

Exhibit No. ___ T (MDF-1T)
Dockets UE-120436, et al.
Witness: Michael Foisy

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

Michael Foisy

**STAFF OF
WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION**

Working Capital and Property Tax

September 19, 2012

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Exhibit No. ___ (MDF-3), Property Tax

1 I. INTRODUCTION

2

3 Q. Please state your name and business address.

4 A. I am Michael Foisy. My business address is 1300 S. Evergreen Park Drive S.W.,
5 P.O. Box 47250, Olympia, WA 98504.

6

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

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

10

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

12 A. I have been employed by the Commission since February 2009.

13

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

15 A. I graduated from Regis University in Denver, Colorado with a Bachelor of Science
16 degree in Technical Management in 1982. In 1985, I earned a Masters of Arts
17 degree in Personnel Management from Central Michigan University.

18

I began my employment at the Commission in February 2009. During my
19 employment at the Commission, I have performed accounting, revenue requirement
20 calculations and financial analyses.

21

I attended the New Mexico State University, Center for Public Utilities,
22 "Practical Regulatory Training for the Changing Electric, Natural Gas Industries"

23

course in September 2009. I also attended the NARUC sponsored course, Innovative

1 Regulatory Approaches to Accommodate Renewable Energy, Demand-Site
2 Resources and Energy Efficiency Programs presented by New Mexico State
3 University.

4 I previously testified before the Commission in the 2010 PacifiCorp General
5 Rate Case, Docket UE-100749 and the 2009 Puget Sound Energy, Inc. General Rate
6 Case, Dockets UE-090704 and UG-090705.

7

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

9

10 **Q. What issues do you address in your testimony?**

11 A. I present Staff's adjustments on working capital and property taxes.

12

13 **A. Adjustment 1.03, Electric and Gas - Working Capital**

14

15 **1. Introduction**

16

17 **Q. What is working capital?**

18 A. Working capital is the cash available for day-to-day operations of the organization.

19 The accounting definition of working capital is the difference between current assets

20 and current liabilities.

21

1 **Q. What is the goal of working capital in ratemaking?**

2 A. The goal of working capital in ratemaking is to determine if investors actually supply
3 working capital, and if so, it is necessary to include the amount that investors supply
4 in rate base and apply a return to that capital.

5
6 **Q. What method did Staff use to determine the amount of working capital
7 investors supplied to Avista?**

8 A. Staff used the investor-supplied working capital (ISWC) method.

9

10 **2. The Investor-Supplied Working Capital Method**

11

12 **Q. Please explain the basics of the investor-supplied working capital method.**

13 A. Investor-supplied working capital measures the difference between the amount
14 capital invested in a business and the amount of investments of the business. More
15 simply, ISWC is the amount of capital invested in the company by investors and
16 available for use by the company. This investment is over and above the company's
17 own investment in plant and other facilities.

18 If there is an excess of invested capital over investments, that amount is
19 ISWC. ISWC is included in rate base and earns a return.

20 The ISWC calculation requires a detailed analysis of the balance sheet to
21 determine which accounts belong in Invested Capital and which accounts belong in
22 Investments. In addition, some accounts are classified as non-utility or non-
23 operating. Once the classifications are made, Investments are subtracted from

1 Invested Capital, and the difference is the Company's total investor-supplied
2 working capital. This total is then allocated among the jurisdictions, the industry
3 type (electric or gas), and non-utility operations to derive state-specific, industry-
4 specific amounts.

