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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF AVISTA CORPORATION'S ANNUAL POWER COST ADJUSTMENT (PCA) FOR THE PERIOD JULY 1, 2007 TO JUNE 30, 2008	)	**CASE NO. AVU-E-07-7** **COMMENTS OF THE COMMISSION STAFF**

The Staff of the Idaho Public Utilities Commission, by and through its Attorney of Record, Donald L. Howell II, Deputy Attorney General, submits the following comments in response to Order No. 30402 issued on August 10, 2007.

BACKGROUND

On July 31, 2007, Avista Corporation dba Avista Utilities filed its annual Power Cost Adjustment (PCA) Application. Since 1989 the PCA mechanism has permitted Avista to adjust its PCA rates upward or downward to reflect differences from normal in the Company's "power supply costs." Due to its substantial reliance on hydroelectric generation, Avista's actual cost of providing electricity (its power supply costs) varies from year to year depending on changes in streamflow. Available streamflow dictates hydropower generation and the amount of hydropower generation affects the use of the Company's coal and natural gas fired resources along with its purchases and sales. The PCA captures differences from normal costs associated with the amount and cost of fuel and differences in purchase costs and opportunity sales revenues. Ninety percent of these differences from normal costs are charged to or credited to customers through the PCA rate. The other ten percent of the cost difference is absorbed by Company shareholders. The annual PCA surcharge or credit is combined with the Company's "base rates" to produce a customer's overall energy rate.

In Order No. 30361 issued June 29, 2007, the Commission approved two major changes to Avista's PCA methodology. First, the Commission changed Avista's PCA from a "trigger and cap" mechanism to a single, annual PCA rate adjustment. Order No. 30361 at 6. Second, the Commission changed the PCA rate design from an equal "percentage" basis to an equal "cents per kilowatt hour (kWh)" basis. *Id.* The Commission also authorized continuation of the existing 2.448% PCA surcharge until September 30, 2007. The Commission directed that these changes be implemented in this docket.

COMPANY FILING

In this PCA Application, Avista proposes to collect approximately $9.6 million from its Idaho customers during the October 2007 through September 2008 year for above normal power supply costs deferred during the 2006/2007 PCA deferral period. Because the current PCA surcharge recovers about $5.0 million annually, an increase of $4.6 million is required. The Company estimates that this increase results in an overall PCA rate increase of 2.22%. Application, Exh. RLM-1 at page 1. The Company proposes that the new PCA rate become effective October 1, 2007.

For the PCA year (July 1, 2006 through June 30, 2007), the Company reports that 90% of the unrecovered deferral balance was $10,573,518. Application at 3. The Company attributed above normal power supply costs to slightly reduced hydro generation and above normal natural gas fuel costs. Storro Direct at 2.

The deferral balance of $10,573,518 is reduced to $9,609,989 by adjustments that reflect expected surcharge revenues for July, August and September (-1,341,810), expected interest during the recovery period (323,110) and adjustments for Commission Fees and Uncollectibles (55,171). Consequently, Avista seeks a PCA surcharge of 0.267¢/kWh ($9,609,989/3,594,894,412 kWh = 0.00267 $/kWh).

Under the Company's proposal, the PCA surcharge rate for residential customers will increase from 0.163¢ per kWh to 0.267¢ per kWh, an increase of 0.104¢ per kWh. If approved, the monthly bill for the average residential customer using 1,000 kWh per month would increase by $1.04. The average monthly bill for a residential customer using 1,000 kWh would increase from $69.38 to $70.42, or an increase of approximately 1.5%.

With the implementation of an equal cent per kWh PCA rate, the percentage rate increase to the various customer classes will vary. The table below shows the proposed percentage increases in the PCA rates by customer group:

CUSTOMER GROUP (SCHEDULE)	PERCENTAGE CHANGE
Residential (1)	1.53%
General Services (11 & 12)	0.98%
Large General Services (21 & 22)	2.04%
Extra Large General Services (25)	3.86%
Pumping Services (31 & 32)	1.83%
Street and Area Lights (41 - 49)	-0.89%

McKenzie, Exh. RLM-1, Page 1 of 3

In spite of the overall increase proposed by the Company, Street and Area Lighting revenue requirement will decrease under the Company's proposal. The PCA calculations for the customer classes are shown on Company Exhibit RLM-1.

STAFF REVIEW

Audit Results

Staff has performed a review and audit of the amounts that went into the deferral balance in the current filing. Staff's review covered expenses incurred for the period July 2006 through June 2007. Staff was able to look at a representative cross section of transactions included in the Purchased Power account (FERC 555), Thermal Fuel account (FERC 501), CT Fuel account (FERC 547) and the Power Sales account (FERC 447). Based on our review of these transactions, Staff concludes that the accounting transactions appear reasonable at the time they were made. Staff also reviewed the other PCA calculations and amounts. Staff finds the amounts recorded to be correct and recommends that they be included in the deferral balance as of June 30, 2007.

