

No. 49347-1-II

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COURT OF APPEALS DIVISION II  
OF THE STATE OF WASHINGTON

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King County,

Appellant,

v.

Washington Utilities and Transportation Commission, a Washington state  
agency, and Puget Sound Energy,

Respondents.

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APPELLANT KING COUNTY'S REPLY BRIEF

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## ARGUMENT

### A. The WUTC and PSE Effectively Concede Key Points.

By failing to respond to King County's Opening Brief (Opening Brief) on the following points, the Washington Utilities and Transportation Commission ("WUTC" or "Commission")<sup>1</sup> and Puget Sound Energy ("PSE" or "Company")<sup>2</sup> have effectively conceded and admitted them:<sup>3</sup>

1. Schedule 85 governs replacement of electric distribution lines.<sup>4</sup>
2. Schedule 80 is a general tariff and is not specific to the replacement of electric distribution lines.<sup>5</sup>
3. Through their payment of Schedule 24 rates, the Maloney Ridge Line Customers ("Customers") fund capital replacements of parts of PSE's system from which they receive no benefit.<sup>6</sup>

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<sup>1</sup> The Brief of Respondent Washington Utilities and Transportation Commission will be referred to herein as the "WUTC Brief".

<sup>2</sup> Respondent Puget Sound Energy's Response Brief will be referred to herein as the "PSE Brief".

<sup>3</sup> See *Darkenwald v. State Emp't Sec. Dep't.*, 183 Wn.2d 237, 248, 350 P.3d 647 (2015) ("[I]ssues not supported by argument and citation to authority will not be considered on appeal.") (alteration in original) (citation omitted).

<sup>4</sup> See, e.g., Opening Brief at 10 (citing AR000647 and AR000658); Opening Brief at 20 (citing Appx. 149-50 (Logen, TR. 46:1-47:2)); Opening Brief at 36-37.

<sup>5</sup> See, e.g., Opening Brief at 36-37.

<sup>6</sup> See, e.g., Opening Brief at 9 (citing AR000367, lines 3-5 (Gorman Testimony: PSE's Maloney Ridge Line Customers "have for many years and continue today to pay Schedule 24 rates that help fund capital replacements for other parts of the PSE system from which [they] derive no benefit.")); Opening Brief at 44-45 (same)). WUTC's

4. The Maloney Ridge Line needs to be replaced.<sup>7</sup>
5. PSE is the sole and exclusive owner of the line.<sup>8</sup>
6. The Customers have argued throughout this case that the Maloney Ridge Line is part of PSE's system.<sup>9</sup>

**B. This is a Tariff and Contract Interpretation Case; Not a Ratemaking Case.**

This case always has been, and remains, a contract and tariff interpretation case. PSE's and the WUTC's last-ditch efforts to style it a ratemaking case mischaracterize the Customers' petitions and briefs, the regulatory framework of ratemaking, and the proceedings below.<sup>10</sup>

A rate case is a proceeding in which a regulated utility commences an action before the Commission to establish customer rates. RCW 80.04.130(1) ("*whenever any public service company shall file with the commission any schedule, classification, rule, or regulation . . . the commission shall have power . . . to enter upon a hearing concerning such proposed change*") (emphasis added); WAC 480-07-505(1) (defining a

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windfall argument, *see* WUTC Brief at 10, is contradicted by the fact the Customers have paid and continue to pay for capital replacements for which they receive no benefit. At best, a decision ordering PSE to pay to replace the line will allow the Customers to continue to receive service on a line necessary for public safety.

<sup>7</sup> *See, e.g.*, Opening Brief at 10-11.

<sup>8</sup> *See, e.g.*, Opening Brief at 39 (citing AR000030, ¶ 2); Opening Brief at 46.

<sup>9</sup> PSE and the WUTC admit the Customers argued throughout that the Maloney Ridge Line is part of PSE's system. *See, e.g.*, PSE Brief at 31; WUTC Brief at 9.

<sup>10</sup> *See, e.g.*, WUTC Brief at 1; PSE Brief at 12-13.

general rate proceeding as a “filing by any regulated company specified in WAC 480-07-500 for an increase in rates”).<sup>11</sup> The WUTC itself defines general rate cases as “formal requests” through which “regulated companies . . . receive approval from the commission to adjust the rates they charge for service.”<sup>12</sup>

The Maloney Ridge Line Customers are not a regulated utility and they did not file a ratemaking case. Rather, they filed a petition asking the WUTC to interpret the Service Agreements and Schedule 85 governing their relationship with PSE for service through the Maloney Ridge Line. At most, the Customers asked the WUTC to interpret contracts and tariffs as a precursor to a general rate case.<sup>13</sup> They did not, however, institute a rate proceeding—that is, they did not file a proposed schedule,

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<sup>11</sup> See also *Gen. Tel. Co. of the Nw. v. Wash. Utils. & Transp. Comm'n*, 104 Wn.2d 460, 465, 706 P.2d 625 (1985) (“The utility commences the ratemaking process by filing with the Commission for a rate increase.”); *Wash. State Att’y Gen.’s Office v. Wash. Utils. & Transp. Comm’n*, 128 Wn. App. 818, 822, 116 P.3d 1064 (2005) (“[A]cting under WAC 480-07-505(1), PacifiCorp filed a general rate increase case with the Commission. It sought a \$25.8 million annual increase in its base rates charged to Washington electric customers.”). In order for the Commission to consider a rate case filed by an electrical company, the company must include particular evidence and exhibits. WAC 480-07-510.

<sup>12</sup> See Wash. Utils. & Transp. Comm’n, *Ratemaking Process* (2012), available at <https://www.utc.wa.gov/consumers/Documents/2012-3%20UTC%20Fact%20Sheet-%20Energy%20Ratemaking.pdf>.

<sup>13</sup> See, e.g., Petition for Declaratory Order, AR000025, ¶ c (“PSE should replace the Maloney Ridge Line and include all the capital costs of such replacement in its generally applicable rates **when it files its next general rate proceeding.**”) (emphasis added). The Customers’ Petition for Declaratory Order to the Commission merely stated certain statutes *may* be implicated by the filing and proceeding. AR000007, ¶ 5. Regardless, because they are not regulated utilities, the Customers cannot initiate a ratemaking proceeding. See, e.g., RCW 80.04.130(1); WAC 480-07-505.

classification, rule or regulation “for an increase in rates.” WAC 480-07-505. Instead, the Customers asked the Commission to interpret existing contracts and tariffs to determine which party should bear the cost of replacing the line.

The WUTC incorrectly argues the Maloney Ridge Line Customers “expressly asked the Commission to exercise its ratemaking authority under RCW 80.28.010.” WUTC Brief at 16. Not only is this argument an inaccurate description of the Customers’ request, the referenced statute merely enumerates the duties of utilities to provide just, reasonable and *sufficient* rates, services, and facilities.<sup>14</sup> The Customers asked the Commission to consider that statutory provision because it shows that by failing to pay to replace the Maloney Ridge Line, PSE violated its duty to provide sufficient service to its Maloney Ridge Line Customers.

Further, because the line has not yet been replaced, related costs are not yet eligible for rate recovery. Absent certain circumstances not applicable here, the Commission may include in its rate calculation only property that is “used and useful”. RCW 80.04.250. Unused or unusable property may not be included in ratemaking determinations. *See People’s Org. for Wash. Energy Res. v. Wash. Utils. & Transp. Comm’n (POWER*

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<sup>14</sup> RCW 80.28.010 (describing electric utility’s duties as to rates, services, and facilities).

*Id.*, 101 Wn.2d 425, 430, 679 P.2d 922 (1984) (Commission may only determine value of property “which is employed for service in Washington and capable of being put to use for service in Washington.”). This requirement is demonstrated in the Commission’s decision in *Wash. Utils. & Transp. Comm’n v. Avista Corp.*, Docket Nos. UE-090134, UE-090135, UG-060518, Order No. 10, 2009 WL 5061998 (WUTC Dec. 22, 2009). In that case, the Commission declined to include a power purchase agreement in its rate calculation because the agreement had not yet been executed by the parties and was not included in the record. *Id.* at ¶¶ 203-04. The Commission found this constituted “not mere technical deficiencies in [Avista’s] case . . . [but] failure on the part of the Company to bring a matter properly before [the Commission].” *Id.* at ¶ 207. The replacement Maloney Ridge Line is not currently “used and useful” for utility service in Washington. For this additional reason, this is not and has never been a ratemaking proceeding.

Even if this were a ratemaking case—it is not—a one-time payment averaging \$46 per Schedule 24 customer would fall squarely within the zone of reasonableness for rates.<sup>15</sup> Rates need not be mathematically precise; a “rate decision [will] be affirmed if it [falls]

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<sup>15</sup> \$5.3 million dollars divided by 115,000 Schedule 24 customers, *see* WUTC Brief at 5 (citing AR 000598), results in an on average one-time payment of \$46 per customer.

within the ‘zone of reasonableness’.” *People’s Org. for Wash. Energy Res. v. Wash. Utils. & Transp. Comm’n (POWER II)*, 104 Wn.2d 798, 811, 711 P.2d 319 (1985). Similarly, according to the end-result doctrine, rates can be determined by any method, so long as they “enable the [utility] to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for risks assumed.” *Id.* (citations and quotation marks omitted). The Schedule 24 increase necessary to replace the Maloney Ridge Line is the very definition of reasonable—the rate impact would be a mere 0.2 percent.<sup>16</sup> This would not constitute unjust discrimination and is well within the zone of reasonableness for rates.

Moreover, the Maloney Ridge Line Customers would expect to—and do—share in the costs to replace lines serving other Schedule 24 customers—from which they receive no benefit—just as those customers should share in the costs to replace the Maloney Ridge Line.<sup>17</sup>

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<sup>16</sup> Order 03, CP 31, ¶ 30 (“PSE could recover [replacement] costs from all Schedule 24 customers with only a *de minimis* 0.2 percent rate increase.”); AR000847 (“[T]he revenue requirement increase to schedule 24 customers would be 0.2 percent assuming that the 5.3 million was applied to schedule 24 customers.”).

<sup>17</sup> The Maloney Ridge Line Customers’ Schedule 24 rates fund capital replacements and improvements on PSE’s distribution system from which other PSE customers derive the sole benefit to the exclusion of the Maloney Ridge Line Customers. AR000175 (“The Petitioners’ payment of Schedule 24 rates cover costs of PSE’s basic distribution system.”); AR000367, lines 3-5 (“Petitioners have for many years and continue today to pay Schedule 24 rates that help fund capital replacements for other parts of the PSE system from which Petitioners derive no benefit.”).

### **C. Schedule 85 Requires PSE to Pay to Replace the Line.**

Contrary to PSE's and the WUTC's arguments and representations, the Maloney Ridge Line is subject to Schedule 85 and the express terms of that tariff obligate PSE to pay to replace the line.

*i. The Maloney Ridge Line is subject to Schedule 85.*

PSE's insistence that "the Maloney Ridge Line was installed pursuant to the original Service Agreement and not Schedule 85" and that therefore Schedule 85 does not apply<sup>18</sup> is directly contradicted by the text of the Service Agreements: "This Agreement is subject to the General Rules and Provisions (Schedule 80) of [PSE's] Electric Tariff G **and to Schedule 85** of such Tariff, **as such Schedules may be revised from time to time**["<sup>19</sup> This language is plain and clear. The Maloney Ridge Line is subject to Schedule 85.

*ii. Schedule 85 applies with special force because it applies specifically to distribution line replacements.*

When interpreting tariffs, courts apply the tariff provision applicable to the particular situation at hand. *See Citoli v. City of Seattle*, 115 Wn. App. 459, 483, 61 P.3d 1165 (2002) (applying the force majeure

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<sup>18</sup> PSE Brief at 22.

<sup>19</sup> AR000032, ¶ 10 (emphasis added). Counter to its own argument that Schedule 85 does not apply, PSE argues that, when the line was installed, Schedule 85 had a paragraph permitting PSE to consider economic feasibility. PSE Brief at 7. The Service Agreements are, however, clear: they are subject to Schedule 85 as it "may be revised from time to time", not as it existed when the line was originally constructed. "The economic feasibility provision is no longer in Schedule 85[.]" PSE Brief at 8.

notice provisions rather than the emergency notice provisions of PSE's utility tariff), *review denied*, 149 Wn.2d 1033 (2003).<sup>20</sup> Schedule 85 expressly addresses the replacement of electric distribution lines—the exact situation here. AR000647, Sheet No. 85 (the tariff “sets forth the circumstances, terms, and conditions under which [PSE] is responsible for the ownership, installation, maintenance, repair *or replacement of distribution facilities*”) (emphasis added). It therefore takes precedence over Schedule 80 and any suggestion to the contrary is unpersuasive at best. *See, e.g., Citoli*, 115 Wn. App. at 483 (describing disagreement over application of PSE's force majeure tariff provision as “somewhat silly”).

*iii. Schedule 85 requires PSE to pay to replace the line.*

Schedule 85 makes PSE responsible for replacing the Maloney Ridge Line, including paying for that replacement. In the context of Schedule 85, responsible is not a vague or ambiguous term. *See N. Pac. Ry. Co. v. Sauk River Lumber Co.*, 160 Wn. 691, 694, 295 P. 926 (1931) (“In interpreting a tariff, the terms used, when they are not defined therein, should be taken in the sense in which they are generally understood and accepted commercially.”). Consistent with its generally understood and

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<sup>20</sup> *See also Waste Mgmt. of Seattle, Inc. v. Utils. & Transp. Comm'n*, 123 Wn.2d 621, 630, 869 P.2d 1034 (1994) (“A specific statute will supersede a general one when both apply.”) (citations omitted).

accepted definition, responsible means liable for the costs to replace, physically replacing, and overseeing replacement. *Webster's Third New Int'l Dictionary* 1935 (Philip G. Gove et al. eds., 1966) (defining responsible as "creditable or chargeable with the result . . . liable"). These responsibilities are PSE's unless altered by conditions in a customer contract. AR000658, Sheet No. 85-k, § 1(A) ("The Company shall . . . replace[ ] . . . facilities if necessary so long as such replacement is not inconsistent with this schedule or a contract governing such facilities."). The Service Agreements require the Maloney Ridge Line Customers to repair and maintain the line, but not replace it. AR000031, ¶ 4 (requiring King County to repair and maintain the line, but not replace it). And, "[r]eplacement, by its nature, is distinct from operating, repairing, or maintaining an existing line." Order 03, CP 26, ¶ 13. *See also Wash. Hydroculture, Inc. v. Payne*, 96 Wn.2d 322, 327, 635 P.2d 138 (1981) ("repair' or 'maintain' does not mean 'rebuild'"; "[t]he plain meaning of maintain or repair is not synonymous with rebuild"). Schedule 85 is clear: PSE must pay to replace the Maloney Ridge Line.

PSE cites a Georgia Court of Appeals case for the proposition that the "common definition of repair is very broad in scope and includes in its meaning to make good by replacing a structure in poor condition." PSE

Brief at 15 n.73 (citing *Parris Props., LLC v. Nichols*, 305 Ga. App. 734, 738, 700 S.E.2d 848 (2010) (citation and quotation marks omitted)). Based on this case, PSE argues the “Commission could have relied solely on the Service Agreements’ language” to find the Maloney Ridge Line Customers must pay to replace the line.<sup>21</sup> In the Georgia case cited by PSE, the court was asked to determine whether a sewer line easement allowed the owners of the dominant estate to replace a sewer pipe that was no longer functioning properly. *Parris Props., LLC*, 305 Ga. App. at 738. Applying the general rules of contract interpretation to ascertain the parties’ intent and construe the plain language used, the court “conclude[d] that the easement unambiguously authorizes the removal and replacement of a malfunctioning or worn-out sewer pipeline.” *Id.* In *Parris* there was no evidence the parties ever contemplated anything other than the easement permitting the owner of the dominant estate to repair, maintain, and replace an existing, worn out sewer pipe. *See id.* at 738-39.

Here, unlike in *Parris*, it is clear PSE views repair, maintenance and replacement as separate and distinct activities. Indeed, Schedule 85 “sets forth the circumstances, terms and conditions under which [PSE] is

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<sup>21</sup> *See* PSE Brief at 15. For its part, unlike PSE, the WUTC does not argue the Service Agreements require the Maloney Ridge Line Customers to pay to replace the line. *See, e.g.*, Order 04, CP 49, ¶ 28 (adopting Order 03’s findings and conclusions). These findings and conclusions included that “[t]he [Service Agreements] do not require [the Customers] to pay the costs to replace the line.” Order 03, CP 34, ¶ 43.

responsible for the ownership, installation, *maintenance, repair or replacement of distribution facilities*[".]” AR000647, Sheet No. 85 (emphasis added). When PSE uses different words in the same tariff, those words are presumed to have different meanings. *See Ass’n of Wash. Spirits & Wine Distribs. v. Wash. State Liquor Control Bd.*, 182 Wn.2d 342, 353, 340 P.3d 849 (2015) (“[d]ifferent statutory language should not be read to mean the same thing”) (citation omitted).<sup>22</sup> The Commission agreed that replacement is different than repair and/or maintenance: “Replacement, by its nature, is distinct from operating, repairing, or maintaining an existing line.” Order 03, CP 26, ¶ 13.<sup>23</sup> It is against this backdrop that the Service Agreements must be understood. PSE’s Georgia case is distinguishable and the Service Agreements do not require the Maloney Ridge Line Customers to pay to replace the line.

To the extent there is any ambiguity in Schedule 85, that ambiguity must be construed against PSE. *N. Pac. Ry. Co. v. Sauk River Lumber Co.*, 160 Wn. 691, 693-94, 295 P. 926 (1931) (“If the tariff as filed is doubtful or ambiguous, any doubt should be resolved against the party

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<sup>22</sup> “[S]tandard principles of statutory construction[, e.g., different words in the same statute mean different things,] apply to the interpretation of [a] tariff.” *Nat’l Union Ins. Co. of Pittsburgh v. Puget Sound Power & Light*, 94 Wn. App. 163, 171, 972 P.2d 481 (internal quotation marks omitted), *review denied*, 138 Wn.2d 1010 (1999).

<sup>23</sup> *See also* Order 04, CP 49, ¶ 28 (adopting Order 03’s findings and conclusions). These findings and conclusions included that “[t]he [Service Agreements] do not require [the Customers] to pay the costs to replace the line.” Order 03, CP 34, ¶ 43.

causing such tariff to be put into effect.”).<sup>24</sup> The WUTC admits that its construction of Schedule 85 in conjunction with the Service Agreements “requires an interpretive approach”,<sup>25</sup> thereby admitting, under its interpretation, that Schedule 85 is ambiguous. As such, the language of Schedule 85 must be construed as requiring PSE to pay to replace the line.

**D. The WUTC and PSE Improperly Rely on an Economic Feasibility Test.**

The ALJ and Commission employed a fact-based analysis—which included an economic feasibility prong among other considerations—borrowed from Commission rules and precedent that have no bearing on replacement of an existing line.<sup>26</sup> The ALJ and Commission applied this ad hoc, fact-based analysis only because they found ambiguities in the Service Agreements and Schedule 85 that do not exist.<sup>27</sup>

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<sup>24</sup> *Adams v. N. Ill. Gas Co.*, 211 Ill.2d 32, 69, 809 N.E.2d 1248, 284 Ill. Dec. 302 (2004) (“[B]ecause the utility company drafts a tariff, it is generally accepted that language in a tariff, especially exculpatory language, is to be strictly construed against the utility company and in favor of the customer.”); *Uncle Joe’s Inc. v. L.M. Berry & Co.*, 156 P.3d 1113, 1118 (Alaska 2007) (“Numerous authorities in other jurisdictions indicate that when a tariff is ambiguous it should be construed like a contract and thus favorably to the customer and against the drafter.”). Citing no authority, PSE contends this principle applies only to contracts, not tariffs. PSE Brief at 23. PSE’s failure to support its contention is fatal. *In re Marriage of Wallace*, 111 Wn. App. 697, 705, 45 P.3d 1131 (2002) (“Contentions unsupported by argument or citation of authority will not be considered on appeal.”).

<sup>25</sup> WUTC Brief at 30.

<sup>26</sup> That is to say, a regulation (WAC 480-100-123) applicable to new or additional service and a Commission order (*In re Petition of Verizon Nw., Inc.*, Docket No. UT-011439, Twelfth Supp. Order, 2003 WL 24122603 (WUTC April 2003)) applicable to requests for extensions of wireline telephone services.

<sup>27</sup> Rather, Schedule 85 is clear and unambiguous: PSE must pay to replace the line. See *supra* Section C(iii).

i. *The ALJ and Commission expressly called into doubt the economic feasibility language of Schedule 80.*

PSE argues the economic feasibility language in Schedule 80 allows the Company to pick and choose among customers as to who will be subjected to an ill-defined economic test for distribution line replacements.<sup>28</sup> In Orders 03 and 04, the ALJ and Commission both rejected direct application of Schedule 80's economic feasibility language.<sup>29</sup> Indeed, the Commission stressed its unease with that provision because it could lead to arbitrary and unjust results, e.g., the very results PSE and the WUTC advocate for here:

Second, the concept of "economic unfeasibility" is overly

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<sup>28</sup> PSE Brief at 16-21. PSE suggests that interpreting Section 9 of Schedule 80 to apply only to new or additional service would result in an absurd outcome, i.e., "PSE would be forced to continue to serve an existing customer even if PSE became aware that the customer had installed hazardous equipment that put people in danger." PSE Brief at 19. That suggestion is nonsense. It is belied by the very terms of Section 9 (Opening Brief at 32-34) and by regulations governing disconnection of service, which authorize PSE to terminate service where it "identifies a hazardous condition in the customer's facilities or in the utility's facilities serving the customer." WAC 480-100-128(2)(c). In other words, the regulation authorizes disconnection in the event an existing service is hazardous, and accordingly, Section 9 of Schedule 80 does not need to, and in fact does not, address existing service. PSE's reading of Section 9, by contrast, would confer unfettered authority on the utility to engage in favoritism based on amorphous concepts of economic feasibility.

<sup>29</sup> The Commission, though it did not directly apply Schedule 80's economic feasibility provision, noted the "standard remains part of PSE's tariff." Order 04, CP 164, ¶ 25. With respect to application of Schedule 80, PSE argues the Maloney Ridge Line Customers were not "blindsided" by its potential application because "PSE stated that Section 9 of the Schedule 80 applied to resolve this case at its first opportunity, in its Statement of Fact and Law filed less than one month after the petitioners filed their Petition for Declaratory Order in June 2014." PSE Brief at 17. This misses the point. As King County stated in its Opening Brief, the Customers had no way of knowing, *at the outset of this proceeding*, that PSE and the WUTC would attempt to rely on Schedule 80's economic feasibility language and, regardless, have strenuously opposed application of that provision since PSE initially suggested its application. Opening Brief at 29-30.

broad and ambiguous. The Commission eliminated this term from the refusal of service rule, at least in part, because the language is “too general and vague to be useful.” Taken to its extreme, a test of economic feasibility could be used to deny or terminate service to any individual customer if the revenues PSE receives do not exceed the Company’s calculations of the costs it incurs to serve that particular customer. Such a result is fundamentally inconsistent with the regulatory principle of averaging costs and demand among customer classes when establishing the rates that apply to that class. PSE cannot refuse service to an individual customer solely because the costs to serve, or the revenues the Company receives from, that customer vary from the class average.

Order 03, CP 27, ¶ 17 (footnote omitted). *See also* Order 04, CP 164, ¶ 25 (“We share the two concerns discussed in Order 03 in relation to Schedule 80, General Rules and Provisions, Section 9, which states in relevant part, ‘The Company shall not be required to provide service if to do so would be economically unfeasible.’”).

The Commission did not directly apply Schedule 80’s economic feasibility language: “the Commission was . . . unwilling to find that the provision was dispositive of who should pay to replace the” line.<sup>30</sup> Nevertheless, by essentially applying the provision through “a fact-specific analysis”, the Commission condoned PSE’s cherry-picking of customers upon which to impose an obscure economic feasibility test. In doing so, the Commission acted arbitrarily and capriciously and

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<sup>30</sup> WUTC Brief at 32 (citing AR000334 and AR000337).

discriminated unjustly against the Maloney Ridge Line Customers.

*ii. The ALJ and Commission improperly relied on an unprecedented fact-based analysis.*

After erroneously determining the Service Agreements and Schedule 85 were vague and ambiguous as to replacement obligations, the ALJ and Commission improperly utilized a fact-based analysis not applicable to replacement of existing electric distribution lines. The Commission's application of the fact-based analysis resulted in numerous errors and an arbitrary and capricious decision.

a. WAC 480-100-123 applies only to new or additional service, not to the replacement of existing lines.

Orders 03 and 04 employed a fact-based analysis borrowed from WAC 480-100-123 to determine who should pay to replace the Maloney Ridge Line.<sup>31</sup> WAC 480-100-123 and the 2001 WUTC order adopting it are clear that the regulation's fact-based analysis is applicable only to *new* or *additional* service. See WAC 480-100-123 (describing when an electric utility may refuse to provide *new* or *additional* service); *In re Adopting and Repealing Rules in Chapter 480-100 WAC Relating to Rules Establishing Requirements for Electric Companies*, Docket No. UE-990473, Order No. R-495, Adopting and Repealing Rules Permanently at

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<sup>31</sup> Order 03, CP 27, ¶ 18; Order 04, CP 162-164, ¶¶ 22-23 and 25.

