

BEFORE THE WASHINGTON UTILITIES & TRANSPORTATION COMMISSION

WUTC V. AVISTA

DOCKETS UE-120436, *et.al.*

TESTIMONY OF JAMES R. DITTMER (JRD-12CT)

IN OPPOSITION TO THE MULTIPARTY SETTLEMENT STIPULATION

ON BEHALF OF

PUBLIC COUNSEL

NOVEMBER 9, 2012

REDACTED VERSION

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EXHIBIT LIST

- | | |
|--------------------|---|
| Exhibit No. JRD-13 | Avista Utilities Impact of Stipulation Cost of Capital Upon Avista's Claimed Electric Operations Revenue Deficiency |
| Exhibit No. JRD-14 | Avista Utilities Impact of Stipulation Costs of Capital Upon Staff's Claimed Electric Operations Revenue Deficiency |
| Exhibit No. JRD-15 | Avista Utilities Impact of Stipulation Cost of Capital Upon ICNU's Claimed Electric Operations Revenue Deficiency |
| Exhibit No. JRD-16 | Avista Utilities Analysis of Settlement Electric Operations Revenue Increase Relative to Parties' Prefiled Direct Position & Concessions Noted in Stipulation |
| Exhibit No. JRD-17 | Avista Utilities Analysis of Settlement Gas Operations Revenue Increase Relative to Parties' Prefiled Direct Position & Concessions Noted in Stipulation |
| Exhibit No. JRD-18 | Avista Utilities Impact of Stipulation Cost of Capital Upon Public Counsel's Claimed Electric & Gas Operations Revenue Deficiency |

1 **I. INTRODUCTION**

2 **Q: Please state your name and address.**

3 A: My name is James R. Dittmer. My business address is Post Office Box 481934, Kansas
4 City, Missouri 64148.

5 **Q: By whom are you employed and in what capacity?**

6 A: I am a Senior Regulatory Consultant with the firm Utilitech, Inc., a consulting firm
7 engaged primarily in utility rate work.

8 **Q: Have you previously filed testimony in this proceeding?**

9 A: Yes. On September 19, 2012, I filed testimony on behalf of Public Counsel, the
10 Industrial Customers of Northwest Utilities (ICNU) and the Northwest Industrial Gas
11 Users (NWIGU) addressing and responding to Avista's request for an attrition
12 allowance.¹ I also filed additional and separate testimony on behalf of the Public
13 Counsel addressing a number of issues other than attrition.²

14 **Q: On whose behalf are you testifying?**

15 A: This testimony is being filed on behalf of Public Counsel opposing the Multiparty
16 Settlement Stipulation (Stipulation) reached in this docket between Avista, the Staff of
17 the Washington Utilities and Transportation Commission (UTC or Commission), ICNU,
18 NWIGU, and The Energy Project.

19

¹ Exhibit No. JRD 10T.

² Exhibit No. JRD 1T.

- 1 • The 9.8 percent rate of return on equity (ROE) appears to be based on the most
2 recent Washington authorized levels for Puget Sound Energy (PSE) and
3 PacifiCorp. However, those cases contain characteristics that can be
4 distinguished from the instant case that call into question the validity of the
5 comparison. Both Staff and ICNU witnesses testified in this docket that the cost
6 of capital has been trending down since those prior cases were decided.
- 7 • The settlement, as a “black box,” fails to address, or address in any meaningful
8 way, several revenue requirement issues that, in addition to the significant
9 attrition issue, deserve Commission attention. Those issues include executive
10 compensation, the results of the internal accounting audit, 2012 REC revenues,
11 A&G adjustments relating to such items as gifts, dues, memberships, advertising,
12 and smart grid issues.

13 In light of these concerns, I recommend that the Commission reject the proposed
14 Settlement Agreement and conduct a full hearing on attrition, return on equity, and other
15 issues mentioned. This will enable the Commission to independently determine the need
16 for any change in Washington jurisdictional electric or gas base rates, the need or basis
17 for any attrition adjustment, and to fully consider issues previously deemed by this
18 Commission to be of interest and importance.

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1 For the 2014 rate increase, the settling parties propose to use \$9 million in revenues from
2 the ERM balance to offset the electric increase in 2014, if such funds are available, such
3 that on average the net overall average electric bill impact would be 2.0 percent.

4 Pursuant to the terms of the Stipulation, the 2014 ERM offset is subject to availability of
5 a then-existing ERM deferral balance.³ Accordingly, there is no guarantee that the
6 average electric increase in 2014 will be limited to 2.0 percent .

7 It should also be noted that the ERM credit offsets are temporary. Assuming the
8 proposed ERM offsets are employed for 2013 and 2014, they will end on December 31,
9 2014. This will result in a third consecutive bill increase for electric rates of at least 1.0
10 percent on January 1, 2015, in addition to any 2015 increases that might result from a
11 2014 GRC filing by the Company.

12 An integral component of the Stipulation is that Avista will be allowed to
13 implement the first rate increase on January 1, 2013, two full months prior to the
14 expected rate implementation date under the existing case schedule and statutory deadline
15 (March 1, 2013). Avista will be able to collect in excess of \$2 million in incremental
16 electric revenues in 2013 as a result of the early effective date. In other words, the
17 Commission would have to grant Avista an annual electric increase of approximately
18 \$16,380,000 effective on March 1, 2013, in order for Avista to collect the same amount
19 of Washington retail electric revenues in 2013 as it will with a \$13,650,000 increase
20 effective on January 1, 2013.

³ Stipulation, ¶ 5.

