Office of the Secretary
Service Date
September 9, 2004

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF AVISTA CORPORATION FOR AUTHORITY TO INCREASE ITS PURCHASED GAS COST ADJUSTMENT (PGA) RATE.	**CASE NO. AVU-G-04-2** **ORDER NO. 29590**

On July 23, 2004, Avista Utilities (Avista, Company) filed its annual Purchased Gas Cost Adjustment (PGA) Application with the Commission for authority to place into effect on September 9, 2004, new rate schedules that will increase its annualized revenues by $7.8 million. The PGA account is a deferral mechanism for over- and under-collections and a true-up for spot market gas purchases. If its Application is approved, Avista's rates will increase on average by approximately 14.2% over last year's PGA rates. Because these adjustments reflect only changes in its gas-related costs, Avista's earnings will not be affected as a result of the proposed increase in prices and revenues.

The Commission issued a Notice of Application, Modified Procedure, and Comment Deadline on July 29, 2004. Order No. 29554. As of the August 26 comment deadline, the Commission had received comments from Staff and six Avista customers. After reviewing the comments and record in this case, the Commission grants the Application as set out in greater detail below.

THE APPLICATION

Avista believes this Application should be approved because it purchases natural gas from a subsidiary of Avista Corporation, Avista Energy, under the provisions of Tariff Schedule 163 (the Natural Gas Benchmark Mechanism). Avista transports this gas over Williams Pipeline West (d.b.a. Northwest Pipeline Corporation) and Westcoast Pipeline systems, deferring the effect of timing differences due to: 1) implementation of rate changes, and 2) differences between Avista's actual weighted average cost of gas (WACOG) purchased and the WACOG embedded in rates. Avista also defers the revenue received from Cascade Natural Gas for the release of storage capacity at the Jackson Prairie Storage Facility, various pipeline refunds or charges, and miscellaneous revenue received from gas-related transactions.

Avista filed proposed tariff sheet 150 that increases the prospective natural gas cost component included in the rates charged to customers by 11.730 cents per therm. This requested rate change consists of a 10.750 cents per therm increase related to the variable commodity cost of purchasing and transporting gas for customer usage and a .980 cents per therm increase related to fixed pipeline costs.

The commodity cost increase is based on a proposed increase in the present WACOG included in the Company's gas service schedules. Gas prices have increased markedly since the fall of 2003. The Company's present WACOG included in its gas sales rates is 44.989 cents per therm, which was approved by Commission Order No. 29342. The WACOG proposed in this requested increase is 55.739 cents per therm, reflecting the first-of-the-month (FOM) forward gas prices as of July 13 and hedges executed to date. FOM forward prices, weighted by basin, are multiplied by the monthly projected load requirements, less volumes hedged to date. The Company has executed three hedges to date for the coming winter (November-March) at an average price of 58.4 cents per therm. Additional hedges will be executed prior to this winter, with total hedged volumes representing approximately 50% of the total annual projected load requirements for the July 2004 – June 2005 period. Should future FOM or hedged prices substantially change the WACOG requested in this filing, Avista committed to revise this filing or submit an additional PGA filing to reflect those changes.

In this filing, Avista is <u>not</u> proposing to change the present amortization rate(s) set forth under Schedule 155. This amortization rate is used to refund or surcharge customers the difference between actual gas costs and projected gas costs from the last PGA filing. The Company has a deferred gas cost balance of approximately $3.3 million as of June 30, 2004, reflecting gas costs higher than those projected last year. However, the present amortization rate is a surcharge of 3.093 cents per therm. At this level, the present deferral balance will be recovered over an approximate 18-month period. The Company believes this estimated recovery period is reasonable and, given the substantial increase proposed in the WACOG, is not proposing a change to the amortization rate.

If the Commission approves the proposed increase, firm sales customers on Schedules 101, 111, 112, 121 and 122 will see a rate increase of 11.730 cents per therm. Interruptible sales customers on Schedules 131 and 132 will see a rate increase of 10.750 cents per therm. The

Application presumes that upon completion of this PGA tracker case, the Company's Tariff Schedule 150 will be changed to appropriately address both base rate and PGA tracker changes.