¶ 25 (WUTC Dec. 3, 2001) (observing the language in 480-100-123(5) applies to new or additional service).<sup>32</sup> PSE and the WUTC argue WAC 480-100-123 contains a “catch all” provision that makes the regulation applicable to existing line replacements.<sup>33</sup> The rule’s “catch all” provision applies to new or additional service, however—*not* replacements needed to sustain *existing* service: “[t]he utility may refuse to provide *new or additional service* for reasons not expressed in subsections (1) and (2) of this section, upon prior approval of the commission.” WAC 480-100-123(5) (emphasis added). Of course, the Maloney Ridge Line Customers seek only to continue an existing service, not to obtain a new or additional service. Simply put, the fact-based analysis regulation does not apply to existing line replacements, and the WUTC erred by applying it here.

- b. The Commission compounded its error by revitalizing an economic feasibility test—previously rejected by the Commission—that promotes favoritism and produces unfair and unjust results.

Even if WAC 480-100-123’s fact-based analysis applied—it does not—the prior rule’s economic feasibility test is not part of that analysis. In 2001, when the Commission incorporated a fact-based analysis into WAC 480-100-123, the Commission eliminated economic feasibility

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<sup>32</sup> PSE admits WAC 480-100-123 applies to new lines. PSE Brief at 13 n.62.

<sup>33</sup> PSE Brief at 25; WUTC Brief at 21-22.

language because those “terms are too general and vague to be useful.” *In re Adopting and Repealing Rules*, Docket No. UE-990473, Order No. R-495, at ¶ 25. The ALJ and Commission elaborated on the unfairness likely to result from such an analysis: “[t]aken to its extreme, a test of economic feasibility could be used to deny or terminate service to any individual customer if the revenues PSE receives do not exceed the Company’s calculations of the costs it incurs to serve that particular customer.”<sup>34</sup> Nevertheless, Orders 03 and 04 compounded the Commission’s error by inserting the economic feasibility analysis into the fact-based inquiry improperly borrowed from a rule applicable only to new or additional services. This compound error exemplifies the arbitrary and capricious nature of Orders 03 and 04.<sup>35</sup>

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<sup>34</sup> Order 03, CP 27, ¶ 17. *See also* Order 04, CP 164, ¶ 25. The exact reasoning PSE, with WUTC approval, relies on here to refuse to pay to replace the line.

<sup>35</sup> *See Whatcom Cty. v. W. Wash. Growth Mgmt. Hearing Bd.*, 186 Wn. App. 32, 67, 344 P.3d 1256 (finding board acted inconsistently with its own rules when absent explanation it took official notice of documents without notifying or affording parties an opportunity to contest those materials), *rev’d in part on other grounds, Whatcom Cty. v. Hirst*, 381 P.3d 1 (2016); *Skokomish Indian Tribe v. Fitzsimmons*, 97 Wn. App. 84, 85, 982 P.2d 1179 (1999) (holding agency acted arbitrarily and capriciously where it specifically acknowledged its action was inconsistent with state law), *review denied*, 143 Wn.2d 1018 (2000); *Kittitas Cty. v. E. Wash. Growth Mgmt. Hearing Bd.*, 172 Wn.2d 144, 174, 256 P.3d 1193 (2011) (RCW 34.05.570(3)(h) necessitates consistency in agency rulings). *See also Nw. Env’tl. Def. Ctr. v. Bonneville Power Admin.*, 477 F.3d 668, 687 (9th Cir. 2007) (“[A]n agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed . . .”).

c. Connecticut precedent does not support application of an economic feasibility test in this case.

Apparently recognizing the lack of Washington authority to support the application of an economic feasibility test to distribution line replacements, the WUTC cites a Connecticut case that actually supports the Customers' position.<sup>36</sup> The Connecticut case involved a request for *new* service. *Levitt v. Public Utils. Comm'n*, 114 Conn. 628, 159 A. 878, 879 (1932). *See also* WUTC Brief at 23. To the extent the Connecticut Supreme Court considered economic feasibility, then, its decision is consistent with Commission rules and precedent that economic feasibility is to be considered, if ever,<sup>37</sup> when confronted with requests for *new or additional* services. *Levitt*, 159 A. at 879 ("It is clear, however, that in a case like the one before us prospective future returns from the *new undertaking* is a factor not to be overlooked or passed over slightly.") (emphasis added).

Further, like PSE here, the utility company in *Levitt* had tariff provisions applicable to the specific situation at hand. In *Levitt* the utility had "established . . . special provisions governing service where extension

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<sup>36</sup> WUTC Brief at 22-24.

<sup>37</sup> An economic feasibility test may constitute acceptable policy in the context of new or additional service before the customer has come to rely on it and the utility has begun to account for that service. For existing service, however, such a test is bound to leave customers suddenly and unexpectedly in the dark based on a financial analysis outside their control.

lines more than 600 feet in length are required.” *Levitt*, 159 A. at 879. Those provisions required the requesting customer to pay additional costs for any new services beyond 600 feet. *Id.* The Connecticut Supreme Court held the utility’s refusal to provide new electric service that did not comply with its special provisions was reasonable: “[i]n so far as the commission held that the company should not be directed to furnish service to the plaintiff at the regular rates established for its customers living within 600 feet of its service lines, the trial court committed no error in sustaining its conclusion.” *Id.* at 880. Like the special provisions in *Levitt*, PSE’s tariff Schedule 85 is particularly applicable to our situation: it “sets forth the circumstances, terms, and conditions under which [PSE] is responsible for the ownership, installation, maintenance, repair *or replacement of distribution facilities*[.]” AR000647, Sheet No. 85 (emphasis added). *Levitt* supports the application of Schedule 85.

Perhaps most troubling about WUTC’s *Levitt* argument is its statement that the “new or additional service” language in WAC 480-100-123 “is immaterial because the essential economic effect on rates is the same regardless of whether the [Maloney Ridge Line] needs to be [built] or [rebuilt].” WUTC Brief at 23.<sup>38</sup> At best, the WUTC is arguing it can

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<sup>38</sup> The WUTC also posits that “courts have consistently declined to second-guess the Commission’s economic judgments.” WUTC Brief at 14. These cases are

disregard the plain language of its own regulations at its whim and caprice; that it can apply those however it chooses, whenever it chooses, to whoever it chooses. This is the very definition of arbitrary agency action. It is how, with PSE's support, the WUTC has used the economic feasibility test—whether in Schedule 80 or through some ill-defined and misapplied fact-based analysis—as a blunt instrument to run roughshod over its statutory and regulatory obligations and the plain language of tariff Schedule 85 and the Service Agreements.

If the WUTC is free to read an economic feasibility test into its own regulations—where the language of those regulations and the Commission's prior actions and statements are to the contrary—and if PSE is free to read an economic feasibility provision into its tariffs—where those provisions exist only in other, inapplicable tariffs—then both PSE and the WUTC will have carte blanche to do so with any regulation or tariff. The result would be rubber-stamped arbitrary and capricious agency action putting all customers at risk of having to choose between loss of existing service and an untenable cost burden when their lines need to be replaced.

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distinguishable because this is a contract and tariff interpretation case, not a case of the Commission properly exercising its “economic judgment”. *See supra* Section B.

**E. The Maloney Ridge Line Customers Have Challenged and Argued the Commission’s Improper Findings and Conclusions Throughout this Proceeding.**

This Court reviews the Commission’s findings, not those of the superior court. *US W. Commc’ns v. Wash. Utils. & Transp. Comm’n*, 134 Wn.2d 74, 85, 949 P.2d 1337 (1997) (“[R]eview by this Court is of the Commission’s findings and not a review of the superior court’s decision.”).<sup>39</sup> Nonetheless, the WUTC and PSE cite the superior court’s order for the proposition that the Maloney Ridge Line Customers somehow failed to properly challenge the Commission’s findings of fact.<sup>40</sup> In the same vein, the WUTC suggests—without citation<sup>41</sup>—that the Customers “fail[ed] to cite to the APA in their assignments of error” and that their assignments of error are “problematic”.<sup>42</sup> These arguments misconstrue the appropriate status of review and the Customers’ challenges and arguments throughout this proceeding.

King County properly assigned error to the Commission’s

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<sup>39</sup> See also *Kadlec Reg’l Med. Ctr. v. Dep’t of Health*, 177 Wn. App. 171, 177, 310 P.3d 876 (2013) (“On appeal, we review the [agency’s] decision, not the superior court’s decision.”).

<sup>40</sup> WUTC Brief at 3 n.2; PSE Brief at 9, 21 and 29. The WUTC cites no cases in support of this contention and thus it cannot be considered. *In re Marriage of Wallace*, 111 Wn. App. 697, 705, 45 P.3d 1131 (2002) (“Contentions unsupported by argument or citation of authority will not be considered on appeal.”). The only case cited by PSE is a criminal case involving “undisputed” findings of fact entered during a suppression hearing. PSE Brief at 29 (citing *State v. Hill*, 123 Wn.2d 641, 644, 870 P.2d 313 (1994)). For the reasons stated herein, PSE’s criminal case is not applicable here.

<sup>41</sup> “Contentions unsupported by argument or citation of authority will not be considered on appeal.” *In re Marriage of Wallace*, 111 Wn. App. at 705.

<sup>42</sup> WUTC Brief at 12 and 14.

findings, thereby properly challenging those findings of fact and conclusions of law made in error by the Commission, and has argued those errors at every level of this proceeding. This Court only reviews claimed errors included in an assignment of error or clearly disclosed in the associated issues pertaining thereto. *Bircumshaw v. State*, 194 Wn. App. 176, 198, 380 P.3d 524 (2016).<sup>43</sup> Even where an appellant fails to assign error to administrative findings, however, appellate courts will consider challenges as long as the appellant's briefing is clear about which findings it is challenging and on what grounds it is challenging them. *Cummings v. Wash. State Dep't of Licensing*, 189 Wn. App. 1, 11, 355 P.3d 1155 (2015).<sup>44</sup>

In their Petition for Judicial Review of Agency Action to Thurston County Superior Court (Superior Court Petition), the Maloney Ridge Line

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<sup>43</sup> "An appellant must separately assign error to each finding that he challenges on appeal, must identify each challenged finding by number, and must separately assign error to any challenged administrative findings. RAP 10.3(g)-(h)." *Bircumshaw*, 194 Wn. App. at 198 (citation omitted).

<sup>44</sup> "[T]he Rules of Appellate Procedure 'allow appellate review of administrative decisions in spite of technical violations when a proper assignment of error is lacking but the nature of the challenge is clear and the challenged finding is set forth in the party's brief.' . . . Accordingly, we review these challenged findings." *Cummings*, 189 Wn. App. at 11 (citations omitted). See also *Whatcom Cty. v. Hirst*, 381 P.3d 1, 6 n.5 (2016) ("As the Court of Appeals properly found, the nature and extent of the County's challenges to [the findings of fact] are clear. Thus, this court's review is not in any way hindered by the absence of formal assignment of error.") (alteration in original) (citation and quotation marks omitted); *Fuller v. Emp't Sec. Dep't*, 52 Wn. App. 603, 605-06, 762 P.2d 367 (1998) (refusing to consider appellant's challenges to findings because she did not assign error to those findings or set forth the challenged findings in her brief).

Customers followed the requirements of RCW 34.05.546 and argued in briefing and at oral argument each and every point of law and finding of fact the Commission made in error and the nature of that error.<sup>45</sup> In their Opening Brief on appeal to this Court, the Maloney Ridge Line Customers properly followed RAP 10.3(a)(4), (g) and (h).<sup>46</sup> Thus the Customers properly assigned error and have challenged the Commission's findings of fact and conclusions of law throughout this case.<sup>47</sup>

Even if the Maloney Ridge Line Customers had failed to properly assign error challenging the Commission's findings of fact and conclusions of law, the Court would still review those challenges because King County, PSE, and the WUTC argued them in their respective appellate briefs.<sup>48</sup> By briefing issues, a party waives any alleged failure by an opposing party to properly assign error related to those issues. *Ferry Cty. v. Growth Mgmt. Hearings Bd.*, 184 Wn. App. 685, 725-26, 339 P.3d 478 (2014) ("Futurewise thoroughly addressed the issue in its brief and

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<sup>45</sup> CP 8-19 (Superior Court Petition); CP 52-80 (Petitioners King County and BNSF Railway Company's Opening Brief); CP 133-146 (Petitioners King County and BNSF Railway Company's Reply Brief).

<sup>46</sup> Opening Brief at 1-5.

<sup>47</sup> It is worth noting the imprecise drafting in both Orders 03 and 04. Neither of which clearly distinguish between findings of fact and conclusions of law. But rather clump the two together in one umbrella category appropriately, but not helpfully, titled "Findings and Conclusions". See Order 03, CP 33; Order 04, CP 49 (adopting Order 03's "Findings and Conclusions").

<sup>48</sup> See, e.g., Opening Brief at 39 (arguing the line is part of PSE's system); PSE Brief at 29 (arguing the line is not part of PSE's system).

shows no prejudice by Ferry County’s failure to strictly follow the rules. Therefore, we reject Futurewise’s argument and address the merits of the appeal.”). The Customers also clearly briefed and argued, among other things, that the line is part of PSE’s distribution system at the superior court level.<sup>49</sup> PSE and the WUTC also argued this issue and others at the superior court.<sup>50</sup> The WUTC and PSE have thus waived any alleged failures to properly assign error in this case.

### CONCLUSION

Apparently recognizing the weakness of their contract and tariff interpretation arguments, the WUTC and PSE have gone all in to recast the clear contract and tariff interpretation questions presented by this case as ratemaking. The attempt fails. No rates would or can result from any decision on the Customers’ Petition for Declaratory Order in this case. Rather, this case is designed to resolve the legal questions necessary for a proper interpretation and understanding of the Service Agreements and Schedule 85—setting the stage for ratemaking proceedings, if necessary, at a later time.

The Court should correct the Commission’s errors of law and

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<sup>49</sup> *See, e.g.*, CP 17-18 (challenging the conclusion as unsupported by substantial evidence and as arbitrary and capricious); CP 74 (opening brief argument that the line is part of PSE’s distribution system); CP 137 (arguing the line is part of PSE’s distribution system).

<sup>50</sup> *See, e.g.*, CP 128-130 (arguing the line is not part of PSE’s system).

prevent the Commission from arbitrarily and capriciously discriminating against PSE's Maloney Ridge Line Customers by reversing Order 04 and ordering, or directing the Commission to order, PSE to pay to replace the Maloney Ridge Line. PSE's responsibility to do so is clear and unambiguous in Schedule 85.

DATED this 16th day of December, 2016.

Respectfully submitted,

K&L GATES LLP

By   
Kari L. Vander Stoep, WSBA # 35923  
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Attorneys for Appellant King County

**APPENDIX**

**TO APPELLANT KING COUNTY’S REPLY BRIEF**

<b>Document Title</b>	<b>Pages</b>
Puget Sound Energy Electric Tariff G, Schedule 85, Sheet No. 85	1
Puget Sound Energy Electric Tariff G, Schedule 85, Sheet No. 85-k	2
Puget Sound Energy Electric Tariff G, Schedule 80, Sheet No. 80-d	3
<i>Adams v. N. Ill. Gas Co.</i> , 211 Ill.2d 32, 809 N.E.2d 1248, 284 Ill. Dec. 302 (2004)	4-35
<i>Levitt v. Public Utils. Comm’n</i> , 114 Conn. 628, 159 A. 878 (1932)	36-40
<i>Nw. Env’tl. Def. Ctr. v. Bonneville Power Admin.</i> , 477 F.3d 668 (9th Cir. 2007)	41-61
<i>Parris Props., LLC v. Nichols</i> , 305 Ga. App. 734, 700 S.E.2d 848 (2010)	62-76
<i>In re Adopting and Repealing Rules in Chapter 480-100 WAC Relating to Rules Establishing Requirements for Electric Companies</i> , Docket No. UE-990473, Order No. R-495, Order Adopting and Repealing Rules Permanently (WUTC Dec. 3, 2001)	77-85
<i>In re Petition of Verizon Nw., Inc.</i> , Docket UT-011439, Twelfth Supp. Order, 2003 WL 24122603 (WUTC Apr. 2003)	86-101
<i>Wash. Utils. &amp; Transp. Comm’n v. Avista Corp.</i> , Docket Nos. UE-090134, UE-090135, UG-060518, Order No. 10, 2009 WL 5061998 (WUTC Dec. 22, 2009)	102-229
RCW 34.05.546	230
RCW 34.05.570	231-232
RCW 80.04.130	233-234
RCW 80.04.250	235
RCW 80.28.010	236-237
WAC 480-07-500	238
WAC 480-07-505	239
WAC 480-07-510	240-242
WAC 480-100-123	243
WAC 480-100-128	244-248

Wash. Utils. & Transp. Comm'n, Ratemaking Process PDF, *available* at  
<https://www.utc.wa.gov/consumers/Documents/2012-3%20UTC%20Fact%20Sheet-%20Energy%20Ratemaking.pdf>

249-250

Eighth Revision of Sheet No. 85  
Canceling Seventh Revision  
of Sheet No. 85

WN U-60

**PUGET SOUND ENERGY**  
**Electric Tariff G**

**SCHEDULE 85**  
**LINE EXTENSIONS AND SERVICE LINES**

The Company will extend and construct new or modify existing electric distribution facilities upon written (or verbal, at the discretion of the Company) request based upon the terms and conditions outlined in this tariff. The Company will evaluate the request to identify any required Customer or Applicant payments based upon the following formula (each element of the formula is as further described in this schedule):

	Primary Voltage Line Extension Costs (including Transformation Cost)
+	Secondary Voltage Line Extension Costs
+	Exceptional Transmission & Substation Costs
-	Margin Allowance
<hr/>	
=	Line Extension Cost
+	Service Line Costs
=	Total Cost to Customer or Applicant

This Schedule 85 also sets forth the circumstances, terms and conditions under which the Company is responsible for the ownership, installation, maintenance, repair or replacement of electric distribution facilities, including facilities on the Customer's or Applicant's side (the load side) of the Point of Delivery.

**Definitions**

Applicant – Any person, partnership, firm, corporation, municipality, cooperative organization, governmental agency, etc., who or which is requesting any service under this schedule from the Company. The Applicant may or may not be or become a Customer. For purposes of the General Rules and Provisions contained in this tariff, Applicant shall be included within the term Customer.

Design Costs – Costs include, but are not limited to, costs to produce an estimate of costs, or for engineering, surveying, pre-construction coordination, and for reviewing plans and proposals. (N)  
(N)

Margin Allowance – The amount the Company will contribute toward construction costs for new or modified electric distribution facilities as described in this schedule.

Multi-Family Residential Structure – A structure containing two or more single-family dwelling units, including duplexes, triplexes, condominiums and apartment buildings; provided that for purposes of the charges for transformation, Multi-Family means a structure of five or more units.

Non-Residential – Service to commercial, industrial or lighting (excluding street lighting circuitry) Customers/Applicants and recreational facilities, or to multi-family residential structures (whether through one meter for the structure or individual meters for each unit), mobile home parks or manufactured housing communities in which the individual park/community residents do not own the real property on which their individual mobile or manufactured homes are located (whether through one meter for the park or individual meters for each mobile/manufactured home).

Issued: November 22, 2006  
Advice No.: 2006-31

Effective: December 23, 2006

Issued By Puget Sound Energy

By: Tan DeBoer Tom DeBoer

Title: Director, Rates & Regulatory Affairs

First Revision of Sheet No. 85-k  
Canceling Original  
Sheet No. 85-k

WN U-60

**PUGET SOUND ENERGY**  
**Electric Tariff G**

**SCHEDULE 85**  
**LINE EXTENSIONS AND SERVICE LINES**  
(Continued)

(T)

**Additional Terms of Service**

(M)(K)

1. A. **OWNERSHIP OF FACILITIES:** The Company shall own, operate, maintain and repair all electric distribution facilities installed by or for the Company under this schedule, including replacement of such facilities if necessary so long as such replacement is not inconsistent with this schedule or a contract governing such facilities. Other than as provided in section 1.B., below, the Company shall not own and shall have no responsibility to operate, maintain, repair or replace any electric distribution facilities that were not installed by or for the Company under this schedule.

(C)  
(M)  
(N)

B.(i) With respect to underground Service Lines at mobile home parks or manufactured housing communities in which the individual park residents do not own the property on which their individual mobile or manufactured homes are located and in the case of Multi-Family Residential Structures, the park/community property owner or Multi-Family Residential Structure owner shall be responsible for ownership and operation of all new and existing underground Service Lines (as well as service entrance equipment including meter bases, pedestals and enclosures) and for all costs for installation, maintenance, repair and replacement thereof, *provided that* the Company shall be responsible for existing underground Service Lines that the Company installed prior to May 1, 2006, as determined and as qualified below:

(K)

(a) For underground electric facilities constructed prior to October 21, 1977, there shall be a presumption that the Company installed the Service Lines. This presumption can be overcome if PSE can show that the Company did not install the Service Line that needs repair. PSE shall bear the burden of proving that it did not install the Service Line. Where PSE has records showing that it did not install the Service Line or can show that a Service Line is labeled with a "UL®" (Underwriters Laboratories, Inc.®) designation or similar marking, this is sufficient to prove that the Service Line was not installed by the Company, as neither PSE nor its predecessors install or installed "UL®" designated facilities.

(K)

(b) For underground electric facilities constructed on or after October 21, 1977, there shall be a presumption that the property owner installed the Service Lines. This presumption can be overcome if the property owner can show that the Company in fact installed the Service Line that needs repair. The property owner shall bear the burden of proving installation by the Company.

(N)(K)

(M) Transferred from Sheet No. 85-i

(K) Transferred to Sheet No. 85-n and 85-o Respectively

Issued: July 28, 2006

Effective: August 1, 2006

Advice No.: 2006-19

By Authority of the Washington Utilities and Transportation Commission in Docket Nos. UE-051828 & UE-051966  
Issued By Puget Sound Energy

By:

Tom DeBoer

Tom DeBoer

Title: Director, Rates & Regulatory Affairs

Fourth Revision of Sheet No. 80-d  
Canceling Third Revision  
of Sheet No. 80-d

WN U-60

**PUGET SOUND ENERGY**  
**Electric Tariff G**

**SCHEDULE 80**  
**GENERAL RULES AND PROVISIONS**  
(Continued)

8. ACCESS TO PREMISES - The Company, its agents and employees shall have the right of ingress to or egress from the Premises of the Customer at all reasonable hours as may be necessary for meter reading, performance of necessary maintenance, testing, installation, or removal of its property. In the event the Customer is not the owner of the Premises occupied, he shall obtain all such permissions from the owner thereof. (M)

9. REFUSAL OF SERVICE - The Company may refuse to connect an applicant for service or may refuse to render additional service to a Customer when such service will adversely affect service being rendered to other Customers or where the applicant or Customer has not complied with state, county, or municipal codes or regulations concerning the rendition of such service.

The Company may refuse to serve an applicant or a Customer if, in its judgment, said applicant's or Customer's installation of wiring or electrical equipment is hazardous, or of such character that satisfactory service cannot be provided.

The installation of proper protective devices on the applicant's or Customer's premises at the applicant's or Customer's expense may be required whenever the Company deems such installation necessary to protect its property or that of its other Customers.

The Company shall not be required to connect with or render service to an applicant unless and until it has all necessary operating rights, including rights-of-way, easements, franchises, and permits.

The Company may refuse to connect service to a master meter in any new building with permanent occupants when: there is more than one dwelling unit in the building or property; the occupant of each unit has control over a significant portion of electric energy consumed in each unit; and the long-run benefits of a separate meter for each customer exceed the cost of providing separate meters.

The Company shall not be required to provide service if to do so would be economically unfeasible.

10. CUSTOMER'S LOAD AND OPERATIONS - For single and three phase service, the Customer shall provide adequate protection for equipment, data, operations, work and property under his control from (a) high and low voltage, (b) surges, harmonics, and transients in voltage, and (c) overcurrent. For unidirectional and three-phase equipment, the Customer shall provide adequate protection from "single phasing conditions," reversal of phase rotation, and phase unbalance.

(M) Transferred from Sheet 80-c

Issued: July 28, 2006  
Advice No.: 2006-19

Effective: August 1, 2006

By Authority of the Washington Utilities and Transportation Commission in Docket Nos. UE-051828 & UE-051966  
Issued By Puget Sound Energy

By: Tom DeBoer Tom DeBoer Title: Director, Rates & Regulatory Affairs

KeyCite Yellow Flag - Negative Treatment

Declined to Extend by *Hatt v. Western Plastics, Inc.*, Ill.App. 2 Dist.,  
December 29, 2014

211 Ill.2d 32

Supreme Court of Illinois.

Christy ADAMS, Special Adm'r of the Estate  
of Janice Adams, Deceased, Appellee,

v.

NORTHERN ILLINOIS GAS COMPANY, Appellant.

No. 94748.

|

April 1, 2004.

|

Rehearing Denied May 24, 2004.

### Synopsis

**Background:** Special administrator of estate of gas customer who died as a result of a natural gas explosion and fire at her home brought a wrongful death suit against natural gas company and owner of home. The Circuit Court, Cook County, Sophia Hall, J., granted summary judgment in favor of gas company. Estate appealed. After modifying its opinion, the Appellate Court reversed and remanded, 333 Ill.App.3d 215, 266 Ill.Dec. 411, 774 N.E.2d 850. Gas company petitioned for leave to appeal.

**Holdings:** Upon grant of petition, the Supreme Court, Freeman, J., held that:

[1] gas company that had knowledge of appliance connector danger owed customer a duty to warn her of such danger, and

[2] liability limitation provision in gas company's tariff did not abrogate duty.

Affirmed.

Garman, J., dissented and filed an opinion in which Fitzgerald and Thomas, JJ., joined.