1 Similarly, an annual electric rate increase of approximately \$16,845,000 would
2 need to be authorized on March 1, 2014, in order to allow Avista to collect the same
3 amount of electric revenues in 2014 as will occur if the January 1, 2014, increase of
4 \$14,038,000 is approved. It is important when evaluating the increases proposed in the
5 Stipulation to not overlook the value to Avista of early implementation.

6 **IV. THE AGREED UPON ELECTRIC OPERATIONS REVENUE INCREASES**
7 **INCLUDE A SUBSTANTIAL IMPLICIT ATTRITION ADJUSTMENT**

8 **A. Avista's Prefiled and Updated Positions Relative to Stipulation Increases.**

9
10 **Q: Please summarize why you conclude that the settlement includes a substantial**
11 **implicit electric operations attrition adjustment.**

12 **A:** Avista's original electric rate request in this docket consists of two main components: (1)
13 the base rate increase justified on the basis of 2011 adjusted test year operating results of
14 \$20,469,000 million,⁴ and (2) an attrition adjustment of \$20,514,000 million, for a total
15 requested electric rate increase of \$40,983,000 million.

16 As a first step in analyzing the settlement, one should set aside the \$20.51 million
17 electric attrition adjustment, and consider the case in terms of the electric base rate
18 increase of \$20.46 million based upon a 2011 test year adjusted for traditionally accepted
19 restating and proforma adjustments, as one would in a standard GRC. From the
20 traditionally developed 2011 adjusted test year revenue requirement proposed by Avista,
21 it is appropriate to then subtract the impact of items specifically agreed to by the parties

⁴ This is Avista's 2011 adjusted test year revenue deficiency, also adjusted to reflect new proposed depreciation rates, but exclusive of any claim for attrition.

1 to the Stipulation – including the updated power supply costs⁵ and the agreed upon
2 capital structure including the cost rates agreed to for the debt and equity components.⁶
3 Also, Avista witness Mr. Kelly Norwood delineates two other fairly significant
4 corrections⁷ in the Joint Testimony that were stated to be appropriate adjustments to the
5 Company’s originally calculated electric operations revenue deficiency.

6 When the agreed upon power supply and capital costs and the corrections noted in
7 Mr. Norwood’s testimony are reflected within the Company’s calculation of a traditional
8 2011 adjusted test year revenue deficiency, Avista can justify only a \$709,000 electric
9 operations base rate increase *without considering its attrition request*. In other words, as
10 summarized on Table I below, if this were simply a standard GRC, and Avista had agreed
11 to the stipulated power supply and capital costs, and reflected the other needed
12 corrections to its filing, it would be agreeing to a total base rate revenue increase of only
13 \$709,000.

14 / /

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⁵ Joint Direct Testimony of Kelly O. Norwood, Kenneth L. Elgin, Michael C. Deen and Charles M. Eberdt In Support of the Multiparty Settlement Stipulation (Joint Testimony), p 22. The impact of reflecting updated power supply costs set forth within Appendix I to the Stipulation is to reduce Avista’s original electric rate request by \$5.4 million.

⁶ Stipulation, ¶ 7.

⁷ Joint Testimony, p. 22. Mr. Norwood lists the need for an FIT/DFIT correction (\$3.0 million decrease) and a Transmission Revenue Correction (\$1.1 million increase).

1

Table I	
Avista's Requested Electric Operations Increase After Reflecting Cost Components Within the Stipulation and Corrections Noted in Joint Testimony	
Electric Operations Revenue Deficiency as Reflected Within Avista's Original Application – Including a Request for an Attrition Allowance	\$40,983,000
Less: Electric Operations Attrition Allowance Included Within Avista's Original Revenue Deficiency Calculation	(20,514,000)
Avista's Original Electric Operations Revenue Deficiency – Exclusive of its Separate Attrition Request	\$20,469,000
Plus/(Minus) Impact of Cost Elements Specifically Set Forth Within the Stipulation as well as Other Corrections Noted in Joint Testimony Supporting the Stipulation:	
Reduced Cost of Capital Including 9.8% ROE ⁸	(12,460,000)
Updated Power Supply Costs	(5,400,000)
FIT/DFIT Correction	(3,000,000)
Transmission Revenue Correction	1,100,000
Avista's Electric Operations Revenue Deficiency – Exclusive of Attrition – Adjusted for Stipulated Power Supply and Capital Costs as well as Other Required Corrections Noted in Joint Testimony Supporting the Stipulation	\$709,000

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Again, the small electric operations revenue deficiency calculated on Table I represents the maximum increase that Avista can justify in this case, after removing its original attrition request.⁹ The settlement, however, provides for a January 1, 2013, electric operations rate increase of \$13,650,000, and a January 1, 2014 incremental electric operations increase of \$14,038,009 – or a total cumulative rate increase by 2014 of \$27.68 million above existing base rates. Thus, by any calculations that can be undertaken from record evidence, the vast majority of the January 1, 2013, increase, and

⁸ The calculation of the impact of reflecting the stipulated cost of capital upon the Company's originally filed case can be found on Exhibit No. JRD-13.

⁹ Note that Avista is claiming, by far, the largest electric operations revenue deficiency of any party filing testimony in this docket. The same analysis applied to other parties' recommendations will yield even lower revenue requirements, as demonstrated later in my testimony.

1 all of the January 1, 2014, electric operations increase, must reflect an attrition allowance.

2 In other words, virtually the only justification for the electric operations increase in this
3 record are the attrition recommendations of Avista and/or the Commission Staff.

