ORDER NO. 02-671

ENTERED SEP 27 2002

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UG 150/ UM 1060

In the Matter of	)	
	)	ORDER
AVISTA UTILITIES	)	
	)	
Applications for rate change proposing to reduce annual revenue by about 7.1% or about $4.8 million. **UG 150 and UM 1060**	)	

DISPOSITION: APPLICATIONS APPROVED

On August 15, 2002, the Public Utility Commission of Oregon (Commission) received two applications from Avista Utilities proposing: (1) a rate decrease, effective October 1, 2002; and (2) reauthorization to use deferred accounting pursuant to its Purchased Gas Adjustment deferred accounts. The filing decreases the company's annual revenues by about $4.6 million, or 7.1 percent.

Based on a review of the applications and the Commission's records, the Commission finds that the applications satisfy applicable statutes and administrative rules. At its special public meeting on September 26, 2002, the Commission adopted Staff's recommendation to approve the applications. Staff's recommendation is attached as Appendix A and is incorporated by reference.

ORDER

IT IS ORDERED that:

1. Amortization of deferred accounts, base gas cost changes, and rate changes as requested in Docket No. UG 150 is approved.

2. The reauthorization of deferred accounting for Avista Utilities' Purchased Gas Balancing Account mechanism, Schedule No. 464, for one year beginning October 1, 2002, is approved.

3. Tariff sheets included in Advice No. 02-11-G are allowed to go into effect October 1, 2002.

Made, entered and effective ________________________________.

____
Roy Hemmingway
Chairman

____
Lee Beyer
Commissioner

____
Joan H. Smith
Commissioner

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A request for rehearing or reconsideration must be filed with the Commission within 60 days of the date of service of this order. The request must comply with the requirements of OAR 860-014-0095. A copy of any such request must also be served on each party to the proceeding as provided by OAR 860-013-0070(2). A party may appeal this order to a court pursuant to applicable law.

ITEM NO. 3 and 4

PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: September 26, 2002

REGULAR X **CONSENT** ____ **EFFECTIVE DATE** **October 1, 2002**

DATE: September 27, 2002

TO: John Savage through Lee Sparling, Ed Busch and Bonnie Tatom

FROM: Ray Nuñez and Ed Krantz

SUBJECT: AVISTA UTILITIES: (Docket No. UG 150/Advice No. 02-11-G) Reflects the changes in the cost of purchased gas and technical adjustments resulting in a decrease of $4,782,173, or 7.1 percent.
(Docket No. UM 1060) Requests reauthorization of the PGA deferral mechanism.

STAFF RECOMMENDATION:

We recommend that Avista Utilities' proposed tariff sheets in Advice No. 02-11-G be allowed to go into effect on October 1, 2002. This filing decreases the company's annual revenues by about $4.8 million, or 7.1 percent.

We also recommend the Commission approve the company's request for reauthorization of the purchased gas adjustment (PGA) deferred accounts.

DISCUSSION:

On August 15, 2002, Avista Utilities filed its annual gas cost tracking and technical adjustment application, commonly known as its PGA filing. The filing, docketed as UG 150, proposes a $4,782,173 rate decrease, effective October 1, 2002, to reflect changes in the cost of purchased gas, and amortization of deferred revenue and gas cost accounts. This decrease follows an earlier decrease that became effective on April 2, 2002, when the Commission approved an overall decrease of 15.3 percent. In a separate filing docketed as UM 1060, the company also requested authorization to continue deferring revenues and gas costs under its PGA mechanism.

UG 150

In this filing, Avista proposes to pass on a 7.1 percent overall rate decrease to its Oregon customers. This decrease consists of a decrease in the base cost of the company's system gas supplies, and a decrease from adjusting the amortization rates for deferred revenue and gas cost accounts. The total change in annual revenues is summarized below and shown in Attachment A.

