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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF AVISTA CORPORATION FOR AUTHORITY TO CHANGE ITS RATES AND CHARGES (2011 PURCHASED GAS COST ADJUSTMENT).

CASE NO. AVU-G-11-04

COMMENTS OF THE COMMISSION STAFF

The Staff of the Idaho Public Utilities Commission comments as follows on Avista Corporation's Application for authority to change its rates and charges (2011 Purchased Gas Cost Adjustment).

BACKGROUND

Initial Application

On August 15, 2011, Avista Corporation dba Avista Utilities (Avista; Company) filed its annual Purchased Gas Cost Adjustment (PGA) Application requesting authority to increase its annualized revenue by about $1.1 million (1.53%). Application at 1. The PGA mechanism is used to adjust rates to reflect annual changes in Avista's costs for the purchase of natural gas from suppliers – including transportation, storage, and other related costs. Avista says the proposed changes will not increase its earnings. The Company requests that its Application be processed by Modified Procedure and that its proposed rates become effective on October 1, 2011.

The Company states that if the proposed changes are approved, its annual revenue would increase by $1.1 million or 1.53%. The average residential or small commercial customer using 62 therms per month will see an increase of $0.99 or approximately 1.63%.

The Company buys natural gas for customer usage and then transports this gas through 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. The Company also defers various pipeline refunds or charges and miscellaneous revenue received from gas-related transactions.

Avista's Application proposes decreasing the WACOG from the currently approved $0.461 per therm to $0.423 per therm.

Avista proposes an amortization rate of approximately 4.7 cents per therm to refund approximately $1.6 million to customers over the 13-month period beginning October 1, 2011. Typically, the PGA rate adjustment takes effect on November 1. However, given several different rate adjustments proposed by Avista in other cases taking effect on October 1st this year, the Company timed its 2011 PGA filing to coincide with the effective date in those other cases, necessitating the need for a 13-month amortization of the PGA contra-balance.

Amended Application

On August 25, 2011, the Company updated its Application to further reduce the proposed WACOG to $0.418 per therm. Recent forward 30 day-average natural gas costs, which impact planned hedges and the pricing of index volumes, have decreased to a level lower than what the Company included in its original filing. The updated filing proposes to increase annualized revenues by approximately $0.7 million or about 0.98%, as opposed to the $1.1 million or 1.53% increase proposed in the original filing.

STAFF ANALYSIS

Staff reviewed the Company's Application (as amended) to determine whether its proposed adjustments to Schedules 150 and 155 reasonably capture its fixed (demand) and variable (commodity) costs. More specifically, Staff reviewed the Company's pipeline transportation and storage costs, fixed price hedges, estimates of future commodity prices, and its risk management policies. In addition, Staff reviewed the appropriateness of the Schedule 155 change in amortization rates that "true up" the expenses from the 2010 PGA. Each component of the rate changes will be discussed in greater detail below.

The Company requested the following rate changes that would result in an increase of approximately $0.7 million in annual revenue, or approximately 0.98%.

Table 1:

Schedule	Service	Proposed Schedule 150 Change per Therm	Proposed Schedule 155 Amortization Rate Change Per Therm	Proposed Total Rate Change per Therm	Overall Proposed Percentage Change
101	General	($0.03614)	$0.04697	$0.01083	1.10%
111	Large General	($0.03614)	$0.04697	$0.01083	1.40%
131	Interruptible	($0.04304)	$0.04777	$0.00473	0.81%

Under the proposed rates, a Schedule 101 residential or small business customer using an average of 62 therms per month will see an increase of $0.67 per month, or approximately 1.10%. Actual customer increases will vary based on the amount of therms consumed.

Schedule 150 – Purchased Gas Cost Adjustment

The Schedule 150 portion of the PGA consists of commodity costs (WACOG) and demand costs. The WACOG is the Company's forward-looking price of purchased gas and storage gas embedded in base rates. This also includes the benefit of some off system transactions, **(this section of Staff's Comments contains confidential information).**

The Company proposes a WACOG of $0.41797 per therm with this Application. The proposed WACOG is a reduction of 8.77% from the present $0.45817 per therm WACOG established by Order No. 32102. The demand costs represent the cost of pipeline transportation to the Company's distribution system. The Company proposes a demand cost increase of $0.00690 per therm. The Company attributes this increase in demand cost to a proposed rate case settlement between TransCanada – Gas Transmission Northwest (GTN) and their shippers (including Avista).

