ORDER NO. 01-837

ENTERED SEP 28 2001

BEFORE THE PUBLIC UTILITY COMMISSION

OF OREGON

UG 145
UM 1032

In the Matter of AVISTA UTILITIES' 2001 Gas Cost Tracking and Technical Adjustment Filing and Application for Reauthorization to Continue Deferring Certain Revenues and Expenses.	)	ORDER

DISPOSITION: APPLICATIONS APPROVED

On August 15, 2001, the Public Utility Commission of Oregon (Commission) received the annual gas cost tracking and technical adjustment filing from Avista Utilities; the case was docketed as UG 145. On August 21, 2001, Avista Utilities filed an application for reauthorization to continue deferring certain expenses and revenues related to its Purchased Gas Adjustment (PGA) balancing account mechanism; this application was docketed as UM 1032.

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 public meeting on September 25, 2001, 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 Avista Utilities' 2001 Gas Cost Tracking and Technical Adjustment filing (UG 145) and application for reauthorization to continue deferring certain revenues and expenses related to its Purchased Gas Adjustment balancing account mechanism (UM 1032) are approved, effective October 1, 2001, as further described in Appendix A.

Made, entered and effective ___________________________________.

BY THE COMMISSION:

____

Vikie Bailey-Goggins
Commission Secretary

A party may request rehearing or reconsideration of this order pursuant to ORS 756.561. A party may appeal this order to a court pursuant to ORS 756.580.

ITEM NO. 7 and 8

PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: September 25, 2001

REGULAR X **CONSENT** ____ **EFFECTIVE DATE** **October 1, 2001**

DATE: September 19, 2001

TO: Phil Nyegaard through Lee Sparling, Ed Busch and Bonnie Tatom

FROM: Ray Nuñez and Ed Krantz

SUBJECT: Avista Utilities – 2001 Gas Cost Tracking and Technical Adjustment Filing (Docket No. **UG 145**, Advice No. 01-6-G) and Application for Reauthorization of the PGA Deferred Accounts (Docket No. **UM 1032**)

SUMMARY RECOMMENDATION:

We recommend the Commission allow Avista Utilities' proposed tariff sheets in Advice No. 01-6-G to become effective with service on and after October 1, 2001. This filing decreases the company's annual revenues by about $112,000, or 0.14 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, 2001, Avista Utilities submitted its annual gas cost tracking and technical adjustment filing, commonly known as its PGA filing. In its filing, docketed as UG 145, Avista proposed a $111,898 rate decrease, effective October 1, 2001, to reflect changes in the cost of purchased gas, and amortization of deferred revenue and gas cost accounts. The company also filed a request for authorization to continue deferring revenues and gas costs under its PGA mechanism. This application was filed August 21, 2001, and docketed as UM 1032.

UG 145

In this filing, Avista proposes to pass on a 0.14 percent rate decrease to its Oregon customers. This decrease consists of a decrease in the base cost of the company's system gas supplies, and an increase 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	$ (9,204,350)
Removal of Temporary Credit Increment	(1,410,450)

Adding New Temporary Increment	10,502,902
Total Proposed Decrease	$ (111,898)

Summary of Bill Effects

This filing has no effect on residential customer rates. A typical residential customer using 56 therms per month will see no change to their monthly bill of $55.17. A summary of the proposed tariff and revenue changes for Avista's major rate schedules is shown in Attachment A. The bill of a typical residential customer using 117.0 therms in January will be $110.90. A summary of the impact of the rate changes on Avista's customers on both an annual and January 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 (addressed in agenda items 12 and 9).

Staff Review of Gas Costs

National/Regional/Local Trends

Natural gas prices in the Northwest have become increasingly volatile in the last several years. The trends identified last year regarding the erosion of our regional price advantage, integration of national and regional markets and corresponding price volatility and uncertainty, continue to characterize Northwest regional gas markets.

