

Exhibit No. ___ CT (KHB-1TC)
Dockets UE-120436, et al.
Witness: Kathryn H. Breda
REDACTED VERSION

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

AVISTA CORPORATION, d/b/a
AVISTA UTILITIES,

Respondent.

DOCKETS UE-120436/UG-120437
(consolidated)

WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION,

Complainant,

v.

AVISTA CORPORATION d/b/a AVISTA
UTILITIES,

Respondent.

DOCKETS UE-110876/UG-110877
(consolidated)

TESTIMONY OF

Kathryn H. Breda

STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

*Attrition Study, Overall Electric and Natural Gas Revenue Requirement, Deferred
Maintenance, Allocations, and Renewable Energy Credit Revenues*

September 19, 2012

CONFIDENTIAL PER PROTECTIVE ORDER IN DOCKETS UE-120436 ET AL.

TABLE OF CONTENTS

I. INTRODUCTION 1

II. SCOPE AND SUMMARY OF TESTIMONY 2

III. STAFF’S OVERALL ELECTRIC AND NATURAL GAS REVENUE
REQUIREMENT ANALYSIS 4

IV. CONTESTED ADJUSTMENTS 5

 A. Staff Adjustment 1.04, Electric and Natural Gas - Federal Income
 Tax Correction 5

 B. Staff Adjustment 2.16, Electric - Colstrip and Coyote Springs 2
 Maintenance 6

 C. Staff Adjustments 2.18, Electric, and 2.16, Natural Gas –
 Booz & Company Contract 6

 D. Adjustment 3.00, Electric - Pro Forma Power Supply 7

 E. Adjustment 3.07, Electric Adjustment 3.06, Natural Gas –
 Restating 2011 Capital; Adjustment 4.00, Electric and Natural Gas –
 Planned Capital Additions 2012; Adjustment 4.01, Electric and
 Natural Gas - Planned Capital Additions 2013 AMA; Adjustment 4.02,
 Electric – DSM; Adjustment 4.03, Electric – Other, Adjustment 4.06
 Electric and 4.03 Natural Gas - O&M Offsets 8

 F. Staff Adjustment 3.08, Electric - Noxon Rapids Unit 4 Runner Upgrade 9

 G. Staff Adjustment 3.09, Electric - Pullman Smart Grid Adjustment 10

 H. Adjustment 4.04, Electric - Retail Revenue Credit 10

V. DEFERRED MAINTENANCE 10

VI. ALLOCATIONS 16

VII. RENEWABLE ENERGY CREDITS REVENUE 17

VIII. ATTRITION ANALYSIS 19

 A. Background..... 19

B.	Scenarios Explaining How Attrition Works	21
C.	How an Attrition Analysis is Performed; Complicating Factors	24
D.	Staff's Attrition Study	26
1.	Summary	26
2.	Staff's General Approach to Estimating Attrition	27
3.	Evaluating Changes in Revenues – Electric Operations	27
4.	Evaluating Changes in Revenues – Gas Operations	30
5.	Evaluating Changes in Expenses	32
6.	Evaluating Changes in Rate Base	35
7.	Results of Staff's Attrition Study	36

List of Exhibits

- Exhibit No. ___ (KHB-2), Overall Electric and Natural Gas Revenue Requirement
- Exhibit No. ___ (KHB-3), Staff Adjustment 1.04, Electric and Gas - Federal Income Tax Correction
- Exhibit No. ___ (KHB-4), Adjustment 2.16, Electric - Colstrip and Coyote Springs 2 Maintenance
- Exhibit No. ___ (KHB-5), Staff Adjustment 2.18, Electric and Adjustment 2.16, Natural Gas, Booz & Company Contract
- Exhibit No. ___ (KHB-6), Adjustment 3.00, Electric - Pro Forma Power Supply
- Exhibit No. ___ (KHB-7), Staff Adjustment 3.08, Electric - Noxon Rapids Unit 4 Runner Upgrade
- Exhibit No. ___ (KHB-8), Staff Adjustment 3.09, Electric - Pullman Smart Grid Adjustment
- Exhibit No. ___ (KHB-9C), Electric Attrition Study
- Exhibit No. ___ (KHB-10C), Natural Gas Attrition Study

1 I. INTRODUCTION

2
3 Q. Please state your name and business address.

4 A. My name is Kathryn H. Breda. My business address is The Richard Hemstad
5 Building, 1300 S. Evergreen Park Drive S.W., P.O. Box 47250, Olympia, WA
6 98504. My email address is kbreda@utc.wa.gov.

7
8 Q. By whom are you employed and in what capacity?

9 A. I am employed by the Washington Utilities and Transportation Commission
10 (Commission) as a Regulatory Analyst.

11
12 Q. How long have you been employed by the Commission?

13 A. I have been employed by the Commission since 2008.

14
15 Q. Would you please state your educational and professional background?

16 A. I graduated from the University of Washington in 1980, receiving a Bachelor of Arts
17 in Business Administration with a major in Accounting. I am a licensed Certified
18 Public Accountant in the State of Washington.

19 My responsibilities at the Commission generally comprise financial,
20 accounting and other analyses in general rate cases, accounting petitions, other tariff
21 filings, and compliance filings. I testified in Dockets UE-111190, UE-100749 and
22 UE-090704, and participated in Staff's review of Dockets UE-110876/UG-110877,

1 UE-100467/UG-100468, UE-090134/UG-090134, UE-090205, UE-080220 and UG-
2 080546.

3 Prior to my employment with the Commission, I held various corporate
4 accounting and regulatory management positions from 1980 through 2000 with
5 Qwest Communication in Seattle and Pacific Gas and Electric Company in San
6 Francisco.

7

8 **II. SCOPE AND SUMMARY OF TESTIMONY**

9

10 **Q. What is the purpose of your testimony?**

11 A. The primary purpose of my testimony is to present Staff's recommendation
12 regarding attrition. I have prepared an attrition study and discuss the results in
13 Section VIII.

14 I also address the disposition of Avista Colstrip and Coyote Springs 2
15 deferred maintenance mechanism (Section V), future considerations for allocations
16 (Section VI), and proper treatment of revenues from sales of renewable energy
17 credits (RECs) (Section VII).

18 In Section IV, I present Staff's recommendation for the following
19 adjustments:

- 20 1) Staff Adjustment 1.04, Electric and Natural Gas - Federal Income Tax
- 21 Correction
- 22 2) Adjustment 2.16, Electric - Colstrip and Coyote Springs 2
- 23 Maintenance
- 24 3) Staff Adjustment 2.18, Electric and Adjustment 2.16, Natural Gas -
- 25 Booz & Company Contract
- 26 4) Adjustment 3.00, Electric - Pro Forma Power Supply

- 1 5) Adjustment 3.07, Electric and Adjustment 3.06, Natural Gas -
2 Restating 2011 Capital
- 3 6) Adjustment 4.00, Electric and Natural Gas - Planned Capital
4 Additions 2012
- 5 7) Adjustment 4.01, Electric and Natural Gas - Planned Capital
6 Additions 2013 AMA
- 7 8) Adjustment 4.02, Electric - DSM, Adjustment 4.03, Electric - Other
- 8 9) Adjustment 4.06, Electric and Adjustment 4.03, Natural Gas - O&M
9 Offsets
- 10 10) Staff Adjustment 3.08, Electric - Noxon Rapids Unit 4 Runner
11 Upgrade
- 12 11) Staff Adjustment 3.09, Electric - Pullman Smart Grid Adjustment,
13 and
- 14 12) Adjustment 4.04, Electric - Retail Revenue Credit
15

16 **Q. Please summarize your recommendations.**

17 A. I recommend the Commission accept Staff's case on the above listed twelve
18 adjustments, and:

- 19 • Accept Staff's attrition study and the resulting attrition-adjusted revenue
20 requirement.
- 21 • Discontinue Avista's deferred maintenance mechanism for Colstrip and
22 Coyote Springs 2 after 2012.
- 23 • Order Avista in its next general rate case to provide full justification for the
24 allocation methodologies it uses and to fully support those factors the
25 Company deems appropriate.
- 26 • Order Avista to track REC revenues separately within the Company's energy
27 recovery mechanism (ERM), not subject to the ERM sharing bands.
28

1 test period base case. Staff's attrition-adjusted revenue requirement uses projections
2 to 2013, the rate year. I discuss attrition further in Section VII of my testimony.

