

DECISION MEMORANDUM

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

FROM: JOHN R. HAMMOND

DATE: AUGUST 14, 2003

RE: IN THE MATTER OF THE APPLICATION OF AVISTA CORPORATION FOR DETERMINATION OF THE INTEREST RATE TO APPLY TO THE POWER COST ADJUSTMENT DEFERRAL BALANCE. CASE NO. AVU-E-03-4.

On May 16, 2003, Avista Corporation dba Avista Utilities (Avista; Company) filed an Application requesting that the Commission issue an Order setting the interest rate that applies to the Company's Power Cost Adjustment (PCA) deferral balance at a higher level starting from January 1, 2003. The current rate is 2%, the rate for customer deposits as set by Commission Order No. 29158, Case No. GNR-U-02-2. *See also* IDAPA 31.01.01.106.02. On June 12, 2003, the Commission issued Notice of Application, Notice of Intervention Deadline, Notice of Modified Procedure and Notice of Comment Deadlines. Order No. 29264. The Commission Staff and the Company submitted written comments.

APPLICATION

Avista requests that the Commission grant it an exception to applying the Customer Deposit Rate to its PCA deferral balance because: 1) the current interest rate applicable to its PCA deferral balance is far below its cost of borrowing; 2) the large size of the Company's deferral balance; and 3) the use of a multi-year process to fully recover the balance. Avista requests that the Commission authorize it to apply a 2% adder or 200 basis points above the Customer Deposit Rate to its PCA deferral balance until that balance is fully recovered. Tallying the 2% adder with the 2003 interest rate would result in a rate of 4%. Avista currently expects the deferral balances to be fully recovered sometime in 2005. The Company requests that the increased interest rate apply to its PCA

balance until it is fully recovered. At that time, Avista contends the interest rate would revert to the Customer Deposit Rate without the adder.

SUMMARY OF COMMENTS

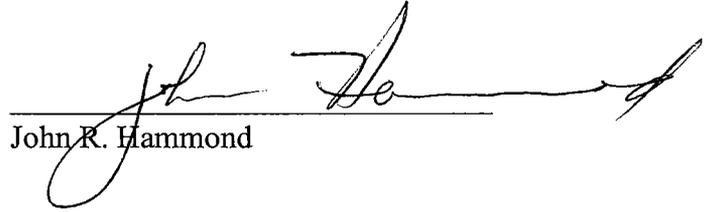
There are two primary issues to be decided; 1) the interest rate and 2) the time frame. Both Staff and Avista agree that a 200 basis point increase would be appropriate. The differences come when determining what balance the rate should be applied to and for how long. Avista argues it should apply to the full current balance for as long as there is a net balance. Avista notes it is like using the last in first out (LIFO) method of accounting for the surcharge. Staff's argument is like using the first in first out (FIFO) method of accounting where the balances accrued first are paid first. Staff's position is that only the balances left after a typical one-year recovery period should receive the higher interest rate. Staff recommended the higher rate be applied to any carry-over balances for two years, 2003 and 2004. If the recovery period is longer, Avista could request an additional exemption.

Subsequent to filing comments, Staff and Avista discussed and agreed to a compromise solution that allows a 200 basis point increase in the interest rate applied to year end deferral balances during recovery based on the first in first out (FIFO) method of accounting. The customer deposit interest rate would continue to apply to new deferral balances accrued during the calendar year.

This interest rate methodology would begin January 1, 2003 and continue through June 30, 2005. An example calculation of the methodology is shown on the attached spreadsheet. Staff and Avista believe that allowing the interest rate increase in this manner during the period proposed is reasonable given the continued large balances of deferred costs to be recovered. Both parties also agree that the period the interest rate methodology remains in place may be reassessed if actual deferrals or deferral recovery differ materially from current projections or from changes due to a general rate case.

COMMISSION DECISION

Does the Commission accept the 200 basis point increase as proposed by Staff and Avista?



