



October 24, 2006

Oregon Public Utility Commission
550 Capitol Street N.E., Suite 215
Salem, OR 97301-2551

Attention: Ms. Vikie Bailey-Goggins
RE: Docket No. UG 176/Advice No. 06-06-G

The purpose of this letter is to briefly respond to the OPUC Staff Report, dated October 18, 2006, in the Docket referenced above, related to Avista's Purchased Gas Adjustment (PGA) filing before the Commission.

In reviewing the Staff Report, it is important to note that there is only one area of disagreement between Avista and the Commission Staff that affects the current filing that is pending before the Commission. That area of disagreement relates to the percentage of natural gas load that has been hedged for the upcoming operating year (Nov 2006 – Oct 2007). Avista hedged approximately 91% of the load, and Staff believes that the Company should have hedged no more than 80%.

There is no disagreement between the Staff and the Company with regard to the reasonableness of the prices for both the hedged transactions and the unhedged portion of the Company's retail load.

As noted earlier, the one area of disagreement between Avista and the Commission Staff that affects the current filing is the percentage of natural gas load that has been hedged for the upcoming operating year (91% vs 80%). Avista believes the hedging plan carried out by the Company is reasonable and the costs associated with the transactions should be approved as filed for the reasons outlined below.

1. Avista developed and executed a disciplined hedging strategy for the November 2006 – October 2007 operating year. Avista communicated the details of its hedging plan with OPUC Staff prior to and during the procurement season. There were numerous discussions with Staff about the details of the procurement plan, including the level of hedging. These discussions occurred as part of the Integrated Resource Planning process and the quarterly updates between Avista and OPUC Staff. Specific documentation was provided to Staff and discussed on February 28, 2006 and June 1, 2006, and that documentation included specific information about the level of hedging.
2. At no time in these meetings did Staff communicate to Avista that it should hedge at a level less than 90%. It is only now at this late date that Staff is taking a position on an appropriate level of hedging for Avista. Staff's references to its communications related to appropriate amounts to hedge are obscure at best.

3. In its Report on Page 8 Staff comments on the level of hedging by Avista this year as compared to last year, “This portfolio is virtually the same as that proposed and approved for Avista as part of its 2005 PGA filing.” (emphasis added) If fact, Avista hedged slightly less this year than last year. Nowhere in Staff’s memo related to the 2005 PGA filing is there a statement that Avista hedged too much. The primary concern expressed last year by Staff was that Avista hedged a large portion of the portfolio within a short period of time – not that hedging 90%+ of the total portfolio was inappropriate.
4. In recent weeks Avista has asked Staff to produce any form of communication that was provided to Avista either prior to or during the period that natural gas was being hedged, that suggested that hedging 90% for the upcoming operating year was not appropriate. Staff has been unable produce any evidence of communications.
5. In its Report on Page 7 (Item 5), Staff acknowledged that “There is no ‘one size fits all’ in portfolio construction.” (emphasis added) Furthermore, on Page 17 of the Report Staff stated that, “There is no algorithm for computing the precise level of financial hedging an LDC should enter into.”
6. In Staff’s discussion (on Page 21) of the lower amount of natural gas storage available for Avista’s Oregon service area, as compared to Washington and Idaho, it stated that “This difference would justify some additional financial hedging in Oregon.” (emphasis added) With regard to any OPUC Staff references to Avista’s hedging activities in Washington and Idaho, it is imperative that what the Company does in Washington and Idaho not dictate what is reasonable and/or appropriate for Oregon. The loads, available resources and circumstances are different for those service areas.

In its Report, Staff recognized the need to further discuss the PGA mechanism and appropriate hedging levels, and indicated that it plans to request that the Commission initiate an investigation into the PGA mechanism prior to the end of the year – to be conducted in 2007 (Page 6). Furthermore, on Page 18 Staff states that, “During the upcoming workshops on the PGA the appropriate level of financial hedging and the related criteria will be discussed further. Staff hopes those workshops will lead to a specific agreement on appropriate hedging levels for LDCs of various sizes and circumstances.” We could not agree more. There needs to be an open discussion, with all interested parties involved, on hedging.

For almost two years now, Avista has participated with OPUC Staff and other parties in workshops to discuss the PGA mechanism itself, as well as appropriate hedging strategies. In its Report on Page 21, Staff states that, “As noted above, the informal workshops did not result in an agreement between the parties. Staff plans to open a formal review of the PGA mechanism later this year.”

A workshop process is the appropriate way to establish some guidance on hedging strategies and hedging levels, if guidance is to be provided. That guidance should be up front prior to the hedging season, and not after the fact when the hedging is all done.

Avista established a hedging plan for this year, that was approved by Avista's Risk Management Committee, and was communicated up front to OPUC Staff on a number of occasions. The plan called for hedging volumes that were slightly less than that hedged for the prior year, which was approved by the Commission last year as reasonable and appropriate. Only now is Staff taking a position that the plan for this year resulted in hedging too much.

The Company respectfully requests that the Commission approved Avista's PGA filing as filed, and then initiate a process to evaluate appropriate hedging strategies and hedging levels for all three LDCs.

Sincerely,



Kelly Norwood
Vice President, State & Federal Regulation

- c. Chairman Lee Beyer
Commissioner John Savage
Commissioner Ray Baum
Lee Sparling
Ed Busch
Bonnie Tatom