3
4 **IV. CONTESTED ADJUSTMENTS**

5
6 **A. Staff Adjustment 1.04, Electric and Natural Gas -Federal Income Tax**
7 **Correction**

8
9 **Q. Please explain Staff's Adjustment 1.04, Federal Income Tax Correction.**

10 A. Adjustment 1.04 for both Electric and Natural Gas Service is a Staff adjustment,
11 which corrects errors to federal income tax expense Avista included in the
12 Washington results of operations. Through discovery, Avista corrected
13 inconsistencies between the actual federal income tax calculation and what was
14 included in the Company's unadjusted results. The corrections involved an
15 adjustment for the allowance for funds used during construction (AFUDC), a
16 correction to Section 199 Manufacturing Deductions and other adjustments or
17 corrections.

18 Adjustment 1.04, Electric increases Washington net operating income by
19 \$1,826,000 and decreases the electric revenue requirement by \$2,941,000.

20 Adjustment 1.04, Natural Gas increases Washington net operating income by
21 \$20,000 and decreases the natural gas revenue requirement by \$32,000.⁵

22

⁵ Breda, Exhibit No. ____ (KHB-3) details this adjustment.

1 **B. Staff Adjustment 2.16, Electric - Colstrip and Coyote Springs 2**
2 **Maintenance**
3

4 **Q. Please explain Staff Adjustment 2.16, Colstrip and Coyote Springs 2**
5 **Maintenance.**

6 A. Staff's Adjustment 2.16 reflects updated information on Colstrip and Coyote Springs
7 2 maintenance expense for 2012. Avista provided this updated information through
8 discovery. This adjustment decreases electric net operating income \$709,000 and
9 increases revenue requirement by \$1,142,000.⁶

10 These deferrals are the result of the Settlement Stipulation the Commission
11 approved in Avista's last rate case, Dockets UE-100876 and UG-100877.⁷ Overall,
12 Staff recommends the Commission discontinue this deferral after 2012. I discuss the
13 deferral mechanism and Staff's recommendation more fully in Section V below.

14
15 **C. Staff Adjustments 2.18, Electric, and 2.16, Natural Gas - Booz &**
16 **Company Contract**
17
18

19 **Q. Please explain this Staff adjustment for the Booz and Company Contract.**

20 A. Booz and Company is a consultant the Company retained to look at efficiencies and
21 implement the "Performance Excellence Initiative". In total, Avista paid Booz and
22 Company \$5,691,521⁸ for this contract.

⁶ Breda, Exhibit No. ____ (KHB-4) details this adjustment.

⁷ *Utilities and Transp. Comm'n v. Avista Corp.*, Dockets UE-110876 and Docket UG-110877, Settlement Stipulation (September 30, 2011), at 7-8.

⁸ Avista response to Public Counsel Data Request 305, Attachment A.

1 Work under this contract will be complete in 2012. Therefore, this contract
2 does not represent an on-going expense, and Staff removes it as non-recurring.

3

4 **Q. Please identify the effect of this adjustment on revenue requirement.**

5 A. Staff Adjustment 2.18 increases Washington net operating income for electric
6 operations by \$734,000, thereby reducing the revenue requirement by \$1,182,000.
7 Staff Adjustment 2.16 increases Washington net operating income for natural gas
8 operations \$200,000, with a corresponding decrease in revenue requirement of
9 \$322,000.⁹

10

11 **Q. Did Avista adjust the test period for the Booz & Company contract?**

12 A. Not in this rate case. However, in Avista's direct evidence in its prior rate case,
13 Dockets UE-110876 and UG-110877, Avista removed this contract¹⁰. Staff's
14 adjustments in this case are consistent with that prior treatment by Avista.

15

16 **D. Adjustment 3.00, Electric - Pro Forma Power Supply**

17

18 **Q. Please explain Adjustment 3.00, Electric - Pro Forma Power Supply.**

19 A. This adjustment reflects a revised electric power supply calculation. Staff witness
20 Alan Buckley explains this adjustment.¹¹ Adjustment 3.00 decreases Washington net

⁹ Breda, Exhibit No. ___ (KHB-5) details this adjustment.

¹⁰ Avista response to Public Counsel Data Request 305.

¹¹ Buckley, Exhibit No. ___ (APB-1CT), at 5, line 1 to 9, line 17.

1 operating income by \$1,913,000 and increases the electric revenue requirement by
2 \$3,081,000.¹²

3
4 **E. Adjustment 3.07, Electric and Adjustment 3.06, Natural Gas - Restating**
5 **2011 Capital; Adjustment 4.00, Electric and Natural Gas - Planned**
6 **Capital Additions 2012; Adjustment 4.01, Electric and Natural Gas -**
7 **Planned Capital Additions 2013 AMA; Adjustment 4.02, Electric - DSM;**
8 **Adjustment 4.03, Electric – Other, Adjustment 4.06 Electric and 4.03**
9 **Natural Gas – O&M Offsets**
10

11 **Q. Please explain why you have grouped Adjustments 3.06, 3.07, 4.00, 4.01, 4.02,**
12 **4.03, and 4.06.**

13 A. Each of these adjustments is related to the issue of attrition. Because Staff addresses
14 attrition through a separate attrition study, these adjustments are duplicative and
15 therefore Staff does not separately address them.

16 Avista presents Adjustments 4.00 through 4.03 as attrition-related
17 adjustments. However, Avista's Adjustments 3.06 and 3.07 are also attrition-related
18 because they reflect rate base on an end-of-period basis, rather than an average of the
19 monthly averages basis.

20 The Commission has recognized that average of monthly averages rate base
21 "is most favored", but year-end rate base is a tool the Commission can use to address
22 attrition.¹³ Because both Staff's and the Company's attrition studies consider plant
23 additions through the rate year, Adjustments 3.06 and 3.07 are duplicative.

¹² Breda, Exhibit No. ____ (KHB-6) details this adjustment.

¹³ *Utilities and Transp. Comm'n v. Wash. Natural Gas Co.*, Cause U-80-111, Third Supplemental Order (September 24, 1981), at 6. The Commission listed four conditions under which year-end rate based could be used: "a) Abnormal growth in plant; b) Inflation and/or attrition c) As a means to mitigate regulatory lag d)

1 Similarly, Avista's adjustments 4.06, Electric and 4.03, Natural Gas, O&M
2 Offsets, include projected reductions in operations and maintenance expense related
3 to capital additions through the rate year 2013. Staff removes these adjustments as
4 separate items because, again, I consider operations and maintenance expense
5 growth in my attrition study.

