

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

**IN THE MATTER OF THE APPLICATION)
OF AVISTA CORPORATION DBA AVISTA) CASE NO. AVU-E-07-10
UTILITIES FOR AN ACCOUNTING)
ORDER AUTHORIZING DEFERRAL OF) ORDER NO. 30492
SETTLEMENT 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 and interest accruals. 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 related to the Company's ownership of the Noxon Rapids and Cabinet Gorge hydroelectric projects located on the Clark Fork River. Without prior approval of deferral, a utility request for recovery of interim costs in its next general rate case could be denied under regulatory principles that prohibit retroactive ratemaking. The Commission in this Order authorizes the deferral of settlement lease payments and defers a decision on interest.

Background

In October 2003, a lawsuit was 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 and 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 (\$1.37 million) 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.

On November 21, 2007, the Commission issued a Notice of Application and Modified Procedure in Case No. AVU-E-07-10. The deadline for filing written comments was December 19, 2007. The Commission Staff was the only party to file comments. Staff recommends approval of the Company's request except for accrual of interest on the deferral. Avista in reply comments filed on January 14, 2008, argues the equity of permitting the accrual of interest from the time the initial \$4 million annual payment is made to the State of Montana on February 1, 2008 until such time as deferred lease payments are included in rates following a review in the Company's next general rate case.

In recommending denial of the Company's request for accrual of interest on the deferral, Staff contends that granting the Company the right to defer the underlying settlement payments is sufficient relief. No law, Staff states, directs the Commission to allow a carrying charge (accrual of interest) on deferral accounts. The Commission, Staff contends, has discretionary authority, affirmed by the Idaho Supreme Court, in determining whether to approve a carrying charge on a deferral account. Reference *Idaho Power Company v. Idaho State Tax Commission*, 141 Idaho 316 at 323; and Order No. 30235, p. 3, in Case No. IPC-E-06-06. (Deferral of costs related to the development of Grid West.)

When a utility requests an order authorizing deferred accounting in advance of the expenditure, the Commission is provided an opportunity to evaluate the necessity and anticipated benefit for customers before the Company incurs the expense. When the Commission has

ordered a carrying charge for a deferred expense, Staff notes that the carrying charge has been at the customer deposit rate. The customer deposit rate for 2007 and 2008 is 5%. Reference Order No. 30200 in Case No. GNR-U-06-03 and Order No. 30469 in Case No. GNR-U-07-01.

Staff recommends that recovery of an amortization of deferred lease payments be reviewed in the Company's next general rate case. Staff emphasizes that the Company is not currently seeking recovery of these costs and Staff makes no assurances on the level of these costs to be recommended for recovery during the Company's next general rate case.

In its reply comments, Avista acknowledges that there are past instances where, in the discretion of the Commission, interest was not accrued on a deferred balance. However, it is also true, Avista states, that the Commission has recognized the need to provide recovery of prudent investment in utility assets, and a return on investment, for assets that will be used in providing service to customers. This is also the case where dollars are spent that will either provide future benefits to customers, or will result in lower costs than would otherwise occur. Avista believes that that is the case here, where the prudent resolution of the litigation has resulted, in the Company's best judgment, in lower costs than otherwise would have occurred.

The Company notes that in the underlying lawsuit, the State of Montana asserted claims of \$200 million for prior trespass back to the 1950s, and future payments of \$8.4 million per year. Through negotiations, Avista was able to eliminate any prior payments, and reduced future payments to \$4 million per year with some escalation. The State of Montana was adamant, however, that payment should begin immediately, i.e., on February 1, 2008.

If accrual of interest is not approved in this proceeding, Avista states that it will not recover the cost of resolving this litigation. The payment to Montana, the Company contends, must be financed until the costs are recovered from customers, which is a direct cost to the Company. The Company believes that, when pursuing the best deal it can get on behalf of its customers, it is appropriate to have the opportunity to recover the prudently incurred costs, including financing costs. For those investment and expense items which can be anticipated, the Company has some opportunity to plan ahead for cost recovery through some form of regulatory filing. Lawsuits, however, the Company contends, may linger for years until a change in circumstances creates an opportunity for successful resolution through settlement. These opportunities, and the ultimate outcomes, are difficult to predict; therefore, it is also difficult to plan for timely rate treatment apart from deferred accounting with a carrying cost.