5
6 **3. Summary of Results**

7
8 **Q. Please state the working capital allowances Staff determined are appropriate**
9 **for Avista's electric and gas operations in this case, and compare those amounts**
10 **to the allowances proposed by Avista.**

11 A. Using the investor-supplied working capital method or balance sheet approach, I
12 calculate an ISWC allowance of \$21,932,000 for Avista's Washington electric
13 operations and \$3,568,000 for Avista's Washington gas operations.¹

14 The Company's proposes an ISWC allowance of \$31,877,000 for
15 Washington electric operations and no ISWC allowance for Washington gas
16 operations.²

17
18 **Q. Please state the amounts of working capital Staff includes as adjustments for**
19 **working capital, and how those amounts compare to the Company's**
20 **adjustments.**

21 A. As shown in Exhibit No. ___ (JH-2), Staff's working capital adjustment for electric
22 operations adds \$3,744,000 to the "per books" rate base. As shown in Exhibit

¹ Exhibit No. ___ (MDF-2), at 2, lines 26 and 28, respectively.

² Exhibit No. ___ (EMA-1T), at 19, line 3

1 No. ___ (EJK-2), Staff's working capital adjustment for gas operations adds
2 \$3,568,000 to rate base.

3

4 **Q. Please explain why Staff's "adjustment" amount for gas equals your working**
5 **capital "allowance" amount for gas operations, but Staff's "adjustment"**
6 **amount for electric operations does not equal your working capital "allowance"**
7 **for electric operations.**

8 A. For electric operations, Avista includes \$18,188,000 of working capital in its "per
9 books" column, as shown in Ms. Andrews' Exhibit No. ___ (EMA-2), page 1,
10 column (b), line 47. Therefore, it is necessary for Staff's working capital adjustment
11 for electric operations to adjust from that \$18,188,000 figure. To arrive at Staff's
12 working capital allowance of \$21,932,000, my Adjustment 1.03 is a positive
13 \$3,744,000 ($\$21,932,000$ less $\$18,188,000 = 3,744,000$).

14 The Company's working capital adjustment for electric operations also
15 adjusts from that \$18,188,000 "per books" figure. To arrive at Avista's proposed
16 working capital allowance of \$31,877,000, Avista's Adjustment_1.03 is \$13,689,000
17 ($\$18,800,000 + \$13,689,000 = \$31,877,000$).

18 Because Avista did not include any working capital figure in its per books
19 column for gas operations, my working capital allowance equals my adjustment.

20

1 **Q. Does Avista actually record working capital on its books of accounts?**

2 A. No. Avista states the balance “reflected in results of operations is the amount of
3 ISWC approved in Docket No. UE-100467”³.

4

5 **4. Explanation of Staff’s Working Capital Calculation**

6

7 **Q. Have you prepared an exhibit showing Staff’s working capital calculation?**

8 A. Yes. Pages 3 and 4 of my Exhibit No. ___ (MDF-2) contain Staff’s working capital
9 calculation.

10

11 **Q. Please provide an overview of pages 3 and 4 of your Exhibit No. ___ (MDF-2).**

12 A. As I described earlier, the ISWC method calculates Investments and Invested
13 Capital, and the difference is total company investor-supplied working capital. The
14 resulting amount is split between operating and non-operating, and the operating
15 portion is then allocated to the services within each jurisdiction.

16 On page 3, line 55 of my Exhibit No. ___ (MDF-2), I show total company
17 investor-supplied working capital of \$43,819,307. This is the difference between the
18 Invested Capital amount of \$2,356,394,232 on line 9, and the Total Average
19 Investments amount of \$2,312,574,925 on line 53.

20 I use the Investor Supplied Working Capital Ratio to determine how much
21 ISWC is the responsibility of utility operations and how much is non-utility
22 operations. The Investor Supplied Working Capital Ratio of 1.959 percent is
23 determined by dividing the Total ISWC by the Total Investment, Net of CWIP and

³ Exhibit No. ___ (EMA-1T), at 19, lines 1-2

1 Preliminary Survey.⁴ The ISWC Ratio times the Total Average Operating
2 Investment gives us the Total Operating Working Capital of \$42,139,824.

3 Similarly, Non-Operating investments times the ISWC Ratio assigns
4 \$1,679,484 of working capital to non-utility operations.

