

Avista distributes natural gas in northern Idaho, eastern and central Washington, and southwestern and northeastern Oregon. *Id.* at 2.² The Company buys natural gas and then transports it through pipelines for delivery to customers. *Id.* at 2. 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. *Id.* The Company also defers various pipeline refunds or charges and miscellaneous revenue received from natural gas related transactions, including pipeline capacity releases. *Id.* In its annual PGA filing, the Company proposes to (1) pass any change in the estimated cost of natural gas for the next 13 months to customers (Schedule 150); and (2) revise the amortization rates to refund or collect the balance of deferred gas costs (Schedule 155). *Id.* at 2, 4.

STAFF REVIEW

Staff has reviewed the Company's Application and performed an audit to verify the Company's earnings will not change as a result of the filing. Staff reviewed the Company's adjustments to Schedule 150 to determine if they reasonably capture Avista's fixed (demand) and variable (commodity) costs. More specifically, Staff has reviewed the Company's pipeline transportation and storage costs, fixed price hedges, estimates of future commodity prices, and its risk management policies. Additionally, Staff has reviewed the proposed Schedule 155 amortization rate to ensure that it properly captures all of the deferral account components. When combined, Schedules 150 and 155 make up the PGA. Each component will be discussed in greater detail below.

The Company proposes the following rate changes that would result in a decrease of approximately \$3.6 million in annual revenue, or approximately 5.4%

Service	Schedule No.	Commodity Change per Therm	Demand Change per Therm	Total Sch. 150 Change	Amortization Change per Therm	Total Rate Change per Therm	Overall Percent Change
General	101	(\$0.02931)	(\$0.00849)	(\$0.03780)	(\$0.00890)	(\$0.04670)	(5.02%)
Lg. General	111	(\$0.02931)	(\$0.00849)	(\$0.03780)	(\$0.00890)	(\$0.04670)	(6.31%)
Interruptible	131	(\$0.02931)	\$0.00000	(\$0.02931)	(\$0.00203)	(\$0.03134)	(6.06%)

² The Company also generates, transmits, and distributes electricity in northern Idaho and eastern Washington. *Id.*

Under the proposed rates, a Schedule 101 residential or small business customer using an average of 60 therms per month will see a decrease of \$4.42 per month, or approximately 7.9%. Actual customer decreases will vary based on the actual amount of therms consumed.

Schedule 150 – Purchased Gas Cost Adjustment

The Schedule 150 portion of the PGA is comprised of two parts: the commodity costs (WACOG) and the demand costs. The WACOG is the Company's forward-looking price of purchased gas and storage gas embedded in base rates. The demand costs represent the cost of pipeline transportation to the Company's distribution system, as well capacity releases which are credited back to customers. The proposed WACOG in this case is 33.3 cents per therm, which compares to 41.8 cents per therm approved in the Company's last annual PGA. However, the Company filed an interim PGA effective March 1, 2012 decreasing the WACOG to 36.2 cents per therm and providing customers with a decrease in rates of approximately 6%.

Weighted Average Cost of Gas (WACOG)

The WACOG is calculated in mid-July based on the cost of the Company's executed hedges, current underground storage, and its estimated index price for future deliveries. As of the date of this filing, the Company has already hedged 60% of its estimated load requirements for the upcoming year at fixed prices (including 20% underground storage), leaving 40% open to market variations. Throughout the last year there have been declines in the wholesale cost of natural gas, which have allowed Avista to purchase gas for the coming year at favorable rates. The weighted average cost of this year's planned hedged volumes is \$3.09 per dekatherm, including the weighted average cost of underground storage at \$2.10 per dekatherm. The Company estimates its index volumes will be procured at an annual weighted average price of \$2.98 per dekatherm.

For reference, the table below shows historical WACOG amounts, the difference to residential customer (Schedule 101) total bills, and the percentage change from previous years.