4 **Q: Can the cumulative electric operations increase effective on January 1, 2014, be**
5 **justified by simply adding back Avista's *original* attrition request?**

6 A: No. As can be gleaned from a review of amounts contained on Table I, merely adding
7 back Avista's *original* electric operations attrition request of \$20,514,000 falls well short
8 of the cumulative electric operations increase of \$27,688,000 proposed for January 1,
9 2014.¹⁰ However, Avista states in the Joint Testimony that it has revised its original
10 calculation for the need for an electric operations attrition request, such that it now claims
11 a total attrition adjustment of \$28,714,000 is justified.¹¹ The cumulative \$27,688,000
12 million increase in 2014 for electric revenues approximates the amount of Avista's
13 revised and updated electric operations attrition request.

14 **Q: Why is it a concern if the settlement can only be explained if understood to**
15 **incorporate a substantial attrition adjustment?**

16 A: It is a concern for several reasons. First, the adoption of an attrition adjustment is not an
17 inconsequential matter. This Commission has not adopted an attrition adjustment in over
18 25 years. Further, the Commission has previously observed that an attrition adjustment

¹⁰ Avista's revised electric operations revenue deficiency calculated on Table I without consideration of an attrition adjustment in the amount of \$709,000 *plus* Avista's original electric operations attrition adjustment in the amount of \$20,514,000 sum to only \$21,222,820.

¹¹ Avista's original electric operations attrition adjustment was in the amount of \$20,514,000. In the Joint Testimony Mr. Norwood indicates that an update to its original electric operations attrition request to reflect a revised retail load forecast has the impact of increasing its original attrition request by \$8.2 million. Thus, in total Avista purports to now be able to justify an updated attrition adjustment of \$28,714,000. The update was provided in Avista's Supplemental Response to Staff Data Request No. 178.

1 “is an extraordinary measure, not generally included in general rate relief” and further
2 found that a “request for such an adjustment should be based on extraordinary
3 circumstances...”¹² Those circumstances have yet to be examined or determined by the
4 Commission within this docket

5 Second, the Commission has recently indicated that it is willing to consider
6 attrition proposals filed by companies as a way to address concerns of regulatory lag.
7 Avista’s proposal is the first to come before the Commission in response to this
8 invitation. But for the settlement, the Commission would have the opportunity to
9 consider the issue in detail, hear arguments and evidence from all sides of the question,
10 and issue an order providing guidance and precedent to Avista, other industry
11 participants, and stakeholders.

12 Third, the settlement purports to put the attrition issue in the “black box.” The
13 parties appear to downplay the assumption that any type of attrition adjustment was
14 incorporated in arriving at the agreed upon increases, stating in the Stipulation that “[t]he
15 Settling Parties have explicitly not agreed to a specific attrition allowance, but have taken
16 into account the respective litigation positions of the parties in reaching this
17 agreement.”¹³ However, as Table I and the related discussion above demonstrate,
18 without consideration of an attrition adjustment, virtually none of the first step, and
19 absolutely no amount of a second step electric increase could have been justified.

20 / /

¹² *WUTC v. Washington Natural Gas Company*, Docket UG-920840, Order No. 04, 1993 WL 500058, 20.

¹³ Stipulation, ¶ 8.

1 **B. UTC Staff’s Prefiled Revenue Deficiency Position Relative to Stipulation**
2 **Increase.**

3
4 **Q: Please provide your understanding of the UTC Staff’s calculation of Avista’s**
5 **Washington jurisdictional electric operations revenue deficiency**

6 A: The UTC Staff’s initial case, as set forth in prefiled testimony and exhibits, justifies a
7 revenue *reduction* of \$20,381,000 for Avista’s electric operations, before considering
8 Staff’s proposed attrition allowance.¹⁴ This is a difference of approximately \$40 million
9 from the Company’s filed case, without an attrition allowance. Even after including
10 Staff’s annual attrition allowance of \$19,066,000, Staff still calculates that an electric rate
11 *reduction* of \$1,315,000 is required, based on a recommended return on equity of 9.0
12 percent.

13 **Q: Have you calculated what impact the rate of return agreed to by the parties in the**
14 **Stipulation would have upon Staff’s prefiled electric operations revenue reduction**
15 **recommendation?**

16 A: Yes. As reflected on Exhibit No. JRD-14, I demonstrate that the stipulated return on
17 equity would increase Staff’s electric operations revenue requirement by \$7,924,000. In
18 other words, reflection of the stipulated return would cause Staff’s justified electric
19 revenue *reduction* calculated without consideration of an attrition adjustment to go from
20 \$20,381,000 to \$12,457,000.¹⁵

21 Comparing Staff and Company positions, Avista’s 2011 test year adjusted
22 revenue *deficiency* without attrition, again as shown above in Table I, is \$709,000.

¹⁴ Staff’s initial position is also reflected in the Joint Issues List filed by the parties on October 1, 2012.

¹⁵ Staff’s initial case incorporates the FIT correction and the power cost update. I am not certain as to whether the transmission correction is included.

1 Staff's comparable revenue calculation, without attrition but also reflecting the stipulated
2 power supply and capital costs, shows excess revenues and results in a recommended
3 *reduction* in existing electric rates of \$12,457,000. The Company's recommended
4 electric revenues are nearly \$12 million more than Staff's recommendation – when both
5 parties' recommendations are calculated without attrition and consistently calculated to
6 reflect stipulated power supply and capital costs. Even when Staff's proposed electric
7 operations \$19,066,000 attrition allowance is included, Staff's calculation would change
8 to a revenue *deficiency* of \$6,609,000 after considering the stipulated return on equity of
9 9.8 percent.

