BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

CASE NO. AVU-E-01-11

DIRECT TESTIMONY OF DON M. FALKNER
REPRESENTING THE AVISTA CORPORATION

Q. Please state your name, business address, and present position with Avista Corp.

A. My name is Don M. Falkner. My business address is East 1411 Mission Avenue, Spokane, Washington. I am employed by Avista Corp. (Company) as a Senior Rate Analyst.

Q. Would you please describe your education and business experience?

A. I graduated from Washington State University in February of 1981 with a Bachelor of Arts Degree in Business Administration majoring in Accounting. That same year, I passed the May Certified Public Accountant exam and joined The Company in June. I have served in various positions within the sections of the Finance Department, including Power Supply Accounting, Subsidiary Accounting, Budget and Forecasting, Plant Accounting and Corporate Accounting. For the past 9 years, I have served in the Rates and Tariff Administration Section, which is part of the Company's External Relations Department.

Q. As a Senior Rate Analyst, what are your responsibilities?

A. As a Senior Rate Analyst, aside from special projects, I am responsible for preparation of normalized semi-annual Commission Basis reporting in the various jurisdictions in which the Company provides utility services. I also have been the lead revenue requirements witness in the Company's most recent general rate filings.

Q. What is the scope of your testimony in this proceeding?

A. I will be presenting the Company's calculation of the overall revenue requirement and will also include an explanation of how an existing balance sheet credit, known as the "PGE" credit, is proposed to be used by the Company to reduce the magnitude of the PCA increase to its customers.

Q. Are you sponsoring any exhibits to be introduced in this proceeding?

A. Yes. I am sponsoring Exhibit No.___(DMF-1), which was prepared under my supervision and direction.

REVENUE REQUIREMENT

Q. Please explain the development of the overall increase?

A. The rates set forth under the proposed PCA Schedule 66 reflect an annual revenue increase amount of $23.6 million, or 19.4%. The present Schedule 66 includes a surcharge of $5.7 million, or approximately 4.8%, which is due to expire January 31, 2002. The proposed incremental rate increase to customers is approximately 14.7%. In developing the PCA increase of 14.7%, the Company attempted to achieve a balance of mitigating the overall impact to customers, while also reducing the surcharge balance to zero as quickly as possible to address the concerns of the financial community. The starting point for the calculation is the actual deferral balance at June 30, 2001. Projected deferral entries beyond June 30, 2001 and through December 2003 are then added to the actual balance.

That calculation shows that absent a recovery plan, the deferral balance for our Idaho jurisdiction would grow to approximately $70 million by the end of 2001 and be slightly under $90 million by the end of 2003. The derivation of the deferral entries is explained in more detail by Mr. Norwood. The Company is proposing to amortize a deferred credit on the Company's balance sheet related to the monetization of the Portland General Electric (PGE) Sale Agreement as an offset to the power cost deferral balance to reduce the overall rate impact to customers. The Company is then proposing that the remaining balance of the deferred costs be recovered by the end of 2003 through the surcharge. This is illustrated by the chart on page 2 of Exhibit No. ____ (DMF-1).

Q. Why was the end of December 2003 chosen as the end of the amortization and recovery period?

A. December 2003 was chosen in an effort to balance a number of competing considerations including the size of the surcharge, the duration of recovery of the deferral balance, the need to immediately improve the financial health of the Company, as well as taking into consideration the timing of the need for additional power resources. A surcharge period shorter than December 2003 would improve the financial health of the Company sooner, but would result in a significantly higher surcharge rate increase. A surcharge period beyond December 2003 would extend into a period when the Company shows a need for new firm energy resources and would not lead to needed financial improvement soon enough. The Company's existing 200 MW purchase from TransAlta expires in December 2003, and Avista will need additional firm energy resources beginning in 2004. The costs associated with these new resources may cause an increase in retail rates, therefore, the Company is proposing a surcharge period that ends prior to 2004.

Q. The Company's PCA mechanism allows the Company to record the difference between <u>actual</u> and authorized power costs under certain parameters, and request implementation of a increase or rebate once that difference reaches $3 million. Is the Company proposing to be allowed to recover a level of <u>projected</u> power cost differences, or differences in costs that have not been recorded or incurred yet, in the proposed increase?

A. No. Projections were utilized in the initial determination of the surcharge, level. However, only <u>actual</u> cost differences will be recovered; the proposed increase rates will be adjusted based on the actual cost differences. The Company has added the following language under the proposed PCA Schedule 66 to insure clarity on this issue: "The rates set forth under this Schedule are subject to periodic review and adjustment by the IPUC based on the actual balance of deferred power costs."

Q. Under the approved parameters of the PCA mechanism, the Company would normally request the recovery of actual deferred power costs over a 12-month period. What would the proposed increase be if the Company requested to recover only actual deferred power costs over a 12-month period?

A. An increase to recover the actual balance of deferred costs at the end of June 2001 ($30 million) over a 12-month period would result in an incremental rate increase of 20%, as compared to the proposed increase of 14.7%.