Deferral Balance Components

The Company is requesting Commission approval for recovery of the Unrecovered Deferral Balance of $10,573,518 as of June 30, 2007. The Unrecovered Deferral Balance at June 30, 2007 is calculated by starting with the unrecovered balance at June 30, 2006, adding in the net deferral activity for the current period of July 1, 2006 through June 30, 2007, subtracting the amortizations related to surcharge revenues, and including interest on the deferral balance as directed by Commission Orders. In this year's balance, the Company is also requesting recovery of the over-refunded amount attributed to the Centralia gain recorded in November 2006.

• Unrecovered Balance at June 30, 2006	$1,517,103
• Net Deferral Activity (July 2006 - June 2007)	13,239,763
• Amortizations Related to Surcharge Revenues (July 2006 - June 2007)	-4,691,623
• Interest	501,895
• Centralia gain over-refund (recorded in November 2006)	6,380
• Unrecovered Balance at June 30, 2007	$10,573,518

Net Deferral Activity

The net deferral activity represents the Idaho jurisdictional share of the excess power costs and associated revenue adjustments deferred under the PCA mechanism by Avista for the twelve months ended June 30, 2007. The main component of the net deferral is the Net Increase in Power Supply Costs. Because power plants are economically dispatched, these PCA accounts also reflect additional power purchases when market prices are lower than generation costs. The associated reduced generation costs are also captured along with off-system sales revenues. The total net increase in power supply cost, $13,239,763, is comprised of the following eight items; an explanation of each item also follows:

1.	FERC Account 555 - Purchased Power	$40,492,050
2.	FERC Account 501 - Thermal Fuel	2,342,056
3.	FERC Account 547 - CT Fuel	8,813,479
4.	FERC Account 447 - Sales for Resale	-22,153,909
5.	All Potlatch Revenues and Expenses	-6,602,437
6.	Resource Optimization - Loss on Natural Gas Resold	743,271
7.	Idaho Retail Revenue Adjustment	-10,226,039
8.	Second Half Coyote Springs 2 Transmission Credit	-168,708
	Total	$13,239,763

1. Purchased Power costs reflect 90% of the Idaho jurisdictional share of the difference in costs the Company incurred for power purchases in the review period compared to normalized purchased power costs included in base rates. In the review period, the Company incurred more purchased power costs than are included in base rates. The positive amount represents a cost to customers.

2. "Thermal Fuel," primarily coal, is used to produce electricity. The amount is 90% of the Idaho jurisdictional share of the difference in costs the Company incurred for thermal fuel compared to the normalized amount included in base rates. During the review period the Company incurred more coal costs than are currently included in base rates. The positive amount represents a cost to customers.

3. "CT Fuel" is natural gas burned in the Company's gas fired generators. This amount represents 90% of the Idaho jurisdictional share of the difference in costs the Company incurred for gas generator fuel compared to the amount included in normalized base rates. In the review period, the Company incurred more natural gas costs than are currently included in base rates. The positive amount represents a cost to customers.

4. "Sales for Resale" are long-term and short-term off-system sales. The negative amount represents 90% of the Idaho jurisdictional share of the increase in off-system sales revenues above the amounts included in base rates. This negative amount represents a decrease in costs during the review period and is a benefit or credit to customers.

5. The Potlatch component is a direct assignment to Idaho of the difference in Potlatch costs and revenues (for its Lewiston facility) relative to the normalized Potlatch costs and

revenues established in the Company's last general rate case. The negative net amount indicates that, during the review period, the cost of serving Potlatch was less than the amount included in base rates. This negative amount is a PCA benefit to Idaho customers.

6. "Resource Optimization" amounts result when natural gas purchased in advance for use in generating plants is later sold because it is less expensive to sell the gas and purchase electricity than it is to generate electricity with the gas. Ninety percent of the Idaho jurisdictional share of the gain or loss on the sale of the gas is included in the PCA. Staff has verified that at the time the gas was initially purchased, the cost of producing electricity at Avista's natural gas plants, primarily the Coyote Springs facility, was less expensive than purchasing electricity on the open market to meet native load. Furthermore, Staff has verified that at the time the gas was resold, and electricity purchased to meet native load, that the resale of the gas and corresponding electricity purchased was the least expensive and most cost-effective alternative. The loss during the review period, shown as a positive amount, is a cost to Idaho customers.

7. The Idaho Retail Revenue Adjustment has three components. First, the load change adjustment is an adjustment to revenues that removes the power supply cost of serving new load from PCA calculations. Increases in power supply costs associated with load growth are reserved for consideration in general rate cases. The revenue adjustment for retail load growth is computed using the marginal cost of power supply. This amount is established whenever base power supply costs are reset. The marginal power supply cost for the current review period is $36.31/MWh. Marginal power supply costs are multiplied by the growth in load to produce the adjustment. The other two retail revenue components include a customer credit associated with Schedule 95 wind revenue and a customer credit for the purchase of Potlatch generation. Ninety percent of the Idaho Retail Revenue Adjustment is included in the PCA. The negative amount represents a benefit to customers.