West Headnotes (44)

### [1] Judgment

~ Nature of summary judgment

228 Judgment

228V On Motion or Summary Proceeding

228k178 Nature of summary judgment

Purpose of summary judgment is not to try a question of fact, but rather to determine whether a genuine issue of material fact exists.

120 Cases that cite this headnote

### [2] Judgment

~ Presumptions and burden of proof

228 Judgment

228V On Motion or Summary Proceeding

228k182 Motion or Other Application

228k185 Evidence in General

228k185(2) Presumptions and burden of proof

In determining whether a genuine issue as to any material fact exists so as to preclude summary judgment, a court must construe the pleadings, depositions, admissions, and affidavits strictly against the movant and liberally in favor of the opponent.

129 Cases that cite this headnote

### [3] Judgment

~ Absence of issue of fact

228 Judgment

228V On Motion or Summary Proceeding

228k181 Grounds for Summary Judgment

228k181(2) Absence of issue of fact

A triable issue precluding summary judgment exists where the material facts are disputed, or where, the material facts being undisputed, reasonable persons might draw different inferences from the undisputed facts.

80 Cases that cite this headnote

### [4] Judgment

~ Nature of summary judgment

Judgment

## KC REPLY APPENDIX 4

~ Necessity that right to judgment be free from doubt

228 Judgment

228V On Motion or Summary Proceeding

228k178 Nature of summary judgment

228 Judgment

228V On Motion or Summary Proceeding

228k181 Grounds for Summary Judgment

228k181(4) Necessity that right to judgment be free from doubt

The use of the summary judgment procedure is to be encouraged as an aid in the expeditious disposition of a lawsuit; however, it is a drastic means of disposing of litigation and, therefore, should be allowed only when the right of the moving party is clear and free from doubt.

64 Cases that cite this headnote

**[5] Appeal and Error**

~ Cases Triable in Appellate Court

30 Appeal and Error

30XVI Review

30XVI(F) Trial De Novo

30k892 Trial De Novo

30k893 Cases Triable in Appellate Court

30k893(1) In general

In appeals from summary judgment rulings, review is de novo.

47 Cases that cite this headnote

**[6] Negligence**

~ Elements in general

272 Negligence

272I In General

272k202 Elements in general

To prevail in an action for negligence, the plaintiff must establish that the defendant owed a duty of care, that the defendant breached that duty, and that the plaintiff incurred injuries proximately caused by the breach.

22 Cases that cite this headnote

**[7] Negligence**

~ Duty as question of fact or law generally

**Negligence**

~ Negligence as question of fact or law generally

**Negligence**

~ Proximate Cause

272 Negligence

272XVIII Actions

272XVIII(D) Questions for Jury and Directed Verdicts

272k1692 Duty as question of fact or law generally

272 Negligence

272XVIII Actions

272XVIII(D) Questions for Jury and Directed Verdicts

272k1693 Negligence as question of fact or law generally

272 Negligence

272XVIII Actions

272XVIII(D) Questions for Jury and Directed Verdicts

272k1712 Proximate Cause

272k1713 In general

The existence of a duty is a question of law for the court to decide; however, the issues of breach and proximate cause are factual matters for a jury to decide provided there is a genuine issue of material fact regarding those issues.

9 Cases that cite this headnote

**[8] Negligence**

~ Necessity and Existence of Duty

**Negligence**

~ Breach of Duty

272 Negligence

272II Necessity and Existence of Duty

272k210 In general

272 Negligence

272IV Breach of Duty

272k250 In general

There can be no recovery in tort for negligence unless the defendant has breached a duty owed to the plaintiff.

5 Cases that cite this headnote

**[9] Negligence**

~ Relationship between parties

272 Negligence

272II Necessity and Existence of Duty

272k214 Relationship between parties

Duty is a question of whether the defendant and the plaintiff stood in such a relationship to one another that the law imposed upon the defendant an obligation of reasonable conduct for the benefit of the plaintiff.

10 Cases that cite this headnote

**[10] Negligence**

-- Necessity and Existence of Duty

272 Negligence

272II Necessity and Existence of Duty

272k210 In general

In determining whether a duty exists, a court looks to certain relevant factors, including: (1) the reasonable foreseeability that the defendant's conduct may injure another; (2) the likelihood of an injury occurring; (3) the magnitude of the burden of guarding against such injury; and (4) the consequences of placing that burden on the defendant.

7 Cases that cite this headnote

**[11] Gas**

-- Care required in general

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k17 Care required in general

Gas is a dangerous substance or commodity when it is not under control.

1 Cases that cite this headnote

**[12] Gas**

-- Nature and grounds of liability

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k16 Nature and grounds of liability

A gas company is not liable as an insurer for injuries sustained as the result of the escape of gas; rather, the company is liable for its negligence in permitting the gas to escape.

Cases that cite this headnote

**[13] Gas**

-- Care required in general

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k17 Care required in general

A gas company must exercise a degree of care to prevent the escape of gas from its pipes commensurate with or proportional to the level of danger which it is the company's duty to avoid.

Cases that cite this headnote

**[14] Gas**

-- Care required in general

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k17 Care required in general

While a gas company must exercise the requisite degree of care so that no injury occurs in the distribution of gas while it is under the company's control, such responsibility is limited to the time the gas is in the company's own pipes.

Cases that cite this headnote

**[15] Gas**

-- Defects, acts or omissions causing injury

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k18 Defects, acts or omissions causing injury

Where a gas company does not install the pipes or fixtures on a customer's premises, and does not own them and has no control over them, the company is not responsible for their condition or for their maintenance, and as a result is not liable for injuries caused by a leak therein of which the company had no knowledge.

Cases that cite this headnote

**[16] Negligence**

~ Necessity and Existence of Duty

272 Negligence

272II Necessity and Existence of Duty

272k210 In general

A person's duty can extend no further than the person's right, power, and authority to implement it.

3 Cases that cite this headnote

**[17] Gas**

~ Inspection

190 Gas

190k11 Inspection

Gas company employees do not have the right to enter the premises of their customers to inspect pipes or fixtures except upon the license or permission of the owner.

Cases that cite this headnote

**[18] Gas**

~ Care required in general

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k17 Care required in general

The consumer, by application for gas service, assumes the burden of inspecting and maintaining the pipes and fittings on the consumer's property in a manner reasonably suited to meet the required service.

Cases that cite this headnote

**[19] Gas**

~ Defects, acts or omissions causing injury

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k18 Defects, acts or omissions causing injury

The gas company has the right to assume that the customer's interior system of pipes and fittings is sufficiently secure to permit the gas to be introduced with safety.

Cases that cite this headnote

**[20] Negligence**

~ Knowledge or notice

272 Negligence

272II Necessity and Existence of Duty

272k212 Knowledge or notice

In a negligence action, knowledge of the facts out of which the duty to act arises is essential; in order that an act or omission may be regarded as negligent, the defendant must have knowledge, or ought to have known from the circumstances, that the allegedly negligent act or omission endangered another.

2 Cases that cite this headnote

**[21] Gas**

~ Defects, acts or omissions causing injury

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k18 Defects, acts or omissions causing injury

The common law rule of no duty of a gas company with respect to a consumer's pipes or fittings is premised on the gas company's lack of knowledge or notice of a gas leak.

1 Cases that cite this headnote

**[22] Gas**

~ Defects, acts or omissions causing injury

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k18 Defects, acts or omissions causing injury

Where it appears that a gas company has knowledge that gas is escaping in a building occupied by one of its consumers it becomes the duty of the gas company to shut off the gas supply until the necessary repairs have been made although the defective pipe or apparatus does not belong to the company and is not in its charge or custody.

1 Cases that cite this headnote

## KC REPLY APPENDIX 7

**[23] Gas**

~ Care required in general

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k17 Care required in general

Whenever a gas company is in possession of facts that would suggest to a person of ordinary care and prudence that an appliance of a customer is leaking or is otherwise unsafe for the transportation of gas, the company has a duty to investigate, as a person of ordinary care and prudence similarly situated and handling such a dangerous substance would do, before it continues to furnish additional gas.

Cases that cite this headnote

**[24] Gas**

~ Care required in general

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k17 Care required in general

The duty to exercise reasonable diligence to inspect or shut off the gas supply is measured by the likelihood of injury; circumstances may be such as to require a gas company to investigate immediately and shut off the gas supply until repairs are made.

Cases that cite this headnote

**[25] Gas**

~ Care required in general

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k17 Care required in general

(Formerly 190k18)

Knowledge that would impose on a gas company a duty to investigate a gas leak in an appliance on a customer's premises is not limited to actual knowledge, but may include constructive knowledge or notice; it is sufficient if the gas company received facts

which would have made the defects known to an ordinary prudent person.

1 Cases that cite this headnote

**[26] Gas**

~ Nature and grounds of liability

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k16 Nature and grounds of liability

The rule in Illinois as to the liability of a gas company is such company is responsible for a customer's pipe if it has knowledge of a leak or of a possible defect therein.

Cases that cite this headnote

**[27] Products Liability**

~ Care required

**Products Liability**

~ Component parts

**Products Liability**

~ Foreseeable or intended use

313A Products Liability

313AII Elements and Concepts

313Ak115 Care required

(Formerly 313Ak10)

313A Products Liability

313AII Elements and Concepts

313Ak132 Warnings or Instructions

313Ak139 Component parts

(Formerly 313Ak14)

313A Products Liability

313AII Elements and Concepts

313Ak151 Foreseeable or intended use

(Formerly 313Ak15)

When a party can reasonably foresee that its product will be used as an integral component of a defective and unreasonably dangerous product, there is a duty upon that party to undertake corrective action to alleviate, if possible, the hazard; the duty is simply to use reasonable care in dealing with the hazard, including a duty to warn.

1 Cases that cite this headnote

**[28] Gas**

**KC REPLY APPENDIX 8**

~ Care required in general

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k17 Care required in general

Natural gas company owed customer a common law duty of reasonable care to warn of danger associated with brazed gas appliance connector; company had actual knowledge that the sulfides in gas corroded brazed connectors, ultimately causing a gas leak.

1 Cases that cite this headnote

**[29] Public Utilities**

~ Regulation of Charges

317A Public Utilities

317AII Regulation

317Ak119 Regulation of Charges

317Ak119.1 In general

A "tariff" is a public document setting forth services being offered, rates and charges with respect to services, and governing rules, regulations, and practices relating to those services.

8 Cases that cite this headnote

**[30] Public Utilities**

~ Regulation of Charges

317A Public Utilities

317AII Regulation

317Ak119 Regulation of Charges

317Ak119.1 In general

A public utility tariff is usually drafted by the regulated utility, but when duly filed with the Illinois Commerce Commission, it binds both the utility and the customer and governs their relationship. S.H.A. 220 ILCS 5/9-102.

5 Cases that cite this headnote

**[31] Public Utilities**

~ Regulation of Charges

317A Public Utilities

317AII Regulation

317Ak119 Regulation of Charges

317Ak119.1 In general

Once the Illinois Commerce Commission approves a public utility tariff, it is a law, not a contract, and has the force and effect of a statute. S.H.A. 220 ILCS 5/9-102.

3 Cases that cite this headnote

**[32] Public Utilities**

~ Regulation

317A Public Utilities

317AII Regulation

317Ak111 In general

A liability limitation tariff provision provides the source for, and determines the nature and extent of, a public utility's service obligations to its customers.

1 Cases that cite this headnote

**[33] Carriers**

~ Rates of freight

70 Carriers

70II Carriage of Goods

70II(J) Charges

70k189 Rates of freight

The filed rate doctrine's purpose is to ensure that the filed rates are the exclusive source of the terms and conditions by which the common carrier provides to its customers the services covered by the tariff; it does not serve as a shield against all actions based in state law.

1 Cases that cite this headnote

**[34] Public Utilities**

~ Regulation

317A Public Utilities

317AII Regulation

317Ak111 In general

Where a utility tariff speaks to a specific duty, the tariff may be controlling; however, where the tariff does not address a particular situation, the common law applies and a common law duty analysis must be applied.

1 Cases that cite this headnote

**[35] Gas**

**KC REPLY APPENDIX 9**

~ Defects, acts or omissions causing injury

190 Gas

190k15 Injuries from Escape or Explosion of Gas

190k18 Defects, acts or omissions causing injury

Limitation of liability provision in natural gas tariff that stated that the customer was responsible for maintaining all gas utilization equipment on customer's premises did not abrogate gas company's common law duty to warn customer of a gas leak in a customer's gas appliance if the company had knowledge of such a leak or knowledge that the appliance was unsafe for transporting gas, where the tariff did not expressly disavow the common law duty.

2 Cases that cite this headnote

**[36] Public Utilities**

~ Regulation of Charges

317A Public Utilities

317AII Regulation

317Ak119 Regulation of Charges

317Ak119.1 In general

Although a utility tariff is not a legislative enactment, its interpretation is governed by the rules of statutory construction.

Cases that cite this headnote

**[37] Statutes**

~ Intent

361 Statutes

361III Construction

361III(A) In General

361k1071 Intent

361k1072 In general

(Formerly 361k181(1))

The cardinal rule of interpreting statutes, to which all other canons and rules are subordinate, is to ascertain and give effect to the intent of the legislature.

2 Cases that cite this headnote

**[38] Statutes**

~ Presumptions, inferences, and burden of proof

361 Statutes

361IV Operation and Effect

361k1402 Construction in View of Effects, Consequences, or Results

361k1406 Presumptions, inferences, and burden of proof

(Formerly 361k212.3)

Although a court should first consider the statutory language, a court must presume that the legislature, in enacting a statute, did not intend absurdity or injustice.

3 Cases that cite this headnote

**[39] Municipal Corporations**

~ Construction and operation

**Statutes**

~ Reason, reasonableness, and rationality

268 Municipal Corporations

268IV Proceedings of Council or Other Governing Body

268IV(B) Ordinances and By-Laws in General

268k120 Construction and operation

361 Statutes

361III Construction

361III(A) In General

361k1066 Reason, reasonableness, and rationality

(Formerly 361k181(2))

A statute or ordinance must receive a sensible construction, even though such construction qualifies the universality of its language.

3 Cases that cite this headnote

**[40] Public Utilities**

~ Nature and extent in general

317A Public Utilities

317AII Regulation

317Ak119 Regulation of Charges

317Ak120 Nature and extent in general

Utility rate regulation is one of legislative control and is not a judicial function.

Cases that cite this headnote

**[41] Public Utilities**

## KC REPLY APPENDIX 10

~ Constitutional and statutory provisions

317A Public Utilities

317A1 In General

317Ak102 Constitutional and statutory provisions

The Public Utilities Act is in derogation of the common law; accordingly, the Act is to be strictly construed in favor of persons sought to be subjected to its operation, and thus, the statute is to be strictly construed in favor of the utility company. S.H.A. 220 ILCS 5/9-102.

6 Cases that cite this headnote

**[42] Public Utilities**

~ Regulation of Charges

317A Public Utilities

317A11 Regulation

317Ak119 Regulation of Charges

317Ak119.1 In general

Because the utility company drafts a tariff, it is generally accepted that language in a tariff, especially exculpatory language, is to be strictly construed against the utility company and in favor of the customer.

2 Cases that cite this headnote

**[43] Statutes**

~ Liberal or strict construction

361 Statutes

361111 Construction

361111(G) Other Law, Construction with Reference to

361k1203 Common or Civil Law

361k1206 Statutory Alteration or Abrogation of Common Law

361k1206(3) Liberal or strict construction (Formerly 361k239)

A court cannot construe a statute in derogation of the common law beyond what the words of the statute expresses or beyond what is necessarily implied from what is expressed.

10 Cases that cite this headnote

**[44] Statutes**

~ Common or civil law

361 Statutes

361111 Construction

361111(M) Presumptions and Inferences as to Construction

361k1381 Other Law, Construction with Reference to

361k1384 Common or civil law (Formerly 361k239)

In construing statutes in derogation of the common law, a court will not presume that an innovation thereon was intended further than the innovation which the statute specifies or clearly implies.

12 Cases that cite this headnote

**Attorneys and Law Firms**

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Barbara Baran and Darren J. Hunter, of Ross & Hardies, Chicago, for amici curiae The Peoples Gas Light & Coke Co. et al.

**Opinion**

Justice FREEMAN delivered the opinion of the court:

Plaintiff, Christy Adams, as special administrator of the estate of Janice Adams, **\*\*1253 \*\*\*307** brought a wrongful-death action in the circuit court of Cook County against Northern Illinois Gas Company (NI-Gas). The circuit court granted NI-Gas' motion for summary judgment. The appellate court reversed the grant of summary judgment in favor of NI-Gas and remanded the cause for further proceedings. 333 Ill.App.3d 215, 266 Ill.Dec. 411, 774 N.E.2d 850. We allowed NI-Gas' petition for leave to appeal (177 Ill.2d R. 315(a)), and now affirm the appellate court.

## BACKGROUND

The record contains the following pertinent evidence. Since 1971, Janice Adams (decedent) resided in a house located at 1294 Greenbay Avenue in Calumet City. Decedent's mother, Lucia Georgevich, bought the house, but decedent paid the mortgage and the utilities. Various appliances in the house, including a range, were fueled by natural gas.

\*37 On the evening of December 7, 1995, decedent arrived home, opened a door, and stepped inside. The house exploded and was engulfed in flames, causing her death.

First at the scene was the Calumet City fire department. Assistant chief Dan Smits and fire investigator Joe Ratkovich investigated the cause and origin of the explosion. Smits saw the fire and saw that the walls of the house had been blown out. He observed the body of decedent just inside what had been an entrance to the house. Smits inspected the gas meter, gas piping, and gas appliances and directed that all those items be removed and preserved.

The Calumet City fire department determined that the cause of the explosion and fire was the failure of the flexible brass gas connector that connected the kitchen range to the gas supply. The brand name of the connector was "Cobra." Failure of the connector permitted a large amount of natural gas to escape and accumulate in the house. When decedent entered the house and turned on an electric light, a small spark from the switch ignited the gas. The Illinois State Fire Marshall, the United States Bureau of Alcohol, Tobacco and Firearms, and the private fire investigator employed by the homeowner's insurance carrier also investigated the explosion and all agreed that it was caused by the failure of the gas connector to the range.

Plaintiff, one of decedent's daughters, brought a wrongful-death action in a two-count, first amended complaint. Count II named NI-Gas as a defendant.<sup>1</sup> Plaintiff alleged that NI-Gas "knew that Cobra brand natural gas appliance connectors were defective and prone to failure resulting in natural gas leaks and explosions." Plaintiff alleged that NI-Gas "had a duty to warn its customers, including plaintiff's decedent, about the existence of

Cobra brand \*38 natural gas appliance connectors and the dangers of natural gas leak, explosion and fire associated with these connectors." Plaintiff alleged that NI-Gas breached this duty to warn in that NI-Gas: failed to provide (a) any or (b) adequate \*\*1254 \*\*\*308 warning; (c) used an ineffective means to inform customers; (d) failed to initiate an inspection program to identify and remove Cobra brand natural gas appliance connectors from customer homes and businesses; and (e) failed to properly inspect decedent's home "to cause the removal of the aforesaid Cobra brand connector."

The record includes the depositions of several opinion witnesses, including Charles Lamar, Wayne Genck, Norman Breyer, and Edward Karnes. Their testimony adduced the following additional evidence.

The connector in this case was manufactured by the Cobra Hose Company, which has been out of business since 1979. Made as early as 1953, Cobra connectors were widely used in Illinois and other states. The Cobra connector essentially was a corrugated flexible brass tube with threaded brass connectors at each end that connect a gas appliance to the hard pipe gas source. The threaded connectors were telescoped and fastened to the ends of the corrugated brass tube by a process known as brazing. The compound used in the brazing process is composed of phosphorized brazing alloys containing a substantial portion of phosphorous and a high percentage of copper.

\*39 It is undisputed that natural gas, in its original state, is odorless. The chemical ethyl mercaptan, which is a sulfur component, is added as an odorant to give natural gas its distinctive smell. In addition to sulfur that is intentionally added, natural gas itself produces sulfur compounds through intrinsic chemical reactions. By law, NI-Gas is required to supply odorized gas to its customers as a safety precaution, so that customers more easily can detect a gas leak. The natural gas that NI-Gas supplied to decedent was as the law required it to be.

However, when sulfur is added to natural gas, as in the present case, a chemical reaction begins to occur between the phosphorous brazing alloy and the sulfur. This chemical reaction causes the brazed joint to corrode and deteriorate. Over time, the deterioration of the brazed joint results in its separation from the corrugated tube and the consequent release of natural gas into the home. Even

the naturally occurring sulfides in the gas are sufficient to cause the brazed connector eventually to fail.

In 1968, the American National Standards Institute (ANSI)<sup>2</sup> revised its standards on gas connectors and banned phosphorous brazing. ANSI's Z21 subcommittee on connectors is the committee that has jurisdiction over all domestic standards for natural gas ranges, furnaces, water heaters, and connectors. The Z21 specifications were modified to warn that the use of brazing compounds that contain phosphorous can result in a brittle joint and can be deadly.

The record contains evidence that NI-Gas was aware of the potential danger in homes using Cobra connectors.

\*40 In May 1976, NI-Gas' supervisor of Research Services reported to the Z21 subcommittee that the "sudden, mysterious separation of brass connectors and their brazed-on end fittings has been a concern of gas utility people for several years." In a letter dated December 14, 1979, the United States Consumer Product Safety Commission informed \*\*1255 \*\*\*309 the American Gas Association (AGA) that Cobra connectors allegedly caused a number of fires in homes. According to the letter, while some jurisdictions did not allow the installation of Cobra connectors, many such connectors "may still be in service, and therefore may be susceptible to creating a significant hazard to the occupants of those residences equipped with such connectors." On December 19, the president of the AGA sent a letter to all its member companies, including NI-Gas, stating that the Commission had notified AGA that Cobra connectors had an increasing potential to fail over time.

The record also includes copies of "Consumer News" notices that NI-Gas sent to its customers. The August/September 1978, June/July 1980, summer/fall 1981, and December 1981 notices indicated that an old connector could crack, creating an unsafe condition, when the appliance was moved. The December 1981, January 1985, May 1986, and June 1987 notices warned: "The U.S. Consumer Product Safety Commission has warned that certain appliance connectors manufactured prior to 1968 may be unsafe. If you are concerned, do not try to move the appliance to inspect the connector. Instead, call a qualified service agency of NI-Gas to make the inspection."

Also, NI-Gas knew that failed Cobra connectors were determined to have caused many explosions and fires within its service area, including Aurora, Evanston, and Rockford. In the 1970s there were a series of fires in the Village of South Holland associated with brazed connectors. Wayne Kortum, a volunteer firefighter in South Holland and a NI-Gas employee, informed NI-Gas \*41 supervisors at the Glenwood district office, the district that includes the decedent's home, about the connectors involved with these fires. Thereafter, Kortum attended a general meeting at the Glenwood office where NI-Gas supervisors informed him and other service employees that there were problems with brazed connectors and that the service employees should look for these connectors in customers' homes.

In November 1984, NI-Gas representatives participated in a meeting with officials from the Village of Skokie. The Skokie fire department had determined that several fires and an explosion in the Village were related to brazed connector failures. Carol Anderson, one of the NI-Gas attendees, testified that in the 1980s she was aware that brazed connectors were a hazard. According to John Agosti, a Skokie fire official, NI-Gas represented that it would notify its service and construction personnel about replacing brazed connectors. In turn, these employees would warn the NI-Gas customers with whom they came in contact.

Charles Henry, a trained NI-Gas serviceman, testified in a deposition as follows. NI-Gas instructed its service employees on the potential danger of Cobra connectors. When a NI-Gas employee encountered a brazed connector, the employee was required to tag the connector and advise the customer that the connector needed to be replaced as soon as possible.

Decedent's ex-husband, Leonard Adams, testified in a deposition as follows. He had observed NI-Gas employees read the gas meter in the utility room of decedent's home on occasion, but they did not examine anything in the house other than the meter. In 1978 or 1980, after having a new clothes drier installed by the appliance retailer, a gas leak was detected. Decedent telephoned NI-Gas. A NI-Gas employee came to the house and checked the gas pipe between the meter and the clothes \*42 drier. The employee discovered \*\*1256 \*\*\*310 that the pipe was leaking and tightened it; he did not do anything else.

NI-Gas moved for summary judgment against plaintiff. NI-Gas contended that it did not owe decedent a legal duty to warn her that her Cobra connector was potentially hazardous because decedent owned the connector and not NI-Gas. The circuit court granted NI-Gas' motion for summary judgment against plaintiff.<sup>3</sup>

Plaintiff appealed. Initially, the appellate court, with one justice dissenting, affirmed the grant of summary judgment in favor of NI-Gas, holding that NI-Gas did not owe decedent a legal duty. However, the appellate court modified its opinion upon denial of plaintiff's petition for rehearing. In its modified opinion, the appellate court, *inter alia*, reversed the grant of summary judgment in favor of NI-Gas. The appellate court held, "as a matter of law, that a utility company that has actual knowledge of a dangerous condition associated with the use of its product has a responsibility to its customers to warn them of that danger." 333 Ill.App.3d at 224, 266 Ill.Dec. 411, 774 N.E.2d 850.

This court allowed NI-Gas' petition for leave to appeal. 177 Ill.2d R. 315(a). We subsequently granted the People's Gas Light and Coke Company *et al.* leave to submit an *amicus curiae* brief in support of NI-Gas. See 155 Ill.2d R. 345.