Avista proposes that the large transportation and interruptible customers be given the option of receiving/paying their portion of the deferred gas costs either through a lump sum credit/charge or through an amortization rate. If these customers choose the lump sum method, Avista proposes to adjust these billing credits/charges by the amount of interest that accumulates from the end of the test period used in this filing to the date of actual settlement. This proposal would clear out the small residual balances related to interest charges that are carried forward between PGA filings for large customers.

If the Application is approved, Avista states that the Company's estimated annual natural gas revenue will increase by approximately $7.8 million. Avista estimates that the average residential customer using 70 therms per month would see their monthly bill increase by approximately $8.21.

STAFF COMMENTS

Staff has reviewed the Application, performed an audit of the gas purchases from August 2003 through July 2004, and examined additional information supplied by the Company and third parties. Staff recommends that the Commission: 1) approve the Company's request to leave Schedule 155 at $.03093 per therm to recover the deferred balance in approximately 18 months, 2) approve the Company-requested WACOG of $0.55739 per therm, and 3) require the Company to file for an out-of-period rate decrease if the projected WACOG decreases 5% or more.

Staff believes that failure to increase rates to reflect market prices that have been volatile over the past five years would: 1) send an inappropriate price signal to customers, and 2) may also cause significant deferred gas costs accumulate and cause increases next year. Even with the increase proposed by the Company, gas cost deferrals could still occur. If the Company were to file based on August 13, 2004 forward prices, the WACOG would be about 2.5¢ higher than the proposed WACOG. Therefore, Staff recommends approving the Company's WACOG as requested. Considering market volatility and the possibility for price softening, Staff recommends that the Company be directed to file for an out-of-period rate decrease if the projected WACOG decreases 5% or more from the requested level.

In analyzing Avista's proposal, Staff noted that during the prior PGA period, the Company followed its price stabilization practice of systematically fixing portions of gas costs using financial instruments. These hedges provided substantial price protection and provided Idaho customers a benefit of $43,252 for the period.

Staff also discussed the ramifications of a Northwest Pipeline metering error. During a review of gas purchased from suppliers and sold to customers, Avista determined that it sold more gas to customers in the Lewiston area than it had purchased. Upon further investigation, it was determined that one of the Northwest Pipeline (Northwest) meters in the Lewiston area was set at a fixed-flow rate during September 2002 through February 2004. As a result, the deliveries to Lewiston from Northwest were significantly under-recorded and Avista owed the difference to Northwest. Northwest's tariff states that the gas must be replaced, and Avista was faced with purchasing significant amounts of gas from the current high-priced market. Because the gas is currently more expensive than during the time of the incorrectly set meter and the meter error was Northwest's fault, the Company was able to negotiate a settlement with Northwest to return less gas than was undercounted. Staff attached an analysis of the settlement agreement as Confidential Attachment A and the confidential settlement agreement between Avista and Northwest that details the amounts in question as Confidential Attachment B to its comments.

Because the allocation of pipeline and gas costs between Washington and Idaho is based on pipeline meter readings, the costs recorded during the meter error time period were incorrectly allocated. Staff has reviewed Avista's re-allocation of costs between Idaho and Washington and believes it accurately represents actual conditions. Because the error occurred in Idaho, the Idaho allocation will change and Idaho customers will be required to pay the majority of the costs associated with the meter error. The Company has appropriately re-allocated some of the costs originally assigned to Washington back to the Idaho deferral account. The approximately $3.5 million will be paid back through a $2.4 million increase in the Idaho deferral account and a $1.1 million increase in future gas costs.

PUBLIC COMMENTS

As of August 26, 2004, the Commission had received six comments from customers regarding the proposed 14.2% purchased gas cost adjustment. All opposed the increase. Comments from fixed-income customers stated it would be nearly impossible to pay higher rates for natural gas. As one customer stated, "I implore the Utilities Commission to reduce, if not deny outright, Avista's most recent request for rate increases." Several commenters cited the history of sizable rate increases over the past several years and insisted that the previously-approved rate increases should be sufficient for Avista's needs.