Last winter wholesale cash market prices for next-day delivery of natural gas to Northwest points went ballistic as demand outpaced supply through the limited delivery points. Spot market prices that had been in the $2.50 range rocketed to $49.95 per MMBtu in early December, stayed in the double-digits for the remainder of the month and didn't settle back below $5.00 per MMBtu until May.

The spot market alone does not tell the whole story. Spot market prices buy gas for delivery the next day. To buy gas for delivery next winter, utilities must purchase futures contracts or enter into contracts with gas marketers for future delivery. On May 1, 2001, NYMEX contracts for natural gas to be delivered in December 2001 were selling for $5.179 per MMBtu and contracts for delivery in January of 2002 were selling for $5.241 per MMBtu. A futures contract purchased on May 1st to buy the next 12 months (12-month strip) through April 2002 was selling for $4.893 per MMBtu.
During this same period, the U.S. Department of Energy/Energy Information Administration, together with the major trading houses, were predicting that the average price for natural gas in 2001 would not fall below $5. ("average" meaning that $3 gas prices in the summer, when Northwest gas demand is low, could be offset by $7+ gas in the winter, when Northwest gas demand is high.)

A primary component in the equation for predicting natural gas prices was that the new gas-fired electric generators proliferating up and down the West Coast (and the Nation) would be in direct competition with natural gas storage operators for finite gas supplies during the summer months, keeping prices uncharacteristically high. Two unforeseen factors occurred this past year to disrupt that prediction:

- A combination of high gas prices and a lagging national economy reduced industrial and feedstock demand for natural gas, loosening demands on the supply.

- The summer weather across the country has been moderate. Together with price elasticity associated with higher electric costs the result has been lower air conditioning demand.

Consequently, natural gas has been injected into storage at a record pace, resulting in an improved supply picture and lower market prices for natural gas.

The question remains whether the current summer price levels are sustainable. The present balance that is allowing large storage injections is both precarious and fragile. A recent error in the weekly American Gas Association (AGA) storage report set off an upsurge in futures prices that saw a 10% increase in natural gas futures prices occur in less than an hour.

The two wild cards remaining in the supply/demand deck are industrial load and gas-fired electric generation. Separately or together these two have the potential to shift the balance. Compounding this demand volatility is the limitation that virtually all natural gas deliveries to the Northwest must come from one of three receipt points: Sumas, Kingsgate or the Rockies. However, given the declining forward price outlook, increasing storage levels, growing gas production, high drilling rig counts, FERC price caps and the public pressure for a national energy policy, natural gas prices could stabilize over the next twelve months.

To mitigate this demonstrated volatility of Northwest natural gas markets, Avista continues to use the Gas Benchmark Mechanism to provide the best prices for its customers and is likely to seek approval to continue the mechanism beyond its current sunset date.

Avista's Gas Cost Situation under the Gas Benchmark Mechanism

This is Avista's third PGA filing with the Gas Benchmark Mechanism (GBM). Under the 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 November and December 2000, the difference between the FOM index price and the daily index prices was substantial, as prices escalated on a daily basis throughout those months. Further, deferred gas costs have been offset by about $12 million in capacity release and off-system sales revenue since the inception of the GBM (September 1999). Over $1.5 million occurred in December 2000 alone, as Avista Energy was able to take advantage of the large price differential between Sumas and the other basins. Early next year, Staff will prepare an evaluation of the costs and benefits of the experimental GBM as part of the closure of this two and one-half year regulatory experiment.

Staff's Review of Avista's Gas Costs

Avista, along with the other two regulated gas utilities, is required to file for rate changes related to purchased gas costs each year. In work papers submitted to Staff, Avista shows a projected annualized gas cost of $47,838,237, which represents a 15% decrease over the current annual cost. The annual cost of gas includes both natural gas commodity and transportation costs.

Part of the decrease is explained by a projected reduction from $41.1 million to $34.8 million (a 22.8% decrease) in the cost of spot commodity resources. This $10.3 million reduction more than offsets a $1.9 million increase in demand and commodity charges. Of this $1.9 million, $1.5 million is attributable to additional pipeline winter-only capacity of 150,000 therms a day on the Medford Lateral. This resource acquisition is based on Avista's most recent Integrated Resource Plan.