## ANALYSIS

[1] This matter is before us on the grant of summary judgment in favor of NI-Gas. The purpose of summary judgment is not to try a question of fact, but rather to determine whether a genuine issue of material fact exists. *Happel v. Wal-Mart Stores, Inc.*, 199 Ill.2d 179, 186, 262 Ill.Dec. 815, 766 N.E.2d 1118 (2002); *Gilbert v. Sycamore Municipal Hospital*, 156 Ill.2d 511, 517, 190 Ill.Dec. 758, 622 N.E.2d 788 (1993). Summary judgment is appropriate only where "the pleadings, depositions, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." 735 ILCS 5/2-1005(c) (West 2002).

[2] [3] [4] [5] In determining whether a genuine issue as to any material fact exists, a court must construe the pleadings, depositions, admissions, and affidavits strictly against the movant and liberally in favor of the opponent.

A triable issue precluding summary judgment exists where the material facts are disputed, or where, the material facts being undisputed, reasonable persons might draw different inferences from the undisputed facts. The use of the summary judgment procedure is to be encouraged as an aid in the expeditious disposition of a lawsuit. However, it is a drastic means of disposing of litigation and, therefore, should be allowed only when the right of the moving party is clear and free from doubt. *Gilbert*, 156 Ill.2d at 518, 190 Ill.Dec. 758, 622 N.E.2d 788 (and cases cited therein); accord *Espinoza v. Elgin, Joliet & Eastern Ry. Co.*, 165 Ill.2d 107, 113-14, 208 Ill.Dec. 662, 649 N.E.2d 1323 (1995). In appeals from summary judgment rulings, review is *de novo*. *Outboard Marine Corp. v. Liberty Mutual Insurance Co.*, 154 Ill.2d 90, 102, 180 Ill.Dec. 691, 607 N.E.2d 1204 (1992).

\*\*1257 \*\*\*311 [6] [7] Plaintiff alleged negligence on the part of NI-Gas. To prevail in an action for negligence, the plaintiff must establish that the defendant owed a duty of care, that the defendant breached that duty, and that the plaintiff incurred injuries proximately caused by the breach. *Espinoza*, 165 Ill.2d at 114, 208 Ill.Dec. 662, 649 N.E.2d 1323; *Ward v. K mart Corp.*, 136 Ill.2d 132, 140, 143 Ill.Dec. 288, 554 N.E.2d 223 (1990). The existence of a duty is a question of law for the court to decide; however, the issues of breach \*44 and proximate cause are factual matters for a jury to decide (*Thompson v. County of Cook*, 154 Ill.2d 374, 382, 181 Ill.Dec. 922, 609 N.E.2d 290 (1993)), provided there is a genuine issue of material fact regarding those issues (*Espinoza*, 165 Ill.2d at 114, 208 Ill.Dec. 662, 649 N.E.2d 1323).

In this case, the sole inquiry before us concerns the existence of a legal duty. Plaintiff asserts that NI-Gas owed decedent a duty to warn her that Cobra connectors were potentially hazardous. NI-Gas denies that it had such a duty because decedent owned the connector and not NI-Gas.

[8] [9] [10] There can be no recovery in tort for negligence unless the defendant has breached a duty owed to the plaintiff. *Boyd v. Racine Currency Exchange, Inc.*, 56 Ill.2d 95, 97, 306 N.E.2d 39 (1973); accord *LaFever v. Kemlite Co.*, 185 Ill.2d 380, 388, 235 Ill.Dec. 886, 706 N.E.2d 441 (1998). Duty is a question of whether the defendant and the plaintiff stood in such a relationship to one another that the law imposed upon the defendant an obligation of reasonable conduct for the benefit of

the plaintiff. In determining whether a duty exists, a court looks to certain relevant factors, including: (1) the reasonable foreseeability that the defendant's conduct may injure another, (2) the likelihood of an injury occurring, (3) the magnitude of the burden of guarding against such injury, and (4) the consequences of placing that burden on the defendant. *Happel*, 199 Ill.2d at 186–87, 262 Ill.Dec. 815, 766 N.E.2d 1118; *Ward*, 136 Ill.2d at 140–41, 143 Ill.Dec. 288, 554 N.E.2d 223; *Kirk v. Michael Reese Hospital & Medical Center*, 117 Ill.2d 507, 526, 111 Ill.Dec. 944, 513 N.E.2d 387 (1987). In support of their respective positions, the parties invoke two sources of law: (1) the common law, and (2) NI–Gas' tariff on file with the Illinois Commerce Commission.

### I. Common Law

American consumers have been using gas as fuel for illumination or heat for over a century. Courts from across the nation, including Illinois courts, long ago considered the factors in determining the existence of a duty with respect to the duties that gas distributors owe \*45 to their customers concerning escaping gas. The common law, which is always heedful of realities when it formulates rules to govern conduct (*Graham v. North Carolina Butane Gas Co.*, 231 N.C. 680, 684–85, 58 S.E.2d 757, 761 (1950)), has established the following principles.

[11] [12] [13] Gas is a dangerous substance or commodity when it is not under control. *Metz v. Central Illinois Electric & Gas Co.*, 32 Ill.2d 446, 450, 207 N.E.2d 305 (1965); *McChure v. Hoopston Gas & Electric Co.*, 303 Ill. 89, 97, 135 N.E. 43 (1922); accord *Suiter v. Ohio Valley Gas Co.*, 10 Ohio St.2d 77, 78, 39 O.O.2d 65, 225 N.E.2d 792, 793 (1967); *Bellefuiil v. Willmar Gas Co.*, 243 Minn. 123, 126, 66 N.W.2d 779, 782 (1954); *Graham*, 231 N.C. at 684, 58 S.E.2d at 761. However, a gas company is not liable as an insurer for injuries sustained as the result of the escape of gas. Rather, the company is liable for its negligence in permitting the gas to escape. \*\*1258 \*\*\*312 *Pappas v. Peoples Gas Light & Coke Co.*, 350 Ill.App. 541, 548, 113 N.E.2d 585 (1953); accord *Bellefuiil*, 243 Minn. at 126, 66 N.W.2d at 782; *Graham*, 231 N.C. at 685, 58 S.E.2d at 761; 27A Am.Jur. 2d *Energy & Power Sources* § 368, at 278 (1996); 38A C.J.S. *Gas* § 119, at 143 (1996). Expressions of the degree of care that a gas company must exercise range from “reasonable” (see, e.g., *Graham*, 231 N.C. at 685, 58 S.E.2d at 761) to “high” (see,

e.g., *McChure*, 303 Ill. at 97, 135 N.E. 43). This variety of expression simply means that a gas company must exercise a degree of care to prevent the escape of gas from its pipes commensurate with or proportional to the level of danger which it is the company's duty to avoid. *Metz*, 32 Ill.2d at 450, 207 N.E.2d 305; *Cosgrove v. Commonwealth Edison Co.*, 315 Ill.App.3d 651, 654–55, 248 Ill.Dec. 447, 734 N.E.2d 155 (2000); accord *Lewis v. Vermont Gas Corp.*, 121 Vt. 168, 182, 151 A.2d 297, 306 (1959); *Doxstater v. Northwest Cities Gas Co.*, 65 Idaho 814, 826–27, 154 P.2d 498, 504 (1944); *Bellefuiil*, 243 Minn. at 126, 66 N.W.2d at 782; 27A Am.Jur.2d *Energy & Power Sources* § 373, at 281 (1996); 38A C.J.S. *Gas* § 120, at 145–46 (1996); L. Tellier, \*46 Annotation, *Liability of Gas Co. for Injury or Damage Due to Defects in Service Lines on Consumer's Premises*, 26 A.L.R.2d 136, 146 (1952).

[14] While a gas company must exercise the requisite degree of care so that no injury occurs in the distribution of gas while it is under the company's control, such responsibility is limited to the time the gas is in the company's own pipes. *Doxstater*, 65 Idaho at 827, 154 P.2d at 504 (collecting cases). In Illinois, the seminal example of the common law rule pertaining to gas distribution in a consumer's pipes and fixtures is *Clare v. Bond County Gas Co.*, 356 Ill. 241, 190 N.E. 278 (1934).

In *Clare*, the plaintiff opened a shop and hired a plumber to install a gas stove for heat. After the installation, she noticed an offensive odor that irritated her eyes and gave her a headache. She notified the gas company. The president of the gas company visited the shop several times and made suggestions to remedy the situation. His suggestions were followed, but the problem continued. The smell was so strong in the closet where the gas meter was located that the plaintiff kept the door to the closet closed. Several weeks after the unsuccessful attempts to locate the source of the problem, a friend of the plaintiff was looking for a screwdriver. He lit a match to help him look for it in the dark closet. He opened the closet door and an explosion occurred. It was subsequently discovered that the gas pipe that ran beneath the floor contained holes caused by rust. The gas that escaped from the pipe had accumulated in the closet. *Clare*, 356 Ill. at 241–43, 190 N.E. 278. Appealing a judgment in favor of plaintiff, the gas company contended that “there was no evidence in the record to warrant the finding that it [the gas company] had notice and knowledge that the pipes were leaking and gas was escaping into the building; that without such notice or

knowledge there was no duty incumbent upon it to shut off the gas supply.” *Clare*, 356 Ill. at 243, 190 N.E. 278.

[15] \*47 Reversing the judgment in favor of plaintiff, *Clare* relied on established common law: “In the absence of notice of defects it is not incumbent upon a gas company to exercise reasonable care to ascertain whether or not service pipes under the control of the property owner or the consumer are fit for the furnishing of gas.” *Clare*, 356 Ill. at 244, 190 N.E. 278. Where a gas company does not install the pipes or fixtures on a customer's premises, and does not own them and has no control over them, the company is not responsible for their condition or for their maintenance., \*\*1259 \*\*\*313 and as a result is not liable for injuries caused by a leak therein of which the company had no knowledge. *Clare*, 356 Ill. at 244, 190 N.E. 278 (collecting cases). *Clare* looked to the common law as evolved up to that time and today continues to accord with our understanding of the common law rule. Accord *Oliver v. Peoples Gas Light & Coke Co.*, 5 Ill.App.3d 1093, 1099, 284 N.E.2d 432 (1972); accord *Bellefui*, 243 Minn. at 126, 66 N.W.2d at 782 (discussing rule in context of gas appliances); *Doxstater*, 65 Idaho at 827–28, 154 P.2d at 504, quoting *Kelley v. Public Service Co. of Northern Illinois*, 300 Ill.App. 354, 362, 21 N.E.2d 43 (1939); 27A Am.Jur.2d *Energy & Power Sources* §§ 394, 395 (1996) (stating rule in context of appliances); 27A Am.Jur.2d *Energy & Power Sources* § 403 (1996) (stating general rule); 38A C.J.S. *Gas* § 123, at 151–53 (1996); 26 A.L.R.2d at 156.

[16] [17] [18] [19] Courts reason that a person's duty can extend no further than the person's right, power, and authority to implement it. Gas company employees do not have the right to enter the premises of their customers to inspect pipes or fixtures except upon the license or permission of the owner. *Clare*, 356 Ill. at 244, 190 N.E. 278. The consumer, by application for gas service, assumes the burden of inspecting and maintaining the pipes and fittings on the consumer's property in a manner reasonably suited to meet the required service. The company has the right to assume that the customer's interior system of pipes and \*48 fittings is sufficiently secure to permit the gas to be introduced with safety. *Clare*, 356 Ill. at 244–45, 190 N.E. 278 (collecting cases); accord *Bellefui*, 243 Minn. at 126–27, 66 N.W.2d at 782–83; *Graham*, 231 N.C. at 685, 58 S.E.2d at 761; *Moran Junior College v. Standard Oil Co. of California*, 184 Wash.

543, 552, 52 P.2d 342, 346 (1935); 27A Am.Jur.2d *Energy & Power Sources* § 403 (1996).

[20] [21] Courts also reason that, in a negligence action, knowledge of the facts out of which the duty to act arises is essential. In order that an act or omission may be regarded as negligent, the defendant must have knowledge, or ought to have known from the circumstances, that the allegedly negligent act or omission endangered another. *Weber v. Interstate Light & Power Co.*, 268 Wis. 479, 482, 68 N.W.2d 39, 41 (1955). Accordingly, the common law rule of no duty of a gas company with respect to a consumer's pipes or fittings is premised on the gas company's lack of knowledge or notice of a gas leak. See, e.g., *Clare*, 356 Ill. at 244, 190 N.E. 278 (stating rule with proviso of gas company's lack of knowledge or notice); *Bellefui*, 243 Minn. at 129, 66 N.W.2d at 784 (“the duty, by reason of actual or constructive notice of some dangerous condition, must arise before the gas company can be found negligent for its failure to inspect or shut off the gas supply”).

[22] [23] [24] [25] Considering the requirement of the gas company's knowledge or notice of a gas leak, the exception to the common law rule is evident:

“Where it appears that a gas company has knowledge that gas is escaping in a building occupied by one of its consumers it becomes the duty of the gas company to shut off the gas supply until the necessary repairs have been made although the defective pipe or apparatus does not belong to the company and is not in its charge or custody.” *Clare*, 356 Ill. at 243–44, 190 N.E. 278.

Accord *Graham*, 231 N.C. at 685, 58 S.E.2d at 761–62 (citing *Clare* ); \*49 27A Am.Jur.2d *Energy & Power Sources* § 413, at 309–10 (1996); 38A C.J.S. *Gas* § 123, at 153–54 (1996); 26 A.L.R.2d at 150. In the \*\*1260 \*\*\*314 specific context of gas appliances, courts have gone so far as to impose on a gas company that has knowledge of a gas leak a duty to inspect:

“[W]henver a gas company is in possession of facts that would suggest to a person of ordinary care and prudence that an appliance of a customer is leaking or is otherwise unsafe for the transportation of gas, the company has a duty to investigate, as a person of ordinary care and prudence similarly situated and handling such a dangerous substance would do, before it continues to furnish additional gas. The duty to

exercise reasonable diligence to inspect or shut off the gas supply is measured by the likelihood of injury. Circumstances may be such as to require a gas company to investigate immediately and shut off the gas supply until repairs are made. The nature of the notice may also affect the extent of inspection necessary.” *Bellefui*, 243 Minn. at 128–29, 66 N.W.2d at 783–84.

It is clear that the knowledge that would impose on a gas company this duty is not limited to actual knowledge, but may include constructive knowledge or notice. It is sufficient if the gas company received facts which would have made the defects known to an ordinary prudent person. For example, *Clare* was rendered in the context of the gas company's denial of “notice or knowledge.” (Emphasis added.) *Clare*, 356 Ill. at 243, 190 N.E. 278. Further, this court expressly—and correctly—stated the common law rule with the accepted proviso of a gas company's lack of knowledge (*Clare*, 356 Ill. at 243, 190 N.E. 278 (“Where it appears that a gas company has knowledge”)) or notice (*Clare*, 356 Ill. at 244, 190 N.E. 278 (“In the absence of notice”)). See *Mrdalj v. Public Service Co. of Northern Illinois*, 308 Ill.App. 424, 430, 31 N.E.2d 978 (1941); *Kelley*, 300 Ill.App. at 362, 21 N.E.2d 43; *Kilmer v. Browning*, 806 S.W.2d 75, 83 (Mo.App.1991); *Ruberg v. Skelly Oil Co.*, 297 N.W.2d 746, 751 (Minn.1980); *Fore v. United Natural Gas Co.*, 436 Pa. 499, 504–05, 261 A.2d 316, 318–19 (1970); *Bellefui*, 243 Minn. at 128–29, 66 N.W.2d at 783–84.

[26] \*50 Further, *Clare* was directed not only to actual gas leaks, but also to defects. *Clare*, 356 Ill. at 244, 190 N.E. 278 (“In the absence of notice of defects” (emphasis added)). “The rule in Illinois as to the liability of a gas company is such company is responsible for a customer's pipe if it has knowledge of a leak or of a possible defect therein.” (Emphasis added.) *Oliver*, 5 Ill.App.3d at 1099, 284 N.E.2d 432; accord *Bellefui*, 243 Minn. at 128–29, 66 N.W.2d at 783–84 (speaking of a customer's gas appliance that “is leaking or is otherwise unsafe for the transportation of gas” (emphasis added)); 27A Am.Jur.2d *Energy & Power Sources* § 413, at 310 (1996) (stating “that if a gas company has notice of a leak or defect in pipes or lines owned or controlled by a consumer, it is under a duty to notify the consumer and see that the leak or defect is repaired, or shut off the gas”).

This common law rule and corresponding exception serve the concept that a gas company is not an insurer for any injury sustained as a result of escaping gas, but rather is

liable only for its negligence. “To apply any other rule would make the gas supplier an insurer if anything went wrong with any of the appliances over which it had no control.” *Wilson v. Home Gas Co.*, 267 Minn. 162, 172, 125 N.W.2d 725, 732 (1964).

As the appellate court in this case recognized, Illinois courts have not addressed a gas company's duty to warn its customers of the possible deterioration of the customer's fixtures when they are damaged, in part, due to the gas product itself. \*\*1261 \*\*\*315 333 Ill.App.3d at 220, 266 Ill.Dec. 411, 774 N.E.2d 850. However, addressing the same facts as in this case, two decisions from other jurisdictions recognize that gas companies who have notice of the danger caused by sulfides in their gas coming in contact with brazed connectors owe common law tort duties: *Lemke v. Metropolitan Utilities District*, 243 Neb. 633, 502 N.W.2d 80 (1993), and \*51 *Halliburton v. Public Service Co. of Colorado*, 804 P.2d 213 (Colo.App.1990). We agree with the appellate court that these cases are instructive. 333 Ill.App.3d at 220–22, 266 Ill.Dec. 411, 774 N.E.2d 850.

In *Lemke*, a gas explosion destroyed the home of Lorraine and Kenneth Lemke and severely injured Lorraine. *Lemke*, 243 Neb. at 634–37, 502 N.W.2d at 82–84. The trial court found that the cause of the explosion was a Cobra connector, which failed due to the interaction of the phosphorous brazing alloy and the gas. Although there was evidence that the Metropolitan Utilities District (MUD) installed thousands of Cobra connectors in the homes of MUD customers, there was no evidence that MUD installed the Cobra connector to the plaintiff's gas range. The court entered judgment in favor of plaintiffs. *Lemke*, 243 Neb. at 642, 502 N.W.2d at 86.

Appealing from the judgment, MUD contended “that it had no duty to notify its customers concerning a potential hazard from Cobra connectors, especially a customer who may not have purchased the connector from MUD.” *Lemke*, 243 Neb. at 648, 502 N.W.2d at 90. The Nebraska Supreme Court rejected this contention.

The *Lemke* court reviewed its past statements of the earlier-discussed common law principles. The court concluded:

“Because a gas company has a nondelegable duty to exercise due care regarding natural gas supplied to a customer, a gas company's duty of care not

only pertains to the company's distribution of gas through its pipelines, but extends to distribution through a customer's service line or gas appliance that the company knows, or should know, is unsafe for conducting or using gas." *Lemke*, 243 Neb. at 651, 502 N.W.2d at 91.

The court noted, as the record in this case shows, that the American Gas Association warned all of its members, including MUD, that Cobra connectors presented a danger in the distribution of natural gas. The court reasoned:

\*52 "When MUD received information about the dangerous condition or potential hazard involving Cobra connectors but did not disseminate this critical information to its customers who were using gas appliances with Cobra connectors, MUD effectively exerted control in a situation that could eventually culminate in injury to customers who continued to use gas supplied by MUD." *Lemke*, 243 Neb. at 648, 502 N.W.2d at 89.

According to the court, that information

"placed MUD on notice that its customers who had gas appliances with Cobra connectors would be endangered when the connector separated from a gas service line or appliance. Consequently, when MUD became aware that the distribution of gas through a Cobra connector presented a risk of injury to customers, MUD had the duty to use due care, such as issuance of a warning, to protect customers \* \* \*." *Lemke*, 243 Neb. at 652, 502 N.W.2d at 92.

As in *Lemke*, NI-Gas' superior knowledge of the risks pertaining to Cobra connectors begat a duty of due care, such as issuing a warning to its customers.

In *Halliburton*, the Public Service Company of Colorado, similar to NI-Gas here, knew at least since the 1970s that a large \*\*1262 \*\*\*316 number of brazed connectors failed because of the interaction of the brazed connector and the sulfides in the gas. The court cited four reasons to impose a duty on the gas company to inspect plaintiff's brazed connector: (1) the relatively insignificant amount of time and expense that defendant would have expended to evaluate the connector and take corrective action; (2) two service calls at plaintiff's home after the gas company knew of this hazard, which affected approximately 45,000

homes in the Denver area; (3) the likelihood of the connector failing and possibly causing an explosion unless corrective action were taken; and (4) defendant's expertise in dealing with such problems. The court continued: "The most compelling reason, however, for imposing a duty upon defendant is that its product, natural gas, which contained the corrosive ethyl mercaptan, was a \*53 substantial factor in causing the deterioration of the connector tube." (Emphasis in original.) *Halliburton*, 804 P.2d at 216.

[27] At oral argument, plaintiff expressly clarified that the extent of NI-Gas' duty of reasonable care in this case should be to warn its customers of the dangers presented by its gas coming in contact with the brazed connectors. Thus, while no issue exists in this case regarding a duty to inspect every connector, we agree with the following from *Halliburton*: "When a party can reasonably foresee that its product will be used as an integral component of a defective and unreasonably dangerous product, there is a duty upon that party to undertake corrective action to alleviate, if possible, the hazard." *Halliburton*, 804 P.2d at 216. The duty is simply to use reasonable care in dealing with the hazard, including a duty to warn. *Halliburton*, 804 P.2d at 216-17. We agree with the appellate court that, "while not controlling, *Halliburton* is also instructive." 333 Ill.App.3d at 222, 266 Ill.Dec. 411, 774 N.E.2d 850.

*Halliburton* and *Lemke* acknowledged the common law rule of a gas company's lack of duty toward a customer's equipment absent knowledge of a defect, but recognized that the gas suppliers in those cases had knowledge of the danger of their product being in contact with brazed connectors. Those cases also noted that the danger in question was not one normally associated with the product and consumers were not in a position to be aware of the danger without adequate warnings. Since the gas companies helped create the danger and had superior knowledge of the hazard, they owed a responsibility to their customers with respect to that danger.

We consider *Halliburton* and *Lemke* to represent a reasoned adaptation of the common law to address the exigency presented by brazed connectors. We recognize that "[t]he growth and adaptation of the common law to our contemporary concerns should not impose impractical \*54 burdens or impossible duties." *Hensley v. Montgomery County*, 25 Md.App. 361, 367, 334 A.2d 542, 545-46 (1975). However, it is equally clear that

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“[r]easonable care is not a standard beyond the reach of any enterprise.” *Weinberg v. Dinger*, 106 N.J. 469, 494, 524 A.2d 366, 379 (1987).

[28] In the present case, as in *Halliburton* and *Lemke*, there is no dispute that NI–Gas had actual knowledge of the danger. NI–Gas knew that sulfides in the gas corroded brazed connectors, ultimately causing the connectors to leak gas; it was only a question of when the connector would fail. Based on its superior knowledge and the fact that it helped to create the dangerous condition, we hold that NI–Gas owed a common law duty of reasonable care with respect to the brazed connectors.

**\*\*1263 \*\*\*317** This holding is directed exclusively to the element of duty and is limited to the evidence contained in the present record. We repeat plaintiff’s clarification at oral argument that NI–Gas’ duty of reasonable care in this case consists only of warning and not inspection. We express no opinion as to the adequacy of NI–Gas’ conduct in this case. It is for the trier of fact to determine whether NI–Gas’ conduct met the standard of care required of it under the circumstances. Based on our disposition of this issue, we do not discuss other tort theories raised by the parties.

## II. Tariff

NI–Gas and supporting *amici* contend that NI–Gas’ tariff on file with the Illinois Commerce Commission “is the sole source” of its duties to its customers. NI–Gas points to the following provision of its tariff on file with the Commission at the time of the explosion:

“Equipment Furnished and Maintained by Customer.

All gas utilization equipment, piping, and vents furnished by the Customer shall be suitable for the purposes hereof and shall be installed and maintained by the **\*55** Customer at all times in accordance with accepted practice and in conformity with requirements of public health and safety, as set forth by the properly constituted authorities and by the Company.

The Company assumes no responsibility in connection with the installation, maintenance or operation of the Customer’s equipment and reserves the right to discontinue service if such equipment is in unsatisfactory condition.”

NI–Gas contends that the plain language of this provision bars imposition of a duty in this case.

[29] [30] [31] A tariff is a public document setting forth services being offered; rates and charges with respect to services; and governing rules, regulations, and practices relating to those services. *North River Insurance Co. v. Jones*, 275 Ill.App.3d 175, 185, 211 Ill.Dec. 604, 655 N.E.2d 987 (1995). The Public Utilities Act requires public utilities such as NI–Gas to file tariffs with the Illinois Commerce Commission. 220 ILCS 5/9–102 (West 1994). A tariff is usually drafted by the regulated utility, but when duly filed with the Commission, it binds both the utility and the customer and governs their relationship. See *Danisco Ingredients USA, Inc. v. Kansas City Power & Light Co.*, 267 Kan. 760, 765, 986 P.2d 377, 381 (1999). Once the Commission approves a tariff, it “is a law, not a contract, and has the force and effect of a statute.” *Illinois Central Gulf R.R. Co. v. Sankey Brothers, Inc.*, 67 Ill.App.3d 435, 439, 23 Ill.Dec. 749, 384 N.E.2d 543 (1978), *aff’d*, 78 Ill.2d 56, 34 Ill.Dec. 328, 398 N.E.2d 3 (1979).

