as lost margin recovery mechanisms reflect the recovery of Commission approved fixed costs, they should not influence the evaluation of DSM program cost-effectiveness.

Relationship of Conservation Incentives to Utility Return on Equity

- 22) *Effect of Incentive Mechanism on Allowed Return on Equity.* Should adoption of an incentive or lost margin/decoupling mechanism require a downward adjustment in the utility’s return on equity?

Avista’s Response:

No. The Company’s current Natural Gas Decoupling Mechanism, for example, captures only the change in residential customers’ usage resulting from natural gas energy efficiency and other factors on a weather-normalized basis. It does not capture: 1) changes in large customer usage often resulting from changes in business or economic conditions, and 2) changes in customer usage resulting from abnormal weather. The Mechanism simply provides recovery of fixed costs that were previously approved by the Commission in a prior general rate case for recovery from customers. To the extent those fixed costs increase, or escalate, over time, the Mechanism does not provide recovery of that change in costs. The Company continues to bear the risk of changes in those costs between general rate cases.

23) *Incentive Rate of Return.* Should a utility's rate of return be increased for sponsoring and administering conservation programs? If so, please explain. Should a utility earn a return on monies collected from ratepayers to fund its conservation programs? If so, please explain. Would the amount of energy efficiency offered by the utility increase under either of the above circumstances?

Avista's Response:

A utility should have the option of requesting to expense or capitalize its energy efficiency programs. Ultimately, all monies to fund all utility operations are collected from ratepayers. This collection from customers includes monies to pay for debt service and return. Our response to Question #3 describes the impact on our energy efficiency programs of full cost recovery.

Avista looks forward to participating in the upcoming workshop. If you have any questions regarding these issues, please contact Linda Gervais, Manager, Regulatory Policy at 509-495-4975 or myself at 509-495-4267.

Sincerely,



Kelly Norwood
Vice President, State and Federal Regulation
Avista Corporation