Commission Findings

The Commission has reviewed the filings of record in Case No. AVU-E-07-10 including the underlying Application, the comments and recommendations of Commission Staff and the Company's reply. Based on our review of the record, we continue to find it reasonable to process this case pursuant to Modified Procedure. IDAPA 31.01.01.204.

Avista has filed an Application for an order authorizing deferral of settlement lease payments. The proposed accounting treatment would provide the Company with the opportunity to recover February 2008 settlement lease payments in its next general rate case. Without a deferral order, recovery could be denied under principles of retroactive ratemaking. The deferred accounting pertains to costs to be incurred by Avista as a result of the recent settlement of a lawsuit in the State of Montana over use of the riverbed related to the Company's ownership of the Noxon Rapids and Cabinet Gorge hydroelectric projects located on the Clark Fork River. Staff agrees with the Company's proposed accounting treatment with the exception of the Company proposal to accrue interest on the Idaho share of the deferrals (\$1.37 million) at the customer deposit rate.

The Commission finds it reasonable to authorize the deferral of settlement lease payments until the Company's next general rate case. The Commission notes that Avista on January 17, 2008, filed a Notice of Intent to file a combined electric and natural gas general rate case on or after April 1, 2008. Reference IDAPA 31.01.01.122. In authorizing deferral, we note that the Company is not seeking immediate recovery of these costs. The Commission makes no assurances on the level of costs that it will approve for recovery.

The Company also requests that it be allowed to accrue interest on the Idaho share of deferrals. If accrual of interest is not approved in this proceeding the Company contends that it will not recover the costs of resolving this litigation. Recognizing that the Company has filed a Notice of Intent to file a general rate case, we find it unnecessary to make a decision at this time regarding accrual of interest. Because we expect the Company's rate case to be resolved by year-end 2008, we find that a delay in making a decision on interest will not adversely affect the Company's financial statements.

In authorizing the deferral of settlement lease payments, the accounting treatment that we authorize is as follows:

- Record the deferred lease payments in Account 186 – Miscellaneous Deferred Debits without Interest.
- Record the lease payments in separate Washington and Idaho accounts based on the production/transmission jurisdictional allocation in effect at the time that the deferrals are made.
- Delay amortization of the deferred costs until new rates are established in the next general rate case.

CONCLUSIONS OF LAW

The Idaho Public Utilities Commission has jurisdiction over Avista Corporation dba Avista Utilities, an electric utility, pursuant to authority granted in Title 61 of the Idaho Code and the Commission's Rules of Procedure.

ORDER

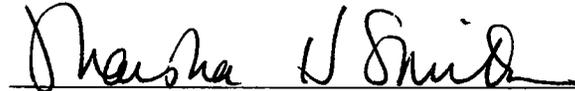
In consideration of the foregoing and as more particularly described above, IT IS HEREBY ORDERED and the Commission does hereby approve a deferral of settlement lease payments in the manner described above.

IT IS FURTHER ORDERED that the Commission's determination regarding authorized recovery of settlement expense including any amortization period and interest will be decided as part of the general rate case that Avista has indicated it will file later this year.

THIS IS A FINAL ORDER. Any person interested in this Order may petition for reconsideration within twenty-one (21) days of the service date of this Order. Within seven (7) days after any person has petitioned for reconsideration, any other person may cross-petition for reconsideration. See *Idaho Code* § 61-626.

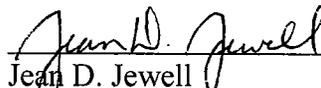
DONE by Order of the Idaho Public Utilities Commission at Boise, Idaho this 24th
day of January 2008.


MACK A. REDFORD, PRESIDENT


MARSHA H. SMITH, COMMISSIONER


JIM KEMPTON, COMMISSIONER

ATTEST:


Jean D. Jewell
Commission Secretary

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