

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION)
OF AVISTA CORPORATION FOR) CASE NO. AVU-E-05-1
AUTHORITY TO INCLUDE IN BASE RATES)
THE OWNERSHIP AND OPERATING) NOTICE OF APPLICATION
COSTS OF THE REMAINING SHARE OF)
THE COYOTE SPRINGS 2 GENERATING) NOTICE OF MODIFIED
PLANT AND TO REDUCE THE POWER) PROCEDURE
COST ADJUSTMENT (PCA) SURCHARGE)
TO OFFSET THE INCREASE IN BASE) ORDER NO. 29694
RATES)

On January 19, 2005, Avista Corporation filed an Application requesting authority to increase its Idaho electric rate base by \$62.5 million based upon its recent purchase of Mirant-Oregon's half of the Coyote Springs 2 generating plant. Prior to the purchase, Avista and Mirant-Oregon each owned half of the plant. Avista calculates that the addition to rate base would increase the Company's annual revenue requirement by approximately 1.89%, or \$3.235 million. Rather than increasing its rates, Avista proposes a \$3.2 million reduction in the customer PCA surcharge. Consequently, purchase of the plant would result in no net rate change to customers. The proposed reduction in the PCA surcharge would extend recovery of the deferred power cost balance by approximately 12 months to September 2007. Application at 7.

BACKGROUND

Coyote Springs 2 is a 280 MW natural gas-fired, combined-cycle combustion turbine plant located in Morrow County, Oregon. The Coyote Springs site was originally developed by Portland General Electric (PGE) and was designed for two gas-fired units. Coyote Springs 1 was completed in 1995 and is owned and operated by PGE. Avista began construction of the adjacent Coyote Springs 2 in January 2001 in conformance with its 2000 Integrated Resource Plan (IRP). Avista has an operating agreement with PGE for PGE to operate both units at Coyote Springs. Application at 11-12.

Like other hydro-based electric utilities in the West, Avista experienced extremely low water conditions coupled with unprecedented high wholesale market prices in 2000-2001. The combination of these conditions created serious financial challenges for Avista. In

particular, the Company was not able to secure financing for Coyote Springs 2. It subsequently entered into an Agreement with Mirant Corporation to sell half of the Coyote Springs 2 project to Mirant-Oregon.¹ In their Agreement, Mirant agreed to pay one-half of the capital costs of building the plant. Avista's costs for its half of Coyote Springs 2 were \$108 million. *Id.* at 13; n.11.

Although Coyote Springs 2 was originally scheduled to begin commercial operation in June 2002, operation of the project was delayed until July 2003 "because of the Enron bankruptcy, and problems with the generator step-up transformer" *Id.* at 13 (footnote omitted). After replacement of the transformer, Avista claims that Coyote Springs 2 has operated with a high availability factor of 97.6% and a forced-outage rate of less than 2%. Recent tests conducted in December 2004 also showed a favorable heat rate of 6,814 Btu/kWh. To avoid re-occurrence of problems with the step-up transformer, Avista has purchased a spare transformer from a different manufacturer. The spare transformer is now located at the plant and is included in Avista's incremental investment of Coyote Springs 2. *Id.*

NOTICE OF APPLICATION

A. The Purchase Transaction

YOU ARE HEREBY NOTIFIED that in July 2003, Mirant filed for Chapter 11 bankruptcy protection. Mirant and Avista subsequently entered into discussions about Avista purchasing Mirant's half of the plant. *Id.* at 14. Avista and Mirant-Oregon executed a Letter of Intent and subsequently executed a Purchase and Sales Agreement on October 13, 2004. *Id.*; Exh. L. As set out in greater detail in the Purchase and Sale Agreement, the negotiated purchase price is \$62.5 million. According to Avista, the \$62.5 million purchase price equates to a cost of \$439/kWh of installed capacity (140 MW). This price represents approximately 58% of Mirant's equivalent cost, i.e., \$108 million. *Id.* at 20. To satisfy bankruptcy concerns, the Purchase Agreement also contained a competitive auction provision that allowed other parties to bid for Mirant's half of the project. No other bids were submitted. The bankruptcy court approved Avista's \$62.5 million bid for the plant on December 15, 2004. *Id.* at 26.