Year	Weighted Avg. Cost of Gas \$/Therm	% Change From Previous Year	Resulting Total General Service Schedule 101 Tariff, \$/Therm	% Change From Previous Year
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%	0.91464	-0.10%
2012	0.36216	-13.35%	0.85883	-6.10%
Proposed	0.33285	-8.09%	0.81213	-5.44%

*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.

Staff reviewed the natural gas industry fundamentals to determine whether the Company's executed hedges and estimated index prices for future delivery are reasonable. Staff utilized several sources, including: (1) the Energy Information Administration (EIA); (2) the Northwest Gas Association (NWGA); (3) the NYMEX Futures Index; and (4) the Natural Gas Exchange Inc. (NGX). The Short-Term Energy Outlook (STEO) published monthly by the EIA reports information on anticipated demand, production, imports/exports, inventories, and prices. The NWGA is made up of industry participants directly serving Washington, Oregon, Idaho and British Columbia. Each year it publishes a detailed ten-year look at expected natural gas demand, supply availability, and prices in the Northwest.

Price Fundamentals

Staff analyzed the EIA and Northwest Power and Conservation Council (NPCC) pricing forecasts, and the NYMEX and NGX forward prices. According to the EIA, the average Henry Hub price in July was just under \$3.00 per dekatherm, which is 33% lower than July 2011 prices.³ For comparison purposes, the Company's July 2012 WACOG dropped nearly 50% from last year, from \$3.52 to \$1.86 per dekatherm. According to the NPCC, the prices of natural gas

³ The 2011 AECO basis differential from Henry Hub was approximately (\$0.47) per dekatherm, whereas the Company's forward looking AECO basis differential for the PGA time frame averages (\$0.42) per dekatherm.

in 2011 and the first two quarters of 2012 were the lowest since 2002. EIA anticipates Henry Hub prices to finish the year at \$2.67 per dekatherm, 20% lower than the \$3.34 per dekatherm average price it expects in 2013. The NPCC expects Henry Hub prices to average \$3.20 per dekatherm in 2013 given its medium case scenario. Based on the Company's assumption that its purchases will be predominantly from AECO, it forecasts an average price of approximately \$2.98 per dekatherm during the 2013 PGA year.

The Company's forward-looking forecast for its index prices is developed based on a 30-day historical average of forward prices (ending July 19, 2012) from the AECO basin. Since approximately 70% of the Company's estimated monthly volumes typically come from AECO, the total volume was multiplied by the (30-day) average price. Staff compared the Company's forward looking price estimates for index gas purchases to a weighted average that also includes volumes purchased from Rockies and Sumas. After looking at the weighted average that included NYMEX prices for Rockies and Sumas, and the NGX forward prices for AECO, Staff determined the prices were similar to the Company's estimates.

Staff also evaluated the forward price trends shown in the Company's recently filed 2012 Integrated Resource Plan (IRP), primarily because the Company solicits the forecasting expertise of third party consultants. 2012 IRP, Figure 6.3, p. 6.5. Although there were differences in opinion when forecasting forward prices given the current market fundamentals, the near term 2013 price forecast of one consultant is similar to the Company's forecast given typical basin differentials.

The Company will continue to watch the market for changes that could materially impact natural gas prices moving forward. Similar to last year, if spring and summer prices significantly deviate from the proposed rates, Staff would expect the Company to return to the Commission with a new filing.

Based on its review of the market fundamentals to evaluate the Company's weighted average cost of its current hedges and its estimated cost of forward-looking index purchases, Staff believes the Company's hedges were prudent and its approach for estimating the forward prices reasonable. Staff recommends the Commission accept the Company's proposed WACOG of \$0.33285 per therm.

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 issued to customers. However, if the Company pays less for gas than what is estimated in the preceding WACOG, a credit is issued to customers. Gas prices have continued to fall throughout the year compared to the WACOG anticipated in the Company's last filing. In this Application, the Company proposes to increase the Schedule 155 amortization refund rate by \$0.00890 per therm (from \$0.02885 per therm to \$0.03775 per therm) which will refund approximately \$3.1 million to customers over the next 13 months, assuming normal weather.