PGA Base Gas Cost Decrease	$ (3,822,139)
Removal of Temporary Credit Increment	(387,002)
Adding New Temporary Increment	(573,033)
Total Proposed Decrease	$ (4,782,173)*

* Does not add due to rounding

Summary of Bill Effects

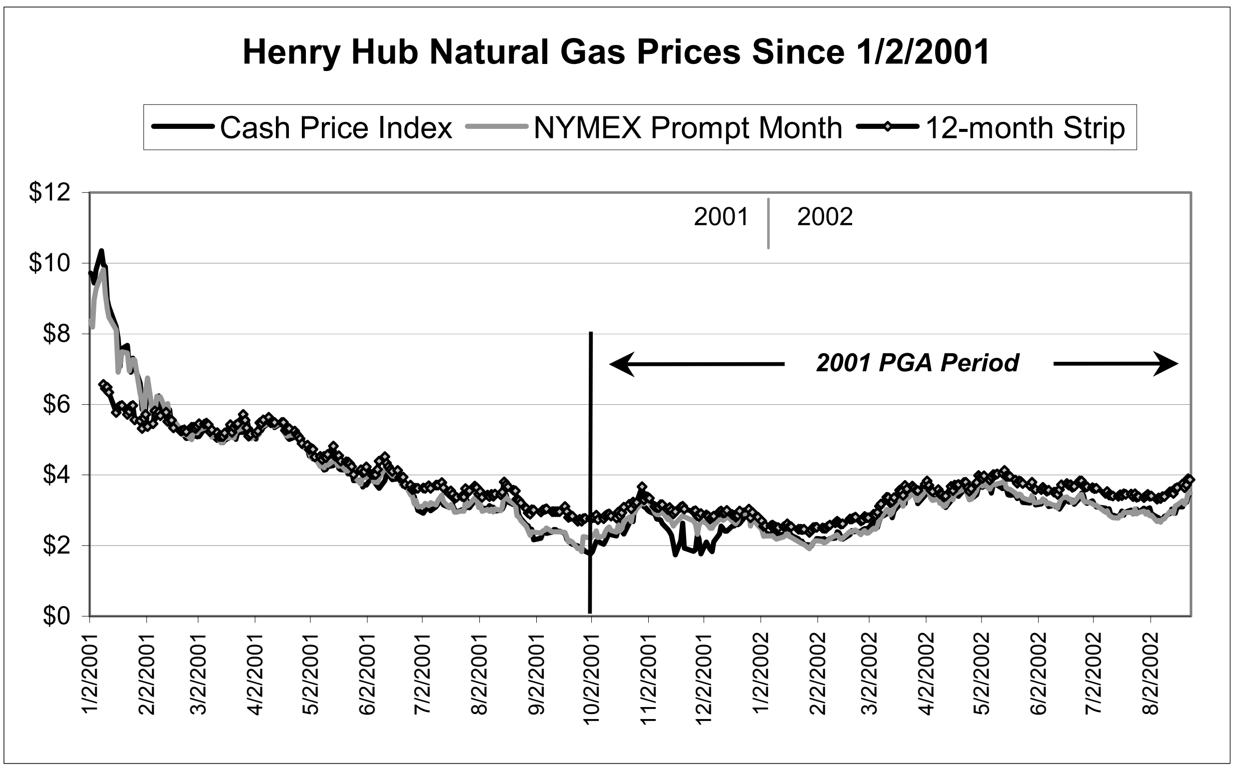
This filing reduces residential customer bills by 7%. A typical residential customer using 54 therms per month will see a reduction of $3.18 toward a lower monthly bill of $42.15. Commercial customers bills are reduced by nearly 8%. A commercial customer using 221 therms per month will see a reduction of $13.03 toward a lower monthly bill of $150.62. A summary of the proposed tariff and revenue changes for Avista's major rate schedules is shown in Attachment A. A summary of the impact of the rate changes on Avista's customers on both an annual and monthly basis is shown in Attachment B, along with the current rates and rate and bill impacts on Cascade and NW Natural customers of their PGA filings.