The Company delivers transported natural gas to its Idaho and Washington city- gates via two interstate transportation natural gas pipeline providers, Northwest Pipeline and TransCanada – Gas Transmission Northwest (GTN). Each provider has transmission pipelines running through the Company's service territory. The Company benefits directly from the geographic proximity to these transmission lines, each of which transmits natural gas from separate and distinct supply basins. This allows the Company to procure natural gas from the lowest cost supply basin to minimize commodity cost. Available capacity on these pipelines remains a key component in serving customers and maintaining supply diversity. The Company maintains that it continuously determines when its contracted interstate transportation supply is under-utilized due to warmer weather or industrial demand declines and will post for release to others with the release payments received benefiting the Company's customers.

Northwest Pipeline (NWP) supplies natural gas to northwest utilities from both Sumas and the Rockies. The utilities can purchase natural gas from either basin based on pricing; however, NWP retains the right to require the utilities to align their natural gas supply to the original design/contract **(this section of Staff's Comments contains confidential information).**

According to the Company, Sumas gas prices have typically been higher than both Rockies and AECO and, due to the price allocation established by Northwest Pipeline, the Company has utilized its proximity to GTN to acquire gas supply at lower commodity prices without incurring significant demand costs to acquire the gas supply.

Lower Rockies Basin prices have benefited natural gas utilities in the Northwest due to the Rockies' lack of pipeline infrastructure capable of moving Rockies gas east. However, Rockies Express pipeline, a 639 mile pipeline built to move gas east, was recently completed. This pipeline enables Rockies direct access to the eastern markets for the first time. In the past, the utilities in the Northwest holding NWP firm transport have benefited from lower priced Rockies gas caused by limited pipeline takeaway ability from the Rockies. This lower priced Rockies gas did act as a market indicator for the development of additional pipeline capacity (both new construction/greenfield, as well as through various expansions). Rockies Express was one of the new pipelines built to access the lower priced Rockies supply. This development caused Rockies prices to increase for a short period of time but production continued to grow and Rockies pricing again moved lower than other supply basins.

More recently, Ruby Pipeline was constructed as a response to lower Rockies prices. It was built from the Rockies to Malin, Oregon (the California/Oregon border). This increased pipeline infrastructure has since shifted pricing in the forward markets. For example, in the summer (Apr-Oct), Rockies gas was at a premium over the other delivery points and, for the winter Rockies, now is priced between Sumas and AECO.

The Company's diversity of supply basins has enabled it to hedge expected winter flowing gas requirements at favorably contracted prices to provide customers with lower priced natural gas.

Weighted Average Cost of Gas

Throughout the last year, the wholesale cost of natural gas has been low, which has allowed the Company to purchase gas for the coming year at favorable rates. This request reflects the fourth decrease within the Company's past five PGA filings, and makes the Company's proposal the lowest rate since a 2003 filing. The table below illustrates the changes in the natural gas market over the past nine years and the volatility experienced over the same period.

Year	Approved Weighted Avg. Cost of Gas $/Therm	% Change From Previous Year	Resulting Total General Service Schedule 101 Tariff, $/Therm	% Change From Previous Year
2002	0.34572	Base Year	0.75722	Base Year
2003	0.44989	30.13%	0.77716	2.63%
2004	0.55739	23.89%	0.95315	22.64%
2005	0.76786	37.76%	1.18692	24.53%
2006	0.76085	-0.91%	1.16175	-2.12%
2007	0.75544	-0.71%	1.1056	-4.83%
2008	0.78646	4.11%	1.15103	4.11%
2009*	0.75984	-3.38%	1.07507	-6.60%
2009	0.49093	-35.39%	0.88199	-17.96%
2010	0.45817	-6.67%	0.91553	3.80%
2011	0.41797	-8.77%	0.92636	1.10%

*The WACOG change was part of the AVU-G-09-01 settlement intended to offset the impact of the residential base rate increase approved in Order No. 30856.