YOU ARE FURTHER NOTIFIED that in November 2004, Avista submitted a Section 203 petition to FERC requesting permission to transfer the plant from Mirant to Avista.

¹ Mirant-Oregon LLC is a subsidiary of Mirant and was the actual half-owner of Coyote Springs 2.

No person commented or intervened in the FERC proceeding. Consequently, FERC approved the transfer to Avista on December 30, 2004. On January 20, 2005, Avista assumed ownership and began operating the entire plant. *Id.*

B. Benefits from the Purchase

YOU ARE FURTHER NOTIFIED that Avista maintains the purchase of the plant is very advantageous to ratepayers. Avista retained Navigant Consulting to conduct an analysis of the transaction. Exhibit K. As part of its analysis, Navigant reviewed other comparable transactions of combined cycle plants and determined that the average value of comparable natural gas plants in the western United States was \$569/kW – well in excess of Avista’s cost of \$439/kW for Mirant’s share. Application at 6; Table at 24. Navigant also determined that Avista’s purchase price was below the economic value of the plant, which was in the range of \$67 million.

YOU ARE FURTHER NOTIFIED that Avista asserts the purchase is also in compliance with the Company’s most recent IRP from April 2003. In its IRP, the Company identified a need to acquire approximately 149 aMW from natural gas-fired combined-cycle resources. Thus, acquiring the remaining half of Coyote Springs (140 MW) is consistent with the Company’s 2003 IRP long-term resource strategy. Application at 14-15. In terms of the Company’s annual loads and resources, acquisition of Mirant’s share of Coyote Springs 2 mitigates the forecasted supply deficits identified in the first, third, and fourth quarters of CYs 2005-2007. *Id.* at 15-19; Exh. H.

YOU ARE FURTHER NOTIFIED that Avista insists full ownership of Coyote Springs 2 improves the Company’s ability to economically operate the plant. Full ownership allows Avista to now make unilateral dispatching decisions days and months ahead of actual operations. In addition, decisions can be made faster in the event of unexpected plant outages or in the event capital upgrades or repairs are necessary. *Id.* at 21.

YOU ARE FURTHER NOTIFIED that as of January 20, 2005, Avista asserts that 90% of any margins earned from the recently purchased half will be credited to customers through the PCA. The proposed operating results and net power supply expenses, are contained in Exhibits A and M, respectively.

C. No Net Change in Rates

YOU ARE FURTHER NOTIFIED that the Company states in its Application that it “is not seeking an increase in overall rates presently in effect.” Application at 2. Avista maintains that adding the \$62.5 million purchase price to rate base would increase its annual base rates by \$3.235 million, or 1.89%. To offset this increase, Avista proposes to decrease the present PCA surcharge by \$3.182 million or 1.9%. These offsetting adjustments would allow the Company to earn its authorized rate of return of 9.25% (recently approved in the Company’s 2004 rate case, Case No. AVU-E-04-1).

D. Transmission

YOU ARE FURTHER NOTIFIED that Coyote Springs 2 is physically interconnected to the transmission system of the Bonneville Power Administration (BPA) which wheels power to Avista’s system. In its Application Avista notes that at present no additional annual long-term firm transmission capability is available from BPA to move more power from Coyote Springs 2 to the Company’s system. This transmission constraint is primarily limited to the second quarter of each year when BPA’s spring hydroelectric run-offs are at high levels. However, the Company reports that transmission capacity is generally available in the first, third and fourth quarters of the year when Avista normally needs generation. *Id.* at 22.

YOU ARE FURTHER NOTIFIED that Avista notes it has the option to acquire Mirant’s higher position in BPA’s queue for long-term transmission requests. Avista has also made its own long-term firm transmission request to BPA. Avista plans to participate in BPA’s 2005 open season for upgrade to the John Day-McNary Transmission Line that connects Coyote Springs 2 to Avista’s system. Avista does not foresee problems with acquiring sufficient natural gas transportation.