6
7 **F. Staff Adjustment 3.08, Electric – Noxon Rapids Unit 4 Runner Upgrade**

8
9 **Q. Please explain Staff Adjustment 3.08, Electric - Noxon Rapids Unit 4 Runner**
10 **Upgrade.**

11 A. Avista is making upgrades to its hydroelectric facility at Noxon. Mr. Buckley,
12 Staff's power supply witness, includes the impact of these upgrades on power supply
13 costs. Therefore, it is appropriate to reflect the impact of the upgrades on rate base.
14 Staff's Adjustment 3.08 includes the plant additions related to the production assets
15 Staff considered in the dispatch of power in the rate year. Staff witness Alan
16 Buckley describes this adjustment in detail.¹⁴

17 Staff Adjustment 3.08 decreases Washington net operating income by
18 \$15,000 and increases net rate base \$5,173,000, thereby increasing the electric
19 revenue requirement by \$625,000.¹⁵

20

Failure of utility to earn its authorized rate of return over a historical period." Staff considers each of these conditions as indications of attrition.

¹⁴ Buckley, Exhibit No. ____ (APB-1CT) at 9, line 19 to 13, line 2.

¹⁵ Breda, Exhibit No. ____ (KHB-7) details this adjustment.

1 **G. Staff Adjustment 3.09, Electric - Pullman Smart Grid Adjustment**

2
3 **Q. Please explain Staff Adjustment 3.09, Electric - Pullman Smart Grid**
4 **Adjustment.**

5 A. This adjustment relates to Staff's recommended disallowance of certain smart grid-
6 related investment from rate base. Staff witness Mr. Nightingale explains this
7 adjustment.¹⁶

8 Staff Adjustment 3.09 decreases Washington net operating income by \$9,000
9 and net rate base \$827,000, thereby reducing the revenue requirement by \$82,000.¹⁷

10
11 **H. Staff Adjustment 4.04, Electric - Retail Revenue Credit**

12
13 **Q. Please explain Staff Adjustment 4.04, Electric - Retail Revenue Credit.**

14 A. As Staff witness Mr. Buckley explains, because Staff has accepted the Company's
15 proposed change to the way the retail revenue credit is calculated within the Energy
16 Recovery Mechanism (ERM), Adjustment 4.04 is moot.¹⁸ Therefore, I remove it.

17
18 **V. DEFERRED MAINTENANCE**

19
20 **Q. Please provide the background for Avista's Adjustment 2.16, Deferred**
21 **Maintenance for Colstrip and Coyote Springs 2.**

¹⁶ Nightingale, Exhibit No. ____ (DN-1CT), at 31, line 12 to 55, line 11.

¹⁷ Breda, Exhibit No. ____ (KHB-8) details this adjustment.

¹⁸ Buckley, Exhibit No. ____ (APB-1CT), at 24, line 17 to 25, line 7.

1 A. Avista's Adjustment 2.16 applies a deferral mechanism described in the Settlement
2 Stipulation the Commission approved in Avista's last general rate case¹⁹. Under that
3 mechanism, Avista established a regulatory asset through a deferral of certain
4 Coyote Springs 2 and Colstrip maintenance expenses.

5 The amounts to be deferred depend on a moving baseline level of expense.
6 The Settlement Stipulation also specified that the future deferrals or pre-approved
7 regulatory assets would be amortized over a four year period and would not accrue
8 carrying charges or otherwise earn a return. Essentially, this mechanism allows for
9 the automatic deferral of certain maintenance costs over a threshold level.

10 According to the Settlement Stipulation, the deferral will occur annually and
11 amortized beginning January of the following year.²⁰ Avista witness Elizabeth
12 Andrews confirms this in her direct testimony.²¹

13
14 **Q. In approving the Settlement Stipulation, did the Commission express any**
15 **reservations about this deferral mechanism?**

16 A. Yes. In its order, the Commission characterized the mechanism as "provisional" and
17 subject to review again in this case:

18 We approve the deferral mechanism as a part of the overall Settlement
19 package, but only because it appears to reduce immediate costs to ratepayers
20 and it will only operate provisionally. The fact that Avista will not collect a
21 return on the deferred amount, as well as the reasonableness of a smoothing
22 of only maintenance expenses above the baseline, allow us to conclude that
23

¹⁹ *Utilities and Transp. Comm'n v. Avista Corp.*, Dockets UE-110876 and Docket UG-110877, Settlement Stipulation (September 30, 2011), at 7-8.

²⁰ *Id.* at 8.

²¹ Andrews, Exhibit No. ____ (EMA-1T), at 70, lines 24-25.

1 approval on a provisional basis is appropriate. The Company has also
2 indicated that we can revisit the mechanism at a future time without undue
3 administrative difficulty.²² By providing this limited approval of the
4 mechanism, *we caution the parties and, especially Avista, that we will revisit*
5 *this issue on an expanded basis and in a future proceeding*, possibly on an
6 industry-wide basis so that other public utilities affected by the expenses at
7 these units might also participate. *If this proceeding has not commenced*
8 *prior to Avista's next rate filing, we expect the Company to include a*
9 *proposal for such a tracker in that initial filing so that we can evaluate*
10 *whether or not to terminate the provisional mechanism.*²³ (Emphasis
11 added, footnotes included).
12

13 **Q. Since the Commission issued that order, has the Commission further clarified**
14 **its views regarding the deferral and creation of regulatory assets for**
15 **maintenance expense?**

16 A. Yes. In its recent order in the Puget Sound Energy rate case, Dockets UE-111048
17 and UG-111049, the Commission stated:

18 PSE also fails to establish any reason to allow automatic deferral of new
19 major maintenance expense that it incurs between rate cases. The Company
20 can protect itself from any arguable inability to recover such costs by filing
21 an appropriate accounting petition that, if approved, will relate back to the
22 date of filing in terms of costs allowed for recovery on a prospective basis.²⁴
23

²² COMMISSIONER JONES: If the Commission were to approve this on a pilot basis, a year or so, and then we – since you're filing about every 18 months, we have a chance to review these things frequently. And in the next case we were to reject it, say it's really not working the way it is, wouldn't that create an issue on for – the company on a[n] earnings perspective?

MR. NORWOOD: If the Commission were to choose to not approve it at some point in the future, it would be important that the opportunity would be there to recover the dollars that are already deferred. And so if there's an understanding that what's already been deferred would be amortized, then that would not create an accounting issue.

TR 190:20-191:1; 191:12-18 in Dockets UE-110876 and UG-110877.

²³ *Utilities and Transp. Comm'n v. Avista Corp.*, Dockets UE-110876 and UG-110877, Order 06 ((December 16, 2011), at 15-16, ¶¶ 35-37.

²⁴ *Utilities and Transp. Comm'n v. Puget Sound Energy, Inc.* Dockets UE-111048 and UG-111049, Order 08 (May 7, 2012), at 112, ¶ 321 (see full discussion at 110-13, ¶¶ 315-21.