10 **Q: Given that, at most, Staff's pre-filed testimony and exhibits – including its attrition**
11 **allowance - adjusted for the stipulated cost of capital, supports a revenue deficiency**
12 **of \$6,609,000, does Staff explain how it determined that a January 1, 2013, increase**
13 **of \$13,650,000 is reasonable?**

14 A: No. Unlike Avista's settlement testimony, Staff identifies no corrections or updates it
15 may have considered to arrive at a determination that the stipulated 2013 increase, which
16 is more than double its filed position after adjustment for the stipulated return, is
17 reasonable. And again, it should be remembered that the early effective date actually
18 yields Avista an additional \$2 million in 2013 revenue.¹⁶ Considering the value of early
19 implementation of new rates, the gap between Staff's stipulation-adjusted position -
20 including its attrition adjustment - and the agreed upon increase, becomes even greater.

¹⁶ As explained earlier, it would require an equivalent increase of \$16.3 million effective on March 1, 2013, to achieve the revenues agreed to in the settlement.

1 **Q: Does Staff provide any specific explanation of how the total increase of \$27 million**
2 **in rates by 2014 is justified, given that its stipulation-adjusted position only supports**
3 **an increase of \$6.6 million, including an attrition adjustment?**

4 A: No. As discussed in my previous answer, Staff testimony supporting the Stipulation does
5 not explain how it justifies even the first step January 1, 2013 electric operations increase
6 – much less the second step January 1, 2014 increase.

7 **C. ICNU’s Prefiled Revenue Deficiency Position Relative to Stipulation**
8 **Increase.**
9

10 **Q: Please summarize your understanding of ICNU’s revenue requirement position in**
11 **its initial case?**

12 A: ICNU did not address all issue areas in prefiled direct testimony filed in this proceeding
13 on September 19, 2012, but instead focused on the a set of key issues including power
14 supply costs, cost of capital and attrition.¹⁷ However, in the Joint Issues List filed by the
15 parties on October 1, 2012, ICNU proposed an electric operations revenue *decrease* of
16 \$7,728,888, based on consideration of the impact of its positions on cost of capital,
17 attrition, power supply costs, as well as adopting a number of Staff issues.

18 **Q: Does ICNU testimony supporting the Stipulation provide a road map to what lead to**
19 **its decision to support the two-step rate increase?**

20 A: No. Testimony filed by ICNU witness Mr. Michael Deen places a great deal of emphasis
21 on the benefits of “rate stability” provided by the Stipulation. However, Mr. Deen’s

¹⁷ My testimony in this docket opposing Avista’s attrition proposal was originally jointly sponsored by ICNU, as well as Public Counsel and NWIGU. In addition to my jointly sponsored testimony, ICNU separately filed testimony prepared by Mr. Michael Gorman that opposed the Company’s attrition adjustment, as well as addressing cost of capital.

1 testimony supporting the Stipulation provides no bridge between ICNU’s recommended
2 electric operations revenue *reduction* of \$7,728,000 and the total stipulated cumulative
3 two-step *increase* of \$27,688,000 million.

4 **Q: What is the impact of the stipulated ROE on ICNU’s recommendation in testimony?**

5 A: Reflecting the stipulated return on equity of 9.8 percent has the impact of raising ICNU’s
6 recommended revenue requirement by \$2,945,000.¹⁸ This translates to an ICNU revenue
7 reduction recommendation of \$4,783,000, adjusting only for the stipulated ROE .¹⁹

8 **Q: Does ICNU explain its support for the revenue increases as being related in any way**
9 **to incorporation of an attrition adjustment?**

10 A: No, to the contrary, Mr. Deen’s testimony in support of the settlement states: “The
11 Settlement Stipulation specifically states the parties have not agreed upon an attrition
12 adjustment. ICNU does not believe an attrition adjustment is appropriate, and would not
13 have supported the Stipulation if it had included such an adjustment.”²⁰ As I have
14 explained above, however, it is not possible to justify the 2013 and 2014 revenue
15 increases contained in the Stipulation without an assumption that a very significant
16 attrition adjustment is incorporated in the agreement.

17 **Q: You have discussed and described the prefiled testimonial positions of various**
18 **signatory parties, as well as the impact of concessions made by the parties regarding**
19 **power supply and capital costs in the Stipulation. Have you prepared an exhibit**
20 **that summarizes the parties’ prefiled positions, as well as the impact of known**

¹⁸ See Exhibit No. JRD-15.

¹⁹ \$7,728,000-\$2,945,000 = \$4,783,000. See also Exhibit No. JRD-16.

²⁰ Joint Testimony, p. 33.

1 **changes and concessions made either in the Stipulation itself or within testimony**
2 **supporting the Stipulation?**

3 A: Yes. In Exhibit No. JRD-16, I summarize the prefiled positions of each signatory who
4 prepared electric operations revenue requirement positions, the impact on each party's
5 prefiled position of the various concessions agreed to within the Stipulation, as well as
6 known corrections in the Company's case as set forth in testimony supporting the
7 Stipulation. The impact of all changes are then compared to the stipulated increases for
8 electric operation – including the valuation of early implementation of rates on January 1,
9 2013 and January 1, 2014.

10 **Q: You have thus far discussed impact of the Stipulation on Avista's, Staff's and**
11 **ICNU's claimed revenue deficiency. Have you also calculated what Public**
12 **Counsel's electric and gas operations revenue deficiency or excess would be**
13 **assuming the stipulated cost of capital?**

14 A: Yes. However, I would first point out that Public Counsel did not address all issue areas.
15 The impact of Public Counsel's prefiled testimony recommendations, without
16 consideration of other party positions, is a revenue deficiency of \$8.94 million. On
17 Exhibit No. JRD-18, page 1, I calculate that the stipulated cost of capital would have the
18 impact of reducing Public Counsel's otherwise calculated electric operations revenue
19 deficiency by \$11,436,000. I would also note that Public Counsel's prefiled testimony
20 and exhibits did not address power supply costs, and accordingly, the updated and agreed
21 upon reduction in power supply costs reflected within the Stipulation were not included
22 in Public Counsel's calculations or exhibits accompanying any Public Counsel witnesses'

1 prefiled direct testimony. On Table II below I reflect Public Counsel’s initial electric
2 operations revenue deficiency, as well as the impact of the stipulated power supply and
3 capital costs. The result shows a revenue *excess* for Avista of \$7.89 million.