5 The final step is to allocate the Total Operating Working Capital among the
6 Company operations. This allocation is based on the investments in each state and
7 each industry, gas or electric. The plant investments by state and industry are shown
8 in lines 92 through 96 on page 4. The derivation of the percentage for each is shown
9 just above with Washington – Electric Operations representing 52.0 percent of the
10 Company’s total operations and Washington – Gas Operations at 8.5 percent of the
11 total.

12 The final resulting ISWC for Washington – Electric Operations is
13 \$21,932,177. The resulting ISWC for Washington – Gas Operations is \$3,567,691.

14

15 **5. Explaining Staff/Company Differences**

16

17 **Q. Does part of your Exhibit No. ____ (MDF-2) also portray how Staff’s working**
18 **capital calculation differs from the Company’s calculation?**

19 **A.** Yes. My adjustments to the Company’s ISWC calculation are shown on Pages 5 and
20 6 of Exhibit No. ____ (MDF-2).

21 The first column on Page 5, entitled “31-Dec-11 AMA Per Company”, is the
22 Company’s calculation of total investor-supplied working capital.⁵ The ensuing

⁴ As shown on Exhibit No. ____ (MDF-2), at 4, line 66 divided by line 64 (or $\$43,819,307 \div \$2,237,202,209 = 1.959\%$)

1 columns of page 5 and 6 are Staff's adjustments to that balance as discussed below.
2 All numbers are total Company and are allocated as I discussed earlier in my
3 testimony.

4
5 **Q. Please explain the column entitled "ISWC Adjustment #1".**

6 A. Adjustment 1 removes working gas inventory as a direct rate base investment.
7 Avista included \$10,772,781 in FERC account 164.1, Gas Stored-Current, a subset
8 of the regulatory asset accounts. This amount represents Washington's portion of the
9 working gas inventory at Jackson Prairie. This is the inventory amount expected to
10 turn-over at least once within a year's time. As such, it should be considered a
11 current asset similar to materials and supplies inventory. Therefore, it belongs in
12 working capital.

13
14 **Q. Please explain why removing the gas inventory value from Investments places it
15 in working capital?**

16 A. Recall the basic ISWC equation:

$$\text{Invested Capital} - \text{Investments} = \text{Total ISWC}.$$

17
18 An account such as the Working Gas normally will carry a debit, or in this instance,
19 a "positive" balance. Adjustment 1 reduces the investment on line 23 and
20 consequently increases the Total Investor Supplied Capital shown on line 53.

21 In other words, reducing the "Investments" part of the equation makes "Total
22 ISWC" larger, because the "Invested Capital" amount is unaffected by that change.

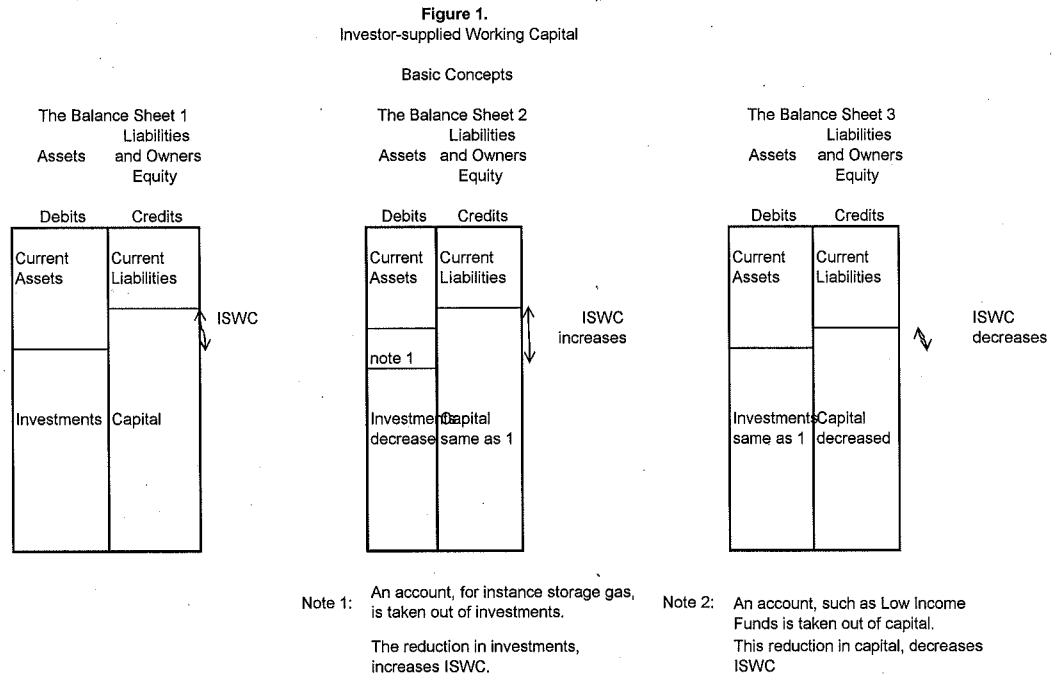
⁵ From Ms. Andrews' workpapers, at 1-03-3.