1 **Q. Is Avista's deferral mechanism of Colstrip and Coyote Springs 2 maintenance**
2 **an "automatic" deferral mechanism?**

3 A. Yes. An automatic deferral mechanism is one that defers costs without prior review
4 or approval by the Commission. Avista's deferral mechanism meets this definition
5 because Avista defers Colstrip and Coyote Springs 2 maintenance currently, subject
6 to later review.

7
8 **Q. What amounts has Avista deferred for maintenance of Coyote Springs 2 and**
9 **Colstrip?**

10 A. For 2011, Avista's expenses were \$516,251²⁵ less than the threshold level. This is
11 deferred a credit balance which will reduce future expenses.

12
13 **Q. What deferral amounts does Avista reflect for 2012 in its Adjustment 2.16?**

14 A. Avista's adjustment anticipates that the Company will incur \$4,880,262²⁶ more than
15 the 2012 threshold. Avista would amortize this debit balance over the subsequent
16 four years. Avista's Adjustment 2.16 increases maintenance expense by \$1,091,000
17 for this anticipated amortization.²⁷

18
19 **Q. Is maintenance expense an unusual expense for an electric utility company?**

20 A. No. Maintenance expense is an ongoing, substantial portion of an electric utility
21 company's operating expenses. As with any ongoing expense, maintenance expense

²⁵ Avista response to Public Counsel Data Request 93.

²⁶ Id.

²⁷ Breda, Exhibit No. ____ (KHB-4) details this adjustment.

1 may fluctuate over time, and therefore an adjustment may be included in the test
2 period to “normalize” the expense. This would include considering an average
3 expense level over time.

4 This is how accounts are commonly treated, such as injuries and damages
5 expense,²⁸ which, for ratemaking purposes, is based on a six year average of
6 expense.

7
8 **Q. Is such a normalization technique always appropriate?**

9 A. No. Normalization is appropriate only if the utility can prove the test period level of
10 expense is unrepresentative. For example, in its recent order in the PSE rate case,
11 Dockets UE-111048 and UG-111049, the Commission used the current test period
12 expense for maintenance rather than a five-year average.²⁹

13
14 **Q. What is Avista’s test period 2011 maintenance expense compared to prior**
15 **periods?**

²⁸ Andrews, Exhibit No. ____ (EMA-1T), at 20, lines 12-18, and 50, lines 3-8. Electric Adjustment 2.04 and Gas Adjustment 2.05.

²⁹ *Utilities and Transp. Comm’n v. Puget Sound Energy, Inc.* Dockets UE-1111048 and UG-111049, Order 08 (May 7, 2012), at 74-77, ¶¶ 209-18. Especially ¶ 217: “*Commission Determination:* In PSE’s most recently completed general rate case, the Commission rejected the proposed use of a five-year average for this category of expenses stating: “O&M is an ongoing expense and there is no evidence that the more recent historic data upon which PSE would have us rely requires any normalizing adjustments.”²⁹ We find on the basis of the record here that the same is true today. Considering PSE’s changing use of its fleet of thermal production facilities, as described by Mr. Gould, we are not surprised that maintenance costs are trending upward. As PSE’s use of intermittent renewable resources such as wind farms continues to increase in response to state-mandated RPS, the pattern of more frequent start-ups, shorter run times, and total run times at thermal facilities that facilitate wind integration may lead to a continuing trend of increasing O&M costs. Absent evidence of a change in this regard, it is reasonable to continue our reliance on the more recent test year data rather than averages of historic data.”

1 A. Avista's 2011 maintenance expense in total is higher than the past two years for both
2 electric and natural gas service, as shown by the following figures:³⁰

\$000	Year		
	2009	2010	2011
Electric Maintenance	34,085	31,344	39,509
Gas Maintenance	7,316	7,963	8,701

3
4 It is important to note that this is all maintenance, not just Colstrip and Coyote
5 Springs 2 contract maintenance.

6

7 **Q. What has Staff included in the test period for maintenance expense?**

8 A. Staff includes the 2011 test period maintenance expense plus the anticipated
9 amortization of the deferred maintenance. In my attrition study, I escalate only the
10 2011 test period amount to determine the rate year level.

11

12 **Q. What is Staff's recommendation for the deferred maintenance mechanism?**

13 A. Staff recommends the Commission discontinue the mechanism beginning January 1,
14 2013, but allow Avista to amortize the deferred 2011 and 2012 major maintenance
15 expenses.

16 First, Staff recommends the Commission discontinue this deferral mechanism
17 because it is not consistent with the Commission's recent decision in the PSE rate
18 case, which I discussed earlier.

19 Second, Staff believes that deferral mechanisms should only be for truly
20 extraordinary circumstances, and only when a normalization technique or a pro

³⁰ This chart summarizes information provided in Avista's response to Public Counsel Data Request 131.

1 forma analysis is not practical or appropriate for policy reasons. Facility
2 maintenance is not extraordinary, and a reasonable level can be determined for rate
3 making purposes without the necessity of a deferral.

4 Nonetheless, to properly “wind down” the mechanism, Staff recommends the
5 Commission allow the mechanism to continue through December 2012, because
6 Avista incurred the majority of this cost through the current period. The
7 Commission should order Avista to true-up the 2012 expenses to actual when
8 implementing the amortization. The Commission should allow Avista to amortize
9 the deferred costs over four years. Staff Adjustment 2.16 reflects this treatment.³¹

11 VI. ALLOCATIONS

12
13 **Q. In this case, does Staff take issue with how the Company allocates costs between**
14 **jurisdictions and between services?**

15 A. No, with one exception: Staff Witness Ms. Huang adjusts the allocation of certain
16 officer and other employee salaries to non-regulated operations of Avista
17 subsidiaries.

18
19 **Q. Does Staff have any concerns about the allocation factors Avista uses?**

20 A. Yes. Avista’s current allocation methods have been in place since the early 1990s,
21 with only minor modifications over the years. Staff recommends the Commission
22 order Avista in its next general rate case to provide full justification for the allocation

³¹ Breda, Exhibit No. ____ (KHB-4).

1 methodologies it uses and to fully support those factors the Company deems
2 appropriate.

3
4 **VII. RENEWABLE ENERGY CREDITS REVENUE**

5
6 **Q. What are RECs and REC revenues?**

7 A. RECs are intangible assets that represent proof that 1 megawatt-hour of electricity
8 was generated from an eligible renewable energy resource. RECs represent the right
9 to claim the environmental or other non-power attributes of the power produced from
10 renewable energy facilities and can be “unbundled” and bought and sold separately
11 from the underlying physical electricity associated with the generating renewable
12 resource. REC revenues are the revenues a company receives from the sale of RECs.

13
14 **Q. Please summarize Commission policy regarding the proper regulatory
15 treatment of REC revenues.**

16 A. The Commission’s policy is that “all REC revenues should be returned to the
17 ratepayers who pay rates to cover all the costs of the related resource...”.³² In
18 PacifiCorp Docket UE-100749, the Commission confirmed this fundamental
19 determination³³.

20

³² *Utilities and Transp. Comm’n v. Puget Sound Energy Co.*, Docket UE-070725, Order 03 (May 20, 2010), at 28, ¶ 68.

³³ *Utilities and Transp. Comm’n v. PacifiCorp d/b/a Pacific Power & Light Co.*, Docket UE-100749, Order 06 (March 25, 2011), at 71, ¶ 200.

