DECISION MEMORANDUM

TO: COMMISSIONER KJELLANDER
COMMISSIONER SMITH
COMMISSIONER HANSEN
COMMISSION SECRETARY
COMMISSION STAFF
LEGAL

FROM: DONOVAN E. WALKER

DATE: SEPTEMBER 19, 2006

SUBJECT: AVISTA'S 2006 PURCHASED GAS COST ADJUSTMENT (PGA), CASE NO. AVU-G-06-03

On September 14, 2006, Avista Utilities filed its annual Purchased Gas Cost Adjustment (PGA) Application with the Commission requesting authority to place new rate schedules in effect as of November 1, 2006 that will increase its annual natural gas revenues by approximately $2.7 million (3.2%). The PGA mechanism is used to adjust rates to reflect changes in the costs for the purchase of gas from wholesale suppliers including transportation, storage, and other related costs of acquiring natural gas. Avista's earnings will not be increased as a result of the proposed changes in prices and revenues. The Company requests that the Application be processed by Modified Procedure.

THE APPLICATION

According to Avista's Application if the requested price increase is approved the Company's annual revenue will increase by approximately $2.7 million or about 3.2%. The average residential or small commercial customer using 65 therms per month would see an estimated increase of $2.41 per month (3%).

Avista states that it purchases natural gas for customer usage and transports this gas over various pipelines for delivery to customers. The Company defers the effect of timing differences due to implementation of rate changes and differences between the Company's actual Weighted Average Cost of Gas (WACOG) purchased and the WACOG embedded in rates. Avista also defers the revenue received from the release of its storage capacity as well as various pipeline refunds or charges and miscellaneous revenue received from gas related transactions.

Avista requests an increase in the WACOG from its present 78.600 cents per therm to 84.712 cents per therm, an increase of approximately 6.112 cents. The proposed WACOG is based on a weighting of forward natural gas prices on August 16, 2006, and the Company's hedges executed to date. The Company executes hedges to fix the price of gas on approximately 66% of its estimated annual gas sales for the year, and uses a dollar-cost averaging approach for volumes to be hedged, with those volumes divided into 45-day execution windows between February 15 and November 15. The Company states that it has completed approximately 85% of its scheduled hedges for the upcoming PGA year, November 2006 through October 2007 at a weighted average price of $0.873 per therm.

This past year the Company has begun incorporating an amount of longer-term hedges into its purchase portfolio to provide an additional degree of rate stability. Approximately 11% of the total purchases for the next year have been hedged at a three-year fixed price. The Company's plan is to keep layering-in three-year fixed price hedges until these hedges represent one-third of the portfolio going forward. This plan has been incorporated into the Company's Risk Management Policy and provided to Commission Staff.

The Company's proposed rates in this filing also incorporate the proposed rate increases filed by the Company's two main pipeline suppliers, Northwest Pipeline and Gas Transmission Northwest. The proposed pipeline rates, while not yet approved, are set to begin being billed to Avista on January 1, 2007. The Company states that while these pipeline rate increases are substantial, the effect on the Company's proposed rates in this filing is completely mitigated by an increase in the estimated revenue to be received from pipeline capacity releases.

The Company is also proposing a change in the present amortization rate, which is used to refund or surcharge customers the difference between actual gas costs and projected gas costs from the last PGA filing over the past year. Avista proposes to decrease the amortization rate from the present surcharge of 5.027 cents per therm to 3.420 cents per therm. The Company states it has an estimated deferred gas cost balance of approximately $2.8 million as of October 31, 2006, reflecting higher gas costs than projected during the past year. The proposed amortization rate of 3.420 cents per therm is expected to recover this balance over 12 months.

The Company states that notice of its proposed increase in price has been accomplished by posting a notice at each of the Company's district offices in Idaho, a press release distributed to various informational agencies, and a separate notice to each of its Idaho gas customers included in their billing. Avista attached copies of these notices to its Application.

STAFF RECOMMENDATION

Given the proposed effective date of November 1, 2006, Staff recommends that this case be processed by Modified Procedure with comments due by October 24, 2005.

COMMISSION DECISION

1. Does the Commission preliminarily find that the public interest may not require a hearing to consider the issues presented, and that this proceeding may be processed under Modified Procedure?

2. Does the Commission wish to direct Staff to conduct a Public Workshop, pursuant to Rule 125, prior to Staff filing comments in this case?

3. Does the Commission wish to schedule a Public Hearing for this matter?

Donovan E. Walker