1 A current asset such as working gas inventory could potentially be supported by
 2 investors as working capital.

3 By the same token, increasing Investments will reduce the amount of ISWC.

4 Figure 1 below may assist in visualizing the concept.

5



6

7

8 Balance Sheet 1 shows the normal account balance, either debit or credit. Balance

9 Sheet 2 shows the effects of Staff's Adjustment 1, crediting account 164100 and

10 debiting Current Assets. Lastly, Balance Sheet 3 shows a liability, Low Income

11 Funds, a credit in non-operating investments, being debited and Current Liabilities

12 being credited. The increase to current liabilities relative to invested capital

13 decreases ISWC.

14

1 **Q. Do any Staff Adjustments increase Average Operating Investments?**

2 A. Yes. My Adjustments 4, 8, 9, 10 and 11 each increase Investments, and thus reduce
3 ISWC. Each of these adjustments relate to proper treatment of current liabilities in
4 the ISWC analysis.

5
6 **Q. Please explain Adjustment 4 as an example of how to properly treat a current**
7 **liability in the ISWC analysis.**

8 A. Adjustment 4 adds the Tariff Rider debit balance of \$426,542 to the Other
9 Regulatory Assets/Liabilities on line 23, in Average Operating Investment. A debit
10 balance in the Tariff Rider Account indicates that the Company spent more in DSM
11 measures than it collected from ratepayers. Under the terms of the Commission's
12 approval of the tariff rider as the recovery mechanism for DSM expenditures, the
13 Company is not allowed to earn a return on a debit balance⁶.

14 Adjustment 4 ensures that no return is allowed through the working capital
15 calculation. This can easily be seen by evaluating the Company's treatment of this
16 item. As line 23 of the first column shows, the Company excluded this debit balance
17 from its calculation. Therefore, the Company's ISWC amount is higher by
18 \$426,542, and thus (after allocations, etc.), ratepayers would pay a return on this
19 money. Staff's Adjustment 4 precludes this from occurring.

20

⁶ *Utilities and Transp. Comm'n v. Avista Corp.*, Docket UE-991606, Third Supplemental Order (September 29, 2000), at 112

1 **Q. Please explain Adjustments 8, 9, 10 and 11.**

2 A. Staff's Adjustment 8 removes the balance of Account 235400, Transmission Service
3 Deposits from line 21, Customer deposits and Advances. Removing this credit from
4 an asset account and transferring it to current liabilities decreases working capital by
5 \$792,293.

6 Staff's Adjustment 9, removes Account 242375, Miscellaneous Liability –
7 MT Lease Payments from line 23, Other Regulatory Assets/Liabilities. Removing
8 this credit from investments and transferring it to a current liability decreases ISWC.

9 Staff's Adjustment 10, Accounts Payable – Jackson Prairie Storage also is a
10 current liability in the investments, similar to Adjustment #9. Removing the
11 \$356,645 from investments and transferring it to a current liability decreases ISWC.