Illinois law in this area originates in federal law. In *Western Union Telegraph Co. v. Esteve Brothers & Co.*, 256 U.S. 566, 571–72, 41 S.Ct. 584, 586, 65 L.Ed. 1094, 1097–98 (1921), the United States Supreme Court considered the legal effect of tariffs filed pursuant to the Interstate Commerce Act:

“The Act of 1910 [36 Stat. 539, 544] introduced a new principle into the legal relations of the telegraph companies with their patrons which dominated and modified the principles previously governing them. Before the act the **\*56** companies had a common-law liability from which they might or might not extricate themselves according to views of policy prevailing in the several states. Thereafter, for all messages sent in interstate or foreign commerce, the outstanding consideration became that of uniformity and equality of rates. Uniformity demanded that the rate represent the **\*\*1264 \*\*\*318** whole duty and the whole liability of

the company. It could not be varied by agreement; still less could it be varied by lack of agreement. The rate became, not as before a matter of contract by which a legal liability could be modified, but a matter of law by which a uniform liability was imposed.”

Accord *In re Illinois Bell Switching Station Litigation*, 161 Ill.2d 233, 249, 204 Ill.Dec. 216, 641 N.E.2d 440 (1994) (Miller, J., specially concurring); *J. Meyer & Co. v. Illinois Bell Telephone Co.*, 88 Ill.App.3d 53, 57, 42 Ill.Dec. 942, 409 N.E.2d 557 (1980) (both citing *Esteve Brothers*, 256 U.S. 566, 41 S.Ct. 584, 65 L.Ed. 1094).

The United States Supreme Court has described the federal filed-rate doctrine as follows: “The rights as defined by the tariff cannot be varied or enlarged by either contract or tort of the carrier.” *American Telephone & Telegraph Co. v. Central Office Telephone, Inc.*, 524 U.S. 214, 227, 118 S.Ct. 1956, 1965, 141 L.Ed.2d 222, 236 (1998), quoting *Kcogh v. Chicago & Northwestern Ry. Co.*, 260 U.S. 156, 163, 43 S.Ct. 47, 49, 67 L.Ed. 183, 187 (1922). The filed-rate doctrine serves two goals: prevention of price discrimination among rate payers, and preservation of the role of regulatory agencies in deciding reasonable rates for public utilities and services. *Fax Telecommunicaciones, Inc. v. AT & T*, 138 F.3d 479, 489 (2d Cir.1998); *Wegoland Ltd. v. NYNEX Corp.*, 27 F.3d 17, 19 (2d Cir.1994); *Qwest Corp. v. Kelly*, 204 Ariz. 25, 35, 59 P.3d 789, 799 (2002) (and cases cited therein); *Lovejoy v. AT&T Corp.*, 92 Cal.App.4th 85, 99, 111 Cal.Rptr.2d 711, 721 (2001).

Tariff provisions, such as NI-Gas' tariff, are usually referred to as liability limitations. See, e.g., *Illinois Bell Switching Station Litigation*, 161 Ill.2d at 247, 204 Ill.Dec. 216, 641 N.E.2d 440 (Miller, \*57 J., specially concurring); *Danisco*, 267 Kan. at 768, 986 P.2d at 383. Liability limitations reflect: the status of public utilities as regulated monopolies whose operations are subject to extensive restrictions; the requirements of uniform, nondiscriminatory rates; and the goal of universal service, achieved through the preservation of utility prices that virtually all customers can afford. *Illinois Bell Switching Station*, 161 Ill.2d at 249, 204 Ill.Dec. 216, 641 N.E.2d 440 (Miller, J., specially concurring). The underlying theory of liability limitations is that, because a public utility is strictly regulated, its liability should be defined and limited

so that it may be able to provide service at reasonable rates. A reasonable rate is in part dependent on a rule limiting liability. *Illinois Bell Switching Station*, 161 Ill.2d at 244–46, 204 Ill.Dec. 216, 641 N.E.2d 440 (and cases cited therein); *Danisco*, 267 Kan. at 769, 986 P.2d at 384 (collecting cases). The goal is “to secure reasonable and just rates for all without undue preference or advantage to any. Since that end is attainable only by adherence to the approved rate, based upon an authorized classification, that rate ‘represents the whole duty and the whole liability of the company.’ ” *Western Union Telegraph Co. v. Priester*, 276 U.S. 252, 259, 48 S.Ct. 234, 235, 72 L.Ed. 555, 565 (1928), quoting *Esteve Brothers*, 256 U.S. at 572, 41 S.Ct. at 586, 65 L.Ed. at 1097.

[32] To be sure, in an action for negligence, the issue of a legal duty is generally distinguished from the issue of liability for breach of that duty. See, e.g., *Thompson*, 154 Ill.2d at 382, 181 Ill.Dec. 922, 609 N.E.2d 290. However, a “plaintiff cannot prevail against a defendant who is under no duty and equally cannot prevail against a defendant who is immune and to that extent the two concepts are the same.” 1 D. Dobbs, *Law of Torts* § 225, at 576 (2001). Illinois courts have long held that \*\*1265 \*\*\*319 a tariff provision such as the one at issue in this case provides the source for, and determines the nature and extent of, a public utility's service obligations \*58 to its customers. *Illinois Bell Switching Station*, 161 Ill.2d at 248, 204 Ill.Dec. 216, 641 N.E.2d 440 (Miller, J., specially concurring); *J. Meyer & Co.*, 88 Ill.App.3d at 55, 42 Ill.Dec. 942, 409 N.E.2d 557; *Sarelas v. Illinois Bell Telephone Co.*, 42 Ill.App.2d 372, 374–75, 192 N.E.2d 451 (1963).

[33] “Nonetheless, all state law causes of action are not necessarily precluded.” *Pink Dot, Inc. v. Teleport Communications Group*, 89 Cal.App.4th 407, 416, 107 Cal.Rptr.2d 392, 398 (2001). As explained in *Adamson v. WorldCom Communications, Inc.*, 190 Or.App. 215, 222, 78 P.3d 577, 582 (2003):

“The filed-rate doctrine bars only an action that seeks to vary the terms of an applicable tariff. [Citation.] Thus, the effect of a tariff on a particular claim depends on the nature of the claim and the specific terms of the tariff. If the claim is one that implicates the provisions of a tariff, then the tariff controls

according to its terms, which may either limit relief available or bar a claim entirely. But if the claim is unrelated to the tariff, then the claim is not limited or barred. In other words, merely because a tariff exists does not necessarily mean that a claim is barred.”

In the context of the federal filed-rate doctrine, we are reminded: “In order for the filed rate doctrine to serve its purpose, therefore, it need pre-empt only those suits that seek to alter the terms and conditions provided for in the tariff.” *Central Office*, 524 U.S. at 229, 118 S.Ct. at 1966, 141 L.Ed.2d at 237 (Rehnquist, C.J., concurring). Further:

“The tariff does not govern \* \* \* the entirety of the relationship between the common carrier and its customers. For example, it does not affect whatever duties state law might impose \* \* \*. The filed rate doctrine's purpose is to ensure that the filed rates are the exclusive source of the terms and conditions by which the common carrier provides to its customers the services covered by the tariff. It does not serve as a shield against all actions based in state law.” *Central Office*, 524 U.S. at 230–31, 118 S.Ct. at 1966–67, 141 L.Ed.2d at 238 (Rehnquist, C.J., concurring).

Illinois law accords with this reasoning.

\*59 In 1921, the General Assembly enacted the Public Utilities Act (Ill.Rev.Stat.1921, ch. 111 <sup>2</sup>/<sub>3</sub>, par. 1 *et seq.*). This court has described the legislative intent of the Act as follows:

“The Public Utilities Act [citation], under which the Commerce Commission regulates all public utilities, was enacted to assure the provision of efficient and adequate utility service to the public at a reasonable cost. Because unrestrained competition prior to adoption of the Act had often resulted in the financial failure of many utilities, the Act adopted a policy of regulated monopoly to assure that utilities would be able to earn a reasonable rate of return on their investment and thus would be able to provide the required service.” *Local 777, DUOC, Seafarers International Union of North America v. Illinois Commerce Comm'n*, 45 Ill.2d 527, 535, 260 N.E.2d 225 (1970) (and cases cited therein).

This court also has observed: “it cannot be doubted that the Public Utilities Act supersedes the common law liability of the carrier *so far as rates and unreasonable discrimination are concerned.*” (Emphasis added.) *Terminal R.R. Ass'n of St. Louis v. Public Utilities Comm'n*, 304 Ill. 312, 317, 136 N.E. 797 (1922). This court recognized: “The law is well settled in this State that the matter of rate regulation \*\*1266 \*\*\*320 is essentially one of legislative control. The fixing of rates is not a judicial function \* \* \*.” *Illinois Bell Telephone Co. v. Illinois Commerce Comm'n*, 55 Ill.2d 461, 469–70, 303 N.E.2d 364 (1973), quoting *Produce Terminal Corp. v. Illinois Commerce Comm'n ex rel. Peoples Gas Light & Coke Co.*, 414 Ill. 582, 589, 112 N.E.2d 141 (1953).

However, this court in *Pioneer Hi-Bred Corn Co. of Illinois v. Northern Illinois Gas Co.*, 61 Ill.2d 6, 329 N.E.2d 228 (1975), applied the established common law duty analysis as explained in *Clare* to the defendant utility, which is the same defendant utility in this case, *Pioneer Hi-Bred*, 61 Ill.2d at 12–14, 329 N.E.2d 228. In *Pioneer Hi-Bred*, plaintiff customer brought an action against NI-Gas to recover damages for an explosion and fire due to the failure of plaintiff's gas- \*60 fueled equipment. Plaintiff alleged, *inter alia*, common law negligence. The trial court refused plaintiff's proffered jury instruction that NI-Gas was negligent in that it failed to inspect the plaintiff's equipment. The jury found for NI-Gas. The appellate court reversed, holding that the trial court erred in refusing plaintiff's proffered jury instruction. This court reversed the appellate court and affirmed the judgment in favor of NI-Gas. Citing *Clare*, this court held that NI-Gas did not have a duty to inspect plaintiff's equipment and, therefore, plaintiff's proffered instruction was erroneous. *Pioneer Hi-Bred*, 61 Ill.2d at 13–14, 329 N.E.2d 228.

We presume that the court in *Pioneer Hi-Bred* was not unaware of the federal filed-rate doctrine as explained in the above-cited *Priester* and *Esteve Brothers* decisions from the United States Supreme Court. Additionally, according to NI-Gas, the tariff at issue in this case has been on file with the Commission “[s]ince at least 1955.”

However, despite this court's prior decisions interpreting the Public Utilities Act and recognizing that rate regulation is not a judicial function, despite prior decisions from the United States Supreme Court establishing the federal filed-rate doctrine, and despite the existence of the

*specific tariff in this case*, this court applied the established common law duty analysis to NI-Gas. Neither this court nor NI-Gas believed that this tariff precluded a common law analysis in a negligence action for personal injury.

[34] Similarly, this court in *Metz* applied the common law doctrine of *res ipsa loquitur* to the defendant utility. *Metz*, 32 Ill.2d at 448–52, 207 N.E.2d 305. Why did the appellate court and this court in each of these cases fail to mention the Public Utilities Act, the filed-rate doctrine, or any particular tariff? Because Illinois courts have recognized that where a utility tariff speaks to a specific duty, the tariff may be controlling; however, where the tariff does not address a \*61 particular situation, the common law applies and a common law duty analysis must be applied.

For example, in *Sarelas*, the defendant telephone company, due to a clerical error, disconnected one of the extensions of the plaintiff's office telephone for 2 ½ hours. The plaintiff sued the telephone company and its president for damages, alleging that defendant owed him a duty of continuing service, and that defendant violated this duty by interrupting service. The trial court dismissed plaintiff's complaint. *Sarelas*, 42 Ill.App.2d at 373–74, 192 N.E.2d 451.

On appeal, the appellate court held that the defendant's duty to plaintiff was based on the tariff that the defendant filed with the Illinois Commerce Commission. In so holding, the court reasoned:

\*\*1267 \*\*\*321 “[T]he extent to which defendants owed plaintiff ‘a legal duty’ is determined by the particular provisions of the tariff on file with the commission; there is no contract in this case on which plaintiff can rely, nor are his allegations of a breach of duty sufficient to constitute a claim in tort. He complains simply of the disconnection of his telephone extension, and claims a breach of duty which arises either from the tariff or not at all.” (Emphasis added.) *Sarelas*, 42 Ill.App.2d at 375, 192 N.E.2d 451.

In *Sarelas*, since the plaintiff could not plead a breach of duty sufficient to constitute a claim in tort, his duty was defined by the tariff. *Sarelas* clearly leaves open the existence of common law duties had the plaintiff been able to plead them.

More recently, in *Cosgrove*, our appellate court, applying a common law analysis, reinstated negligence and *res ipsa*

*loquitur* counts against NI-Gas. *Cosgrove*, 315 Ill.App.3d at 654–57, 248 Ill.Dec. 447, 734 N.E.2d 155. The court concluded: “NI-Gas is ‘subject to liability in tort’ ” pursuant to section 2 of the Joint Tortfeasor Contribution Act. *Cosgrove*, 315 Ill.App.3d at 658, 248 Ill.Dec. 447, 734 N.E.2d 155, quoting 740 ILCS 100/2 (West 1998).

Indeed, Illinois case law reveals that Illinois courts have long applied common law principles to defendant \*62 utilities subsequent to the 1921 enactment of the Public Utilities Act and despite the existence of tariffs filed with the Illinois Commerce Commission. See, e.g., *Metz*, 32 Ill.2d 446, 207 N.E.2d 305; *Clare*, 356 Ill. 241, 190 N.E. 278; *Cosgrove*, 315 Ill.App.3d 651, 248 Ill.Dec. 447, 734 N.E.2d 155; *Oliver*, 5 Ill.App.3d 1093, 284 N.E.2d 432; *Mrdalj*, 308 Ill.App. 424, 31 N.E.2d 978. Thus, whether NI-Gas' tariff bars plaintiff's cause of action depends on the nature of plaintiff's lawsuit and the meaning of the tariff's language.

In this case, NI-Gas contends that the appellate court's decision “cannot stand” in light of *Illinois Bell Switching Station*. We disagree, finding that case to be distinguishable. In *Illinois Bell Switching Station*, a telephone switching station caught fire, allegedly due to the negligent or willful failure of Illinois Bell to take fire prevention measures. The fire left many customers without telephone service for about a month. The customers filed a class action to seek to recover economic losses incurred due to that loss of service. Illinois Bell argued that its filed tariff defined the limits of its liability for interruptions in service. The class plaintiffs contended that the tariff should not bar their claims because the tariff was against public policy and conflicted with provisions of the Public Utilities Act. *Illinois Bell Switching Station*, 161 Ill.2d at 242–43, 204 Ill.Dec. 216, 641 N.E.2d 440.

In holding that the tariff controlled in that case, this court found no duty on which to base the class plaintiffs' claims. This court initially noted that Illinois Bell was nowhere charged with the duty to provide completely uninterrupted service. Rather, its duty was to provide adequate, efficient, and reliable service, which is not tantamount to infallible service. Temporary disruptions may occur without reducing Bell's service to a level less than adequate, efficient, or reliable. Further, this court held that the exculpatory language in Bell's tariff properly limited claims from disruption of service to a rebate of the costs for the missed service, and concluded \*63 that the

tariff's provision, which limited Bell's liability in the event of a service disruption, was not contrary to the Act. *Illinois Bell Switching Station*, 161 Ill.2d at 243–44, 204 Ill.Dec. 216, 641 N.E.2d 440.

Unlike *Illinois Bell Switching Station*, where no duty existed on the part of Illinois Bell, we have concluded in this case **\*\*1268 \*\*\*322** that NI–Gas owed a duty to plaintiff. Further, in *Illinois Bell Switching Station*, the class plaintiffs contended that the tariff applied, but conflicted with the Public Utilities Act. However, in this case, plaintiff contends that NI–Gas' tariff, as written, does not apply to her claim, an issue that was never addressed in *Illinois Bell Switching Station*.

**[35]** Turning to the NI–Gas tariff provision in this case, it is evident that the tariff essentially codifies the common law rule that a gas company has no duty with respect to a consumer's gas pipes and fittings, based on the consumer's responsibility for maintaining his or her own equipment and the company's lack of control and knowledge. See, e.g., *Clare*, 356 Ill. at 243–45, 190 N.E. 278 (stating common law rule). However, NI–Gas contends that the tariff provision eliminates the common law exception to this rule. According to NI–Gas, the tariff provision absolves it from any duty with respect to a consumer's pipes and equipment even if it has knowledge that a customer's appliance is leaking or is otherwise unsafe for the transportation of gas. See, e.g., *Bellefleur*, 243 Minn. at 128–29, 66 N.W.2d at 783–84 (stating common law exception).

We agree with the appellate court's rejection of this contention. 333 Ill.App.3d at 223, 266 Ill.Dec. 411, 774 N.E.2d 850. NI–Gas' position is untenable for several reasons.

Initially, allowing this cause of action to proceed would not contravene the above-stated policies underlying liability limitations. Plaintiff is not seeking rate preferences that are not accorded to other NI–Gas customers; she is not seeking to enforce “side agreements” which vary from our interpretation of the tariff. **\*64** Rather, if proved, awarding damages on plaintiff's claim would neither discriminate against other NI–Gas customers nor involve the court in tariff setting. See, e.g., *Lovejoy*, 92 Cal.App.4th at 101, 111 Cal.Rptr.2d at 723; *Day v. AT & T Corp.*, 63 Cal.App.4th 325, 336, 74 Cal.Rptr.2d 55, 62 (1998).

**[36] [37] [38] [39]** “Although a utility tariff is not a legislative enactment, its interpretation is governed by the rules of statutory construction.” *Bloom Township High School v. Illinois Commerce Comm'n*, 309 Ill.App.3d 163, 174, 242 Ill.Dec. 892, 722 N.E.2d 676 (1999); accord *Danisco*, 267 Kan. at 772, 986 P.2d at 385. The cardinal rule of interpreting statutes, to which all other canons and rules are subordinate, is to ascertain and give effect to the intent of the legislature. *McNamee v. Federated Equipment & Supply Co.*, 181 Ill.2d 415, 423, 229 Ill.Dec. 946, 692 N.E.2d 1157 (1998); *Illinois Bell Switching Station*, 161 Ill.2d at 246, 204 Ill.Dec. 216, 641 N.E.2d 440. Although a court should first consider the statutory language, a court must presume that the legislature, in enacting a statute, did not intend absurdity or injustice. *McNamee*, 181 Ill.2d at 423–24, 229 Ill.Dec. 946, 692 N.E.2d 1157; *State Farm Fire & Casualty Co. v. Yapejian*, 152 Ill.2d 533, 540–41, 178 Ill.Dec. 745, 605 N.E.2d 539 (1992); *Illinois Crime Investigating Comm'n v. Buccieri*, 36 Ill.2d 556, 561, 224 N.E.2d 236 (1967). “A statute or ordinance must receive a sensible construction, even though such construction qualifies the universality of its language.” *Illinois Bell Switching Station*, 161 Ill.2d at 246, 204 Ill.Dec. 216, 641 N.E.2d 440.

**[40]** Specifically, as earlier noted, rate regulation is one of legislative control and is not a judicial function. Therefore, the right to review the conclusion of the Commission acting under authority delegated by the legislature is accordingly limited. This deference to the judgment of the Commission is especially appropriate in **\*\*1269 \*\*\*323** the area of setting rates. *Illinois Bell*, 55 Ill.2d at 469–70, 303 N.E.2d 364 (and cases cited therein).

Applying these principles to the tariff provision at issue in this case, we conclude that the Commission did **\*65** not intend to completely immunize NI–Gas with respect to a gas leak of which it has notice. It must be remembered:

“Public utilities do not enjoy a general tort immunity; they owe a duty of care to the general public. Thus, if a utility company recognizes that its conduct under certain circumstances creates an unreasonable risk of harm to another, it has a duty to take reasonable precautions to prevent that risk of harm from occurring.” 64 Am.Jur.2d *Public Utilities* § 14, at 456 (2001).

Remembering that gas is a dangerous substance and commodity (*Metz*, 32 Ill.2d at 450, 207 N.E.2d 305; *McChure*, 303 Ill. at 97, 135 N.E. 43), the far-reaching consequences of NI-Gas' interpretation of this tariff provision are readily apparent. In effect, NI-Gas argues that if it had omitted language regarding duty and liability from its tariff, it would owe no duty whatsoever to anyone under any circumstances. The Commission's own decisions and orders belie such an unreasonable contention. See *Nordine v. Illinois Power Co.*, 32 Ill.2d 421, 428, 206 N.E.2d 709 (1965) (observing that orders and decisions of the Illinois Commerce Commission are public records "and as such we take judicial notice of them").

For example, in *Citizens Utilities Co. of Illinois*, No. 94-0481, 1995 WL 612576 (Illinois Commerce Comm'n September 13, 1995), the utility company (CUCI) filed with the Commission a revised tariff which proposed, *inter alia*, changes to its conditions of service. Regarding one such condition, the Commission observed: "CUCI proposes sweeping language for its fire protection service which would absolve it from any liability for damages of any nature to persons or property caused by fire. The Commission agrees with Staff's criticism of this proposal."

Indeed, the Commission has rejected the very argument that NI-Gas makes before this court. In *Teleport Communications Group, Inc.*, No. 96-AB-001, 1996 WL 769745 (Illinois Commerce Comm'n November 4, 1996), Teleport Communications Group, Inc. (TCG), filed a petition for \*66 arbitration with the Commission, seeking arbitration of the disputed portions of an interconnection agreement with Ameritech.

One disputed provision in the agreement required each party to indemnify the other against losses suffered by customers of the ultimate service provider. Ameritech's proposal would require Ameritech and TCG each to limit its liability, in the event of a transmission delay or defect, to an amount equivalent to the proportionate charge to the end user customer for the period of service during which the delay or defect occurred.

TCG responded that it should not be required to include a limitation of liability provision in contracts with its customers. The Commission noted that TCG's intention was "to assign the responsibility for loss to the party that has the ability to control or prevent the loss from occurring in the first place." Further, TCG

viewed Ameritech's proposal as "insulating Ameritech from any harm caused by its actions. Ameritech would have no liability or responsibility to TCG or its customers, even if they are harmed by grossly negligent or deliberate wrongdoing." TCG believed that "Ameritech's position would give Ameritech the right to dictate, unilaterally, an important aspect of TCG's relationship with its customers." The Commission noted that its staff believed that Ameritech's \*\*1270 \*\*\*324 proposal was "improper and should not be adopted."

The Commission rejected Ameritech's proposed indemnity provision, disagreeing with Ameritech's portrayal of its risks. The Commission reasoned that any claim against Ameritech by a TCG customer would have to be founded on contract or tort. The evidence showed that Ameritech did not anticipate having a contractual relationship with TCG's end users. Thus, the Commission reasoned, a TCG customer could not maintain a successful lawsuit against Ameritech based on a contract claim.

\*67 The Commission continued as follows:

"With respect to tort claims against Ameritech, the Illinois Supreme Court has spoken authoritatively on this very point. The Court in *In Re Illinois Bell Switching Station Litigation* \* \* \* reaffirmed the Moorman doctrine. This doctrine stands for the proposition that under the common law purely economic damages are generally not recoverable in tort actions. Three exceptions were articulated (1) where the plaintiff has sustained damage resulting from a sudden or dangerous occurrence (2) where the plaintiff's damages are the proximate result of a defendant's intentional, false representation and (3) where the plaintiff's damages are a proximate result of a negligent misrepresentation by a defendant in the business of supplying information for the guidance of others in their business transactions. The Court held that a tort claim for economic damages incurred from a loss of service arising from a fire at an Illinois Bell switching station was precluded in the absence of any exceptions to the Moorman doctrine.

The Commission believes that the Moorman doctrine provides Ameritech with ample protection in the vast majority of situations it has identified in the record.

In its Brief \* \* \* Ameritech maintains that the Proposed Arbitration Decision overlooks the substantial exposure to direct damages in tort left open by the Moorman doctrine. Essentially, Ameritech turns to potential claims for personal injury and property damage to demonstrate its exposure. Providing telecommunications services is not an inherently dangerous activity and it is difficult to imagine many scenarios in which Ameritech's provision of interconnection services will put third parties at risk. Even if such situations do arise, the public interest does not require that we attempt to insulate either party from the effects of its own improper conduct. *We believe that it is entirely appropriate that a telecommunications carrier remain responsible for personal injury or property damage which results from its own negligence or willful misconduct. Moreover, as Staff noted there is no general rule or policy which allows the Commission to grant utilities limitations on liability for personal injury and property damage.* This is particularly true with respect to utilities' conduct toward individuals \*68 who are not customers of the utility under tariff." (Emphasis added.)

The Commission concluded: "There is potential that [Ameritech's] proposal would shield Ameritech from responsibility for actions far beyond what is intended by the Commission's discretionary approval of limitations of liability in Ameritech's tariffs."

We agree with the Commission. The Commission stated: (1) it is entirely appropriate that a utility remain responsible for personal injury or property damage that results from its own negligence or willful misconduct, and (2) there is no general \*\*1271 \*\*\*325 rule or policy that allows the Commission to grant utilities limitations on liability for personal injury and property damage. Although the dispute in *Teleport* involved Ameritech's relationship with third parties, *i.e.*, TCG customers, the Commission's general statement of the public interest clearly refers also to a utility's relationship with its own customers.

These administrative decisions are examples of the Commission's rejection of the theory of absolute immunity that NI-Gas now proposes. We do likewise.

