

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UG 288

In the Matter of

AVISTA CORPORATION, DBA
AVISTA UTILITIES

Request for a General Rate Revision

NORTHWEST INDUSTRIAL GAS
USERS AND CITIZENS' UTILITY
BOARD PREHEARING BRIEF

Pursuant to the Administrative Law Judge's Ruling in this matter dated June 5, 2015, Northwest Industrial Gas Users ("NWIGU") and the Citizens' Utility Board ("CUB") submit this Prehearing Brief in advance of the hearing currently scheduled for December 2nd and 4th, 2015. The purpose of this memorandum is to summarize NWIGU's and CUB's testimony and positions taken in this matter at this time. NWIGU and CUB reserve the right to make additional arguments at hearing and in post hearing briefs.

I. INTRODUCTION

On May 1, 2015, Avista Corporation ("Avista") filed revised tariff schedules to increase rates for Oregon retail customers in the amount of \$8,557,000, or 8.0 percent of its annual revenues. The filing was suspended by the Commission on May 6, 2015, in Order No. 15-143.

On October 16, 2015, Commission Staff ("Staff"), CUB, and NWIGU filed Opening Testimony in response to the Company's original filing. NWIGU and CUB filed joint testimony and are sharing an expert witness—Mike Gorman—on cost of capital and revenue requirement issues. NWIGU and CUB also sponsored separate testimony on rate spread issues and CUB addressed certain other issues in its testimony. NWIGU and CUB will be filing

separate prehearing briefs on the issues addressed in their respective individual testimony in this docket.

As a result of multiple settlement discussions, the Parties have settled certain issues in this Docket, including specific adjustments to the revenue requirement, agreement on a natural gas decoupling mechanism, agreement on the Company's energy efficiency programs and rate design issues. The parties entered into a Partial Settlement Stipulation, which was recently filed with the Commission for review and approval.

II. NWIGU AND CUB'S TESTIMONY AND POSITIONS

A. Partial Settlement Stipulation

NWIGU and CUB believe the Partial Settlement Stipulation is in the public interest and urge the Commission to approve it. The best interests of Avista's natural gas customers are served by the underlying fair compromise on certain revenue requirement and other issues. While NWIGU, CUB and the other parties each hold different positions on the individual components of Avista's natural gas revenue requirement, decoupling and energy efficiency programs addressed in the Partial Settlement Stipulation, NWIGU and CUB support the partial settlement as it has brought down the overall gas revenue requirement increase by \$1.816 million to \$6.741 million. The overall result contained in the Partial Settlement Stipulation is a fair compromise between Avista and its customers on those issues.

While NWIGU and CUB urge the Commission to approve the Partial Settlement Stipulation, NWIGU and CUB believe further adjustments to Avista's filed case are warranted. These adjustments are discussed below.

B. Contested Issues

1. Return on Equity

NWIGU and CUB believe that the Return on Equity (ROE) and capital structure requested by Avista would result in unjust and unreasonable rates. Avista is requesting an ROE of 9.9 percent, and claims a lower ROE will impair Avista's ability to attract investors in today's capital markets. The record in the case lacks any credible evidence of Avista's inability to attract capital and should be rejected.

Mr. Gorman, on behalf of NWIGU and CUB, argues that an appropriate return on equity for Avista would be 9.35%, which is the midpoint of Mr. Gorman's recommended range of 8.9% to 9.8%. NWIGU and CUB believe that Mr. Gorman's recommended return on equity will fairly compensate Avista for its current market cost of common equity, and it will mitigate the claimed revenue deficiency in this proceeding by providing Avista fair compensation with the lowest cost to customers.

Commission Staff proposes an ROE of 9.11%, which is the midpoint of Staff's recommended ROE of 8.76 percent and 9.45 percent. Staff's recommended ROE is in the range of returns recommended by Mr. Gorman, and would fairly balance the interest of customers and shareholders. NWIGU and CUB agree with Staff that a 9.11% ROE meets the *Hope*¹ and *Bluefield*² standards for ratemaking, as well as the requirements of ORS 756.040.

Reducing Avista's authorized return on equity from 9.9% down to 9.35% lowers its claimed revenue deficiency by \$1.03 million. Avista's requested ROE of 9.9 percent is simply too generous to shareholders to the detriment of ratepayers, especially considering that Avista

¹¹ *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944).

²² *Bluefield Water Works & Improvement Co., v. Pub. Serv. Comm'n*, 262 U.S. 679, 694 (1923).

currently has an ROE of 9.5 percent. NWIGU and CUB urge the Commission to adopt either Mr. Gorman's or Staff's recommended ROE.

2. Capital Structure

NWIGU and CUB, through Mr. Gorman, recommend using a capital structure composed of 48.5% common equity and 51.5% debt to establish Avista's overall rate of return. Avista proposes a capital structure composed of 50% debt and 50% equity, which doesn't fairly balance the interests of shareholders and ratepayers. Staff recommends an equity capital structure of 49.86 percent.

Avista argues that Mr. Gorman's proposed capital structure is unreasonable because Mr. Gorman included short term debt in his calculation, but Avista is mistaken. Mr. Gorman did not include short term debt in the calculation of the proper capital structure. As explained in the testimony of Mr. Gorman, he developed the proposed "capital structure by starting with Avista's total capital structure recorded in its FERC Form 1, and removing investments funded by common equity that are not related to utility plant and equipment."³ NWIGU and CUB believe the capital structure recommended by Mr. Gorman is more appropriate and has been regarded as supportive regulatory treatment by credit rating agencies. Accordingly, an increase in the common equity ratio as proposed by Avista is imbalanced and should be rejected.