A reconciliation of the deferral balance in this case is as follows:

Beginning Deferred Costs Balance	(1,584,903)
Wholesale Gas Costs Below WACOG	(2,925,726)
Demand Deferral and Capacity Release	(220,584)
Interest on Deferrals	(19,826)
Transfer to Amortization Account	1,078,948
Unamortized Balance from Prior PGA	625,694
Idaho Deferred State Income Tax Amortization	(6,165)
Total Deferred Amount Credited to Customers	(3,052,562)

The Settlement Stipulation in the Company's 2010 general rate case included an offset to the Company's natural gas revenues of \$0.5 million in Deferred State Income Tax (DSIT) credits to be amortized over a one-year period. The Company includes the remaining \$6,165 in the deferral balance being credited to customers in this case, which true's up the original amortization amount.

Hedging Policies

The Company develops its procurement plan based on a load forecast consistent with the methodology used for budgeting, rate making, and IRP planning. The Company's procurement plan includes hedging on a short-term (one year or less) and long-term (3 winters beyond the prompt year) basis. The hedges from the previous year's long-term discretionary hedging and anticipated storage withdrawals are deducted from the forecasted load. The remaining load requirements are served with either index (spot/cash) purchases or short-term hedges. The

short-term plan utilizes hedge windows which are open for a predetermined period of time and have upper and lower pricing levels that are market based. The long-term plan is driven by pricing targets that allow the Company flexibility to hedge at potentially favorable pricing levels. This flexibility in the procurement plan reduces costs to customers by allowing the Company to make discretionary adjustments when the wholesale gas market changes.

According to the Company, this year's market fundamentals indicate continued low prices during the 2012-2013 procurement plan year. In response to anticipated continued low prices, the portion of the Company's portfolio consisting of index gas is now about 40%, whereas last year it consisted of about 30% index purchases. Correspondingly, the portion of the Company's portfolio comprised of short-term and long-term hedges has decreased to 60% of the Company's portfolio, whereas last year it consisted of about 70% short-term and long-term hedges.⁴ The percentage of its volume met by short-term hedges has been reduced from 32% last year, to 11% this year. However, the Company increased the percentage of its volume met by multi-year hedges from 18% last year, to 29% this year. The Company has continued to keep 20% of its volume in underground storage.

Staff believes the Company's changes to its procurement plan continue to protect customers from the price risks of a changing market. By allocating more of its overall portfolio to index purchases while at the same time increasing the percent of hedged volumes on multi-year contracts, the Company is capturing the benefit of current low gas prices and mitigating customers' upward price risk. Staff encourages the Company to continue closely evaluating upward price risk, and to consider more multi-year hedges if favorable opportunities exist. Multi-year hedges can potentially capture the benefit of current low prices and maintain stable rates given changes in market fundamentals.

The Company meets with Staff semi-annually to discuss the Company's procurement plan. Throughout the year, the Company communicates with Staff when it makes decisions outside the scope of the normal procurement plan.

Other Considerations

On August 10, 2012, Avista filed a Notice of Intent to File a General Rate Case. Under the Commission's Rules this rate case could be filed as soon as October 10, 2012. See RP 122

⁴ The short-term and long-term hedge percentages include 20% of estimated throughput in underground storage.