1 **Q. How does the ERM treat REC revenues?**

2 A. The ERM tracks REC sales revenues above a baseline level, and deferrals, the
3 difference is subject to the ERM sharing bands.³⁴ Sharing is not consistent with the
4 Commission's policy that REC revenues should be returned to the ratepayers in full.

5
6 **Q. How should the Commission return REC revenues to ratepayers?**

7 A. The Commission should apply its policy that Washington ratepayers are entitled to
8 100 percent of a utility's Washington-allocated REC revenues. The Commission
9 should order Avista to implement a separate line item within the ERM³⁵, not subject
10 to the ERM sharing bands in order to return all REC revenues in full to customers.

11 The Commission should further direct Avista to include a rebate of these
12 REC revenues each time an ERM-related rate adjustment is triggered. The
13 Commission can exercise its discretion at that time whether to rebate the REC
14 revenues in full, in part, or to hold the amounts for future rate treatment. During the
15 ERM annual review, the Commission could determine whether a separate trigger for
16 the REC revenues independent of the ERM rate trigger is warranted.

17
18 **Q. Please summarize your recommendations.**

19 A. I recommend the Commission order Avista to create a separate line item within the
20 Company's Energy Recovery Mechanism (ERM) to track separately REC revenues
21 to be available for a credit to customers. Consequently, these REC revenues would

³⁴ A rate adjustment is triggered when the total variation in power supply expense exceeds 10 percent of total revenues.

³⁵ This line item would have a unique deferral account to track REC revenues separately from other ERM deferrals and be subject to the same interest accrual as the ERM deferrals.

1 not be subject to the ERM sharing bands and would accrue interest at the rate
2 authorized in the ERM. The Commission should review this deferral and its
3 disposition during the annual ERM review.

4 5 VIII. ATTRITION ANALYSIS

6 7 A. Background

8 9 Q. What is attrition?

10 A. Attrition refers to the change in the relationship of test period revenues, expenses,
11 rate base and cost of capital that results in an impact on rate year earnings. As the
12 Commission has observed:

13 Attrition is the change in relationships among revenues, expenses, and rate
14 base over time, in which growth in expenses exceeds growth in revenues
15 from factors beyond the company's control.³⁶
16

17 An attrition allowance may be warranted to provide a utility a reasonable
18 opportunity to earn a fair return. The Commission used attrition allowances during
19 periods of high inflation, high capital costs, and high construction costs to serve
20 growing demand.³⁷ Only one of these factors exists today: high construction costs,

³⁶ *Utilities and Transp. Comm'n v. Wash. Natural Gas Co.*, Docket UG-920840, Fourth Supplemental Order (September 27, 1993), at 29.

³⁷ *Utilities and Transp. Comm'n v. Wash. Water Power Co.*, Causes U-82-10 and U-82-11, Second Supplemental Order (December 30, 1982), at 31-33; *Utilities and Transp. Comm'n v. Pacific Power and Light Co.*, Cause U-82-12, Fourth Supplemental Order (February 13, 1983), at 30-31; *Utilities and Transp. Comm'n v. Puget Sound Power and Light Co.*, Cause U-82-38, Third Supplemental Order (July 25, 1983), at 29; *Utilities and Transp. Comm'n v. Wash. Water Power Co.*, Cause U-83-26, Fifth Supplemental Order (January 19, 1984), at 29-30; *Utilities and Transp. Comm'n v. Pacific Power and Light Co.*, Cause 83-33, Second Supplemental Order (February 9, 1984), at 29-30; *Utilities and Transp. Comm'n v. Pacific Power and Light*

1 though with low growth in demand. Inflation and capital costs are low and should
2 not be causes of attrition currently.

3
4 **Q. According to Avista, what are the current circumstances facing the Company?**

5 A. According to Mr. Morris, Avista's Chairman of the Board, President and Chief
6 Executive Officer:

7 A large part of our need for a rate increase is driven by the costs associated
8 with continuing to expand and replace the facilities we use every day to serve
9 our customers. When we remove the old equipment and replace it with new,
10 it results in higher overall costs to serve customers. This was the primary
11 reason for the proposed increase in our last rate increase request and it is
12 expected to continue to cause a need for increased rates in the future.³⁸
13

14 He also refers to increases in expenses of:

15 ...approximately \$72 million over the six-year period from 2005 to 2011....
16 In recent years there has been a significant increase in costly, mandatory
17 requirements on utilities related to, among others things, reliability,
18 environmental compliance, safety, and security. These mandates, together
19 with litigation and other claims related to the ownership and operation of
20 hydroelectric resources, have added, and continue to add, significant costs to
21 run the utility.³⁹
22
23

24 **Q. In the testimony you quoted, Avista focused on the 2005-2011 time period. Did**
25 **Avista omit any significant information relevant to that the period?**

26 A. Yes. Avista failed to mention it has increased rates to cover the expense and capital
27 costs described by the Company. While Avista's current claims may be valid, it is

Co., Cause 84-65, Fourth Supplemental Order (August 2, 1985), at 34-37; *Utilities and Transp. Comm'n v. Puget Sound Power and Light Co.*, Cause U-85-53, Second Supplemental Order (May 16, 1986), at 56-57; and *Utilities and Transp. Comm'n v. Pacific Power and Light Co.*, Cause 86-02, Second Supplemental Order (September 19, 1986), at 32-33.

³⁸ Morris, Exhibit No. ____ (SLM-1T), at 2, lines 5-10.

³⁹ Morris, Exhibit No. ____ (SLM-1T), at 10, line 11 to 11, line 39.

1 misleading to discuss the increases in expenditures without identifying the increases
2 in revenues, or the rate increases the Company received.⁴⁰ Staff witness Mr. Elgin
3 identifies Avista's recent rate increase history.⁴¹

4
5 **B. Scenarios Explaining How Attrition Works**

6
7 **Q. Do varying growth patterns in revenues, expenses, rate base and cost of capital**
8 **always result in attrition or earnings erosion?**

9 A. No. Table 1 below explains this, by showing different changes in relationships of
10 revenue, expenses and rate base between any test and rate year, assuming a constant
11 utility cost of capital of 8.00 percent.

12
13
14 Remainder of page intentionally left blank

15

⁴⁰ This discussion is referring to Mr. Morris's direct testimony, Exhibit No. ___ (SLM-1T), at 9, line 3 to 11, line 39, particularly Illustration 3, and Mr. Norwood's direct testimony, Exhibit No. ___ (KON-1T), at 3, line 6 to 4, line 11.

⁴¹ Elgin, Exhibit No. ___ (KLE-5).

Table 1

	Rate Order	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5
Revenue	\$ 540	\$ 551	\$ 556	\$ 551	\$ 551	\$ 551
Expenses	399	407	407	407	415	403
Taxes	49	50	52	50	48	52
NOI	\$ 92	\$ 93	\$ 97	\$ 93	\$ 88	\$ 96
Rate Base	\$ 1,145	\$ 1,168	\$ 1,214	\$ 1,214	\$ 1,214	\$ 1,179
ROR	8.00%	8.00%	8.00%	7.70%	7.27%	8.15%

Scenario 1 reflects a rate year during which revenue, expenses and rate base all grew at a rate of two percent. The result is that the utility earned the 8.00 percent rate of return (ROR). The relationships between revenues, expenses and rate base were maintained and no earnings erosion (attrition) resulted.