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, and submitted data requests to Avista Energy and Avista Utilities. Staff also reviewed the statistical performance, or history, of the FOM index.

Last year, Avista's supply portfolio had volumes totaling 84,506,910 therms and a weighted average cost of gas of $0.53126. The weighted average cost of gas, or WACOG, is the annual commodity cost per therm. In this filing, the company forecasted volumes totaling 84,889,496 therms, an increase of a mere 0.45%. However, the major change for the 2001 PGA occurs with a reduction in the weighted average cost of gas from $0.53126 to $0.40700, a decline of 23%. The annual commodity cost decrease is $10,329,354. Following is a table of Avista's Weighted Average Cost of Gas since 1991. These numbers are unadjusted for the effects of inflation.

Year	WACOG	% Change
1991	.16839	
1992	.16475	-2%
1993	.18835	14%
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%

Based on Staff's review, the proposed WACOG of $.40700 is an accurate reflection of the company's annual commodity cost. In addition, this filing shows demand charge increases of $1,484,860, and adjustments for uncollectibles, city franchise fees and gross revenue fees of $(359,856). Adding these changes to the commodity cost decrease of $10,329,354 results in the decrease in base gas cost of $9,204,350. 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?

- 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 had been static the past two years. This year the volume of requests for new energy audits has increased and actual work completed is projected to exceed last year's level. Avista continues to re-evaluate the cost-effectiveness of weatherization measures and activities to reflect current avoided costs in a timely fashion.

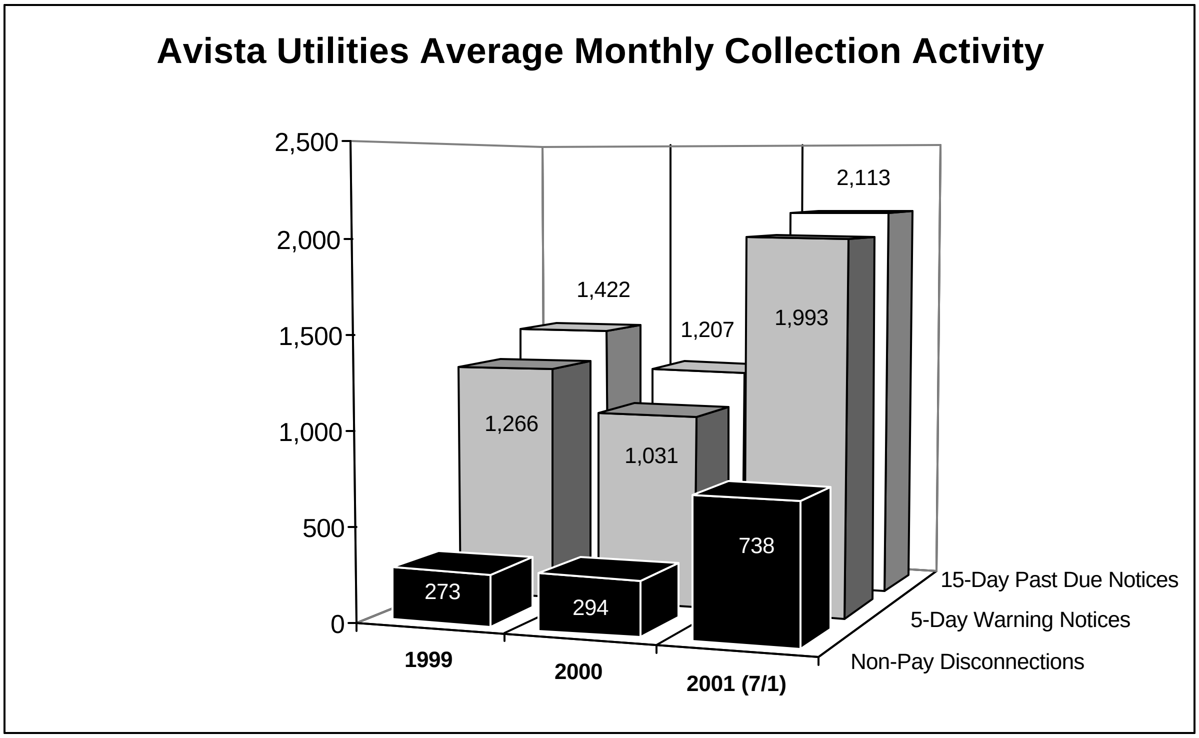
- Avista will continue its Commercial/Industrial DSM Incentive Program that offers partial funding for the installation of cost-effective energy conservation measures.