DISCUSSION AND FINDINGS

Avista gas rates are determined by adding variable PGA commodity rates to fixed base rates. In most years the base rate does not change – just the PGA rate changes. However, on September 9, 2004, both the base rates[1] and the PGA rates will change simultaneously. Consequently, the rate calculations in this Order that compare this year's rates to last year's rates are more complex than in most PGA Orders.

After reviewing the utility's Application, the record, and comments filed in this case, the Commission is required to establish "just and reasonable" rates. *Idaho Code* § 61-502. As we stated in the Notice of Application, the annual PGA tracker reflects only those changes in gas costs that are generally recognized as outside the Company's control. Order No. 29554 at 5. To collect the deferred balance owed by customers, the Commission finds it reasonable and appropriate to leave Schedule 155 at $0.03093 per therm. This will spread the deferral balance over 18 months rather than 12, mitigating the impact on customer rates. We further find that the projected gas prices found in Avista's proposed WACOG are just and reasonable in light of current market conditions. Should forward commodity prices decrease by 5% or more over the WACOG, we direct Avista to file for an out-of-period rate decrease to realign PGA rates with commodity prices.

For the foregoing reasons, we find it reasonable to increase the WACOG from $0.44989 to $0.55739 per therm. When combined with the adjustments, surcharges and credits, PGA rates per therm will increase on average by 14.2% over last year's PGA rate. The following table indicates the annualized change in PGA rates per customer class when viewed in isolation and in combination with the base rate changes approved in Order No. 29588:

[1] The Commission approved new base rates for Avista's gas and electric operations in Order No. 29588.

Customer Class	Schedule	PGA Rate Approved in this Order ($/therm)	PGA % Rate Change over Last Year's Rates	Ave. Overall Rate (PGA rates set in this Order + Base Rates set in O.N. 29588)	Ave. Overall % Increase over Last Year's Rates
General	101	$0.11730	14.23%	$0.99790	21.39%
Large General	111	$0.11730	15.92%	$0.87068	18.88%
Extra Large General	121	$0.10730	17.24%	$0.81034	19.09%
Interruptible	131	$0.10750	18.06%	$0.71130	19.51%
Transportation	146	none	none	$0.11360	7.43%

For example, an average customer taking general service under Schedule 101[2] using 73 therms will pay $72.85 per month, an average monthly increase of $12.84 (21.39%) over last year's overall rate.

The PGA rate approved in this Order shall become effective on September 9, 2004. The Commission orders Avista to adjust its billing and file new tariffs prior to implementing the new rate. *Idaho Code* § 61-618.

ORDER

IT IS HEREBY ORDERED that Avista's Application is granted. The Company shall file tariffs in conformance with a WACOG of $0.55739 per therm to be effective September 9, 2004. For meters read after September 9, 2004, usage will be pro-rated back to September 9, 2004. Avista shall promptly seek a rate adjustment if forward commodity prices decrease by 5% or more below this WACOG.

IT IS FURTHER ORDERED that Avista pass through its proposed permanent adjustments and temporary surcharges and credits to customers as filed.

IT IS FURTHER ORDERED that Avista continue to file updated WACOG projections quarterly.

THIS IS A FINAL ORDER. Any person interested in this Order (or in issues finally decided by this Order) or in interlocutory Orders previously issued in this Case No. AVU-G-04-2 may petition for reconsideration within twenty-one (21) days of the service date of this Order with regard to any matter decided in this order or in interlocutory Orders previously issued in this

[2] According to customer bills, nearly 99% of Avista's Idaho customers take service under General Schedule 101.

Case No. AVU-G-04-2. For purposes of filing a petition for reconsideration, this order shall become effective as of the service date. *Idaho Code* § 61-626. 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 8th day of September 2004.

Paul Kjellander

PAUL KJELLANDER, PRESIDENT

Marsha H. Smith

MARSHA H. SMITH, COMMISSIONER

Dennis S. Hansen

DENNIS S. HANSEN, COMMISSIONER

ATTEST:

Barbara Barrows

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