Q. The Company is proposing that the deferral balance be recovered over a 27 month period. How was the annual revenue requirement determined?

A. The actual calculation is reasonably straight-forward. The starting point is the beginning deferral balance at June 30, 2000. Additional deferrals as outlined by Mr. Norwood were added, as well as the benefits of the "PGE" credit which will be described below. The annual amount was determined through an iterative process that produced the annual revenue level necessary to reduce the deferral balance to approximately zero by December 31, 2003.

Q. Did that revenue level need to be adjusted to determine a final revenue requirement?

A. Yes. The annualized PCA revenue level necessary to reduce the deferral balance to zero by December 31, 2003 was $21,901,500. That figure is the starting point for the final revenue requirement calculation, as can be seen on page 1 of Exhibit No.___(DMF-1). The $21,901,500 amount must then be adjusted for revenue sensitive expenses, such as Commission Fees and Uncollectible Expense. Additionally, equity return deferrals associated with the Company's small generation projects, plus the Coyote Springs II Project, required an income tax gross up. The conversion factors used were the same calculations authorized in the Company's most recent general case, WWP-E-98-11, updated for actuals through December 31, 2000, and as filed with the Commission. The resulting revenue requirement is $23,567,942 for an overall surcharge increase of 19.4%. This calculation is illustrated on page 1 of Exhibit No. ___(DMF-1). This amount is ultimately reduced by the PCA surcharge that is currently in effect.

PGE CREDIT

Q. Please explain the Company's utilization of the "PGE" Credit in the determination of the surcharge increase?

A. The Company is currently amortizing the PGE monetization credit balance over a sixteen-year period (1999-2014) to match the original revenue stream under the PGE contract. The Company is proposing in this filing to accelerate the amortization of the PGE credit balance, beginning in October 2001, and apply the increased amortization against the deferred power cost balance, which would reduce the amount of deferred power costs that must be collected from customers through the surcharge. The Company is proposing that the amortization be increased to a level that would cause the PGE balance on Avista's balance sheet at October 1, 2001 to be fully amortized by December 31, 2002. This is one year earlier than the targeted date of December 31, 2003 to eliminate the power cost deferral balance. By using the PGE credits at a faster rate than the December 31, 2003 date, the overall surcharge to customers is decreased. The accelerated amortization of the PGE balance would not improve the Company's cash flow, since these entries would be non-cash accounting entries, but would mitigate the overall impact to customers from the power cost deferrals. The accelerated amortization of the PGE balance would reduce the deferred power cost balance by $34.6 million by December 31, 2002.

Q. How would the Company account for this accelerated amortization of the PGE credit?

A. The proposed accounting entries related to the accelerated amortization of the PGE balance would be to debit the PGE deferred revenue account and to credit the power cost deferral account, thereby reducing the power cost deferral balance to be recovered through the cash surcharge to customers.

Q. The Company's current proposal is for a 19.4% increase. What would the overall increase to customers have been if the PGE credit had not been used to mitigate the increase?

A. The overall increase to customers would have been approximately 33%.

Q. Does that conclude your direct testimony?

A. Yes, it does.

EXH. No.______

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CASE NO. AVU-E-01-11

EXHIBIT NO. ____ (DMF-1)

WITNESS: DON M. FALKNER, AVISTA CORP.

AVISTA CORP.
SURCHARGE REVENUE REQUIRMENT CALCULATION
IDAHO JURISDICTION

Line No.			ID
1	a	Annual State Surcharges Amounts before Conversion Factor Analysis	$21,901,500
		GROSS UP CALCULATION FOR EQUITY RETURN INCLUDED IN DEFERRAL	
2		Total Equity Deferrals for Owned Capital Projects	$6,108,901
3		Recovery Period in Months	27
4		Monthly Net of Tax Recovery	226,256
5		Annualized Net of Tax Recovery	2,715,067
6		Conversion Factor per 12/2000 CBR Reports	0.638934
7		Annualized Gross Revenue Req	4,249,370
8	b	Incremental Revenue for Equity Return Deferral Surcharge Gross Up	1,534,303
		GROSS UP CALCULATION FOR MISC REVENUE RELATED EXPENSES	
9		Annual State Surcharges before Conversion	21,901,500
10		Annualized Equity Return Recovery Component	2,715,067
11		Annual State Surcharges Net of Equity Return Recovery	19,186,433
12		Revenue Related Expense Conversion Factor per 12/2000 CBR Reports	0.99316
13		Annualized Gross Revenue Req for non-Equity Deferral Surcharge	19,318,572
14	c	Incremental Revenue for non-Equity Return Deferral Surcharge Gross Up	132,139
15	d	Total Surcharge Revenue Requirements d = a + b + c	$23,567,942
16		Normalized General Business Revenues	$121,675,000
		Overall General Business Percentage Increase	19.4%

AVISTA UTILITIES

Projected Idaho Electric Deferral Balances

Based on July 3 Forward Prices

Utilizing Surcharge of 19.4% (10/01 - 12/03) and 15 Month PGE Amortization