12 Staff's Adjustment 11 is the same situation as the prior two. Account 232681,
13 Accounts Payable Lake CDA Current Fund, is a liability in the investment account.
14 Removing the \$183,333 from investments and transferring it to a current liability
15 decreases ISWC.

16

17 **Q. Please explain Adjustment 3.**

18 A. Staff Adjustment 3 relates to Account 183000, Preliminary Survey and
19 Investigations. The account balance of \$4,058,188 is appropriately assigned in line
20 33, Preliminary Surveys as part of average investments, consistent with prior
21 Commission's decision on this issue in Docket U-77-25.⁷

⁷ *Utilities and Transp. Comm'n v. Pacific Power & Light Co.*, Docket U-77-25, Second Supplemental Order (January 19, 1978), at 5 and 6.

1 Adjustment 3 removes this amount from working capital and reclassifies it as
2 an investment to prevent the preliminary surveys expenditures from earning a return.

3 As the Commission determined in its order in PacifiCorp Docket U-77-25⁸:

4 Company proposed the inclusion of materials and supplies Accounts 151,
5 152, and 154) and miscellaneous electric surveys, investigation and research
6 (Accounts 183, 186, and 187) as a part of the rate base. Commission Staff
7 opposes such inclusions because the final determinations of the accounts
8 have not yet been established – as in the future the Company will capitalize
9 or expense the accounts. Commission Staff, following the investor supplied
10 working capital approach, contends that no allowance for working capital is
11 required. The Commission is of the opinion that the latter approach should
12 be continued; such determination can be made from the record, and by
13 analysis, no working capital is required. The Company position is rejected.
14

15 **Q. Your Adjustments 2, 12, 13 and 14 are adjustments to Non-utility/Non-**
16 **operating Investments. Please explain these adjustments.**

17 **A.** Based on Staff's detailed review of Avista's balance sheet accounts, Avista does not
18 include the following as investments:

19 Account 136000, Temporary Cash Investments - \$5,837,560;

20 Account 134150, Other Special Deposits - Energy, \$1,600,000;

21 Account 134120, Other Special Deposits - Newedge, \$9,113,203; and

22 Account 165550, Prepayments - Wilmington Trust, \$211,816.

23 These accounts are properly classified as Investments because they are either
24 already earning a return, or they are investments in Avista subsidiaries for which
25 ratepayers should not be responsible to pay a return. Staff cures this with its
26 Adjustment 2, Temporary Cash Investments; Adjustment 12, Other Special Deposits
27 – Energy; Adjustment 13, Other Special Deposits – Newedge; and Adjustment 14,

⁸ Id.

1 Prepayments-Wilmington Trust. In each instance, the debit to Non- Operating
2 Regulatory Investments reduces ISWC.

3
4 **Q. Please explain Staff's ISWC Adjustment 5, Notes Receivable.**

5 A. Avista includes Account 141150, Notes Receivable Miscellaneous as a current asset.
6 While that may be true from a strict accounting view, this account earns interest.
7 Therefore, it is appropriate to consider this account a Non-utility/Non-operating
8 Investment to avoid allowing it to earn additional return through ISWC. This
9 adjustment removes \$287,381 from current assets and adds the same amount to
10 Other Accounts and Notes Receivable. This increase to investments decreases
11 ISWC.

12
13 **Q. Please explain Adjustment 6, Low Income Assistance, and Adjustment 7,
14 Margin Call Deposit.**

15 A. These two ISWC entries are net liabilities within investment accounts. Account
16 242770, Low Income Funds represents a liability for monies collected for low-
17 income assistance that has not yet been disbursed. It would be unfair for this
18 reduction to investments to have the effect of allowing the Company to earn a return
19 on this money. Staff transfers the credit balance of the account (\$3,239,944) to
20 current liabilities. This increases investments thereby reducing ISWC.

21 Account 242050, Miscellaneous Liability – Margin Call Deposit carries a
22 credit balance of \$678,333. As a liability, it reduces the investment account. Staff

1 Adjustment 7 removes this credit from investments and transfers it to current
2 liabilities. This increases investments, thereby reducing ISWC.