Staff Review of Gas Costs

National/Regional/Local Trends

Wholesale prices for natural gas did not exhibit the extreme volatility this past year that was experienced in the winter of 2000-2001, when cash prices for delivery at Sumas were bouncing around $50.00/MMbtu. In contrast, wholesale prices last heating season reflected a relatively mild winter, record storage inventories and an absence of industrial gas demand in a floundering economy. Supplies outpaced demand and the unprecedented storage inventory compressed wholesale natural gas prices. At the same time, many wholesale customers acted on lessons learned the previous winter and entered into longer-term contracts to hedge the risk of cash market volatility. By effectively removing those loads from active trading in both cash and futures markets, the increase in long-term pre-purchasing actually exacerbated the deteriorating demand picture and weakened support for natural gas prices.

The $5.00/MMbtu to $7.00/MMbtu cash prices for the 2001–2002 heating season that were predicted by several trading houses as late as July 2001, never materialized. At the same time, storage volumes remained high, as cash prices undercut the withdrawal price of much of the huge volume in storage. (Consequently, almost 1.5 Trillion cubic feet of that expensive gas remains in storage going into the 2002-2003 heating season.)
Within West Coast markets, the implementation of electric price-caps in December of 2001 further pulled the rug out from under prices for Northwest delivery of natural gas, by eliminating the motivation for electric generators to bid natural gas up to the exorbitant levels seen in the winter of 2000-2001.



Since October 1, 2001, cash prices for Northwest delivery have ranged from a nickel shy of $3.50/MMbtu at Stanfield down to a one-time low of $0.53/MMbtu for NW Domestic gas. In a complete reversal from traditional trends, wholesale natural gas prices bottomed in January, and have been progressively increasing since. Meanwhile, the failure of industrial loads to return to the marketplace as predicted has enabled the diversion of large volumes of gas into storage facilities.

Yet despite this continuing absence of industrial load, the federal Energy Information Administration (EIA) projects that U.S. demand for natural gas will increase by 3% during 2002. At the same time, the EIA projects that domestic gas production will have fallen by

2.3% by year's end, and some industry analysts estimate that decline in production is now between 3% and 4%. The increasing demand and declining production are currently on a collision course, with that huge mountain of gas in storage serving to both obscure and delay the point of impact.

On September 3, 2002, the price for the twelve-month strip for natural gas futures at NYMEX settled at $3.695/MMbtu, and the winter strip for 2002–2003 delivery settled at $3.768/MMbtu, after topping $4.00/MMbtu the previous week.

Avista's Gas Cost Situation

Under the Gas Benchmark Mechanism (GBM), Avista Utilities delegates daily gas purchasing to an affiliate, Avista Energy. Avista Energy folds the daily gas requirements of Avista Utilities into its much larger natural gas portfolio. Avista Utilities retains title to the gas, manages the affiliate relationship, and performs state regulatory reporting functions.

Prior to implementation of the GBM, gas costs were based on specific contract prices and volumes bought by Avista Utilities for WP Natural Gas (Avista Utilities operated as WPNG in its Oregon service territories until January 1999). Since then, annual gas costs are determined under the GBM. Under the mechanism the commodity cost of gas is calculated as the First-Of-The-Month (FOM) weighted average of three market indices (Alberta Energy Company (AECO) at 50%, Sumas at 25%, Rockies at 25%) plus $.005 a therm. As a result, the annual commodity cost of gas directly reflects general market increases and decreases. The FOM index price under the GBM is designed to provide lower gas costs to customers over time by eliminating the day-to-day price volatility that can occur in the market. Even though some gas must be purchased on a daily basis to meet customer load requirements, all gas supplied during a month is priced at the FOM. During the winter and spring months of 2001-2002 the FOM index price captured the declining prices throughout those months. Further, deferred gas costs have been offset by about $20 million in capacity release and off-system sales revenue since the inception of the GBM. The off-system sales revenue has been consistently modest this year due to lower gas prices. Off-system sales revenues have declined while capacity release revenues remained stable. Thus, for the 2001-2002 PGA period, deferred gas costs have been offset by about $3.5 million in capacity release and off-system sales revenue.