E. Request for Modified Procedure

YOU ARE FURTHER NOTIFIED that Avista maintains that this Application represents a single-issue case. The Company also notes this case follows closely on the heels “of a thorough examination of the Company’s books and records in the context of its just-completed rate case.” *Id.* at 8. Consequently, Avista requests that this Application be processed under Modified Procedure. The Company proposes an extended comment period until March 1 and a two-week reply period for the Company. The extended comment period would allow interested

parties to also conduct discovery. The Company states it “stands ready to quickly respond to discovery requests. To this end, Avista invites Staff and Interested Parties to immediately provide any discovery requests to Avista.” *Id.* at 9.

NOTICE OF MODIFIED PROCEDURE

YOU ARE FURTHER NOTIFIED that the Commission has reviewed the Application and has preliminarily determined that the public interest may not require a hearing to consider the issues in this case. Consequently, the Commission intends to process this Application under Modified Procedure, IDAPA 31.01.01.201-204. The Commission notes that Modified Procedure and written comments have proven to be an effective means for obtaining public input and participation.

YOU ARE FURTHER NOTIFIED that any person desiring to state a position on this Application may file a written comment in support or opposition with the Commission **no later than Tuesday, March 1, 2005**. The comment must contain a statement of reasons supporting the comment. Persons desiring a hearing must specifically request a hearing in their written comments. Written comments concerning this Application shall be mailed to the Commission and the Applicant at the addresses reflected below:

Commission Secretary
Idaho Public Utilities Commission
PO Box 83720
Boise, ID 83720-0074

Street Address for Express Mail:

472 W. Washington Street
Boise, ID 83702-5983

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These comments should contain the case caption and case number shown on the first page of this document. Persons desiring to submit comments via e-mail may do so by accessing the

Commission's home page located at www.puc.idaho.gov. Click the "Comments and Questions" icon, and complete the comment form, using the case number as it appears on the front of this document. These comments must also be sent to the Applicant at the e-mail addresses listed above.

YOU ARE FURTHER NOTIFIED that if no written comments or protests are received within the time limit set, the Commission will consider this matter on its merits and enter its Order without a formal hearing. If written comments are received within the time limit set, the Commission will consider them and, in its discretion, may set the same for formal hearing.

YOU ARE FURTHER NOTIFIED that Avista may file reply comments with the Commission **no later than March 15, 2005**.

YOU ARE FURTHER NOTIFIED that the Application, supporting workpapers and exhibits have been filed with the Commission and are available for public inspection during regular business hours at the Commission offices. The Application and supporting documents are also available on the Commission's Website at www.puc.idaho.gov under the "File Room" icon.

YOU ARE FURTHER NOTIFIED that all proceedings in this case will be held pursuant to the Commission's jurisdiction under Title 61 of the Idaho Code and specifically *Idaho Code* §§ 61-307, 61-336, 61-503, 61-523, and 61-622.

YOU ARE FURTHER NOTIFIED that all proceedings in this matter will be conducted pursuant to the Commission's Rules of Procedure, IDAPA 31.01.01.000 *et seq.*

ORDER

IT IS HEREBY ORDERED that this Application be processed under Modified Procedure. Persons interested in submitting written comments regarding this matter should do so no later than March 1, 2005.

IT IS FURTHER ORDERED that Avista may file a response to comments no later than March 15, 2005.

DONE by Order of the Idaho Public Utilities Commission at Boise, Idaho this 27th
day of January 2005.



PAUL KJELLANDER, PRESIDENT

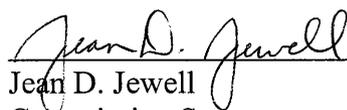


MARSHA H. SMITH, COMMISSIONER



DENNIS S. HANSEN, COMMISSIONER

ATTEST:



Jean D. Jewell
Commission Secretary

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