(Utility must file notice of intent at least 60 days before filing a general rate case). In anticipation of a rate increase that may result from a general rate case, Staff proposes to hold back a portion of the decrease proposed by Avista in this case. Rather than increase the Schedule 155 amortization refund from \$0.02885 per therm to \$0.03775 per therm, Staff proposes to reduce the rate to \$0.01785 per therm. The effect of the Staff's proposal is to refund approximately \$1.55 million over the next 13 months instead of the \$3.1 million proposed by the Company. The remaining \$1.55 million un-refunded credit balance will remain in the PGA deferral account and accumulate interest until it is used to offset base rate increases or is returned to customers in a future PGA. Staff believes that the holdback can be used to reduce potential rate increases that could occur in the spring and fall of 2013, thereby improving rate stability in the long-run. Staff's proposal results in an October 1, 2012 rate decrease of approximately \$2.14 million in annual revenue, or about 3.2%. Staff's proposed rate adjustments are as follows:

Service	Schedule No.	Commodity Change per Therm	Demand Change per Therm	Total Sch. 150 Change	Amortization Change per Therm	Total Rate Change per Therm	Overall Percent Change
General	101	(\$0.02931)	(\$0.00849)	(\$0.03780)	\$0.009975	(\$0.02782)	(2.99%)
Lg. General	111	(\$0.02931)	(\$0.00849)	(\$0.03780)	\$0.009975	(\$0.02782)	(3.76%)
Interruptible	131	(\$0.02931)	\$0.00000	(\$0.02931)	\$0.015550	(\$0.01376)	(2.66%)

CUSTOMER RELATIONS

Customer Notice and Press Release

The Customer Notice and Press Release were included with Avista's Application. The Application was received on July 31, 2012. Staff reviewed the customer notice and press release and determined they were in compliance with the requirements of IPUC Rules of Procedure 125.04 and 125.05. IDAPA 31.01.01.125. Avista issued a Press Release covering four separate cases: the PGA (AVU-G-12-05), the PCA (AVU-E-12-06), the natural Gas Energy Efficiency Tariff Rider Adjustment (AVU-G-12-06) and the Electric Energy Efficiency Tariff Rider Adjustment (AVU-E-12-07).

The customer notices for this PGA case were mailed with cyclical billings beginning August 3, 2012 and ending September 4, 2012. In addition to providing information regarding its PGA request, Avista also included information regarding the natural Gas Energy Efficiency Tariff Rider Adjustment Case No. AVU-G-12-06.

Customer Comments

Customers were given until September 17, 2012 to file comments. As of September 10, 2012, two customers had filed comments. One customer mistakenly believed that Avista had requested a rate increase. That customer was informed by IPUC Staff that the Company had filed for a decrease to its natural gas rates. The second commenter applauded Avista for reducing rates during a time of economic hardship.

Financial Assistance for Paying Heating Bills

If the Company's proposal is approved, residential customers will see an approximate 8% decrease in their natural gas rates. (The PGA requests to lower rates by 5.4% and the Tariff Rider requests a 2.6% reduction to rates). Staff reminds all customers, struggling to pay utility bills, of the energy assistance that is available to qualified customers. Information regarding the federally-funded Low-Income Energy Assistance Program (LIHEAP) and local non-profit and other fuel funds such as Project Share in Avista's northern Idaho service territory can be obtained by calling the nearest Community Action Agency, Avista Utilities, the Idaho Public Utilities Commission, or the 2-1-1 Idaho Care Line.

STAFF RECOMMENDATION

After thoroughly examining the Company's Application and gas purchases for the year, Staff recommends the following:

1. Staff recommends the Commission approve the Company's proposed Schedule 150, including the proposed WACOG of \$0.33285 per therm; and
2. Staff recommends the Commission approve Staff's proposed Schedule 155 amortization rate of \$0.1785 per therm for the deferral balances. The combination of Staff's recommendations results in a decrease of approximately \$2.14 million, or about 3.2% of annual revenues.

Respectfully submitted this 17th day of September 2012.



Karl T. Klein
Deputy Attorney General

Technical Staff: Matt Elam
Donn English
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i:umisc/comments/avug12.5kkmedemp comments

CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 17TH DAY OF SEPTEMBER 2012, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF**, IN CASE NO. AVU-G-12-05, BY E-MAILING AND MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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SECRETARY