Under Scenario 2, the utility did not maintain the rate case relationships between revenues, expenses and rate base, yet still earned an 8.00 percent ROR. In this scenario, rate year revenues grew three percent, expenses grew two percent and rate base grew six percent. This demonstrates that even with rate base increasing more rapidly than other elements, there is no negative impact to earnings due to attrition. It also shows that growth in rate base does not require proportional growth in revenue to avoid attrition.

In Scenario 3, rate year revenues grew two percent, expenses increased two percent and rate base increased six percent. The result is a 7.70 percent ROR, which reflects erosion in earnings due to attrition.

1 Scenario 4 reflects a two percent growth in rate year revenues, a four percent
2 growth in expenses, and a six percent growth in rate base. The resulting 7.27 percent
3 ROR reflects the largest earnings erosion, or attrition, in these examples.

4 Scenario 5 is an example of attrition working in the utility's favor. Rate year
5 revenue grew 2 percent, expenses grew one percent and rate base grew three percent.
6 The result is a ROR of 8.15 percent. This is an example of negative attrition.

7
8 **Q. What critical element of attrition does this table confirm?**

9 A. This table confirms that the Commission must consider all components of revenue
10 requirements: revenues, expenses and rate base. Each scenario illustrates the
11 potential for each of these elements of the rate making equation to have an impact on
12 the utility's opportunity to earn a fair return.

13
14 **Q. You just mentioned revenues, expenses and rate base. You also noted at the
15 outset of your discussion of these scenarios assume an 8.00 percent ROR
16 remained constant. Please explain the importance of that assumption.**

17 A. The assumption of a constant 8.00 percent ROR was a simplifying assumption. The
18 table clearly shows that if the utility's cost of capital decreased to 7.70 percent or
19 7.27 percent, it would offset any attrition the utility might otherwise experience.
20 This demonstrates that cost of capital is also a critical element for the Commission to
21 consider. This is an important element of Staff's presentation in this case and it is a
22 material element influencing the result of my attrition analysis. As Mr. Elgin

1 testifies, the cost of capital is lower today than before.⁴² My attrition analysis
2 captures this effect in order to provide Avista a reasonable opportunity to earn a fair
3 rate of return.

4
5 **C. How an Attrition Analysis is Performed; Complicating Factors**

6
7 **Q. Briefly describe how an attrition analysis is performed.**

8 A. An attrition study starts with the base case historical test period results of operations,
9 with restating and certain pro forma adjustments. The attrition study then estimates
10 how the relationship between expenses, revenues and rate base are likely to change
11 in the rate year from the base case level.

12 If the analysis shows that there is a high probability of changing relationships
13 between revenues, expenses and rate base, then an attrition allowance providing
14 additional revenue may be necessary so the utility will have a reasonable opportunity
15 to earn a fair return.

16
17 **Q. Is an attrition study consistent with the matching principle of ratemaking?**

18 A. Yes. An attrition study honors the matching principle because it evaluates all
19 ratemaking elements for the rate year: revenues, expenses, rate base and rate of
20 return. Moreover, because an attrition study begins with the historical results of
21 operations, including restating and certain pro forma adjustments, an attrition study

⁴² Id. 6, lines 1-2.

1 complements the Commission's longstanding policy of using historical, restated and
2 pro formed results of operations for rate setting purposes.

3

4 **Q. Is an attrition analysis simple to undertake?**

5 A. No. Properly measuring attrition is a very complex undertaking. First, an attrition
6 study measures the likelihood the utility will earn a fair return, which means the
7 attrition study must be consistent with standard rate making principles and practice.

8 Second, attrition analyses use forecasts, trends and/or budgets to estimate
9 growth and are unavoidably subject to uncertainty. Estimates of load and revenue
10 are particularly challenging due to the effects of weather, fuel costs, the economy
11 and other factors. As a result of this uncertainty inherent in forecasts, the attrition
12 study results can vary widely, depending upon assumptions used to estimate the
13 future period.

14 In the end, an attrition analysis should be transparent, and the Commission
15 should be confident that the attrition analysis reasonably reflects the future
16 relationships between costs and revenues.

17

18 **Q. Please provide a specific example of the uncertainties surrounding forecasts.**

19 A. The load forecasts the Company provided for use in the attrition study show a
20 singular result with a 95 percent confidence that actual results may vary by 2.5
21 percent, plus or minus.⁴³ This is a swing of five percent.

⁴³ Avista's supplemental response to Staff Data Request 395 states that the Company's load forecast model approximates a 5% confidence level or a 95% confidence interval. This means plus or minus 2.5 percent.

1 A positive 2.5 percent change in electric revenues is \$11,357,000,⁴⁴ which is
2 enough to support a 14 percent increase in net plant (\$157,299,000) in one year, or
3 about \$60 million more net plant than Avista is requesting in this case for two
4 years⁴⁵. This shows the uncertainty at play when using forecasts.

5
6 **D. Staff's Attrition Study**

7
8 **1. Summary**

9
10 **Q. Please state the amount you recommend that the Commission provide Avista
11 for an attrition allowance, and how that relates to the overall Staff case.**

12 **A.** Staff recommends the Commission provide an attrition allowance for electric service
13 of \$19,066,000. The net impact of including that amount of additional revenue to
14 Staff's base case is an attrition-adjusted revenue surplus of \$1,312,000.

15 For gas service, Staff recommends the Commission provide an attrition
16 allowance of \$2,837,000. The net impact of including that amount of additional
17 revenue to Staff's base case is an attrition-adjusted revenue deficiency of
18 \$3,972,000.

19

⁴⁴ This figure is based on Staff's ROR of 7.22 percent, Staff's base case electric general business revenue of \$454,285,000 and Staff's net rate base of \$1,121,292,000.

⁴⁵ Avista is requesting an increase of \$98,714,000 in net rate base for two years. Andrews, Exhibit No. ____ (EMA-2), at 1, line 48, column f, less line 48, column b.

1 **2. Staff's General Approach to Estimating Attrition**

2
3 **Q. Please summarize the approach you used to conduct your attrition study.**

4 A. My approach is similar to that used by Avista witnesses Mr. Lowry and Ms.
5 Andrews. In general, I developed growth rates for revenues, expenses and rate base.
6 I considered past growth in revenue, expenses and rate base as well as forecasts and
7 budgets for these items. I then applied my estimate of the growth to Staff's test
8 period restated results. I also adjusted the restated test period results for the effect of
9 the Company's depreciation study and other ongoing changes.

10 I explain my attrition analysis in more detail below, where I discuss each cost
11 category and how I applied growth to determine revenues, expenses and rate base for
12 the projected rate year.

13
14 **3. Evaluating Changes in Revenues – Electric Operations**

15
16 **Q. Please explain how you developed growth in electric revenue for the rate year**
17 **2013.**

18 A. My starting point for evaluating revenue growth is the normalized and restated test
19 year of Staff's base case. I separately categorized and analyzed electric service
20 revenue, general business revenue and power supply revenue, which includes sales
21 for resale.

22 For power supply revenues, I used the secondary purchases from Staff's
23 power cost adjustment already modeled to the rate year, consistent with Avista.

1 forecast outcomes, this is a very significant change when considering the effect on an
2 attrition study.