Table II Impact of Stipulated Power Supply and Capital Costs Upon Public Counsel’s Originally Calculated Electric Operations Revenue Deficiency (amount in \$000s)	
Public Counsel’s Calculated Electric Operations Revenue Deficiency as Reflected within Joint Issues List	\$8,944²¹
Reduction to Reflect Stipulated Cost of Capital (Exhibit No. JRD-18, page 1)	(11,436)
Reduction to Reflect Stipulated Power Supply Costs	(5,400)
Public Counsel’s Calculated Electric Operations Revenue Deficiency/ (Excess) After Reflecting Stipulated Power Supply and Capital Costs	(\$7,892)

4 Inasmuch as Public Counsel only addressed limited gas operations revenue requirement
5 issues, no calculated rate base value was presented within the Joint Issues List to reflect a
6 Public Counsel calculated gas operations revenue deficiency. Nonetheless, on page 2 of
7 Exhibit No. JRD-18 I calculate that with no change in gas operations rate base from that
8 filed by Avista, reflection of the stipulated rate of return would reduce the gas operations
9 revenue deficiency by \$2,140,000.

10
11 **Q: Please summarize your analysis of the parties’ positions regarding the electric**
12 **revenue increases that have been agreed to in the Stipulation.**

²¹ The Joint Issues List shows that Public Counsel’s electric operations revenue deficiency after reflecting only Public Counsel adjustments is \$3,581,000. In preparing this testimony it was observed that, when tabulating Public Counsel’s revenue deficiency shown on the Joint Issues List, Company Proforma Adjustment 3.07 Restate 2011 Capital, which Public Counsel supports in testimony, had inadvertently been omitted when summing the value of Public Counsel adjustments. Adding the revenue requirement value of Adjustment 3.07 (\$5,363,000) to Public Counsel’s electric operations revenue deficiency as currently shown on the Joint Issues List (\$3,581,000) yields a corrected Public Counsel starting point revenue requirement value of \$8,944,000.

1 A: Based upon record evidence, no party – including Avista – can justify even the first-step
2 January 1, 2013 increase without significant reliance upon an implicit attrition
3 adjustment. Further, the cumulative second-step increase on January 1, 2014, can only be
4 justified by assuming almost full acceptance of Avista’s updated and revised electric
5 operations attrition adjustment.

6 **V. THERE IS NOT SUFFICIENT FINANCIAL INFORMATION IN THE RECORD**
7 **TO SUPPORT A JANUARY 1, 2014, WASHINGTON ELECTRIC OR GAS RATE**
8 **INCREASE**
9

10 **Q: Please summarize your additional concerns with the support offered for the 2014**
11 **rate increase.**

12 A: As an initial matter, it is important to note that Avista did not develop or file its initial
13 rate request in this docket using 2014 forecasted operating results. The initial filing was
14 based on a 2011 test year, with the purpose of establishing reasonable rates for the 2013
15 rate year. I am not aware of another instance where this Commission has established
16 rates based upon unaudited forecasted operating results estimated for three years beyond
17 the test year. As discussed in more detail below, the forecasted 2014 financial data now
18 relied on in support of the settlement increases is not a sufficient basis for establishing
19 rates.

20 **Q: You have thus far described how the cumulative January 1, 2014 electric operations**
21 **increase can only be supported by assuming full adoption of the Company’s *revised***
22 ***and updated* electric operations attrition adjustment. Is there record evidence of**
23 **2014 forecasted financial data that might support the January 1, 2014, electric and**
24 **gas rate increases?**

1 A: Mr. Norwood’s testimony in support of the Stipulation attempts to make such a claim.²²

2 However, a review of data and documents noted by Mr. Norwood, does not reveal any
3 evidence that can meaningfully support the second step January 1, 2014, increase for
4 electric and gas operations. Further, there is no evidence that any party, beyond Avista,
5 has carefully audited or analyzed the 2014 forecast of financial conditions.

6 **Q: Please expand upon your conclusions regarding the 2014 forecasted financial**
7 **information offered in this case.**

8 A: Mr. Norwood’s testimony in support of the settlement points to a graph that reflects
9 recent actual historic and 2012-2015 projected percentage changes in total Avista Net
10 Plant Investment, Non-Fuel O&M, Retail kWh Sales and Retail Therm Sales.²³ I would
11 note that forecasted amounts reflected were stated as *percentage changes* rather than
12 *nominal dollars*, and further, that such *percentage changes* were for “total Company”
13 rather than Washington jurisdictional operations. Further, I would note that the Company
14 did not include within original workpapers or exhibits any detailed or meaningful support
15 for the projected amounts. The amounts were only presented on a *total Company*
16 *percentage change* basis. In other words, summary values for total Company amounts
17 were provided, but no underlying support or assumptions for such total Company values
18 were included within Company workpapers supporting the noted graphs.

19

²² Joint Testimony, p. 22:32 – p. 23:21. Mr. Elgin references the same information discussed by Mr. Norwood.

²³ Joint Testimony, p. 23. The graph was originally included in his direct testimony as well as within the direct testimony of Company witness Mr. Scott Morris.