Adjusting Avista's capital structure to 48.5%/51.5% equity and debt, compared to Avista's 50%/50% equity and debt proposed capital structure, lowers the claimed revenue deficiency at Mr. Gorman's proposed return on equity of \$346,000.

³ NWIGU-CUB/100, *Gorman/12*. See also NWIGU-CUB/102.

3. Information Technology related to Project Compass:

Staff has proposed a disallowance related to Project Compass. Commission Staff determined that the Company exceeded its budget by \$27 million on a Total System basis, which Staff believes to be excessive. NWIGU and CUB agree. Staff has proposed to remove \$1.75 million in rate base which represents one-half of Oregon's share of the cost overruns. Further, Staff determined that significant bonuses were given to employees involved in Project Compass, which appears questionable for a project that is \$27 million over budget. Staff recommends a disallowance of the Oregon allocated bonuses, of \$68,000. NWIGU and CUB concur with Staff that it is not reasonable to expect ratepayers to absorb bonuses on a project that is grossly over budget.

4. Plant Investment:

Avista is rapidly growing its rate base while customer growth is flat. Indeed, Staff notes that Avista's net plant base has doubled from \$106 million to \$211 million between 2007 and 2014, and Avista advertises to investors the infrastructure investment and rate base growth as a positive factor driving the Company's earnings.⁴ With this rapid rate of growth in mind, it is important to carefully review Avista's capital projects to ensure that ratepayers are protected.

Commission Staff recommends the Commission disallow the Company's East Medford Pipeline Project. While Staff does not dispute that the investment is necessary in general, Avista has not demonstrated why the investment must be placed in service this year. Indeed, the East Medford Pipeline Project is in the Company's 2014 Integrated Resource Plan, and scheduled for completion in 2018. Without more demonstration of need, NWIGU and CUB agree with Staff's proposed disallowance, which is consistent with the Commission's disallowance of NW

⁴ See Staff/600, Moore-6-8.

Natural's Mid-Willamette Valley Feeder project because the project was constructed prematurely, and imprudently.⁵

5. Pension Expense:

NWIGU and CUB filed confidential testimony in this matter on Avista's proposed pension expense and, in particular, Avista's Expected Return on Assets ("EROA"). Avista desires to move a significant portion of its pension assets to fixed income investments for increased security and decreased volatility. As described in the testimony of Commission Staff, however, Avista already has the lowest EROA of any Oregon regulated utility, and is proposing to revise its EROA further downward, which would require ratepayers to make up the difference.⁶ The evidence in this proceeding demonstrates that the actual pension returns for Avista in 2013 and 2014 were significantly higher than the EROA embedded in Avista's rates.

Avista argues that its proposed change in EROA is necessary because it is moving significant assets to fixed income products to decrease the funds volatility. While NWIGU and CUB appreciate the concern with decreasing volatility, this adjustment is not appropriate given the fact that Avista already has the lowest EROA of any regulated utility in Oregon and the returns for both 2013 and 2014 are significantly higher than the proposed EROA.

NWIGU and CUB believe Avista's proposal would result in unjust and unreasonable rates and should be rejected. NWIGU and CUB believe that Mr. Gorman's proposal more fairly balances the interest of ratepayers and shareholders, and should be adopted.

6. Bonus Depreciation:

NWIGU's and CUB's proposed adjustment for bonus depreciation would increase accumulated deferred federal income tax ("ADFIT"), for an additional reduction to rate base for

⁵ See *NW Natural*, Order No. 12-408.

⁶ Staff/800, Bahr/6.

ADFIT. On December 16, 2014 Congress passed the Tax Increase Prevention Act. This legislation extended bonus depreciation, which allows for additional depreciation of 50% on new purchased and installed equipment. However, this was a retroactive extension that, except for aircraft related equipment, only covered the 2014 calendar year. Except for the period 2005 through 2007, bonus depreciation has been in effect from September 2001. In addition, on July 21, 2015 the Senate Finance Committee (“Committee”) voted, by an overwhelming majority of 23 to 3, to extend more than 50 expired tax provisions, including 50% bonus depreciation.

NWIGU and CUB believe the history of this provision and the broad support reflected by the Committee’s recent vote indicate that it is extremely likely that 50% bonus depreciation will be renewed for 2015 and 2016. Accordingly, the Commission should approve an adjustment to include bonus depreciation in the case.

As explained by Mr. Gorman, recognition of bonus depreciation should affect Avista’s revenue requirement by increasing the amount of ADFIT included as a reduction to rate base.⁷ In other words, recognition of bonus depreciation will increase the tax depreciation available to Avista for 2015 and 2016 plant additions. This additional tax depreciation will result in additional ADFIT. By increasing the tax depreciation rates Avista applied to its 2015 and 2016 plant additions, to include the 50% bonus depreciation, Mr. Gorman calculated an additional \$7.5 million reduction to rate base for ADFIT.⁸ This additional ADFIT reduces revenue requirement by \$0.8 million.⁹

⁷ NWIGU-CUB/100, Gorman 67.

⁸ *Id.*

⁹ *Id.*

CONCLUSION

The foregoing represents a summary of NWIGU's and CUB's testimony in this matter and the current position it has taken on various components of Avista's filing. NWIGU and CUB will be filing separate briefs on the issues specifically addressed in their respective individual testimony. NWIGU and CUB will continue to participate in this docket throughout the hearing and post-hearing briefing process, and will offer a final position and argument once the record is fully developed.

Dated this 23rd day of November 2015.

Respectfully submitted,

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