The WACOG decline primarily has occurred because natural gas prices have continued declining due to regional and national economic weakness that reduced the weather-adjusted natural gas demand when natural gas supplies have been plentiful. A national report issued by the Energy Information Administration (EIA) in August 2011 provides insight into the anticipated conditions of the natural gas industry through 2012 in the areas of natural gas consumption, production, inventory and pricing. Natural gas consumption is forecast to increase 1.8% from 2010 levels, to

67.4 billion cubic feet per day (Bcf/d) in 2011 and increase slightly to 67.8 billion Bcf/d in 2012. Natural gas consumption in the industrial sector is projected to remain flat for the rest of 2011 and increase by approximately 1.8% through 2012. Electric power generation natural gas consumption is expected to increase by 3.7% through 2012. Extremely hot weather in the United States this past July contributed to an increase in consumption of natural gas for electric power to meet the increased air conditioning loads. As a result, electric power consumption in July 2011 increased by 4.2% compared to June 2011. Residential and commercial consumption through 2012 is projected to remain at levels comparable to those of 2010.

Natural gas production is expected to average 65.5 Bcf/d in 2011, which is a 5.9% production increase over 2010. This increased production is centered in the onshore production in the Lower 48 States offsetting production declines in the Gulf of Mexico. EIA forecasts that production will continue to increase in 2012, but at a slower pace of 0.9% growth. In addition, EIA forecasts that increased domestic production will decrease import natural gas volumes by 4.3 % in 2011 and by 3.7% in 2012. The EIA Report (August 2011) states that inventories held in underground storage in the lower 48 states is down slightly in 2011, 2.758 trillion cubic feet, as compared to the five-year average of 2.998 trillion cubic feet. Finally, natural gas spot price averaged $0.442 per therm in July 2011—$0.0013 per therm less than June 2010. EIA forecasts natural gas prices for the rest of 2011 to average $0.424 per therm, with an average price of $0.441 per therm in 2012.

Staff reviews publications relating to the natural gas industry throughout the year. However, two primary sources are used to develop forecasts, specifically: (1) NYMEX Futures Index and (2) EIA. For purposes of this Application, Staff reviewed the Company's proposed WACOG of $0.41797 and its forecasted natural gas prices through October 2012. Comparing the data from the above informational sources, forecasts, and the WACOG of other Pacific Northwest natural gas utilities, Staff believes that the Company's forecasted natural gas prices are reasonable.

Schedule 155 – Deferred Expenses

The Schedule 155 portion of the PGA is the amortization component of the Company's deferral account. When the Company pays more for gas than what is estimated in the preceding WACOG, a surcharge is assessed to customers. If the Company pays less for gas than what is estimated in the preceding WACOG, a credit is issued to customers. The proposed change in the amortization rates are an increase of approximately 4.7 cents per therm. This increase is a result of the large one-year refund amortization rate from the 2010 PGA being replaced by a smaller one-year (13-month) amortization rate proposed in this filing. The large refund balance from the 2010 PGA was almost completely amortized during the current PGA year resulting in a reduction in the refund amortization rate in this current PGA application. This reduction, coupled with the current refund balances of approximately $1.6 million, results in the increase of approximately 4.7 cents per therm.

Hedging Policies

As in prior years, the Company's gas procurement plan generally incorporates a structured approach for the hedging portion of the portfolio, while maintaining flexibility so the Company can make discretionary adjustments when wholesale gas markets present opportunities to reduce costs. Discretion is used in evaluating current volatility, forward curve shapes, and alternatives when considering price triggers. The Company continues to hedge utilizing a series of price targets. When prices decrease, target purchase volumes increase. The Company typically develops, establishes and implements the annual procurement plan by November or December of each year.