Additionally, if this tariff provision were a private contract, it would not be interpreted as permitting NI-Gas to absolve itself of any duty to its customers. See *Reeder v.*

*Western Gas & Power Co.*, 42 Wash.2d 542, 551, 256 P.2d 825, 830 (1953) (stating that "it would be unreasonable and against public policy to approve such a contractual limitation on the duty to inspect in cases where the facts themselves suggest a duty to inspect"). Although a utility tariff is considered as a statute and not as a contract, we cannot interpret the tariff provision that NI-Gas wrote to completely absolve it of any duty in this regard, when we would not so interpret the same provision in a contract that NI-Gas wrote. See *Bloom Township High School*, 309 Ill.App.3d at 175, 242 Ill.Dec. 892, 722 N.E.2d 676.

[41] [42] Also, this court has held that the Public Utilities Act is in derogation of the common law; accordingly, the Act \*69 is to be strictly construed in favor of persons sought to be subjected to its operation. *Barthel v. Illinois Central Gulf R.R. Co.*, 74 Ill.2d 213, 220–21, 23 Ill.Dec. 529, 384 N.E.2d 323 (1978). "Thus, the statute is to be strictly construed in favor of the utility company." *Tucker v. Illinois Power Co.*, 232 Ill.App.3d 15, 29, 173 Ill.Dec. 512, 597 N.E.2d 220 (1992). However, because the utility company drafts a tariff, it is generally accepted that language in a tariff, especially exculpatory language, is to be strictly construed against the utility company and in favor of the customer. See, *e.g.*, *Pink Dot*, 89 Cal.App.4th at 415, 107 Cal.Rptr.2d at 397; *Krasner v. New York State Electric & Gas Corp.*, 90 A.D.2d 921, 921–22, 457 N.Y.S.2d 927, 929 (1982); *State Farm Fire & Casualty Co. v. Southern Bell Telephone & Telegraph Co.*, 245 Ga. 5, 7, 262 S.E.2d 895, 897 (1980).

[43] [44] Further, a court cannot construe a statute in derogation of the common law beyond what the words of the statute expresses or beyond what is necessarily implied from what is expressed. In construing statutes in derogation of the common law, a court will not presume that an innovation thereon was intended further than the innovation which the statute specifies or clearly implies. *Russell v. Klein*, 58 Ill.2d 220, 225, 317 N.E.2d 556 (1974); *Cedar Park Cemetery Ass'n v. Cooper*, 408 Ill. 79, 82–83, 96 N.E.2d 482 (1951); *Illinois-American Water Co. v. City of Peoria*, 332 Ill.App.3d 1098, 1105, 266 Ill.Dec. 277, 774 N.E.2d 383 (2002) ("Although the [Public Utilities] Act is in derogation of the common law and is to be strictly construed in favor of those sought to be subjected to its operation, the Act will not be extended any further than what the language of the statute absolutely requires by its express terms or by clear implication"). Illinois courts have limited all manner of statutes in derogation

of the common law to their express language, in order to effect the least—rather than the most—change in the common law. See, e.g., *Bush v. Squellati*, 122 Ill.2d 153, 119 Ill.Dec. 366, 522 N.E.2d 1225 (1988) (interpreting Ill.Rev.Stat.1985, ch. 40, par. 607(b)); *Bagcraft \*70 Corp. v. Industrial Comm'n*, 302 Ill.App.3d 334, 235 Ill.Dec. 736, 705 N.E.2d 919 (1998) (interpreting 820 ILCS 305/11 (West 1996)).

**\*\*1272 \*\*\*326** For example, in *Barthel*, the plaintiffs brought a statutory cause of action against the defendant railroad seeking damages for personal injuries and wrongful death. Plaintiffs alleged that the railroad violated several regulations pertaining to the safety of railroad crossings. Relying on a strict and literal interpretation of the statutory language, the plaintiffs argued that the statute abrogated the common law defense of contributory negligence. As observed in *Barthel*:

“They [plaintiffs] argue that the cause of action, being a creature of the statute, bears no relation to the common law concepts of negligence and contributory negligence, and they conclude that since the statute does not provide that contributory negligence shall be a defense, it imposes strict liability on the utility for any violation.” *Barthel*, 74 Ill.2d at 220, 23 Ill.Dec. 529, 384 N.E.2d 323.

The *Barthel* court rejected this argument. Noting that the Act is in derogation of the common law, the court reasoned that tort principles would not be deemed abrogated unless it plainly appears that the intent of the statute is to do so. This court held that the statute did not abrogate the common law defense of contributory negligence, and that this common law defense was available to the railroad. *Barthel*, 74 Ill.2d at 220–21, 23 Ill.Dec. 529, 384 N.E.2d 323.

In this case, applying the exact reasoning as applied in *Barthel*, we must conclude that NI–Gas' tariff did not abrogate the common law exception to the rule of a gas company's nonliability. Just as the statute in *Barthel* did not abrogate a common law defense, NI–Gas' tariff does not abrogate the common law exception. This rule of statutory construction cannot be used to provide common law doctrines to assist defendants, but withhold common law doctrines that assist plaintiffs.

Specifically, courts in other jurisdictions have avoided interpretations of utility tariffs that would abrogate the

**\*71** common law. For example, in *National Food Stores, Inc. v. Union Electric Co.*, 494 S.W.2d 379 (Mo.App.1973), the Missouri Court of Appeals found that the defendant electric utility owed a common law duty to plaintiff utility customer. *National Food Stores*, 494 S.W.2d at 381–83. The court then rejected the utility's contention that its filed tariff immunized it from common law liability for damages. The court strictly construed the tariff, and found that the plaintiff's allegations fell outside of the tariff's ambit. Acknowledging the tariff, the court emphasized: “the crucial point is that [the utility] cannot divorce itself from the consequences of its own failure to use ordinary care to avoid harm to its consumers.” *National Food Stores*, 494 S.W.2d at 384. See also *Satellite System, Inc. v. Birch Telecom of Oklahoma, Inc.*, 51 P.3d 585, 588 (Okla.2002) (holding that Oklahoma legislature had not expressed intent that filed-tariff doctrine abolished common law fraud claim against utility); *State Farm*, 245 Ga. at 6–7, 262 S.E.2d at 896–97 (holding that utility tariff's limitations period did not abrogate general state law); *Hall v. Consolidated Edison Corp.*, 104 Misc.2d 565, 568–70, 428 N.Y.S.2d 837, 840–41 (1980) (holding that tariff did not relieve defendant utility company from its common law tort liability for termination of electrical service); *Kroger Co. v. Appalachian Power Co.*, 244 Va. 560, 563, 565, 422 S.E.2d 757, 759–60 (1992) (interpreting utility tariff in accord with common law rule, observing that tariff would not shield utility company from “all liability in providing power to a customer beyond the delivery point”).

As we earlier observed, the tariff provision in this case essentially codifies the common law rule that a gas company has **\*\*1273 \*\*\*327** no duty with respect to a consumer's gas pipes and fittings, based on the consumer's responsibility for his or her equipment, and the company's lack of knowledge and control. Absent express language that **\*72** disavows the common law exception based on notice, we cannot say that it was eliminated by the tariff provision. See, e.g., *Bush*, 122 Ill.2d at 161–62, 119 Ill.Dec. 366, 522 N.E.2d 1225 (holding that the statutory provision “cannot, by its silence,” be construed to change the applicable common law); *Bagcraft Corp.*, 302 Ill.App.3d at 340, 235 Ill.Dec. 736, 705 N.E.2d 919 (holding that without “specific language directing application” of a statutory provision to a scenario governed by the common law, “we cannot conclude that the legislature intended to abrogate an entire body of case law”). We note that our appellate court long ago rejected a gas company's

invocation of the Public Utilities Act as a defense to its common law duty. See *Mrdalj v. Public Service Co. of Northern Illinois*, 308 Ill.App. 424, 430, 31 N.E.2d 978 (1941) (holding where gas company had been notified of odor of gas prior to explosion which killed property owner, gas company could not defend on ground that Public Utilities Act prohibited company from shutting off gas to make inspection, since where gas company has knowledge that gas is escaping in a building occupied by consumer it is gas company's duty to shut off gas supply until necessary repairs have been made). Based on the above-stated principles of statutory interpretation, this is precisely the situation "for the General Assembly and not this court" to abrogate NI-Gas' common law duty. See *Bush*, 122 Ill.2d at 162, 119 Ill.Dec. 366, 522 N.E.2d 1225.

We hold that NI-Gas' tariff provision did not absolve the company of its common law duty owed to plaintiff. While a gas company is not an insurer for *any* injury sustained as the result of escaping gas, the company is nonetheless liable for its negligence. See *Pappas*, 350 Ill.App. at 548, 113 N.E.2d 585.

#### CONCLUSION

Based on the present record, we have concluded solely that NI-Gas owed a duty to warn in this case. Accordingly, there remains a genuine issue of material fact as to whether NI-Gas breached this duty and, if so, whether \*73 this breach proximately caused plaintiff's injuries. Summary judgment was thus improper. See *Happel*, 199 Ill.2d at 198, 262 Ill.Dec. 815, 766 N.E.2d 1118. Therefore, we affirm the judgment of the appellate court, which reversed the circuit court's grant of summary judgment and remanded the cause for further proceedings.

*Affirmed.*

Justice GARMAN, dissenting:

I respectfully dissent. I believe that our analysis should begin and end with the tariff filed by NI-Gas and approved by the Illinois Commerce Commission. As a result, I do not think it necessary to reach the question whether the common law governing the duties of gas companies should be expanded to recognize a duty to warn of the risk that a connector neither owned nor installed by the company may deteriorate from exposure

to the odorant that must, by law, be added to the natural gas delivered by NI-Gas to its customers.

The General Assembly enacted the Public Utilities Act (Act) in 1921. An Act concerning public utilities, 1921 Ill. Laws 702, approved June 29, 1921, eff. July 1, 1921. Then, as now, the policy of the state is expressed in the Act:

"It is therefore declared to be the policy of the State that public utilities shall continue to be regulated effectively and comprehensively. It is further declared \*\*1274 \*\*\*328 that the goals and objectives of such regulation shall be to ensure

(a) \* \* \* that:

(iv) tariff rates for the sale of various public utility services are authorized such that they accurately reflect the cost of delivering those services and allow the utilities to recover the total costs prudently and reasonably incurred[.]" 220 ILCS 5/1-102(a)(iv) (West 1994).

In return for the protections provided, the Act imposes certain duties upon the utilities it regulates:

"Every public utility shall furnish, provide and maintain such service instrumentalities, equipment and facilities as \*74 shall promote the safety, health, comfort and convenience of its patrons, employees and public and as shall be in all respects adequate, efficient, just and reasonable.

All rules and regulations made by a public utility affecting or pertaining to its charges or service to the public shall be just and reasonable.

Every public utility shall, upon reasonable notice, furnish to all persons who may apply therefor and be reasonably entitled thereto, suitable facilities and service, without discrimination and without delay." 220 ILCS 5/8-101 (West 1994).

In addition, regarding the duties of public utilities to providing services and facilities, the Act requires that:

"Every public utility subject to this Act shall provide service and facilities which are in all respects adequate, efficient, reliable and environmentally safe and which, consistent with these obligations, constitute the least-

cost means of meeting the utility's service obligations." 220 ILCS 5/8-401 (West 1994).

This court has long acknowledged that the "policy established by legislation for the regulation of public utilities is to provide the public with efficient service at a reasonable rate by compelling an established public utility occupying a given field to provide adequate service and at the same time to protect it from ruinous competition." *Illinois Power & Light Corp. v. Commerce Comm'n*, 320 Ill. 427, 429-30, 151 N.E. 236 (1926). More recently, this court reiterated: "The Public Utilities Act [citation], under which the Commerce Commission regulates all public utilities, was enacted to assure the provision of efficient and adequate utility service to the public at a reasonable cost." *Local 777 v. Illinois Commerce Comm'n*, 45 Ill.2d 527, 535, 260 N.E.2d 225 (1970). See also *Bloom Township High School v. Illinois Commerce Comm'n*, 309 Ill.App.3d 163, 175, 242 Ill.Dec. 892, 722 N.E.2d 676 (1999).

The Act requires the utility to file a tariff with the Illinois Commerce Commission. 220 ILCS 5/9-102 (West 1994). The tariff "plays an integral role" in allowing the \*75 utility to meet the expectations of the General Assembly. *In re Illinois Bell Switching Station Litigation*, 161 Ill.2d 233, 244, 204 Ill.Dec. 216, 641 N.E.2d 440 (1994). The liability limitations contained in an approved tariff serve the public policies of establishing uniform affordable rates and providing universal service by limiting the utility's exposure to liability. Thus, although the tariff may be seen as stating the terms of the contract between the utility and its customers, it is more than a mere contract between buyer and seller. There is a third party to the transaction—the state, which as a matter of public policy has chosen to limit the liability of utilities in return for regulation of their rates. As this court has noted:

" · "The theory underlying [decisions upholding the right of regulated utilities to \*\*1275 \*\*\*329 limit their liabilities] is that a public utility, being strictly regulated in all operations with considerable curtailment of its rights and privileges, shall likewise be regulated and limited as to its liabilities. In consideration of its being peculiarly the subject of state control, 'its liability is and should be defined and limited.' [Citation.] There is nothing harsh or inequitable in upholding such a limitation of liability when it is thus considered that the rates as fixed by the commission are established with the rule of limitation in mind. Reasonable rates are in part dependent upon

such a rule.'" *Illinois Bell Switching Station*, 161 Ill.2d at 245-46, 204 Ill.Dec. 216, 641 N.E.2d 440, quoting *Waters v. Pacific Telephone Co.*, 12 Cal.3d 1, 7, 523 P.2d 1161, 1164, 114 Cal.Rptr. 753, 756 (1974), quoting *Cole v. Pacific Telephone & Telegraph Co.*, 112 Cal.App.2d 416, 419, 246 P.2d 686, 688 (1952).

The tariff limits liability by narrowly defining the duties undertaken by the utility and disclaiming any additional duties. The majority acknowledges our prior case law, which requires that any duty other than those specifically imposed upon the utility by the Act itself must be found in the tariff:

"Illinois courts have long held that a tariff provision such as the one at issue in this case provides the source for, and determines the nature and extent of, a public \*76 utility's service obligations to its customers." 211 Ill.2d at 57-58, 284 Ill.Dec. at 318-19, 809 N.E.2d at 1264-65, citing *J. Meyer & Co. v. Illinois Bell Telephone Co.*, 88 Ill.App.3d 53, 55, 42 Ill.Dec. 942, 409 N.E.2d 557 (1980), and *Sarelas v. Illinois Bell Telephone Co.*, 42 Ill.App.2d 372, 374-75, 192 N.E.2d 451 (1963).

See also *Illinois Bell Switching Station*, 161 Ill.2d at 248, 204 Ill.Dec. 216, 641 N.E.2d 440 (Miller, J., specially concurring).

As the majority also acknowledges, Illinois law on the subject of tariffs has its roots in federal law, specifically, the federal "filed-rate doctrine." 211 Ill.2d at 56, 284 Ill.Dec. at 318, 809 N.E.2d at 1264. Although this doctrine is no longer in effect in the federal courts (see *Tempel Steel Corp. v. Landstar Inway Inc.*, 211 F.3d 1029, 1030 (7th Cir.2000) (noting that the ICC Termination Act, 109 Stat. 803 (1995), abolished the tariff filing requirement and the filed-rate doctrine)), it is still a useful starting point for any analysis of the legal effect of a utility tariff filed and approved pursuant to state law.

In *Western Union Telegraph Co. v. Esteve Brothers & Co.*, 256 U.S. 566, 41 S.Ct. 584, 65 L.Ed. 1094 (1921) (cited in 211 Ill.2d at 57, 284 Ill.Dec. at 317-18, 809 N.E.2d at 1263-64), the issue was whether the plaintiff/customer was "without assent in fact, bound as matter of law by the provision limiting liability, because it is a part of the lawfully established rate." *Esteve Brothers*, 256 U.S. at 570, 41 S.Ct. at 586, 65 L.Ed. at 1097. The Court held that "limitation of liability was an inherent part of the rate. The company could no more depart from it than it could

depart from the amount charged for the service rendered.” *Esteve Brothers*, 256 U.S. at 571, 41 S.Ct. at 586, 65 L.Ed. at 1097. As the majority notes, the federal act at issue in *Esteve Brothers*:

“introduced a new principle into the legal relations of the telegraph companies with their patrons which dominated and modified the principles previously governing them. Before the act the companies had a common law liability from which they might or might not extricate themselves according to views of policy prevailing in the several states. \* \* \* Uniformity demanded that the **\*\*1276 \*\*\*330** rate represent the whole duty and the whole liability of the **\*77** company. It could not be varied by agreement; still less could it be varied by lack of agreement. The rate became, not as before a matter of contract by which a legal liability could be modified, but a matter of law by which a uniform liability was imposed.” *Esteve Brothers*, 256 U.S. at 571–72, 41 S.Ct. at 586, 65 L.Ed. at 1097–98.

Later, in *Western Union Telegraph Co. v. Priester*, 276 U.S. 252, 48 S.Ct. 234, 72 L.Ed. 555 (1928), the Court stated that once the Interstate Commerce Commission approved a tariff, the “established rates \* \* \* became the lawful rates and the attendant limitation of liability became the lawful condition upon which messages might be sent.” *Priester*, 276 U.S. at 259, 48 S.Ct. at 235, 72 L.Ed. at 565. “What had previously been a matter of common law liability, with such contractual restrictions as the states might permit, then became the subject of federal legislation to secure reasonable and just rates for all without undue preference or advantage to any. Since that end is attainable only by adherence to the approved rate \* \* \* that rate ‘represents the whole duty and the whole liability of the company.’ ” *Priester*, 276 U.S. at 259, 48 S.Ct. at 235, 72 L.Ed. at 565, quoting *Esteve Brothers*, 256 U.S. at 572, 41 S.Ct. at 586, 65 L.Ed. at 1097. In response to plaintiff’s argument that the company’s tariff could not limit its liability for “gross negligence,” the Court concluded: “We may not disregard a lawful exercise of the regulatory power which has made no distinction between degrees of negligence, nor may we, upon any theory of public policy, annex to the rate as made conditions affecting its uniformity and equality.” *Priester*, 276 U.S. at 260, 48 S.Ct. at 236, 72 L.Ed. at 565.

More recently, the Court stated that the “ ‘rights as defined by the tariff cannot be varied or enlarged by *either contract or tort* of the carrier.’ ” (Emphasis added.) **\*78**

*American Telephone & Telegraph Co. v. Central Office Telephone, Inc.*, 524 U.S. 214, 227, 118 S.Ct. 1956, 1965, 141 L.Ed.2d 222, 236 (1998), quoting *Keogh v. Chicago & Northwestern Ry. Co.*, 260 U.S. 156, 163, 43 S.Ct. 47, 49, 67 L.Ed. 183, 187 (1922). The majority quotes this language, but overlooks the significance of the mention of torts as well as contracts. 211 Ill.2d at 56, 284 Ill.Dec. at 317–18, 809 N.E.2d at 1263–64.

The General Assembly, by enacting the Public Utilities Act and creating the Illinois Commerce Commission with the power to approve tariffs filed by public utilities, has made clear the public policy of the State, which is to hold public utilities to those duties expressly set out in the Act and the approved tariffs, and to preclude the judicial recognition of additional duties on the basis of common law reasoning. Thus, the majority is correct that whether the tariff bars plaintiff’s cause of action “depends on the nature of plaintiff’s lawsuit and the meaning of the tariff’s language.” 211 Ill.2d at 62, 284 Ill.Dec. at 321, 809 N.E.2d at 1267.

#### Nature of the Lawsuit

The majority correctly states that “ ‘all state law causes of action are not necessarily precluded’ ” by the existence of a filed and approved tariff. 211 Ill.2d at 58, 284 Ill.Dec. at 319, 809 N.E.2d at 1265, quoting *Pink Dot, Inc. v. Teleport Communications Group*, 89 Cal.App.4th 407, 416, 107 Cal.Rptr.2d 392, 398 (2001). The nature of a lawsuit may place it outside the scope of the tariff’s limitation of liability provisions.

Thus, although *Pink Dot* acknowledged that Teleport’s liability for gross negligence was limited by the applicable tariff, **\*\*1277 \*\*\*331** *Pink Dot* argued that its claims against Teleport for breach of contract, fraud, willful misconduct, intentional interference with economic relations, and unfair competition were not barred. *Pink Dot*, 89 Cal.App.4th at 412, 107 Cal.Rptr.2d at 395. This argument was supported by a state statute providing that “ ‘All contracts which have for their object, directly or indirectly, to exempt anyone from responsibility for his own fraud, or willful injury to the person or property of another, or violation of the law, whether willful or **\*79** negligent, are against the public policy of the law.’ ” *Pink Dot*, 89 Cal.App.4th at 413–14, 107 Cal.Rptr.2d at 396, quoting Cal. Civ.Code § 1668 (1994). Further,

the Teleport's tariff was "silent as to the required liability for any willful misconduct, fraud, or violations of law," although it did contain "clauses intended to limit [its] liability to its customers for damages caused by its conduct." *Pink Dot*, 89 Cal.App.4th at 414, 107 Cal.Rptr.2d at 396–97. In the end, *Pink Dot* stands for the unremarkable proposition that when a state statute expressly precludes such a limit, a tariff's \$10,000 limit on liability cannot "eliminate [the utility's] liability for willful misconduct, fraud or violations of law by merely omitting the acknowledgment of such liability from its tariff." *Pink Dot*, 89 Cal.App.4th at 414, 107 Cal.Rptr.2d at 397.

In *Adamson v. WorldCom Communications, Inc.*, 190 Or.App. 215, 78 P.3d 577 (2003) (quoted in 211 Ill.2d at 58, 284 Ill.Dec. at 319, 809 N.E.2d at 1265), plaintiff's claim for unfair trade practices was not barred where the tariff limited the defendant's liability "unless such damages are a result of Company's willful misconduct." *Adamson*, 190 Or.App. at 222, 78 P.3d at 582.

The tariff at issue in the present case expressly states that NI–Gas "assumes no responsibility in connection with the installation, maintenance or operation" of the customer's equipment. Plaintiff has not cited either a state statute (as in *Pink Dot*) or language of the tariff (as in *Adamson*) that precludes the limitation of liability claimed by NI–Gas. Nor has she brought a claim for fraud, negligent driving of a vehicle owned by the utility, or other tortious conduct of the sort that would place it outside the scope of the limitation of liability clause of the tariff. Thus, the duty claimed by plaintiff must be found to exist on the basis of the language of the tariff, or not at all.

#### \*80 Construction of the Tariff

The Act is in derogation of the common law. *Illinois Bell Switching Station*, 161 Ill.2d at 240, 204 Ill.Dec. 216, 641 N.E.2d 440. The majority acknowledges that, as a result, the Act it is to be strictly construed in favor of persons sought to be subjected to its operation, that is, in favor of the utility. 211 Ill.2d at 68–69, 284 Ill.Dec. at 325, 809 N.E.2d at 1271. As the majority also notes, once the tariff is approved by the Commission, it has the force of law. 211 Ill.2d at 56, 284 Ill.Dec. at 317, 809 N.E.2d at 1263 (citing *Illinois Bell Switching Station*, 161 Ill.2d at 244, 204 Ill.Dec. 216, 641 N.E.2d 440, and *Illinois Central Gulf R.R. Co. v. Sankey Brothers, Inc.*, 67 Ill.App.3d 435,

439, 23 Ill.Dec. 749, 384 N.E.2d 543 (1978) (stating that "[a] tariff is a law, not a contract, and has the force and effect of a statute"), *affirmed*, 78 Ill.2d 56, 34 Ill.Dec. 328, 398 N.E.2d 3 (1979)). Further, the majority states that interpretation of the tariff is governed by the rules of statutory construction. 211 Ill.2d at 55, 284 Ill.Dec. at 323, 809 N.E.2d at 1269.

Nevertheless, the majority, citing cases from California, New York, and Georgia, states that the language of the tariff, especially any exculpatory language, should be strictly construed against the utility, based on the canon of construction of *contracts* \*\*1278 \*\*\*332 that *contract terms* should be construed against the drafter. 211 Ill.2d at 69, 284 Ill.Dec. at 325, 809 N.E.2d at 1271. Although it may be "generally accepted" (211 Ill.2d at 69, 284 Ill.Dec. at 325, 809 N.E.2d at 1271) in some jurisdictions that a tariff should be construed as a mere contract, there is also contrary authority. The courts of Washington and Oregon, for example, apply the standard principles of statutory construction to the interpretation of a tariff, including applying the rule of construction that the court is to ascertain the drafters' intent when they promulgated the language. See, e.g., *National Union Insurance Co. v. Puget Sound Power & Light*, 94 Wash.App. 163, 171, 972 P.2d 481, 484 (1999); *U.S. West Communications, Inc. v. City of Longmont*, 924 P.2d 1071, 1079 (Colo.App.1995).

Even in a jurisdiction in which the "construe against the drafter" canon is applied to public utility tariffs, it has been said that "a strict construction against a tariff's \*81 author is not justified where the construction would ignore a permissible and reasonable construction which conforms to the intentions of the framers of the tariff." *Info Tel Communications, LLC v. U.S. West Communications, Inc.*, 592 N.W.2d 880, 884 (Minn.App.1999).

This court has never held that a public utility tariff should be construed against the utility that drafted the language. There are valid arguments to be made on both sides because the tariff has characteristics of both contract and statute. This court may in some future case be called upon to decide whether ambiguous language in a tariff should be construed in favor of or against the drafting utility. This is not such a case. The language at issue is unambiguous. NI–Gas "assumes no responsibility in connection with the installation, maintenance or operation" of the customer's equipment. Our duty is to apply the plain meaning of

these words, in light of the underlying purpose of the Act, which is to provide citizens of Illinois with utility service at reasonable rates and, as a necessary part of that scheme, to limit the liability of utility companies.