1 **Q: Doesn't Mr. Norwood refer to information provided to Staff in discovery?**

2 A: Yes. Mr. Norwood's testimony in support of the settlement also refers to one discovery
3 request from the UTC Staff wherein the Company provided its Financial Forecast for the
4 period 2012 to 2015. According to Mr. Norwood "[t]he need for revenue increases
5 reflected in the Financial Forecast for 2013 and 2014 is well above the electric increases
6 in the Settlement Stipulation of \$34.4 million."²⁴ However, in large part, the confidential
7 data included in response to Staff Data Request No. 137 has been provided on a "total
8 Avista" basis rather than on a specific utility operations basis, much less on a Washington
9 jurisdictional basis. Second, as already stated, Avista did not base any of its original
10 requested increase upon 2014 forecasted financial information. The response to the Staff
11 Data Request simply does not offer the reliability necessary to support the 2014 rate
12 increase.

13 **Q: Does the settlement or supporting Joint Testimony consider possible benefits of**
14 **avoiding a rate increase in 2014 that could be larger than the increase allowed in the**
15 **Stipulation?**

16 A: The Joint Testimony supporting the Stipulation alludes to this possibility.²⁵ However, as
17 noted above, there is no evidence of the specific amount of Washington jurisdictional rate
18 relief that could be justified for calendar year 2014. There is little evidence that any party
19 besides Avista has audited or studied in any detail the 2014 total Avista financial
20 forecast, much less the possible amount of Washington jurisdictional electric or gas rate

²⁴ Joint Testimony, p. 23:20-21.

²⁵ *Id.*

1 relief that might be justified. As a result, there is no basis to quantify the benefits of
2 avoiding a hypothetical 2014 rate increase.

3 On the other hand, there is credible evidence in the record, submitted in Staff's
4 case, that even allowing for a large attrition adjustment, a modest revenue reduction is
5 needed for Avista.²⁶ To summarize, there is simply insufficient information to determine
6 the need for, or possible amount of, a January 1, 2014, electric operations rate increase.
7 Accordingly, there is no way to meaningfully assess the "risk of a rate increase" in 2014.

8 **Q: Please summarize your testimony regarding the support offered for the January 1,
9 2014 increase.**

10 A: Avista's initial filing does not contain, and was not designed to contain financial
11 information to justify a separate rate increase in 2014. It was not based on forecasts of
12 2014 financial conditions. Subsequently, the settling parties have submitted no
13 meaningful utility-specific or jurisdiction-specific forecasted financial information in the
14 record to support the January 1, 2014, electric and gas increases.

15 **VI. RECENTLY ANNOUNCED EMPLOYEE SEVERANCE PLAN**

16
17 **Q: Have you become aware of operational savings that were not known to Stipulation
18 signatories – other than Avista – at the time that the Stipulation was entered into?**

19 A: Yes. On October 22, 2012 –the first business day following the filing of the Stipulation –
20 Avista announced a major voluntary employee severance program as part of a cost-

²⁶ Put another way, under Staff's filed case, Avista can be expected to earn in excess of a reasonable rate of return on its electric operations investment, unless a revenue reduction is approved.

1 cutting plan. The severance plan is estimated on a system wide basis to cut \$14 million
2 or more from budgeted 2013 operating costs.²⁷

3 **Q: Were the signatories to the Stipulation informed of this specific cost cutting**
4 **initiative prior to those parties entering into the Stipulation?**

5 A: **[Begin Confidential]** XXX
6 XX
7 XX
8 XX
9 XX
10 XX.²⁸ **[End**
11 **Confidential]**

12 **Q: Were the cost cuts anticipated from the newly announced severance program**
13 **reflected in the forecasted financial information for 2014 purportedly relied upon in**
14 **support of the settlement?**

15 A: No. The forecasted financial information presented by Mr. Norwood which I have
16 previously discussed does not incorporate this information. Thus, even the very limited
17 forecasted 2014 financial information referenced in the Joint Testimony has not been
18 adjusted for the now-planned cost cuts. This further undercuts the reliability of the
19 support for the reasonableness of the 2014 increases and provides a further reason why

²⁷ Spokesman- Review, October 23, 2012. Available at: <http://www.spokesman.com/stories/2012/oct/23/avista-offering-buyouts/>

²⁸ Public Counsel issued a data request, Public Counsel Data Request 427, to Avista following the public announcement of Avista's severance plan. In its discovery response Avista provided additional information regarding the severance plan. This information was not provided to any party in this proceeding prior to the Settlement Stipulation being filed.

1 the Commission needs to reject the settlement and proceed to hold a full hearing to
2 determine the actual revenue needs of the Company.

3 **VII. THE STIPULATED RETURN ON EQUITY**

4 **Q: What return on common equity have the signatory parties agreed to by the terms of**
5 **the Stipulation?**

6 A: The Stipulation specifically agreed upon a cost of capital which included a 9.8 percent
7 return on common equity, and further, determined that the agreed upon common equity
8 ratio is 47.0 percent.

9 **Q: Do you believe the agreed upon cost of common equity is reasonable?**

10 A: I am not offering any independent opinion as to the appropriate cost of common equity in
11 this proceeding. However, since the Joint Testimony²⁹ specifically bases the
12 reasonableness of the equity return on the Commission authorized levels in PSE's and
13 PacifiCorp's most recently litigated Washington rate cases, I believe it is relevant to point
14 out certain facts and circumstances which distinguish those cases from this one.

15 **Q: Please explain.**

16 A: First, as they did in this docket, Mr. Elgin and Mr. Gorman filed cost of capital testimony
17 in both the most recently litigated PSE and PacifiCorp cases on behalf of the UTC Staff
18 and ICNU, respectively. The ranges for the cost of common equity being recommended
19 by Mr. Elgin and Mr. Gorman in the current Avista case, and in the most recently
20

²⁹ Joint Testimony, p. 24:1-5 (Norwood) and p. 26 (Elgin, referencing PSE).