Procedurally, the Company utilizes a 30-day historical average of forward prices calculated by supply basin to develop an estimated cost for index/spot purchases. The estimated monthly volumes to be purchased by basin are multiplied by this 30-day average price for the corresponding month to determine estimated spot purchase costs. These index/spot purchase volumes represent approximately 30% of the Company's estimated annual load for the coming year. At the time of this Application, the price for this segment of the Company's annual gas volume is $0.390 per therm.

The Company maintains approximately 20% of the estimated annual volume in underground storage at the Jackson Prairie Storage Facility. At the time of this Application, the WACOG for the stored gas is $0.390 per therm.

As outlined in the Application, the Company has hedged gas purchases on both a periodic and discretionary basis throughout 2011 to meet Company needs for the forthcoming PGA year (November 2011 through October 2012). As of the date of the Application, 70% of the Company's estimated annual load requirements for the PGA year will be hedged at a fixed price, comprised of (1) 32% of volumes hedged for a term of one year or less, (2) 18% of volumes multi-year hedges from prior years, (3) 20% of volumes from underground storage. By the end of July 2011, planned hedge volumes have been executed at a weighted average price of $0.476 per therm.

According to the Company, average wholesale prices of natural gas remain similar to 2010 levels. However, cash prices over the storage injection season (April – September) have been slightly higher than 2010. This increased pricing level has caused storage WACOG to be higher than what is currently in rates. While cash prices are currently higher than a year ago, the forward natural gas prices for the upcoming PGA year have continued to drop. This decline has provided an opportunity to hedge natural gas at a cost below what is embedded in rates. The decreased hedge cost more than offsets the storage WACOG increase.

The Company meets with Staff quarterly to collaborate on the procurement plan given the wholesale natural gas environment. The Company will continue to (1) keep long-term hedges open for up to two or three years, depending on which strip triggers first; (2) keep price targets "open" all year; and (3) maintain the current minimum portfolio hedge percentage **(this section of Staff's Comments contains confidential information).**

Throughout the year, the Company communicates with Staff when it believes a decision is being made outside the scope of the normal procurement plan. Over the course of the year, the Company has continued to communicate with Staff regarding the Company's storage and procurement activities, **(this section of Staff's Comments contains confidential information)**.

CUSTOMER RELATIONS

Customer Notice and Press Release

The Customer Notice and Press Release were included with Avista's initial Application. The initial Application was received on August 15, 2011. Staff reviewed the customer notice and press release included with the initial Application and determined they were in compliance with the requirements of IPUC Rules of Procedure 125.04 and 125.05. IDAPA 31.01.01.125. The initial customer notice was mailed with cyclical billings beginning August 19, 2011 and ending September 20, 2011.

After Staff and Avista reached a settlement in Avista's General Rate Case, (AVU-G-11-01), the Company filed its revised Application in this case on August 26. Because Avista reduced its requested overall PGA increase from 1.53% to 0.98%, Staff determined it was not necessary for the Company to revise its customer notices.

Customer Comments

Customers were given until September 21, 2011 to file comments. As of September 19, no comments had been received.

Financial Assistance for Paying Heating Bills

If approved, residential customers will see an approximate 1% increase in their natural gas rates. Because some customers continue to struggle to make ends meet, Staff would like to remind qualified customers to take advantage of the energy assistance available through the federally-funded Low Income Home Energy Assistance Program (LIHEAP) and other non-profit fuel funds such as Project Share in Avista's northern Idaho service territory. For more information on these programs, customers may call the nearest Community Action Agency, Avista Utilities, the Idaho Public Utilities Commission, or the 2-1-1 Idaho Care Line.

STAFF RECOMMENDATION

Staff recommends that the Commission approve the change in natural gas rates as proposed in the Company's amended filing.

Respectfully submitted this 21st day of September 2011.

Weldon B. Stutzman for
Karl T. Klein
Deputy Attorney General

Technical Staff: Donn English
Doug Cox
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CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 21ST DAY OF SEPTEMBER 2011, SERVED THE FOREGOING **NON-CONFIDENTIAL COMMENTS OF THE COMMISSION STAFF,** IN CASE NO. AVU-G-11-04, BY E-MAILING AND MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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