John R. Hammond

Avista Corporation
Idaho PCA Interest Rate
Staff Proposed Method (For Illustrative Purposes)
2% Above Customer Deposit Rate on Carryover Balances
Annual Rollover from Current to Carryover

| Interest Rate | | 4% | 2% | Total |
|--------------------------|------------|---------------------|----------------|---------------------|
| | | <u>Carryover</u> | <u>Current</u> | |
| Carryover Balance | 12/31/2002 | \$30,925,711 | | \$30,925,711 |
| Jan-03 Deferral | Actual | | \$3,454,572 | 3,454,572 |
| Surcharge | Actual | -2,421,489 | | -2,421,489 |
| Interest | Actual | 103,086 | 0 | 103,086 |
| Net PCA balance | 1/31/2003 | \$28,607,308 | \$3,454,572 | \$32,061,880 |
| Feb-03 Deferral | Actual | | 1,245,118 | 1,245,118 |
| Surcharge | Actual | -2,227,385 | | -2,227,385 |
| Interest | Actual | 95,358 | 5,758 | 101,116 |
| Net PCA balance | 2/28/2003 | \$26,475,281 | \$4,705,448 | \$31,180,729 |
| Mar-03 Deferral | Actual | | 1,626,742 | 1,626,742 |
| Surcharge | Actual | -2,184,726 | | -2,184,726 |
| Interest | Actual | 88,251 | 7,842 | 96,093 |
| Net PCA balance | 3/31/2003 | \$24,378,806 | \$6,340,032 | \$30,718,838 |
| Apr-03 Deferral | Actual | | 332,541 | 332,541 |
| Surcharge | Actual | -2,052,187 | | -2,052,187 |
| Interest | Actual | 81,263 | 10,567 | 91,830 |
| Net PCA balance | 4/30/2003 | \$22,407,882 | \$6,683,140 | \$29,091,022 |
| May-03 Deferral | Actual | | 1,488,717 | 1,488,717 |
| Surcharge | Actual | -1,864,170 | | -1,864,170 |
| Interest | Actual | 74,693 | 11,139 | 85,832 |
| Net PCA balance | 5/31/2003 | \$20,618,405 | \$8,182,996 | \$28,801,401 |
| Jun-03 Deferral | Actual | | 1,101,792 | 1,101,792 |
| Surcharge | Actual | -1,885,592 | | -1,885,592 |
| Interest | Actual | 68,728 | 13,638 | 82,366 |
| Net PCA balance | 6/30/2003 | \$18,801,541 | \$9,298,426 | \$28,099,967 |
| Jul-03 Deferral | Estimate | | 740,205 | 740,205 |
| Surcharge | Estimate | -1,851,590 | | -1,851,590 |
| Interest | Estimate | 62,672 | 15,497 | 78,169 |
| Net PCA balance | 7/31/2003 | \$17,012,623 | \$10,054,128 | \$27,066,751 |
| Aug-03 Deferral | Estimate | | 2,289,329 | 2,289,329 |
| Surcharge | Estimate | -1,882,878 | | -1,882,878 |
| Interest | Estimate | 56,709 | 16,757 | 73,466 |
| Net PCA balance | 8/31/2003 | \$15,186,454 | \$12,360,214 | \$27,546,668 |
| Sep-03 Deferral | Estimate | | 1,784,173 | 1,784,173 |
| Surcharge | Estimate | -1,923,249 | | -1,923,249 |
| Interest | Estimate | 50,622 | 20,600 | 71,222 |
| Net PCA balance | 9/30/2003 | \$13,313,827 | \$14,164,987 | \$27,478,814 |
| Oct-03 Deferral | Estimate | | 1,112,634 | 1,112,634 |
| Surcharge | Estimate | -1,847,001 | | -1,847,001 |
| Interest | Estimate | 44,379 | 23,608 | 67,987 |
| Net PCA balance | 10/31/2003 | \$11,511,205 | \$15,301,229 | \$26,812,434 |
| Nov-03 Deferral | Estimate | | 1,050,791 | 1,050,791 |
| Surcharge | Estimate | -2,106,866 | | -2,106,866 |
| Interest | Estimate | 38,371 | 25,502 | 63,873 |
| Net PCA balance | 11/30/2003 | \$9,442,710 | \$16,377,522 | \$25,820,232 |
| Dec-03 Deferral | Estimate | | 1,273,813 | 1,273,813 |
| Surcharge | Estimate | -2,424,350 | | -2,424,350 |
| Interest | Estimate | 31,476 | 27,296 | 58,772 |
| Net PCA balance | 12/31/2003 | \$7,049,836 | \$17,678,631 | \$24,728,467 |