1 litigated PSE and PacifiCorp cases, are summarized on Table III below:

Table III			
Comparison of Staff and ICNU Recommended ROE			
Current Avista Docket Versus Most Recent			
Litigated PSE and PacifiCorp Cases			
	Return on Equity Recommended		
	Avista-Current	PSE	PacifiCorp
Michael Gorman			
- Range	9.1% - 9.7%	9.5 – 9.85%	9.1% - 9.9%
- If No Change to Existing Power Cost Recovery Mechanism is Made	9.4%	9.7%	N/A
- If Company Proposed Changes to Power Cost Recovery Mechanism are Adopted	9.1%	9.5%	9.5%
Ken Elgin			
- Range	8.6% - 9.1%	9.0% – 9.5%	9.0% - 9.75%
- Recommended ROE	9.0%	9.5%	9.5%

2

3 **Q: What relevant observations can be made from Table III above?**

4 A: First, the agreed 9.8 percent ROE in the Stipulation is not only above Messrs. Gorman
 5 and Elgin’s specific ROE recommendation, but also *above the high end* of each witness’
 6 range for a reasonable Avista ROE at this time.

7 Second, the recommended ROE of each of these witnesses in the current Avista
 8 docket is lower than that which the witnesses were recommending in the previous cases.
 9 The reduced recommended ROE in this docket, relative to the previous PSE and
 10 PacifiCorp dockets, is consistent with these witnesses’ current docket testimony, which
 11 describes falling capital costs in recent periods.

12 //

13 ///

14 ///

1 **Q: What comments did Messrs. Gorman and Elgin make regarding the trend in capital**
2 **costs in this docket?**

3 A: When supporting his recommended ROE, Mr. Elgin stated:

4 **Q: Is a ROE estimate of under 9.0 percent for the proxy group a**
5 **reasonable figure given current market conditions?**
6

7 A: Yes. As I stated in the earlier part of my testimony, the
8 cost of capital is declining. The cost of equity to Avista
9 and other comparable companies is lower than it has been
10 in the past, and rates should reflect this fact. Consistent
11 with *Hope* and *Bluefield*, customers should not be burdened
12 with rates supporting excessive profits.³⁰
13

14 When addressing a question of his recommended ROE in the instant case compared to
15 Avista's last authorized return on equity, ICNU's witness Mr. Gorman stated:

16 My recommended return on equity range is lower in this
17 case than the return on equity included in Avista's rate case
18 from November 2010. However, this lower return on
19 equity is justified based on clear evidence that capital
20 market costs today are much lower than they were in 2010
21 when Avista's rates were approved.³¹
22

23 **Q: Are there other facts and circumstances in the instant case that can be distinguished**
24 **from the previous PSE and PacifiCorp general rate cases?**

25 A: I did not participate in either case. However, based on my review of the final orders, I
26 am aware that neither the PSE nor PacifiCorp rate orders granted any explicit or implicit
27 attrition adjustment. As previously noted, the agreed revenue increases in this case most
28 certainly include a substantial, though unstated, attrition adjustment. Mr. Gorman noted
29 in his testimony that the adoption of an attrition adjustment warrants a corresponding
30 reduction in ROE to reflect the reduced risk. Specifically, Mr. Gorman's recommended

³⁰ Exhibit No. KLE-2T, p. 33.

³¹ Exhibit No. MPG-1T, p. 19.

1 ROE changes from 9.4 percent to 9.1 percent in the event an attrition allowance is
2 adopted.³² Since this case includes a significant de-facto attrition adjustment, it does not
3 appear appropriate to mirror the ROE levels of cases that did not contain such an
4 adjustment.

5 **Q: Please summarize your observations and concerns regarding the return on equity**
6 **provided for within the Stipulation.**

7 A: My observations and concerns regarding the reasonableness of the agreed upon return on
8 equity are as follows:

- 9 • The agreed upon 9.8 percent return on common equity is above even the high end
10 of each non-company cost of capital witness' range for a reasonable ROE
11 presented within testimony in this proceeding.
- 12 • The non-company cost of capital witnesses have recommended a lower ROE in
13 this docket than they did in the previous PSE and PacifiCorp general rate cases.
- 14 • The non-company cost of capital witnesses have provided evidence in testimony
15 filed in this docket that capital costs have recently been falling.
- 16 • Because the agreed upon increase necessarily incorporates a significant de-facto
17 attrition allowance – an allowance not included in either the PSE or PacifiCorp
18 general rate cases – those ROE levels do not appear to be directly applicable to
19 this case.

20 / /

³² Gorman testimony cite

VIII. OTHER PUBLIC COUNSEL ISSUES

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Q: Thus far your testimony has largely focused upon the various signatories “filed,” “updated” and/or “revised for Stipulation concessions” revenue requirement positions. Did Public Counsel raise revenue requirement issues that were not addressed in the settlement?

A: Yes. I presented testimony and adjustments in the following areas that were not addressed by the Stipulation:

- Costs for certain employee events, awards and discretionary gifts
- Costs for dues and memberships for civic organizations and charitable contributions
- Promotional and energy efficiency advertising costs
- Non-utility corporate aircraft expenses
- Adjustments based on the results of Avista’s internal accounting audit
- Smart grid costs

Additionally, Mr. Sebastian Coppola filed extensive testimony on behalf of the Public Counsel addressing executive compensation, incentive compensation, and Board of Directors’ compensation that was not addressed within the Stipulation.

Q: Does the Stipulation consider, or take into account, any of Public Counsel’s positions?