8. The Coyote Springs 2 Transmission Credit began after the Company purchased the second half of Coyote Springs 2 and began including it in the PCA calculation in April 2005. The transmission credit for the second half of Coyote Springs 2 is equal to the transmission cost for the second half of Coyote Springs 2 that is included in base rates. This credit is included because the transmission for the second half of Coyote Springs 2 is not being provided through the purchase of transmission, but rather through a sale and purchase arrangement. The net cost of the sale and purchase arrangement is included in the actual power supply expenses in the PCA

deferral. If the credit were not included, the Company would collect twice for transmission costs for the second half of Coyote Springs 2. This credit will continue until base rates are reset.

Amortizations Related to Surcharge Revenues

During the July 2006 through June 2007 review period, a uniform percentage PCA surcharge was in effect. The surcharge level of 2.448% was effective April 15, 2005 from Case No. AVU-E-05-1. This PCA rate level coincided with the approval for purchase and rate base treatment of the second half of the Coyote Springs 2 generating facility. Those PCA rates were continued by the Commission in Order No. 29881, Case No.
AVU-E-05-6, the Company's annual PCA review. They were continued again in Case No. AVU-E-07-1, Order No. 30361.

The amount for amortizations related to surcharge revenues represents the amount of surcharge revenues for the twelve months ended June 30, 2007 net of the revenue related expenses of commission fees and uncollectibles. Staff reviewed the amount of monthly surcharge revenues and found them to be appropriately calculated and recorded.

Interest

The Company calculates interest on the deferral balance per Order No. 29323 in Case No. AVU-E-03-4. Staff reviewed the calculation of the interest and found the amounts included in the filing to be correct. The Company uses the Customer Deposit Rate on current year deferrals and the Customer Deposit Rate plus 2% on carryover balances from one year to the next. The Customer Deposit Rate for 2006 was 3% and the Customer Deposit Rate for 2007 is 5%.

In Order No. 29323 (Case No. AVU-E-03-4) the Commission found that it was appropriate to include a 200 basis point (2%) increase in the interest rate applied to Avista's year-end deferral balances during recovery. The Commission further found that the additional 200 basis point increase would apply beginning January 1, 2003 and continue through June 30, 2005 or until the deferral balance is fully recovered. In Order No. 30361 (Case No. AVU-E-07-1) the Commission found that, "for all practical purposes the PCA deferral balance was eliminated on March 30, 2006, when the deferral balance dropped from a high of $45.6 million to $1.5 million. We find it reasonable that the change in recovery method occur with the Company's year 2007 PCA adjustment (tentatively October 1 2007)."

Due to the way the balance is calculated to reflect the monthly deferrals, the deferral balance subject to the additional interest was not shown as being fully recovered, i.e. the amount booked did not reach a zero balance. It could not reach zero absent reduction in costs below base rates. Because the Commission found that the PCA deferral balance was eliminated in Order No. 30361, Staff believes the deferral balance permitted to earn the additional 2% interest has been eliminated and the additional interest ends.

Staff recommends that the change in interest calculation coincide with the change in recovery method from a uniform percentage basis to equal cents per kWh basis. Staff has discussed the proposed change in interest rate calculation with the Company, and it concurs with Staff, as long as the Company is not required to change the interest rate calculation for prior months. Staff proposes that the additional 200 basis point calculation be eliminated effective October 1, 2007. This prospective change will not require the Company to change prior interest rate calculations retrospectively.

CONSUMER ISSUES

Customer Notice and Press Release

The Press Release and Customer Notice included in Avista's PCA Application were reviewed and deemed to meet the requirements of IDAPA 31.21.02.102. The customer notice was mailed with cyclical billings beginning August 1, 2007 and ending August 30, 2007.

Customer Comments

Customers were given until September 7, 2007 to file comments. As of September 5, six comments had been received, all of which opposed the increase to PCA rates.

Financial Assistance for Paying Heating Bills

If approved, Avista's rates for residential customers will increase only slightly. But regardless of the rate per kilowatt-hour, there will always be some customers that find it difficult to pay their electric bills. Staff encourages those customers who qualify for energy assistance to apply for the federally funded Low Income Home Energy Assistance Program (LIHEAP) and other non-profit fuel funds such as Project Share. For more information regarding assistance programs, customers should contact the local Community Action Agency, Avista Utilities, the Idaho Public Utilities Commission, or the 2-1-1 Idaho Care Line.

STAFF RECOMMENDATION

Staff recommends the Commission accept the audited deferral balances presented in the Company's filing and approve the Company proposed PCA surcharge rate of 0.267 ¢/kWh effective October 1, 2007. Staff further recommends that the Company discontinue the additional 2% interest calculation effective October 1, 2007.

Respectfully submitted this 7th day of September 2007.

Donald L. Howell, II
Deputy Attorney General

Technical Staff: Keith Hessing
Kathy Stockton
Marilyn Parker

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 7TH DAY OF SEPTEMBER 2007, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF,** IN CASE NO. AVU-E-07-07, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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