Staff's Review of Avista's Gas Costs

This is Avista's fifth overall PGA filing with the Gas Benchmark Mechanism (GBM). Each year, Avista, along with the other two regulated gas utilities, is required to file for rate changes related to purchased gas costs with an effective date of October 1. In work papers submitted to Staff, Avista shows a projected annualized gas cost of $39,471,945, which represents a 12% decrease over the current annual cost. The annual cost of gas includes both natural gas commodity and transportation costs.

This 12% decrease is explained by a combination of commodity and demand reductions. First, there is a projected reduction from $31.6 million to $26 million (a 17.7% decrease) in the cost of spot commodity resources. Second, there is a PG&E-GT NW Commodity T-1/T-3 resource that decreases by 67.8%. Third, there is an Alberta resource that has a commodity decrease of 22%. Also, there is a 29% decrease with the cost of Jackson Prairie storage gas. Of note, the Medford lateral has reached the end of a 5-year phase in of its total costs. As a result, the Medford lateral increased gas costs by 8.1%. Avista's Oregon customers have increased their use of the lateral this period by 7.9%.

Staff reviewed the PGA filing to determine the merit and basis for the proposed gas cost decrease. Staff examined GBM input assumptions and GBM monitoring reports. Staff duplicated the gas cost calculations, audited billing records, examined support documents and exhibits.

In October 2001, Avista's supply portfolio had volumes totaling 83,759,298 therms and a weighted average cost of gas of $0.40700. The weighted average cost of gas, or WACOG, is the annual commodity cost per therm. In this filing, the company forecasted volumes totaling 80,441,482 therms, a decrease of 3.96%. The major change for this PGA occurs with a reduction in the WACOG from $0.37500 to $0.31900, a decline of 14.93% just since the April 2002 out-of-cycle PGA. The annual commodity cost decrease is $4,506,332. This number, when added to the adjustments for uncollectibles, city franchise fees, gross revenue fees and demand charges, results in the decrease in the base gas cost shown in Attachment A.

Following is a table of Avista's Weighted Average Cost of Gas since 1993. These numbers are unadjusted for the effects of inflation.

Year	WACOG	% Change
1993	.18835	
1994	.21857	16%
1995	.17283	27%
1996	.12885	-25%
1997	.17921	39%
1998	.17629	-2%
1999	.23000	30%
Oct 2000	.31524	36%
Dec 2000	.53126	69%
Oct 2001	.40700	-23%
Apr 2002	.37500	-8%
Oct 2002	.31900	-15%

Based on Staff's review, the proposed WACOG of $.31900 is an accurate reflection of the company's annual commodity cost. Staff has inspected Avista's proposed tariff sheets and verified their accuracy.

How does Avista expect to work with its customers in the next year?