Avista Corporation
Idaho PCA Interest Rate
Staff Proposed Method (For Illustrative Purposes)
2% Above Customer Deposit Rate on Carryover Balances
Annual Rollover from Current to Carryover

| Interest Rate | | 4% | 2% | Total |
|--------------------------|------------|-------------------------|-----------------------|---------------------|
| | | <u>Carryover</u> | <u>Current</u> | |
| Carryover Balance | | \$24,728,467 | \$0 | \$24,728,467 |
| Jan-04 Deferral | Estimate | | 1,450,597 | 1,450,597 |
| Surcharge | Estimate | -2,678,880 | | -2,678,880 |
| Interest | Estimate | 82,428 | 0 | 82,428 |
| Net PCA balance | 1/31/2004 | \$22,132,015 | \$1,450,597 | \$23,582,612 |
| Feb-04 Deferral | Estimate | | 1,188,718 | 1,188,718 |
| Surcharge | Estimate | -2,465,275 | | -2,465,275 |
| Interest | Estimate | 73,773 | 2,418 | 76,191 |
| Net PCA balance | 2/29/2004 | \$19,740,513 | \$2,641,733 | \$22,382,246 |
| Mar-04 Deferral | Estimate | | 966,852 | 966,852 |
| Surcharge | Estimate | -2,364,425 | | -2,364,425 |
| Interest | Estimate | 65,802 | 4,403 | 70,205 |
| Net PCA balance | 3/31/2004 | \$17,441,890 | \$3,612,988 | \$21,054,878 |
| Apr-04 Deferral | Estimate | | 147,011 | 147,011 |
| Surcharge | Estimate | -2,141,729 | | -2,141,729 |
| Interest | Estimate | 58,140 | 6,022 | 64,162 |
| Net PCA balance | 4/30/2004 | \$15,358,301 | \$3,766,021 | \$19,124,322 |
| May-04 Deferral | Estimate | | 888,825 | 888,825 |
| Surcharge | Estimate | -1,943,100 | | -1,943,100 |
| Interest | Estimate | 51,194 | 6,277 | 57,471 |
| Net PCA balance | 5/31/2004 | \$13,466,395 | \$4,661,123 | \$18,127,518 |
| Jun-04 Deferral | Estimate | | 341,127 | 341,127 |
| Surcharge | Estimate | -1,894,281 | | -1,894,281 |
| Interest | Estimate | 44,888 | 7,769 | 52,657 |
| Net PCA balance | 6/30/2004 | \$11,617,002 | \$5,010,019 | \$16,627,021 |
| Jul-04 Deferral | Estimate | | 84,198 | 84,198 |
| Surcharge | Estimate | -1,898,037 | | -1,898,037 |
| Interest | Estimate | 38,723 | 8,350 | 47,073 |
| Net PCA balance | 7/31/2004 | \$9,757,688 | \$5,102,567 | \$14,860,255 |
| Aug-04 Deferral | Estimate | | 2,206,115 | 2,206,115 |
| Surcharge | Estimate | -1,908,031 | | -1,908,031 |
| Interest | Estimate | 32,526 | 8,504 | 41,030 |
| Net PCA balance | 8/31/2004 | \$7,882,183 | \$7,317,186 | \$15,199,369 |
| Sep-04 Deferral | Estimate | | 1,962,342 | 1,962,342 |
| Surcharge | Estimate | -1,994,990 | | -1,994,990 |
| Interest | Estimate | 26,274 | 12,195 | 38,469 |
| Net PCA balance | 9/30/2004 | \$5,913,467 | \$9,291,723 | \$15,205,190 |
| Oct-04 Deferral | Estimate | | 1,367,542 | 1,367,542 |
| Surcharge | Estimate | -1,893,832 | | -1,893,832 |
| Interest | Estimate | 19,712 | 15,486 | 35,198 |
| Net PCA balance | 10/31/2004 | \$4,039,347 | \$10,674,751 | \$14,714,098 |
| Nov-04 Deferral | Estimate | | 950,089 | 950,089 |
| Surcharge | Estimate | -2,157,100 | | -2,157,100 |
| Interest | Estimate | 13,464 | 17,791 | 31,255 |
| Net PCA balance | 11/30/2004 | \$1,895,711 | \$11,642,631 | \$13,538,342 |
| Dec-04 Deferral | Estimate | | 1,504,239 | 1,504,239 |
| Surcharge | Estimate | -1,902,030 | -581,244 | -2,483,274 |
| Interest | Estimate | 6,319 | 19,404 | 25,723 |
| Net PCA balance | 12/31/2004 | \$0 | \$12,585,030 | \$12,585,030 |