The majority also suggests that the tariff provision should not be given effect because, if it “were a private contract, it would not be interpreted as permitting NI–Gas to absolve itself of any duty to its customers.” 211 Ill.2d at 68, 284 Ill.Dec. at 325, 809 N.E.2d at 1271. This statement misses the point in several respects. First, it defies logic to say that a tariff should be enforced under the same rules as a private contract. The entire concept of a tariff is that it supercedes any contract between the utility and the individual customer. Indeed, the utility is forbidden from privately contracting around the terms of the tariff. Second, the Act and the tariff do not permit the utility to absolve itself of “any duty.” They permit, indeed they require, that the utility undertake precisely defined duties to its customers. Finally, unlike a private company, a public utility \*82 cannot adjust its prices to compensate for increased exposure to liability when the courts recognize a new common law duty.

For example, in *Sarelas* the plaintiff claimed that Illinois Bell Telephone owed him a duty of continuing service, which it violated by interrupting his service for 2 ½ hours as the result of a clerical error. The appellate court noted that “in the case of an ordinary corporation this would be nothing of which to complain, for in general a corporation is entitled to refrain from doing business with its customers unless it is otherwise bound by contract; but a utility is different. It has a duty to its subscribers that goes beyond that of an ordinary corporation. However, *this duty has but one source*, the tariff, which in this \*\*1279 \*\*\*333 instance is on file with the Illinois Commerce Commission.” (Emphasis added.) *Sarelas*, 42 Ill.App.2d at 374, 192 N.E.2d 451. Thus, the court observed, “the extent to which defendants owed plaintiff ‘a legal duty’ is determined by the particular provisions of the tariff on file with the commission; there is no contract \* \* \* on which plaintiff can rely, nor are his allegations of a breach of duty sufficient to constitute a claim in tort.” *Sarelas*, 42 Ill.App.2d at 375, 192 N.E.2d 451. In the end, a breach of duty by the utility “arises either from the tariff or not at all.” *Sarelas*, 42 Ill.App.2d at 375, 192 N.E.2d 451.

Following the mandate to construe the Act strictly in favor of the regulated utility, the court in *Barthel v. Illinois*

*Central Gulf R.R. Co.*, 74 Ill.2d 213, 23 Ill.Dec. 529, 384 N.E.2d 323 (1978), held that section 73 of the Act, which allows the utility to be held liable for certain acts and omissions, did not abrogate the common law defense of contributory negligence because it did not plainly appear that the intent of the statute was to impose strict liability. *Barthel*, 74 Ill.2d at 221, 23 Ill.Dec. 529, 384 N.E.2d 323. See also *Tucker v. Illinois Power Co.*, 232 Ill.App.3d 15, 29, 173 Ill.Dec. 512, 597 N.E.2d 220 (1992) (construing Act as not authorizing award of punitive damages in action for \*83 negligent termination of gas service in below freezing weather when plaintiff would not have been entitled to punitive damages under common law theory of liability).

The majority purports to apply the “exact reasoning” of *Barthel* (211 Ill.2d at 70, 284 Ill.Dec. at 326, 809 N.E.2d at 1272), when it concludes that just as the statute in *Barthel* did not abrogate a pre-existing common law defense, the tariff at issue here “does not abrogate the common law exception.” 211 Ill.2d at 70, 284 Ill.Dec. at 326, 809 N.E.2d at 1272. Plaintiff, however, does not seek to hold NI–Gas liable under an *existing* exception to the common law rule that gas companies have no duty with regard to the fixtures and equipment of their customers. She seeks to expand the existing exception to recognize an *entirely new duty* to warn.

The majority observes that NI–Gas has had opportunities in the past to assert that the tariff precludes imposition of a duty, yet has not done so. 211 Ill.2d at 55, 284 Ill.Dec. at 319–20, 809 N.E.2d at 1265–66. This observation is not persuasive for two reasons. First, simple logic dictates that a party's decision to raise a particular issue or assert a particular defense in one litigation has no preclusive effect in later litigation with an entirely different party. Second, the cases cited by the majority are inapposite. In *Pioneer Hi–Bred Corn Co. of Illinois v. Northern Illinois Gas Co.*, 61 Ill.2d 6, 329 N.E.2d 228 (1975), the plaintiff's theory of liability was that NI–Gas negligently performed an inspection. There was no leak or defect in the plaintiff's equipment. Rather, NI–Gas employees purportedly inspected plaintiff's equipment for the specific purpose of determining the proper pressure for the delivery of gas to the plaintiff's premises. *Pioneer Hi–Bred*, 61 Ill.2d at 9, 329 N.E.2d 228. Previously, in *Clare*, this court had noted that a gas company has no duty to inspect the pipes or fixtures belonging to a customer in the absence of notice of a defect. *Clare*, 356 Ill. at 244, 190 N.E. 278. Indeed, the gas company has no right to

“go upon the premises of one of its customers for the purpose of \*84 inspecting his pipes or other fixtures except upon the invitation, license or permission of the owner.” *Clare*, 356 Ill. at 244, 190 N.E. 278. In *Pioneer Hi-Bred*, as in *Clare*, a gas company employee was invited to enter the plaintiff’s premises for the purpose of making an inspection. The inspections served different purposes: in *Clare*, to determine the \*\*1280 \*\*\*334 source of an offensive odor; in *Pioneer Hi-Bred*, to calculate the proper pressure for the delivery of gas. In *Clare*, the gas company was not liable for the eventual damages and injuries because the evidence showed that the inspection, which was not “negligently or unskillfully made,” did not reveal the source of the leak. *Clare*, 356 Ill. at 245, 190 N.E. 278. In *Pioneer Hi-Bred*, the gas company might have been held liable for negligently conducting an inspection had the plaintiff proven that an inspection actually took place. *Pioneer Hi-Bred*, 61 Ill.2d at 13–14, 329 N.E.2d 228. This court agreed with NI–Gas that the trial court properly refused to give the requested instruction on negligent inspection to the jury, because the tendered instruction assumed a fact in dispute—that there had actually been an inspection. *Pioneer Hi-Bred*, 61 Ill.2d at 13–14, 329 N.E.2d 228. The majority’s statement that “[n]either this court nor NI–Gas believed that this tariff precluded a common law analysis in a negligence action for personal injury” in *Pioneer Hi-Bred* (211 Ill.2d at 59, 284 Ill.Dec. at 320, 809 N.E.2d at 1266), although true, is irrelevant. The common law duty asserted in *Pioneer Hi-Bred* had already been recognized in *Clare*.

The majority also points to this court’s decision in *Metz v. Central Illinois Electric & Gas Co.*, 32 Ill.2d 446, 207 N.E.2d 305 (1965), as further support for its statement that “where a utility tariff speaks to a specific duty, the tariff *may be controlling*; however, where the tariff does not address a particular situation, the common law applies and a common law duty analysis must be applied.” (Emphasis added.) 211 Ill.2d at 61, 284 Ill.Dec. at 320, 809 N.E.2d at 1266. When a tariff speaks to a specific duty, as in this case, it *is* controlling. The majority \*85 asks why the appellate court failed to mention the tariff in this case. 211 Ill.2d at 62, 284 Ill.Dec. at 320, 809 N.E.2d at 1266. *Metz* involved an explosion that occurred as a result of a defect *in the gas main*, which is the responsibility of the gas company both under the tariff and at common law. Thus, the answer to the majority’s question is obvious—the tariff was irrelevant to the gas

company’s alleged negligence to properly maintain *its own equipment*.

The majority is determined to ignore our obligation to determine whether NI–Gas has a duty to warn by looking at the plain language of the tariff, even if that plain meaning departs from the manner in which the common law may have developed in the decades since the Act was adopted and the tariff was approved, or the way in which we would decide the question today. I accept, *arguendo*, the majority’s statement that “it is evident that the tariff essentially codifies the common law rule that a gas company has no duty with respect to a consumer’s gas pipes and fittings.” 211 Ill.2d at 63, 284 Ill.Dec. at 322, 809 N.E.2d at 1268. Thus, I do not dispute the majority’s conclusion that the tariff “did not abrogate the common law exception to the rule of a gas company’s nonliability.” 211 Ill.2d at 70, 284 Ill.Dec. at 326, 809 N.E.2d at 1272. That exception, however, applies only when the gas company has actual or constructive knowledge of a gas leak or a defect on the premises of the individual customer.

NI–Gas had neither actual nor constructive notice of a gas leak in the Adams’ home. At most, NI–Gas was aware that some Cobra connectors might still be in use in its service area, and that these connectors could fail after prolonged exposure to the odorant that NI–Gas is required, by law, to add to natural gas. This does not constitute a “a gas leak of which it has notice.” 211 Ill.2d at 65, 284 Ill.Dec. at 323, 809 N.E.2d at 1269.

\*\*1281 \*\*\*335 The majority even admits that recognizing a duty to warn on the facts of this case would not be based on the common law as it existed at the time the tariff was filed \*86 and approved some fifty years ago. It would, instead, be a “reasoned adaptation” of the preexisting common law. 211 Ill.2d at 53, 284 Ill.Dec. at 316, 809 N.E.2d at 1262. Our prior case law does not permit such “reasoned adaptation” of the common law when it would alter the terms of the applicable tariff.

The majority’s conclusion that “allowing this cause of action to proceed would not contravene” the public policy of this state regarding liability limitations contained in public utility tariffs (211 Ill.2d at 63, 284 Ill.Dec. at 322, 809 N.E.2d at 1268) is similarly flawed. Although plaintiff does not seek a rate preference or enforcement of a “side agreement,” she is seeking to impose liability in tort in excess of that permitted by the tariff. Exposure to liability

in tort bears a direct relationship to rate setting. See *Illinois Bell Switching Station*, 161 Ill.2d at 245, 204 Ill.Dec. 216, 641 N.E.2d 440.

*Meyer* is cited by the majority (211 Ill.2d at 57–58, 284 Ill.Dec. at 319, 809 N.E.2d at 1265) for the proposition that the tariff “provides the source for, and determines the nature and extent of, a public utility’s service obligations to its customers.” The *Meyer* plaintiffs installed an alarm system on their premises and connected it to the defendant’s equipment at a junction box located on a telephone pole. Burglars disconnected the alarm at the junction box and made off with hundreds of thousands of dollars worth of property from the plaintiffs’ warehouse. The issue on appeal was whether the defendant utility owed a duty to the plaintiffs “under the circumstances as alleged.” As in the present case, the circumstances in *Meyer* included a connection between the customer’s equipment and the utility’s equipment. That connection failed and plaintiffs suffered damages as a result. Citing *Sarelas*, the appellate court stated, “It has been established that the source of any duty of Illinois Bell, as a public utility, to its subscribers is only in the tariff as filed.” *Meyer*, 88 Ill.App.3d at 55, 42 Ill.Dec. 942, 409 N.E.2d 557. The portions of the tariff dealing with customer-provided equipment and systems plainly stated that:

\*87 “[W]here such equipment or system is connected to Company facilities the responsibility of the Company shall be limited to the furnishing of facilities suitable for exchange telecommunications service or \* \* \* the Company shall not be responsible for (1) the through transmission of signals generated by the customer-provided equipment or system, or for the quality of, or defects in, such transmission \* \* \*.” *Meyer*, 88 Ill.App.3d at 55, 42 Ill.Dec. 942, 409 N.E.2d 557.

Thus, the appellate court found that the “plain language of this provision exculpates [the telephone company] from liability.” *Meyer*, 88 Ill.App.3d at 55, 42 Ill.Dec. 942, 409 N.E.2d 557. The court affirmed the trial court’s dismissal of the complaint because “the tariff is the sole source of any duty owed by defendant to plaintiffs” and the plaintiffs had failed to establish a duty thereunder. *Meyer*, 88 Ill.App.3d at 56, 42 Ill.Dec. 942, 409 N.E.2d 557.

Further, the *Meyer* court found “a reasonable basis for treating this public utility differently from private corporations and for limiting its liability to subscribers in the rendering of its service.” *Meyer*, 88 Ill.App.3d at 57,

42 Ill.Dec. 942, 409 N.E.2d 557. The Act requires that all rates and charges imposed by a public utility be just and reasonable and, to achieve this end, such rates and charges are fixed by a state agency. “Without the **\*\*1282 \*\*\*336** limitations on liability set forth by the tariff, defendant would be uniquely vulnerable to claims based on signal transmission defects which may result from a variety of causes, adversely affecting its ability to fulfill the public need for reasonable telephone service charges. This would be particularly true of *defects* in the transmission of signals *originating from customer-provided equipment over which the company could have little control.*” (Emphases added.) *Meyer*, 88 Ill.App.3d at 57, 42 Ill.Dec. 942, 409 N.E.2d 557.

In addition to *Sarelas* and *Meyer*, the majority also cites *North River Insurance Co. v. Jones*, 275 Ill.App.3d 175, 211 Ill.Dec. 604, 655 N.E.2d 987 (1995) (211 Ill.2d at 55, 284 Ill.Dec. at 317, 809 N.E.2d at 1263), as a source for the definition of a tariff: “A tariff is a public document setting forth services being offered, rates and charges with **\*88** respect to services and governing rules, regulations and practices relating to those services.” *North River*, 275 Ill.App.3d at 185, 211 Ill.Dec. 604, 655 N.E.2d 987, citing Black’s Law Dictionary 1306 (5th ed.1979). However, the majority fails to note the holding of *North River*. The tariff filed by the defendant utility, Illinois Bell Telephone, described the terms and conditions under which it would provide service, including the limitation of liability provision, which had been in effect for “the past 50 years.” *North River*, 275 Ill.App.3d at 185, 211 Ill.Dec. 604, 655 N.E.2d 987. Once such a tariff is implemented, the court held, the utility is “forbidden from deviating from its terms. It is the filed tariff that defines the scope of duty owed by [the utility]. The source of any duty of [the utility], as a public utility to its subscribers, is only in the tariff as filed.” *North River*, 275 Ill.App.3d at 185, 211 Ill.Dec. 604, 655 N.E.2d 987 (citing *Meyer*, 88 Ill.App.3d at 55, 42 Ill.Dec. 942, 409 N.E.2d 557, and *Sarelas*, 42 Ill.App.2d at 375, 192 N.E.2d 451).

Thus, I conclude that the appellate court in the present case originally reached the correct result when it concluded that *Illinois Bell Switching* was dispositive and held that NI–Gas owed no duty to plaintiff’s decedent. The overwhelming weight of authority from both this court and our appellate court supports this result. Plaintiff has identified no language in the tariff or in the Act from which the duty she claims can be said to arise. Indeed, the

plain language of the tariff expressly disclaims any such duty.

Even if the common law exception imposing a duty based on actual or constructive knowledge of a leak or defect in the customer's equipment is deemed to be incorporated into the tariff, it cannot reasonably be said that the tariff also incorporates any change in the common law of duty that the courts of this state subsequently make. To do so would be to engage in bootstrapping of the most egregious kind. In effect, tariffs would not have the effect of statutes. Rather, they would become mere restatements of the common law, subject to change over \*89 time as the common law of negligence evolves. This is precisely the situation that the legislature sought to avoid.

The majority responds to this statement by citing *Bush v. Squellati*, 122 Ill.2d 153, 119 Ill.Dec. 366, 522 N.E.2d 1225 (1988), for the proposition that it is for the General Assembly, not this court, to abrogate NI-Gas' common law duty. 211 Ill.2d at 69, 284 Ill.Dec. at 327, 809 N.E.2d at 1273. *Bush* is inapposite. The issue was whether the maternal grandparents of a child who was adopted by other relatives on the maternal side of the child's birth family had standing to seek court-ordered visitation. This court found no statutory basis for standing and noted that it was for the legislature to "expand grandparental visitation \*\*1283 \*\*\*337 rights." Subsequent legislative efforts to do so have met with constitutional barriers. See *Wickham v. Byrne*, 199 Ill.2d 309, 263 Ill.Dec. 799, 769 N.E.2d 1 (2002). *Bush* hardly offers support for the majority's conclusion that the tariff does not *already* shield NI-Gas from liability under these facts.

## Conclusion

The death of Janice Adams was tragic. It is a further tragedy that the entity likely to blame for the defect that caused her death is no longer in business. That unfortunate fact, however, is not a sufficient basis for this court to ignore the public policy of this state as expressed in the Act and the plain language of the tariff with regard to limits of liability.

In sum, this court should be guided by our holding in *Illinois Bell Switching Station*, 161 Ill.2d at 244, 204 Ill.Dec. 216, 641 N.E.2d 440, that the exculpatory language in the tariff, which has been "accepted for decades by the General Assembly, is neither in contravention of the Act passed by that same body, the rules passed by the Commission (an agency of that body), nor against public policy." The plain language of the tariff, which not only does not impose a duty to warn of hazards associated with pipes and fixtures installed and owned by the customer, but also expressly disclaims any \*90 such liability, should be given effect by this court. I would affirm the judgment of the circuit court, granting summary judgment in favor of the defendant, NI-Gas.

Justices FITZGERALD and THOMAS join in this dissent.

## All Citations

211 Ill.2d 32, 809 N.E.2d 1248, 284 Ill.Dec. 302

## Footnotes

- 1 Count I named Georgevich as a defendant. Plaintiff alleged that Georgevich owed decedent "a duty of ordinary care to insure the aforesaid premises was reasonably safe for occupancy;" and that Georgevich breached this alleged duty by (a) failing "to inspect and/or cause the inspection of the aforesaid premises for fire safety and prevention;" and (b) permitting the occupancy of the house "when not reasonably safe to do so." Georgevich filed an unopposed motion for summary judgment against plaintiff. Georgevich contended that she had no duty of care with respect to decedent's house. She argued that although she owned decedent's house, it was in decedent's exclusive possession and control. The circuit court granted the motion.
- 2 The American National Standards Institute (ANSI) "is a voluntary membership organization that develops consensus standards nationally for a wide variety of devices and procedures." *Thatcher v. TWA*, 69 S.W.3d 533, 536 (Mo.App.2002); accord *Schultz v. Northeast Illinois Regional Commuter R.R. Corp.*, 201 Ill.2d 260, 269, 266 Ill.Dec. 892, 775 N.E.2d 964 (2002).
- 3 NI-Gas also brought a contribution claim against Georgevich. If found liable to plaintiff, NI-Gas sought contribution from Georgevich in such amount that was attributable to Georgevich's relative fault. Georgevich subsequently moved

for summary judgment on NI-Gas' contribution claim against her. After granting NI-Gas' motion for summary judgment against plaintiff, the circuit court ruled that Georgevich's motion for summary judgment on NI-Gas' contribution claim was moot.

114 Conn. 628

Supreme Court of Errors of Connecticut.

LEVITT

v.

PUBLIC UTILITIES COMMISSION et al.

April 12, 1932.

Appeal from Superior Court, Hartford County; Alfred E. Baldwin, Judge.

Proceedings by Albert Levitt to require the Connecticut Light & Power Company to furnish electric service. Decision of the Public Utilities Commission dismissing plaintiff's application was affirmed by the superior court, on trial to the court, and plaintiff's appeal was dismissed, and plaintiff appeals.

No error.

West Headnotes (8)

**[1] Public Utilities**

-- Service and Facilities

317A Public Utilities

317AII Regulation

317Ak114 Service and Facilities

(Formerly 101k3821/2)

Utility is not required to serve all without discrimination merely because it can do so without materially affecting its financial or rate structure.

Cases that cite this headnote

**[2] Public Utilities**

-- Service and Facilities

317A Public Utilities

317AII Regulation

317Ak114 Service and Facilities

(Formerly 101k3821/2)

Test whether public service company should be required to build extension to serve customer is whether requirement is reasonable.

Cases that cite this headnote

**[3] Public Utilities**

-- Reasonableness of Charges in General

317A Public Utilities

317AII Regulation

317Ak119 Regulation of Charges

317Ak123 Reasonableness of Charges in General

(Formerly 101k3821/2)

Reasonable classification of service and rates by utilities company is permissible, provided it treats alike all those similarly circumstanced.

Cases that cite this headnote

**[4] Electricity**

-- Regulation of Supply and Use

145 Electricity

145k11 Supply of Electricity in General

145k11(4) Regulation of Supply and Use

Decision of public utilities commission refusing to require power company to furnish to isolated house, 3,000 feet from nearest service line, service at regular rates established for customers living within 600 feet of line held justified. Gen.St.1930, § 3598.

Cases that cite this headnote

**[5] Electricity**

-- Judicial Review and Enforcement

145 Electricity

145k11.3 Regulation of Charges

145k11.3(7) Judicial Review and Enforcement

One seeking to require power company to furnish service at regular rates, who failed to establish his claim and failed to question reasonableness of special rates for extension, could not on appeal challenge company's general rate structure.

3 Cases that cite this headnote

**[6] Administrative Law and Procedure**

-- Parties

**Public Utilities**

~ Parties

- 15A Administrative Law and Procedure
- 15AIV Powers and Proceedings of Administrative Agencies, Officers and Agents
- 15AIV(D) Hearings and Adjudications
- 15Ak450 Parties
- 15Ak450.1 In General  
(Formerly 15Ak450)
- 317A Public Utilities
- 317AIII Public Service Commissions or Boards
- 317AIII(B) Proceedings Before Commissions
- 317Ak163 Parties  
(Formerly 317Ak13)

Resident of territory served by utility must be customer or prospective customer, under circumstances involving reasonableness of utility's rate structure, to permit him to challenge rate structure.

Cases that cite this headnote

[7] **Administrative Law and Procedure**

~ Inferences or Conclusions from Evidence in General

**Public Utilities**

~ Review and Determination in General

- 15A Administrative Law and Procedure
- 15AV Judicial Review of Administrative Decisions
- 15AV(E) Particular Questions, Review of
- 15Ak784 Fact Questions
- 15Ak789 Inferences or Conclusions from Evidence in General
- 317A Public Utilities
- 317AIII Public Service Commissions or Boards
- 317AIII(C) Judicial Review or Intervention
- 317Ak188 Appeal from Orders of Commission
- 317Ak194 Review and Determination in General  
(Formerly 317Ak32)

Court on appeal from decision of public utilities commission merely reviews commission's conclusions.

Cases that cite this headnote

[8] **Administrative Law and Procedure**

~ Theory and Grounds of Administrative Decision

**Public Utilities**

~ Review and Determination in General

- 15A Administrative Law and Procedure
- 15AV Judicial Review of Administrative Decisions
- 15AV(D) Scope of Review in General
- 15Ak753 Theory and Grounds of Administrative Decision
- 317A Public Utilities
- 317AIII Public Service Commissions or Boards
- 317AIII(C) Judicial Review or Intervention
- 317Ak188 Appeal from Orders of Commission
- 317Ak194 Review and Determination in General  
(Formerly 317Ak32)

Where public utilities commission reasonably determined that sole issue before it was whether utility should be required to furnish prospective customer service at regular rate, superior court on appeal properly refused to consider reasonableness of rates and conditions imposed for extension service.

Cases that cite this headnote

**Attorneys and Law Firms**

\*878 Albert Levitt, of Redding, pro se.

William E. Thoms of Waterbury, and Edward M. Day, of Hartford, for appellee Connecticut Light & Power Co.

\*879 Warren B. Burrows, Atty. Gen., Ernest L. Averill, Dep. Atty. Gen., and H. Roger Jones, Asst. Atty. Gen., for defendant Public Utilities Commission.

**Opinion**

MALTBIE, C. J.

The plaintiff has appealed from an order of the public utilities commission refusing to direct the Connecticut Light & Power Company to furnish him electric service at his home. The company serves a considerable number of country towns and has established rates for its customers in them, with special provisions governing service where extension lines more than 600 feet in length are required. Under the latter provisions, customers are served at the regular rates if they will agree to use a certain amount of electricity for each 100 feet of the extension: or, if the customer does not wish to use that amount, at an

increase over the regular rate based upon the length of the extension beyond 600 feet: or, if the customer prefers, he may pay the company the cost of the extension in excess of 600 feet: and provision is made for an adjustment of the charges if others are then or later served by the extension, or street lights are installed upon it. The plaintiff's house stands upon a little used country road. The nearest service line of the company is 3,000 feet away, and between the line and the house are no other buildings which might require service. The next house beyond the plaintiff's is about 3,000 feet distant from it, with no other possible users of electricity between. The construction of an extension line upon the road to the plaintiff's house would entail more than ordinary cost, because it would have to run through woods and over a rocky soil. The trial court has also found that there is no prospect of any real estate development upon the road within any reasonable length of time in the future; and, while this finding is attacked, we cannot say that it so lacks reasonable support in the evidence as to justify striking it out. The estimated cost of constructing the extension would be \$1,332.71, the estimated gross annual revenue at the regular rates charged by the company would be \$119.40, and the estimated annual expense of the company in providing the service would be \$151.21. The company is in good financial condition, and the construction of the extension and service to the plaintiff at the regular rates would not materially affect its financial structure or require a change in its present rate structure.