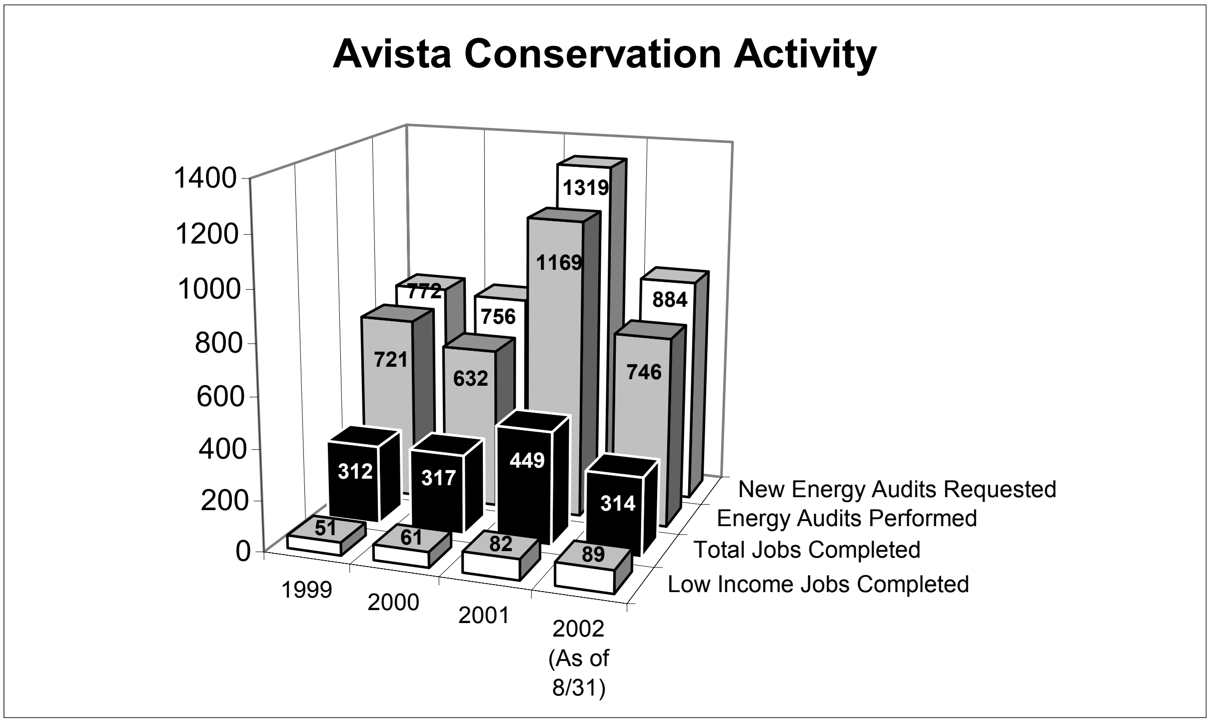
- Avista will continue its Commercial/Industrial DSM Incentive Program that offers partial funding for the installation of cost-effective energy conservation measures.

- The company initiated a mandatory Low Income Rate Assistance Program under ORS 757.315 and began collecting funds for low-income payment assistance in April of this year. Contracts with the respective community action agencies are being finalized and distribution of funds is anticipated to begin in October 2002. Company contributions to the voluntary "Project Share" bill payment assistance program are anticipated to be $12,000 for 2002. Total funding available through this program in 2002 (combined customer, industry and company contributions) will be approximately $31,906.

- The company will continue mandated energy audits under its Residential Energy Conservation and Commercial Energy Conservation Services Programs. Performance and customer participation in this program increased last year, but has returned closer to traditional levels in 2002.

Avista continues to re-evaluate the cost-effectiveness of weatherization measures and activities to reflect current avoided costs.