3

4 **Q. Do the Company's electric load forecasts show loads declining after 2013?**

5 A. No. Both of the Company's electric load forecasts reflect an overall upward trend in
6 load growth after 2013.

7

8 **Q. What do the forecasts show for changes in numbers of customers?**

9 A. Both of the Company's electric load forecasts include an average annual growth in
10 number of customers. The Company's first forecast includes average annual
11 customer growth of ■ percent and the July forecast includes customer growth of ■
12 percent. Both forecasts include 2012 customer growth of ■ percent. For the year
13 2013, the first forecast includes an increase of ■ percent. The July forecast
14 includes an increase of ■ percent, although it averages ■ percent for the period
15 2011 to 2016. The customer growth for the period 2011 to 2013 is ■ percent in the
16 first forecast and ■ percent in the July forecast.

17

18 **Q. How did you incorporate these two different load forecasts in your electric
19 attrition study?**

20 A. Given the inherent uncertainty of load forecasting, the dramatic changes Avista made
21 to its forecast, and the fact that Avista is predicting steady growth over the longer
22 term, I did not use either forecast. I based my forecast on the average growth of the
23 July forecast by smoothing the growth over the 2012-2016 period. This resulted in a

1 growth rate of ■ percent per year or 1.24 percent for that 2011 to 2013. Using
2 Avista's allocation method to determine revenue, this equates to a 0.93 percent
3 increase in revenue for that two year period.⁴⁸

4
5 **Q. Please summarize your electric revenue forecast for the purposes of your**
6 **attrition analysis for electric operations.**

7 A. My rate year forecast includes a revenue increase of \$4,392,000⁴⁹ compared to
8 Staff's base case, for a total attrition revenue forecast of \$527,475,000.

9
10 **4. Evaluating Changes in Revenues – Gas Operations**

11
12 **Q. How did you evaluate changes in revenues for gas operations in your attrition**
13 **study?**

14 A. As with electric service, I separately categorize and analyze general business revenue
15 and transportation revenue. Again, I trended the results in the Company's two load
16 forecasts to determine a reasonable level of revenue growth for the purposes of this
17 attrition analysis.

18
19 **Q. Please discuss the Company's load forecasts for gas revenues for the rate year**
20 **2013.**⁵⁰

⁴⁸Breda, Exhibit No. ___ (KHB-9C), at 5 provides the results of the two forecasts and my trended approach.

⁴⁹Id. at 2, line 1, column h.

⁵⁰Breda, Exhibit No. ___ (KHB-10C), at 5, provides the results of the two load forecasts.

1 A. The Company's natural gas load forecasts reflect similar characteristics as the
2 Company's electric load forecasts. Like its electric load forecast, the Company
3 forecasts an overall increase in gas revenues over the 2011-2016 time frame,
4 although unlike the electric forecast, the Company's natural gas service forecast does
5 not show an overall load decrease in 2012. Instead, the Company forecasts a
6 General Service volume increase of ■ percent in 2012, and this is consistent
7 between the two forecasts.

8 Avista forecasts decreases in General Service volumes for the year 2013 in
9 both forecasts; the first forecast includes a decrease of ■ percent and the July
10 forecast includes a decrease of ■ percent. The percentage volume growth forecast
11 for the two-year period 2011 to 2013 is 1.7 percent in the first forecast and 0.7
12 percent in the July forecast.

13 Transportation volumes for 2012 decrease ■ percent in the first forecast and
14 only decrease ■ percent in the July forecast. For the year 2013, transportation
15 volumes increase ■ percent in the first forecast and ■ percent in the July forecast.
16 For the two year period 2011 to 2013, transportation volumes decrease 2.9 percent in
17 the first forecast and increase 4.0 percent in the July forecast.

18

19 **Q. What do the forecasts include for changes in numbers of gas customers?**

20 A. Both load forecasts include an average annual growth in customers of ■ percent
21 over the period 2011 to 2016. The first forecast includes an increase of ■ percent
22 for 2012 and ■ percent for 2013. The July forecast provides a customer growth of
23 ■ percent in 2012 and ■ percent in 2013 although it averages ■ percent for the

1 period 2011 to 2016. For the two year period 2011 to 2013, the first forecast reflects
2 customer growth of ■ percent and the July forecast includes customer growth of ■
3 percent. As with electric service, the changes between the two natural gas load
4 forecasts again demonstrate how unstable load forecasts can be, even in the near
5 term.

6
7 **Q. How did you use the information from the two load forecasts to determine gas**
8 **revenues for your attrition study?**

9 A. As I did for electric service revenues, I did not accept either Company forecast.
10 Instead, I assumed growth based on the average through 2016.⁵¹ The effect is to
11 smooth forecasted growth for the period and eliminates the anomaly in the data
12 Avista asserts for 2013.

13
14 **Q. Please summarize your natural gas revenue forecast for the purposes of your**
15 **attrition analysis.**

16 A. My rate year forecast reflects an increase of \$3,076,000⁵² compared to Staff's base
17 case, for a total attrition revenue forecast of \$148,794,000.

18
19 **5. Evaluating Changes in Expenses**

20
21 **Q. How did you evaluate changes in expenses in your attrition study?**

⁵¹ Breda, Exhibit No. ___ (KHB-10C), at 5 provides the results of the two forecasts and my trended approach.

⁵² Breda, Exhibit No. ___ (KHB-10C), at 2, line 4, column f.

1 A. To evaluate growth in expenses, as my starting point I used the expenses from Staff's
2 restated test period results⁵³ plus certain pro forma adjustments.

3 First, I reflect the impact of the Depreciation Study and its updated
4 depreciation rates. Second, I reflect Staff witness Ms. Huang's executive
5 compensation adjustment. Third, I remove operations and maintenance expenses the
6 Company states will not exist in the rate year.⁵⁴ Next, I remove the regulatory
7 amortization of the Deferred Colstrip and Coyote Springs 2 maintenance in electric
8 service.⁵⁵

9 After reflecting each of these adjustments, I have my starting point for
10 evaluating growth in expenses other than power supply.⁵⁶

11 I evaluated growth in expenses in a similar fashion to Avista. I accepted
12 Avista's use of aggregated categories. In addition, I accepted the Company's growth
13 rates for aggregated non-energy operations and maintenance expense, and taxes other
14 than income tax as reasonable for the purposes of my attrition study for both electric
15 and natural gas service.⁵⁷

16
17 **Q. Please explain in more detail how you evaluated depreciation expense in your**
18 **attrition study.**

⁵³ Huang, Exhibit No. ___ (JH-2), at 1, column d.

⁵⁴ This was originally provided in Adjustment 4.06, Electric and Adjustment 4.03, Natural Gas. I use Avista's revised figures provided in Avista's response to Staff Data Request 30.

⁵⁵ Breda, Exhibit No. ___ (KHB-3).

⁵⁶ Breda, Exhibit No. ___ (KHB-9C), Electric, at 2, column a, and Exhibit No. ___ (KHB-10C), Natural Gas, at 2, column c.

⁵⁷ Breda, Exhibit No. ___ (KHB-9C), Electric, at 2, lines 7,11,13,15, 17 to 20 and 23, column d, and Exhibit No. ___ (KHB-10C), Natural Gas, at 2, lines 9, 11, 13,15 17 to 20 and 23, column e.