- For 2001, the company has increased its contribution to its "Project Share" voluntary payment assistance program from last year's $ 6,400 to $12,250. Total funding available through this program in 2001 (combined customer and company contributions) will be approximately $19,217, compared to last year's $17,290.

- 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 July 1, 2001, new participation in the company's Level Payment Plan was over 95% of the total participation in 2000. Currently 13,663 Avista customers are participating in this program.

- 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.

- Avista will also provide the required 12-month payment arrangements on arrearages to its customers. As of July 1, 2001 customer participation in arrearage Time Payment Agreements was 56% above 2000 average monthly levels. Avista has also identified substantial increases in the average monthly volumes of disconnect warning notices issued and in actual disconnections of service for non-payment (see bar graph on following page). As with other utilities, the increased collection activity at Avista may be attributable to a combination of higher gas costs and the general economic decline (see bar graph on top of next page).



Technical Adjustments – Deferred Accounts

As shown in Attachment A, the net increase in deferred account amortizations of $9,092,452 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 increment decreases rates by $1,410,450. Over the next 12-month period beginning October 1, 2001, Avista proposes to amortize $10,502,902 in deferred gas ($10,154,818) and DSM costs ($348,084). The effect of removing the current temporary increment, and adding the new one results in a $9,092,452 increase. However, when combined with Avista's proposed decrease in base gas costs of $9,204,350, the net impact on customer rates is a slight decrease of $111,898, or 0.14 percent.

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

The company is proposing a one-year amortization of its PGA deferred account balance. This represents a 14 percent increase, which is above the 3 percent cap requirement of ORS 757.259 (5) and (6). However, the House Bill 2630 amendment provides the Commission authority to allow a higher amortization rate when justified. Staff supports Avista's proposal, as it will save customers at least $470,000 in interest that would be accrued on the outstanding deferral account if a longer amortization period were used. Also, as company testimony states: "as last winter indicated, gas prices have become extremely volatile and unpredictable. One-year amortization allows the company to recover the effects of last year's price volatility quickly and enable customer rates to reflect current wholesale prices as soon as possible. Lastly, the proposed decline in the company's WACOG offsets the higher amortization rates and results in no rate increase to customers."

Rate History

Natural gas rates paid by Avista's customers have increased at a slower pace than the commodity cost of purchased gas. The table below shows the rates the Commission has approved for the company's residential customers on Schedule 410 between 1994 and 2000.

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 *(Proposed)*	$4.00	$0.91367	0.0%

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. 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. 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.

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 above the 3 percent cap and should be implemented as proposed with Staff's support for the reasons previously mentioned.

UM 1032

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 860-027-300. 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, 2001.

STAFF RECOMMENDATIONS:

We recommend the Commission take the following action regarding the Avista filing:

1. Approve amortization of deferred accounts, base gas cost changes, and rate changes as requested in Docket No. UG 145. Allow the tariff sheets included in Advice No. 01-6-G to go into effect on October 1, 2001.

2. Reauthorize deferred accounting for Avista Utilities' Purchased Gas Balancing Account mechanism, Schedule No. 464, for one year beginning October 1, 2001.

Attachments

cc: Ed Busch
Bonnie Tatom