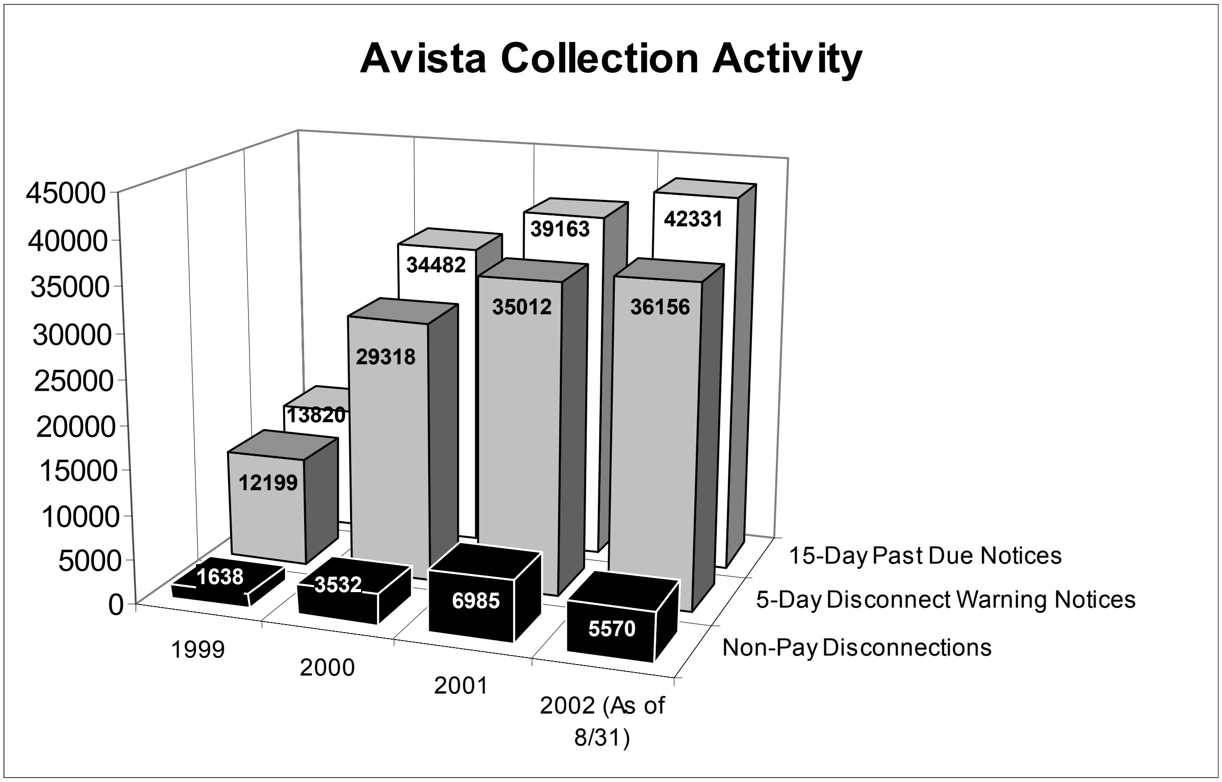
- The company's *CARES* program offers help to customers with special payment arrangements,



minor budgeting advice on other bills, weatherization programs, and referrals to other agencies that can help with special problems.

- The company will continue to offer its customers the required equal payment plans and a *Level Payment Plan* designed to average the monthly payments for gas service of any residential customer. As of August 31, 2002, a total of 4,138 Avista customers are participating in this program, compared to 3,785 last year.

- Avista will also provide the required 12-month payment arrangements on arrearages to its customers. As of August 31, 2002 customer participation in arrearage Time Payment Agreements was within 1% of the 2001 levels. Interestingly, while the volumes of 15-day and 5-day disconnection warning notices have increased this year, the number of accounts actually disconnected for non-payment is down.



Technical Adjustments – Deferred Accounts

As shown in Attachment A, the net decrease in deferred account amortizations of $960,035 results from changes in the amortization rates for the company's deferred gas cost and DSM-related balancing accounts. The Commission previously authorized all of the deferred amounts subject to amortization.

Removing the temporary charge increment decreases rates by $387,002. Over the next 12-month period beginning October 1, 2002, Avista proposes to amortize net credits of $573,033 in deferred gas and DSM costs. The effect of removing the current temporary increment and adding the new one results in a decrease of $960,035. When combined with Avista's proposed decrease in base gas costs of $3,822,139, the net impact on customer rates is a decrease of $4,782,173, or 7.1 percent.

Staff has reviewed the deferred accounts and the weather-adjusted therm sales and verified the accuracy of the changes in amortization rates.

Rate History

The table below shows the rates the Commission has approved for the company's residential customers on Schedule 410 between 1994 and 2002.