3

4 **Q. Please explain Adjustment 15, Other Current Liabilities.**

5 A. The Company includes Other Current and Accrued Liabilities with a credit balance
6 of \$8,235,966 in non-utility investments, as shown on page 5, line 50 of my exhibit.
7 Staff ISWC Adjustments 6 and 7 remove \$3,918,277 of that from investments.

8 ISWC Adjustment 15 addresses three other accounts:

9 Account 242775, Miscellaneous Liability – Enron Settlement, a debit of \$1,076;
10 Account 242790, Miscellaneous Liability – Mobius, a credit of (\$197,917); and
11 Account 243000, Obligation Under Capital Lease, a credit of (\$209,891). Staff
12 considers these accounts as current liabilities, not investments, and transfers the net
13 credit balance of (\$406,732) out of investments and into current liabilities. This
14 transfer reduces ISWC.

15

16 **Q. How do these figures translate to Staff's revenue requirements presentation?**

17 A. As I explained, Avista includes \$18,188,000 of working capital in its electric per
18 books amounts, but no amount of working capital for gas. Therefore, to reflect my
19 \$21,932,000 amount of working capital working for electric operations; I increase
20 the Company's per books electric working capital figure by \$3,744,000. This
21 amount is shown in Ms. Huang's Exhibit No. ___ (JH-2), page 2, column e (electric)

22 For gas, I simply add \$3,568,000 in working capital to rate base. This
23 amount is shown in Mr. Keating's Exhibit No. ___ (EJK-2), page 2, column g (gas).

1

2

3

B. Adjustment 3.06, Electric and Adjustment 3.04, Gas – Property Tax

4

Q. Please explain Staff's Property Tax Adjustments.

5

A. Staff's Property Tax Adjustments 3.06 electric, and 3.04, gas reflect the Company's property tax expense using the most current levy rates, and the assessed value as of June 30, 2012, which is the most recent assessed value. This adjustment meets the definition of a pro forma adjustment because it is known and measurable. The Company supplied these Property Tax calculations in its response to Staff Data Request 333.

6

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Although June 30, 2012, is beyond the test period, Staff recognizes that Washington's method of calculating property tax contributes to the Company's ability to match the tax expense to the appropriate tax year. In a compromise to the Company's forecast of using future plant additions that are not known and measurable, Staff recommends using the last known and measurable property tax calculation.

18

Q. What is the effect of Staff's Property Tax Adjustments 3.06 and 3.04?

19

A. Staff's Property Tax Adjustments decrease electric net operating income by \$29,000. Gas net operating income decreases by \$40,000.

20

21

22

Q. Please describe the Company's Property Tax Adjustments 3.06 and 3.04.

23

A. The Company's Property Tax Adjustments 3.06 (electric) and 3.04 (gas) are based on a forecast of property tax expense for the rate year, as explained in Ms.

24

1 **Q. Please describe the Company's Property Tax Adjustments 3.06 and 3.04.**

2 A. The Company's Property Tax Adjustments 3.06 (electric) and 3.04 (gas) are based
3 on a forecast of property tax expense for the rate year, as explained in Ms.
4 Andrews's direct testimony, Exhibit No. ___ (EMA-1T), page 54. Ms. Andrews
5 states: "the property on which the tax is calculated is the property value as of
6 December 31, 2012."

7
8 **Q. Should the Commission accept the Company's adjustments?**

9 A. No. The Company's adjustments are not known and measureable because they use
10 forecasts of assessed values that may or may not exist in the future. As such, they
11 are not known and measureable and therefore they fail the Commission's definition
12 of a proper pro forma adjustment in WAC 480-07-510.

13 Because the Company's property tax adjustments are forecasts based on
14 judgment rather than known and measureable data, they fail the "known and
15 measurable" standard the Commission should reject them.

16
17 **Q. Does this conclude your testimony?**

18 A. Yes.