1 A. As I stated earlier, my starting point includes the effect of the Depreciation Study
2 presented by Avista in this case. I then developed growth factors based on
3 depreciation expense growth from 2008 through 2011. I limit the years for trending
4 because depreciation rates are updated on a periodic basis, so the more recent past
5 should be most indicative of the future.⁵⁸

6
7 **Q. How did you address regulatory amortizations?**

8 A. I did not adjust regulatory amortizations. I used amortization amounts from Staff's
9 base case. Amortizations of regulatory assets or liabilities are typically straight-line
10 fixed amounts that do not change over time.⁵⁹

11
12 **Q. Please discuss the growth in electric power expense and natural gas purchases.**

13 A. I adjusted the electric 2013 modeled power supply from Staff's base case only for
14 load growth. For natural gas, I priced the change in load for natural gas purchases
15 using the weighted average cost of gas for the test year. My approach is consistent
16 with Avista's approach for these items.

17
18 **Q. What is the overall effect of your analysis of growth in expenses for both electric
19 and natural gas service, compared to Staff's base case?**

20 A. Rate year electric expenses are \$14,682,000 greater than Staff's base case, for a total
21 projected rate year expense of \$414,450,000.⁶⁰

⁵⁸ See Breda, Exhibit No. ____ (KHB-9C), Electric, at 2 lines 9, 14 and 21, column d, and Exhibit No. ____ (KHB-10C), Natural Gas, at 2, lines 10, 14 and 21, column e.

⁵⁹ See Breda, Exhibit No. ____ (KHB-9C), Electric, at 2 lines 10, column d, and Exhibit No. ____ (KHB-10C), Natural Gas, at 2, lines 22, column e.

1 For natural gas service, rate year expenses show an increase of \$4,368,000
2 over Staff's base case, for a total rate year expense of \$132,181,000.⁶¹

3

4 **6. Evaluating Changes in Rate Base**

5

6 **Q. Please discuss your approach to estimating growth in rate base.**

7 A. I use Avista's estimated level of net rate base for 2013, calculated on an average of
8 the monthly averages basis. In its revenue requirement model, Avista calculated
9 Washington rate base additions for 2012 and 2013. I used these figures in my study
10 as a reasonable approximation of net rate base for purposes of attrition.⁶² An
11 attrition study that uses estimates of rate base does not imply Commission pre-
12 approval of any project.

13

14 **Q. Please explain how you address working capital, and other debits and credits.**

15 A. I included these items at the level presented in Staff's base case. The Company does
16 not book amounts of working capital, so I cannot compare historical trends. In any
17 event, trending is not appropriate because working capital does not automatically
18 grow year to year. Working capital depends on the relationship between assets and
19 liabilities on the balance sheet, and it does not necessarily grow over time.

⁶⁰ This is presented on my Exhibit No. ____ (KHB-9C), at 1, line 2.

⁶¹ This is shown on my Exhibit No. ____ (KHB-10C), at 1, line 2.

⁶² Breda, Exhibit No. ____ (KHB-9C), Electric, at 3, lines 31-45, column j equals Exhibit No. ____ (EMA-2) at 10, lines 31-45. Exhibit No. ____ (KHB-10C), Natural Gas, at 3, lines 32-42, column g equals Exhibit No. ____ (EMA-3), at 9, lines 32-42.

1 For similar reasons, I did not grow other debits and credits over the Staff's
2 base case level. This line includes regulatory assets and liabilities that are already
3 adjusted to the rate year.

4
5 **Q. Did you make another adjustment to your projected rate base?**

6 A. Yes. I included the Staff disallowance for the Pullman smart grid project through
7 2013. This adjustment reduced attrition year net rate base by \$3,685,000.⁶³

8
9 **Q. Please summarize your electric and natural gas rate base values for attrition.**

10 A. The electric rate base for the attrition rate year increases by \$83,722,000, to
11 \$1,208,995,000.⁶⁴

12 The natural gas rate base for the attrition year increases by \$13,061,000 to
13 \$202,150,000.⁶⁵

14

15 **7. Results of Staff's Attrition Study**

16

17 **Q. Please explain the results of your attrition study.**

18 A. For electric service, the study shows an attrition-adjusted revenue surplus of
19 \$1,312,000. The calculation is shown in my Exhibit No. ____ (KHB-9C), at 1. Lines
20 1 through 6, column (c), show the projected rate year revenue, expenses, resulting
21 net operating income and rate base. Line 7 indicates a return on rate base of 7.29

⁶³ Breda, Exhibit No. ____ (KHB-8), at 2.

⁶⁴ Breda, Exhibit No. ____ (KHB-9C) Electric, at 1, line 6.

⁶⁵ Breda, Exhibit No. ____ (KHB-10C) Natural Gas, at 1, line 6.

1 percent. The final result is 0.07 percent above Staff's recommended 7.22 percent
2 return on rate base. Therefore, the result is an attrition-adjusted revenue surplus of
3 \$1,312,000, shown on line 14.

4 For natural gas service, Staff's attrition-adjusted revenue requirement is
5 \$3,972,000. My Exhibit No. ___ (KHB-10C) provides the calculation of the revenue
6 deficiency in the same fashion I just explained for electric service. Line 7, column
7 (c) shows the projected rate year return on equity for natural gas service is 5.97
8 percent. Comparing this to Staff's rate of return of 7.22 percent produces an
9 attrition-adjusted revenue deficiency of \$3,972,000, shown on line 14.

10
11 **Q. What other recommendations do you have regarding attrition allowances?**

12 A. Staff recommends the Commission require that Avista include with future attrition
13 study, testimony, exhibits and work papers supporting each forecast relied upon.

14 The testimony should explain the methodology and assumptions used and
15 discuss any changes from prior cases. The Company must explain each assumption
16 and any changes in assumptions and their impact. This data must be segregated by
17 rate schedule, and should include the impact to projected revenue, expense or
18 investment level.

19 In particular, the supporting documentation for testimony needs to include
20 very specific information about the assumptions made in the forecasting process.⁶⁶

21 The information should include a working model with linked workbooks where Staff

⁶⁶ Documentation should include a comprehensive list of assumptions, including both the numerical value of inputs, such as GDP, housing starts, etc., and the assumed relations of such inputs on the load forecast model. The assumed relationships should be further supported by economic/econometric research which supports the relationship. Such research may include income elasticity and price elasticity studies.

1 can input a different numerical assumption and test the input's impact on the final
2 forecasted load.⁶⁷

3

4 **Q. Do you consider your attrition study in this case to be a framework for future**
5 **attrition analyses?**

6 A. Not necessarily. An attrition study develops a forecast of the future relationship
7 between revenues, expenses and rate base. By their nature, any forecast is uncertain
8 and the assumptions underlying a forecast can vary. A good attrition study requires
9 the analyst to consider current facts and circumstances and this may justify a
10 different approach in the future. The framework could also change as Staff gains
11 experience with attrition adjustments.

12

13 **Q, Does that complete your direct testimony?**

14 A. Yes.

⁶⁷ The workbook should be in its native format with each assumption assigned a numerical value, and each value flowing through the entire workbook. Work papers should also be a written explanation which supports that each assumption is reasonable, including information on why each assumption is based on credible sources, highly probable, and will have a material impact on the load.⁶⁷ When the forecaster relies on data or information produced by other entities, the Company should name each entity and provide documentation which supports the inclusion of such data and information. This is meant to include data and information provided by other forecasters and information provided to by the company directly from customers.