Avista Schedule 410, Residential Service			
Date	Customer Charge	Rate	+/-%
December 1, 1994	$3.50	$0.57187	
December 1, 1995	$4.00	$0.52685	-7.9%
December 1, 1996	$4.00	$0.47478	-9.9%
December 1, 1997	$4.00	$0.52651	10.9%
December 1, 1998	$4.00	$0.51375	-2.4%
December 1, 1999	$4.00	$0.56962	10.9%
October 1, 2000	$4.00	$0.69013	21.2%
January 24, 2001	$4.00	$0.91367	32.4%
October 1, 2001	$4.00	$0.91367	0.0%
April 2, 2002	$4.00	$0.76535	-16.2%
October 1, 2002 (Proposed)	**$4.00**	**$0.70640**	**-7.7%**

Earnings Review and Three Percent Test

As a matter of policy, in past years the Commission conducted earnings reviews for both prospective purchased gas costs changes and PGA-related deferrals. In 1999, the Commission concluded its PGA Investigation in dockets UM 903 and AR 357. Order No. 99-284 issued in Docket No. AR 357 adopted a new rule, OAR 860-022-0070, Procedures and Standards for Reviewing Gas Utility Rates in the Context of the Purchased Gas Adjustment Mechanism. This rule enacted an annual spring earnings review to replace the earnings review related to prospective purchased gas cost changes[1]. In addition, Section (8) of this rule states: “An earnings review will not be applicable to amortization of deferred gas costs if the LDC assumes at least 33 percent of the responsibility for commodity cost differences in the risk sharing mechanism.” In 1999, the Commission allowed Avista to implement an experimental natural gas benchmark mechanism (GBM). The company claims this mechanism will provide customers lower costs over time than the 67/33 sharing mechanism and previously the Commission approved a waiver of the earnings review for the duration of the experimental period. At the March 5, 2002 Public Meeting, the Commission approved Avista Utilities request to renew its GBM for a three-year period ending March 31, 2005.

[1] OAR 860-022-0070(7) states that the earnings review mechanism will be effective for four years, and that the mechanism will be reviewed for potential extension after the fourth year. The spring 2002 review was the fourth year the mechanism was applied. Accordingly, staff will contact interested parties to discuss whether the earnings reviews should be continued.

ORS 757.259 (5) and (6) (as amended by House Bill 2630) states that the overall annual average rate impact of the amortizations authorized under the statute may not exceed three percent of the utility's gross revenues for the proceeding calendar year, unless the Commission finds that allowing a higher amortization rate is reasonable under the circumstances. Avista's proposed amortizations are below the 3 percent cap and should be implemented as proposed.

UM 1060

In this filing, Avista requests reauthorization of deferrals pursuant to its automatic adjustment clause, the PGA mechanism. The PGA allows the company to adjust tariffs annually for known and measurable changes in purchased base gas costs and for changes in amortization rates relating to the PGA balancing account.

The information contained in the application is consistent with the requirements of ORS 757.259, 757.210 and OAR 860-027-0300. The application states that continued deferral of these cost and revenue differences minimizes the frequency of rate changes and appropriately matches costs borne and benefits received by ratepayers, consistent with ORS 757.259(2)(e). The reasons cited for reauthorization are still valid. Staff recommends the Commission approve the request for reauthorizing the PGA, effective October 1, 2002.

PROPOSED COMMISSION MOTION:

Avista Utilities' request for: 1) amortization of deferred accounts, base gas cost changes, and rate changes as requested in Docket No. UG 150 and 2) reauthorization of deferred accounting for Avista Utilities' Purchased Gas Balancing Account mechanism, Schedule No. 464, for one year beginning October 1, 2002, be approved and the associated tariff sheets included in Advice No. 02-11-G be allowed to go into effect October 1, 2002.

Attachments

cc: Ed Busch
Bonnie Tatom