1 A: No. While testimony supporting the Stipulation asserts that the final revenue requirement
2 takes into account Public Counsel’s various recommendations,³³ this did not occur in any
3 meaningful or discernible way.

4 **Q: Why do you conclude that Public Counsel’s positions have not been considered in**
5 **any meaningful or discernible way by the terms of the Stipulation?**

6 A: First, there is no specific finding or conclusion regarding any of Public Counsel’s issues.
7 Perhaps this is not unusual given that the Stipulation is largely a “black box” settlement.
8 Nonetheless, there is clearly no trail to determine how or to what extent any of Public
9 Counsel’s issues were considered.

10 Second, and more importantly, as I have discussed and illustrated above, given
11 the power supply cost and cost of capital determinations set forth in the Stipulation, one
12 can only logically conclude that essentially all of the Company’s remaining positions –
13 including its position on attrition development –were adopted in arriving at the stipulated
14 increase. If one were to assume that any meaningful level or amount of Public Counsel
15 *incremental* positions were considered in the settlement rates, one would expect to see a
16 reduced revenue amount.

17 **Q: Is it concerning that the Stipulation does not address, nor preserve for this**
18 **Commission’s consideration, a number of issues raised by Public Counsel that this**
19 **Commission has previously expressed an interest in reviewing?**

20 A: Yes. For example, when approving the stipulation reached in Avista’s last general rate
21 case this Commission stated an interest in reviewing the reasonableness of Avista’s

³³ Joint Testimony, pp. 24-25.

1 executive compensation. In fact, it ordered Avista to file information regarding the
2 reasonableness of its executive compensation prior to its next general rate case. Mr.
3 Sebastian Coppola further discusses in his testimony responding to the settlement, the
4 importance of the Commission being afforded the opportunity to review executive
5 compensation in this case.

6 In addition to the noted executive compensation issue discussed, Avista's
7 treatment of certain A&G costs have been an issue that has persisted over the last few
8 general rate cases. In the two cases leading up to Avista's 2010 general rate case, Public
9 Counsel had identified numerous accounting errors wherein the Company had
10 inappropriately booked non-utility or below-the-line costs to above-the-line utility
11 accounts. Because of these issues, and further accounting issues identified in the 2010
12 general rate case, the parties in the 2010 case agreed to a settlement which required the
13 Company to perform an internal accounting audit for the next three years with the goal of
14 improving A&G cost assignment. Since that time, Public Counsel has continued to
15 uncover inappropriate A&G expenses included in above-the-line operating expense
16 accounts, in both the 2011 rate case and this rate case. Further, the results of the two
17 internal accounting audits completed to-date have shown that the appropriate accounting
18 and allocation of utility expenditures is not occurring within the tolerable rate indentified
19 within the Company's own internal audit.³⁴ The Settlement Stipulation does not provide

³⁴ Exhibit No. EMA-4 p. 6, Dockets Nos. UE-120436 &UG-120437, *et. al.* and Exhibit No. EMA-5, p. 50, Dockets UE-110876 and UG-110877.

1 the Commission the opportunity to address the results of these audits, which continue to
2 demonstrate concerning results.

3 **IX. ANALYSIS OF STIPULATED NATURAL GAS RATE INCREASE**
4

5 **Q: Have you also evaluated Avista’s and Staff’s claimed Washington jurisdictional gas**
6 **operations revenue deficiency relative to the stipulated increase?**

7 A: Yes. While due to resource constraints, my primary focus has been upon Avista’s
8 electric operations, I have nonetheless summarized on Exhibit No. JRD-17 key data
9 drawn from, or calculated from, record evidence that summarizes Avista’s and Staff’s
10 claimed gas revenue deficiency relative to the increases agreed to within the Stipulation.
11 A review of Exhibit No. JRD-17 reveals that using Avista’s or Staff’s gas revenue
12 deficiency calculations as a starting point, the stipulated gas rate increase must have, at
13 least implicitly, given consideration to some level or amount of an attrition adjustment to
14 arrive at the agreed upon two-step increases for Avista’s gas operations.³⁵

15 Further, as can be gleaned from numbers reflected on Exhibit No. JRD-17, and in
16 the absence of any explanation in testimony supporting the settlement, it would appear
17 that the settlement incorporates: (1) a significant move from a 9.0 percent recommended
18 return on equity to the stipulated 9.8 percent return on equity; (2) an attrition adjustment
19 that more than doubled Avista’s otherwise-calculated gas revenue deficiency ; and (3)
20 that resolution of a number of other revenue requirement issues in Avista’s favor. These
21 elements purportedly allow the settling parties to arrive at a determination that a January

³⁵ However, it is the case that the agreed gas revenue increases don’t have to rely upon an attrition adjustment to the same extent as occurred for electric operations.

1 1, 2013, gas increase in the amount of \$5.3 million is reasonable. Finally, as previously
2 noted a March 1, 2013, increase following a fully litigated case would require an annual
3 increase of approximately \$6,360,000 in order for Avista to realize the same amount of
4 revenues in 2013 as will occur with the early implementation of a January 1, 2013,
5 increase of \$5,300,000.

6 **X. CONCLUSION AND SUMMARY OF RECOMMENDATIONS**

7 **Q: Please summarize your testimony in opposition to the Stipulation.**

8 A: For reasons summarized at the beginning of this testimony, and expanded upon in greater
9 detail throughout this testimony, I am recommending that the Stipulation be rejected as
10 unreasonable and unsupported by record evidence. Accordingly, I am further
11 recommending that full hearings be held so that this Commission can engage in a
12 thorough review of the evidence and make a reasoned determination as to whether there
13 is a need for any Washington jurisdictional rate relief for Avista at this time.

14 **Q. Does this conclude your testimony?**

15 A. Yes, it does.