

DECISION MEMORANDUM

TO: COMMISSIONER REDFORD
COMMISSIONER SMITH
COMMISSIONER KEMPTON
COMMISSION SECRETARY
COMMISSION STAFF
LEGAL

FROM: SCOTT WOODBURY

DATE: NOVEMBER 9, 2007

SUBJECT: CASE NO. AVU-E-07-10 (Avista)
APPLICATION FOR A DEFERRAL ACCOUNTING ORDER
(MONTANA LEASE PAYMENTS)

On November 1, 2007, Avista Corporation dba Avista Utilities (Avista; Company) filed an Application with the Idaho Public Utilities Commission (Commission) requesting an accounting order authorizing deferral of settlement lease payments. The deferred accounting request pertains to costs to be incurred as a result of the recent settlement of a lawsuit in the State of Montana over the use of the riverbed resulting from the Company's ownership of the Noxon Rapids and Cabinet Gorge hydroelectric projects located on the Clark Fork River.

Background

In October 2003, a lawsuit was originally filed against private owners of hydroelectric dams in Montana, including Avista. In this lawsuit, the State of Montana alleged that the hydroelectric facilities are located on state-owned riverbeds and the owners of the dams have never paid lease payments to the State for occupying such lands. The lawsuit requested lease payments prospectively and also requested damages for trespassing and unjust enrichment for periods of time dating back to the construction of the respective dams in the 1950s.

The Montana State Court previously ruled on several pre-trial motions for summary judgment, finding that, as a matter of law, the Clark Fork River was navigable and the State of Montana owns the riverbeds, that such lands are school trust fund lands, and therefore, the statutes of limitations have not run on the State of Montana's claims for prior damages. This left only the issue of damages to be decided at time of trial, set for October 22, 2007, with the State

asserting \$200 million owing by Avista for prior trespass since the dams were constructed, and \$8.4 million owing prospectively on an annual basis.

On October 19, 2007, the Company reached a settlement with the State of Montana resolving this matter. Application, Appendix 2, "Memorandum of Negotiated Settlement Terms." Pursuant to the settlement, Avista has agreed to make lease payments in the initial amount of \$4 million per year beginning February 1, 2008, for the calendar year 2007, and continuing through calendar year 2016, adjusted each year by the Consumer Price Index (CPI), with no payment for prior damage claims.

The level of the payments, the start date of the payments, as well as other terms and conditions of settlement, were all integral to the resolution of these claims. Because of the State's insistence on an initial payment in February 2008 for the year 2007, Avista contends it is necessary to have deferred accounting to address recovery of these costs.

On or before June 30, 2016, Avista and the State of Montana will determine whether the annual lease payments remain consistent with the principles of law as applied to the facts and negotiate an adjusted lease payment for the remaining term of Avista's Federal Energy Regulatory Commission (FERC) license for its hydroelectric facilities on the Clark Fork River, which expires in 2046. If Avista and the State of Montana do not agree on an adjusted lease payment, the parties will engage in advisory arbitration and submit the arbitrator's recommendation to the State Board of Land Commissioners (Land Board) for approval. The settlement also contains provisions that could reduce the amount of Avista's lease payments as a result of future judicial determinations in related cases or governmental actions.

Avista Corporation and the State of Montana will request a consent decree from the Montana State Court adopting the terms of settlement, as well as final approval by the State's Land Board.

In this filing, the Company is requesting an Order allowing for the deferral of lease payments. In the Company's next general rate case it will address the prudence and recovery of the settlement lease payments, and propose an appropriate amortization period for future recovery of the deferred costs. Avista contends that the Noxon Rapids and Cabinet Gorge hydroelectric projects are the Company's lowest-cost resources and are integral to the Company's resource base. The proposed accounting treatment would provide the Company with

the opportunity to recover the costs associated with owning and operating these projects, while customers receive the benefit from these low cost resources.

Proposed Accounting Treatment

Avista requests authority to defer the lease payments in Account 186 – Miscellaneous Deferred Debits. The lease payments would be allocated to the Washington and Idaho jurisdictions based on the production/transmission allocation in effect at the time that the deferrals are made and placed in separate Washington and Idaho 186 – Accounts. Interest would accrue on the Idaho share of the deferrals at the customer deposit rate. In the Company’s next general rate case, the Company would propose the recovery of an amortization of deferred lease payments and accrued interest that would be deferred prior to the effective date of rates established in the next general rate case. The amortization period would begin with the effective date of the new rates established in the next general rate case. In that rate case, the Company would also address recovery of the ongoing lease payments.

Commission Decision

Avista has requested an accounting Order allowing the deferral of Montana lease payments related to its ownership of the Noxon Rapids and Cabinet Gorge hydroelectric projects located on the Clark Fork River. The Company requests that the Order be issued by January 11, 2008, to facilitate the year-end closing of the Company’s accounting records. The Company and Staff recommend that this matter be processed pursuant to Modified Procedure, i.e., by written submission rather than by hearing. Reference Commission Rules of Procedure, IDAPA 31.01.01.201-204. Does the Commission agree with the recommended procedure?

Scott Woodbury

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