Avista Corporation
Idaho PCA Interest Rate
Staff Proposed Method (For Illustrative Purposes)
2% Above Customer Deposit Rate on Carryover Balances
Annual Rollover from Current to Carryover

| Interest Rate | | 4% | 2% | Total |
|--------------------------|------------|---------------------|----------------|---------------------|
| | | <u>Carryover</u> | <u>Current</u> | |
| Carryover Balance | | \$12,585,030 | \$0 | \$12,585,030 |
| Jan-05 Deferral | Estimate | | 1,311,740 | 1,311,740 |
| Surcharge | Estimate | -2,678,880 | | -2,678,880 |
| Interest | Estimate | 41,950 | 0 | 41,950 |
| Net PCA balance | 1/31/2005 | \$9,948,100 | \$1,311,740 | \$11,259,840 |
| Feb-05 Deferral | Estimate | | 937,648 | 937,648 |
| Surcharge | Estimate | -2,465,275 | | -2,465,275 |
| Interest | Estimate | 33,160 | 2,186 | 35,346 |
| Net PCA balance | 02-29-2005 | \$7,515,985 | \$2,251,574 | \$9,767,559 |
| Mar-05 Deferral | Estimate | | 709,178 | 709,178 |
| Surcharge | Estimate | -2,364,425 | | -2,364,425 |
| Interest | Estimate | 25,053 | 3,753 | 28,806 |
| Net PCA balance | 3/31/2005 | \$5,176,613 | \$2,964,505 | \$8,141,118 |
| Apr-05 Deferral | Estimate | | -148,515 | -148,515 |
| Surcharge | Estimate | -2,141,729 | | -2,141,729 |
| Interest | Estimate | 17,255 | 4,941 | 22,196 |
| Net PCA balance | 4/30/2005 | \$3,052,139 | \$2,820,931 | \$5,873,070 |
| May-05 Deferral | Estimate | | 391,278 | 391,278 |
| Surcharge | Estimate | -1,943,100 | | -1,943,100 |
| Interest | Estimate | 10,174 | 4,702 | 14,876 |
| Net PCA balance | 5/31/2005 | \$1,119,213 | \$3,216,911 | \$4,336,124 |
| Jun-05 Deferral | Estimate | | 15,129 | 15,129 |
| Surcharge | Estimate | -1,122,944 | -771,337 | -1,894,281 |
| Interest | Estimate | 3,731 | 5,362 | 9,093 |
| Net PCA balance | 6/30/2005 | \$0 | \$2,466,065 | \$2,466,065 |
| Jul-05 Deferral | Estimate | | -151,382 | -151,382 |
| Surcharge | Estimate | | -1,898,037 | -1,898,037 |
| Interest | Estimate | 0 | 4,110 | 4,110 |
| Net PCA balance | 7/31/2005 | \$0 | \$420,756 | \$420,756 |