[1] [2] The basic claim of the plaintiff is that the company was under a duty to build the extension and furnish him service without expense to him or any additional charge beyond its regular rates. Stated broadly, his claim is that a public utility company is obliged to serve all within the territory it is chartered to serve without discrimination in rates, provided it can do so without materially affecting its financial or rate structure. An examination of the numerous authorities cited by him does not substantiate this claim. A moment's consideration shows that the application of such a principle, at least as applied to a company with charter authority to serve a large rural area, would be impracticable. If the company were under a duty to build extensions so long as its financial or general rate structure was not affected, it could very likely for a time build extensions as they were requested. But a situation would inevitably be reached where the construction of further extensions would affect its financial and general rate structure. When that situation

arose, if its financial or general rate structure is not to be affected, two courses would be open: either to permit the company to refuse any further extension where service upon it considered by itself would entail a loss to the company, or, at that time, to apply the very principle followed by the commission in this case; to require of the company thereafter to make only reasonable extensions. The first alternative would be to discriminate between those desiring extensions solely upon the basis of the relative order in time at which their requests were made, and the second would, on the one hand to a considerable extent make the same discrimination and, on the other, would merely postpone the application of the test of the reasonableness of requiring the particular extension. It is generally recognized that in determining whether or not a public service company is to be required to build an extension to serve a customer or customers, the question is whether, in view of all the circumstances of the case, it is reasonable to compel it to do so. "The question of a public service corporation's duty is not one which is determinable by the application of any such simple test as, 'Will the proposed new service be immediately self-supporting or remunerative?' Its duty is measured by what it ought reasonably to be called upon to do. The test sets up reasonableness as the standard, and in its application here as elsewhere it takes into account all relevant circumstances, and has no definite or precise measure. It is clear, however, that in a case like the one before us prospective future returns from the new undertaking is a factor not to be overlooked or passed over slightly." *Root v. New Britain Gas Light Co.*, 91 Conn. 134, 143, 99 A. 559, 562. See also, *New York ex rel. Woodhaven Gas Light Co. v. Public Service Commission*, 269 U. S. 248, 46 S. Ct. 83, 70 L. Ed. 255; *Lukrawka v. Spring Valley Water Co.*, 169 Cal. 318, 322, 146 P. 640, Ann. Cas. 1916D, 277; *Public Service Commission of Maryland v. Brooklyn & Curtis Bay L. & W. Co.*, 122 Md. 612, 619, 90 A. 89; \*880 *Oklahoma Gas & Electric Co. v. State*, 87 Okl. 174, 209 P. 777; *Murray v. Public Utilities Commission*, 27 Idaho, 603, 623, 150 P. 47, L. R. A. 1916F, 756; *Ladner v. Mississippi Public Utilities Co.*, 158 Miss. 678, 131 So. 78; *Zeilda Forsee Investment Co. v. St. Joseph Gas Co.*, 196 Mo. App. 371, 195 S. W. 52.

[3] Section 3598 of the General Statutes provides: "If any public service company shall unreasonably fail or refuse to furnish adequate service at reasonable rates to any person within the territorial limits within which such company has, by its charter, authority to furnish such service, such

person may bring his written petition to the commission alleging such failure or refusal." This statute embodies a recognition by the Legislature of the principles we have stated. It was so construed in the Root Case, and has been so considered by the public utilities commission in its decisions. In re Residents of Maple Hill, P. U. R. 1916B, 308; Stanley v. Danbury & Bethel Gas & Electric Light Co., Pub. Util. Com. Docket No. 5563, October 18, 1930. In so far as the commission held that the company should not be directed to furnish service to the plaintiff at the regular rates established for its customers living within 600 feet of its service lines, the trial court committed no error in sustaining its conclusion.

[4] As a public service company is not under a duty to extend its service at its regular rates except where it is reasonable that it should do so, it necessarily follows that it may, and sound policy dictates that it should, establish rates or conditions upon which it will build extensions beyond those limits. Reasonable classification of service and rates is permissible to a public utilities company, provided it treats alike all those who are similarly circumstanced. Gallaher v. Southern New England Telephone Co., 99 Conn. 282, 121 A. 686; Bilton Machine Tool Co. v. United Illuminating Co., 110 Conn. 417, 426, 148 A. 337, 67 A. L. R. 814; Northern Pacific Ry. v. North Dakota, 236 U. S. 585, 598, 35 S. Ct. 429, 59 L. Ed. 735, L. R. A. 1917F, 1148, Ann. Cas. 1916A, 1; Willcox v. Consolidated Gas Co., 212 U. S. 19, 54, 29 S. Ct. 192, 53 L. Ed. 382, 48 L. R. A. (N. S.) 1134, 15 Ann. Cas. 1034; Phelan v. Boone Gas Co., 147 Iowa, 626, 628, 125 N. W. 208, 31 L. R. A. (N. S.) 319.

[5] [6] If the company has the right to establish two classes of service with differing rates, we do not understand the plaintiff to question the reasonableness of the classification; that is, one applying to its regular service, and the other to service for extensions of more than 600 feet. What he did question in the trial court, and questions here, is the reasonableness of the rates and conditions which are imposed for the extension service. That he would in proper proceedings be entitled to raise this issue is not open to question. An examination of the decision of the public utilities commission discloses that it did make a formal finding, following the words of the statute, that the company had not unreasonably failed or refused to furnish the plaintiff adequate service at reasonable rates; but that it did not in fact definitely consider or rule upon the reasonableness of the special rates or conditions

established by the company for such a situation as that of the plaintiff. The function of the courts upon such appeals as the one before us is to review the conclusions and decisions of the commission; and it is not for the courts in the first instance to pass upon the reasonableness of the rates or requirements established by the company furnishing service. The most the trial court could have done upon the appeal was to find that the commission ought to have ruled upon that question, and, if it ought to have done so, to have sustained the appeal upon that ground. We are thus faced with a procedural question and required to consider the issues presented for determination to the commission in the proceedings before it and to the trial court upon the appeal.

The proceedings before the commission originated in a letter from the plaintiff to it, in which he stated that he had requested the company to furnish him with light and heat for use in his home, that it had declined to do so, except upon conditions which he thought were unreasonable and contrary to law, and that he inclosed a copy of a letter he had written the company. He asked a hearing and also suggested that the company be requested to bring its account book before the commission, as the fundamental questions involved would concern the value of the property of the company in furnishing light, heat, and power to its patrons, and the return it was making on that value. The inclosed letter to the company stated that it confirmed a conversation which the plaintiff had with the company's local manager at which the plaintiff had requested the company to furnish him light and power, and the manager had indicated that it would not serve him unless he was willing to pay for the extension of service or guarantee a minimum usage of electricity above the ordinary reasonable usage he might have; that he declined to meet these conditions upon the ground that they were unreasonable and contrary to law; and that he was taking the matter up with the public utilities commission. These letters did not state with any reasonable definiteness the question or questions which the plaintiff was seeking before the commission. The proceedings before it, all of which the plaintiff annexed to his appeal as an exhibit, disclose that he was interrogated during the hearing before the \*881 commission as to the precise claim or claims he was making, and answered in various ways. The decision of the commission shows that it finally concluded his real claim to be that, if the company could furnish him service at its regular rates without affecting its financial or rate structure, it was under a duty to do so, without regard to

the cost of the extension or the prospective return from it. We cannot say that the conclusion of the commission as to the claim he was really making was not one it could reasonably reach. In fact, the plaintiff's appeal to the superior court adopts that theory of his case, because it begins with a recital that the plaintiff requested a hearing before the commission upon the refusal of the company to extend its lines to his house and furnish him service at the rates usually charged to other residents of the town in which he lived; and no other allegations in the appeal broaden the scope of the issue so made. The superior court was therefore correct in restricting the issues to those which the commission found to have been presented to it, and in not considering the reasonableness of the rates and conditions which the company had established for extensions to persons situated as was the plaintiff; and it follows that this question is not before us.

[7] [8] At the hearing before the commission, the plaintiff sought to challenge the general rate structure of the company, and renewed that effort before the trial court upon the appeal. Had the plaintiff been entitled to the extension he sought upon the basis of the regular rates established by the company, the reasonableness of those rates might have been open to inquiry by the commission. As he was not entitled to the extension at the regular rates, the reasonableness of those rates would only have been of moment, as they might be involved in a determination of the reasonableness of the special rates established by the company for extensions beyond 600 feet from its

service lines. But, as we have said, that question was not considered by the commission, and was not before the trial court. The mere fact that one resides within a district which a public utility corporation has charter authority to serve does not give him such an interest in the rate structure of the company as to permit him to challenge it before the commission or before the courts. He must be either a customer of it, or one honestly seeking to have its service extended to him under circumstances involving the reasonableness of that schedule; and if, because of either of these facts, he is entitled to make such a challenge, he must proceed before the commission in such a way as fairly to apprise it of his claim, and, upon an appeal from its order, must raise the issue before the court by proper pleading. The plaintiff is not a customer of the Connecticut Light & Power Company, and, regarded as a prospective customer, he did not bring before the commission or the trial court the reasonableness of the general rate schedule of the company in such a way as to require it to be considered.

There is no error.

The other Judges concurred.

**All Citations**

114 Conn. 628, 159 A. 878

KeyCite Yellow Flag - Negative Treatment  
Distinguished by Modesto Irr. Dist. v. Gutierrez, 9th Cir.(Cal.), August 20, 2010

477 F.3d 668  
United States Court of Appeals,  
Ninth Circuit.

NORTHWEST ENVIRONMENTAL  
DEFENSE CENTER, Public Employees for  
Environmental Responsibility; Northwest  
Sportfishing Industry Association, Petitioners,  
Northwest Power and  
Conservation Council, Intervenor,  
v.  
BONNEVILLE POWER  
ADMINISTRATION, Respondent.  
Confederated Tribes and Bands of the  
Yakama Indian Nation, Petitioner,  
v.  
Bonneville Power Administration, Respondent.

Nos. 06-70430, 06-71182.

|  
Argued and Submitted Sept. 12, 2006.

|  
Filed Jan. 24, 2007.

### Synopsis

**Background:** Environmental groups and others petitioned for judicial review of actions of federal power marketing agency that operated dams on river in transferring to two contractors the functions of fish passage center (FPC), which provided technical assistance and information on matters related to passage of salmon and steelhead through river and its tributaries to wildlife agencies, Indian tribes, and general public.

**Holdings:** The Court of Appeals, Gould, Circuit Judge, held that:

[1] subject matter jurisdiction existed over petitions for review;

[2] agency acted contrary to law when agency concluded, based solely on committee report language, that it was bound to transfer FPC's functions to contractors; and

[3] agency's decision to transfer FPC's functions to contractors was arbitrary and capricious.

Petition for review granted.

West Headnotes (24)

### [1] Federal Courts

~ Jurisdiction

170B Federal Courts

170BXVII Courts of Appeals

170BXVII(K) Scope and Extent of Review

170BXVII(K)2 Standard of Review

170Bk3576 Procedural Matters

170Bk3581 Jurisdiction

170Bk3581(1) In general

(Formerly 170Bk776)

Court of Appeals considers challenges to its subject matter jurisdiction de novo.

Cases that cite this headnote

### [2] Electricity

~ Environmental considerations in general

145 Electricity

145k8.6 Environmental considerations in general

Pursuant to its original and exclusive subject matter jurisdiction over challenges to final actions and decisions taken under Northwest Power Planning and Conservation Act by federal power marketing agency, or the implementation of such final actions, Court of Appeals had subject matter jurisdiction over petitions for review challenging both agency's solicitation of contractors to take over functions of fish passage center (FPC) and its transfer of FPC's functions to selected contractors, given that solicitation was part of process that led to agency's admittedly final actions in selecting contractors and transferring FPC's functions. Pacific Northwest Electric Power Planning and Conservation Act, § 9(e)(5), 16 U.S.C.A. § 839f(e)(5).

1 Cases that cite this headnote

**[3] Environmental Law**

-~ Organizations, associations, and other groups

149E Environmental Law

149EXIII Judicial Review or Intervention

149Ek649 Persons Entitled to Sue or Seek Review:Standing

149Ek652 Organizations, associations, and other groups

Administrative Procedure Act (APA) gave Court of Appeals the equitable power to set aside action of federal power marketing agency in transferring functions of fish passage center (FPC) to contractors if court determined that agency's action was arbitrary, capricious, or contrary to law, and therefore court had ability to redress claimed injuries required for environmental groups and others to have Article III standing to seek judicial review. U.S.C.A. Const. Art. 3, § 2, cl. 1; 5 U.S.C.A. § 706(2)(A).

5 Cases that cite this headnote

**[4] Federal Civil Procedure**

-~ In general;injury or interest

**Federal Civil Procedure**

-~ Causation:redressability

170A Federal Civil Procedure

170AII Parties

170AII(A) In General

170Ak103.1 Standing in General

170Ak103.2 In general;injury or interest

170A Federal Civil Procedure

170AII Parties

170AII(A) In General

170Ak103.1 Standing in General

170Ak103.3 Causation:redressability

To have Article III standing to challenge agency action, petitioners must satisfy three-part test under which petitioners must have suffered an injury in fact which is both (1) concrete and particularized and (2) actual or imminent, petitioners must show a causal connection between their injury and the conduct complained of, and it must be

likely, as opposed to merely speculative, that petitioners' injury will be redressed by a favorable decision. U.S.C.A. Const. Art. 3, § 2, cl. 1.

Cases that cite this headnote

**[5] Contracts**

-~ Rewriting, remaking, or revising contract

95 Contracts

95II Construction and Operation

95II(A) General Rules of Construction

95k143 Application to Contracts in General

95k143(3) Rewriting, remaking, or revising contract

Court will not create new obligations that do not exist within the four corners of a contract.

Cases that cite this headnote

**[6] Contracts**

-~ Rewriting, remaking, or revising contract

95 Contracts

95II Construction and Operation

95II(A) General Rules of Construction

95k143 Application to Contracts in General

95k143(3) Rewriting, remaking, or revising contract

In a contract case between two private parties, court's remedial power is limited to enforcing the obligations to which the private parties agreed.

Cases that cite this headnote

**[7] Administrative Law and Procedure**

-~ In general;judgment

15A Administrative Law and Procedure

15AV Judicial Review of Administrative Decisions

15AV(F) Determination

15Ak811 In general;judgment

When a public law has been violated, court is not bound to stay within the terms of a private agreement negotiated by the parties, and may exercise its equitable powers to ensure compliance with the law.

Cases that cite this headnote

**[8] Equity**

- ~ Grounds of jurisdiction in general

150 Equity

150I Jurisdiction, Principles, and Maxims

150I(A) Nature, Grounds, Subjects, and  
Extent of Jurisdiction in General

150k3 Grounds of jurisdiction in general

When the public interest is involved, court's equitable powers assume an even broader and more flexible character than when only a private controversy is at stake.

2 Cases that cite this headnote

**[9] Equity**

- ~ Grounds of jurisdiction in general

150 Equity

150I Jurisdiction, Principles, and Maxims

150I(A) Nature, Grounds, Subjects, and  
Extent of Jurisdiction in General

150k3 Grounds of jurisdiction in general

Unless Congress provides otherwise, courts of equity may go much farther both to give and withhold relief in furtherance of the public interest than they are accustomed to go when only private interests are involved.

Cases that cite this headnote

**[10] Administrative Law and Procedure**

- ~ In general;judgment

15A Administrative Law and Procedure

15AV Judicial Review of Administrative  
Decisions

15AV(F) Determination

15Ak811 In general;judgment

Court of Appeals, as a court of equity conducting judicial review under Administrative Procedure Act (APA), has broad powers to order mandatory affirmative relief, if such relief is necessary to accomplish complete justice. 5 U.S.C.A. § 551 et seq.

1 Cases that cite this headnote

**[11] Statutes**

- ~ Reports and analyses

361 Statutes

361III Construction

361III(H) Legislative History

361k1243 Particular Kinds of Legislative  
History

361k1249 Reports and analyses  
(Formerly 361k217.3)

Congressional committee report language unconnected to the text of an enacted statute has no binding legal import.

Cases that cite this headnote

**[12] Electricity**

- ~ Environmental considerations in general

145 Electricity

145k8.6 Environmental considerations in  
general

Federal power marketing agency acted contrary to law when, based solely on language in congressional committee reports that was unconnected to text of enacted statute, agency concluded that it was bound to transfer functions of fish passage center (FPC) that it funded to contractors, contrary to dictates of Northwest Power Planning and Conservation Act; since committee reports were not subject to process outlined in United States Constitution for altering legal duties of persons outside the legislative branch, agency could not give reports binding effect. U.S.C.A. Const. Art. 1, § 7, cl. 2; 5 U.S.C.A. § 706(2); Pacific Northwest Electric Power Planning and Conservation Act, §§ 2(3), 4(d)(2), (h)(10)(A), 5(d)(3), 6(b, c), 16 U.S.C.A. §§ 839(3), 839b(d)(2), (h)(10)(A), 839c(d)(3), 839d(b, c).

Cases that cite this headnote

**[13] Statutes**

- ~ Particular Kinds of Legislative History

361 Statutes

361III Construction

361III(H) Legislative History

361k1243 Particular Kinds of Legislative  
History

361k1244 In general

(Formerly 361k217.4)

Legislative history, untethered to text in an enacted statute, has no compulsive legal effect.

Cases that cite this headnote

**[14] Statutes**

~ Legislative History

361 Statutes

361III Construction

361III(H) Legislative History

361k1241 In general

(Formerly 361k217.4)

Principles in legislative history that have no statutory reference point and do not purport to explain any part of an enacted law do not carry the force of law, and thus do not bind anyone, including administrative agencies.

Cases that cite this headnote

**[15] Administrative Law and Procedure**

~ Annulment, vacation or setting aside of administrative decision

15A Administrative Law and Procedure

15AV Judicial Review of Administrative Decisions

15AV(F) Determination

15Ak816 Annulment, vacation or setting aside of administrative decision

It is "contrary to law," for purposes of provision of Administrative Procedure Act (APA) empowering courts to set aside an agency decision that is contrary to governing law, for an agency to conclude that it is legally bound by language in a congressional committee report. 5 U.S.C.A. § 706(2).

1 Cases that cite this headnote

**[16] Statutes**

~ Plain, literal, or clear meaning; ambiguity

361 Statutes

361III Construction

361III(H) Legislative History

361k1242 Plain, literal, or clear meaning; ambiguity

(Formerly 361k217.4)

When legislative history is tied directly to statutory language and that language is ambiguous, the legislative history

may permissibly inform judgment about interpreting ambiguous statutory terms.

Cases that cite this headnote

**[17] Statutes**

~ Particular Kinds of Legislative History

361 Statutes

361III Construction

361III(H) Legislative History

361k1243 Particular Kinds of Legislative History

361k1244 In general

(Formerly 361k217.4)

When legislative history is not tied to any statutory text, court should give it no weight.

1 Cases that cite this headnote

**[18] Constitutional Law**

~ Nature and scope in general

**Constitutional Law**

~ Encroachment on Executive

92 Constitutional Law

92XX Separation of Powers

92XX(B) Legislative Powers and Functions

92XX(B)1 In General

92k2340 Nature and scope in general

(Formerly 92k50)

92 Constitutional Law

92XX Separation of Powers

92XX(B) Legislative Powers and Functions

92XX(B)3 Encroachment on Executive

92k2390 In general

(Formerly 92k58)

If Congress wishes to alter the legal duties of persons outside the legislative branch, including administrative agencies, it must use the process outlined in the United States Constitution. U.S.C.A. Const. Art. 1, § 7, cl. 2.

Cases that cite this headnote

**[19] Administrative Law and Procedure**

~ Theory and grounds of administrative decision

15A Administrative Law and Procedure

15AV Judicial Review of Administrative Decisions

15AV(D) Scope of Review in General

15Ak753 Theory and grounds of administrative decision  
Court may only sustain an agency's action on the grounds actually considered by the agency.

8 Cases that cite this headnote

**[20] Administrative Law and Procedure**

~ Theory and grounds of administrative decision

**Administrative Law and Procedure**

~ Arbitrary, unreasonable or capricious action; illegality

**Administrative Law and Procedure**

~ Clear error

15A Administrative Law and Procedure

15AV Judicial Review of Administrative Decisions

15AV(D) Scope of Review in General

15Ak753 Theory and grounds of administrative decision

15A Administrative Law and Procedure

15AV Judicial Review of Administrative Decisions

15AV(D) Scope of Review in General

15Ak763 Arbitrary, unreasonable or capricious action; illegality

15A Administrative Law and Procedure

15AV Judicial Review of Administrative Decisions

15AV(E) Particular Questions, Review of

15Ak784 Fact Questions

15Ak785 Clear error

Under arbitrary and capricious standard of review established by Administrative Procedure Act (APA), agency must cogently explain why it has exercised its discretion in a given manner, and, in reviewing that explanation, court must consider whether the decision was based on a consideration of the relevant factors and whether there has been a clear error of judgment. 5 U.S.C.A. § 706(2).

12 Cases that cite this headnote

**[21] Administrative Law and Procedure**

~ Arbitrary, unreasonable or capricious action; illegality

15A Administrative Law and Procedure

15AV Judicial Review of Administrative Decisions

15AV(D) Scope of Review in General

15Ak763 Arbitrary, unreasonable or capricious action; illegality

An agency decision is "arbitrary and capricious," within meaning of Administrative Procedure Act (APA), if the agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise. 5 U.S.C.A. § 706(2).

8 Cases that cite this headnote

**[22] Administrative Law and Procedure**

~ Stare decisis; estoppel to change decision

15A Administrative Law and Procedure

15AIV Powers and Proceedings of

Administrative Agencies, Officers and Agents

15AIV(D) Hearings and Adjudications

15Ak502 Stare decisis; estoppel to change decision

An agency is entitled to change its course when its view of what is in the public's interest changes; however, an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored, and if an agency glosses over or swerves from prior precedents without discussion, it may cross the line from the tolerably terse to the intolerably mute.

13 Cases that cite this headnote

**[23] Administrative Law and Procedure**

~ Theory and grounds of administrative decision

15A Administrative Law and Procedure

15AV Judicial Review of Administrative Decisions

15AV(D) Scope of Review in General

15Ak753 Theory and grounds of administrative decision

In reviewing agency action, court must look to agency's reasoning in making its decision, and not to other reasons for its decision that agency might marshal before the court.

8 Cases that cite this headnote

**[24] Electricity**

Environmental considerations in general  
145 Electricity  
145k8.6 Environmental considerations in general  
Decision of federal power marketing agency to transfer functions of fish passage center (FPC) that it funded to two contractors was arbitrary and capricious under Administrative Procedure Act (APA), given that decision was departure from agency's two-decades-old precedent and agency did not provide reasoned analysis for its change in course, or show how it determined that transfer of FPC's functions was exercise of its authority consistent with fish and wildlife program adopted by interstate compact agency and with purposes of Northwest Power Planning and Conservation Act, 5 U.S.C.A. § 706(2); Pacific Northwest Electric Power Planning and Conservation Act, § 4(h)(10)(A), 16 U.S.C.A. § 839b(h)(10)(A).

5 Cases that cite this headnote

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On Petition for Review of a Final Action of the Bonneville Power Administration.

Before MICHAEL DALY HAWKINS, BARRY G. SILVERMAN, and RONALD M. GOULD, Circuit Judges.

**Opinion**

\*672 GOULD, Circuit Judge.

Salmon and steelhead<sup>1</sup> are two of the great natural resources of the Columbia River. Their continued existence has been threatened by the construction of dams to capture a third great natural resource of the Columbia River, its water power. As these dams were constructed, the number of salmon and steelhead migrating up the Columbia River to reproduce at its headwaters dropped. At one time, an estimated ten to sixteen million adult fish returned to the Columbia River basin each year. Today, only about one million fish return for spawning that is essential to the species' survival in the Columbia River system.

In response to declining salmon and steelhead runs, Congress passed the Northwest Power Planning and Conservation Act of 1980. The Act created the Northwest Power and Conservation Council, an interstate compact agency, and directs the Council to prepare programs to protect and enhance the fish and wildlife of the Columbia River basin while also assuring the Pacific Northwest an adequate, efficient, economical, and reliable power supply. The Act also instructs the Bonneville Power Administration, the federal agency that operates the dams

on the Columbia River, to use its authority in a manner consistent with the programs developed by the Council.

In 1982, the Council called for the creation of what would eventually become the Fish Passage Center. The Fish Passage Center provides technical assistance and information to fish and wildlife agencies, Indian tribes, and the general public on matters related to juvenile and adult salmon and steelhead passage through the Columbia River and its tributaries. Since 1987, the Bonneville Power Administration has funded the Fish Passage Center, and the Fish Passage Center has gathered, analyzed, and publicly-disseminated data regarding fish passage. The Bonneville Power Administration has used this information, in consultation with fisheries and Indian tribes and in conjunction with its control over water flow past the dams, to help improve the survival rates of fish migrating up and down the Columbia River.

In light of language in two 2005 congressional committee reports, however, the Bonneville Power Administration decided to transfer the functions performed by the Fish Passage Center to Battelle Pacific Northwest Laboratory and Pacific States Marine Fisheries Commission. In this consolidated case, Northwest Environmental Defense Center, Public Employees for Environmental Responsibility, Northwest Sportfishing Industry Association, and the Confederated Tribes and Bands of the Yakama Nation (collectively, "petitioners") petition for review of the Bonneville Power Administration's action transferring the functions of the Fish Passage Center to Battelle Pacific Northwest Laboratory and Pacific States Marine Fisheries Commission and creating a new model Fish Passage Center ("new model").

I

A

Created by the Bonneville Project Act of 1937, 16 U.S.C. §§ 832–832m, the Bonneville Power Administration ("BPA") is a federal agency within the Department of Energy. BPA sells and transmits wholesale electricity from thirty-one federal hydroelectric \*673 plants, one non-federal nuclear power plant in Hanford, Washington, and other non-federal power plants in the Columbia River basin. About BPA Home, <http://www.bpa.gov/>

corporate/About\_BPA/ (last visited Jan. 17, 2007). BPA's customers include federal agencies, public and private utility companies, and direct service industrial customers. *See Kaiser Aluminum & Chem. Corp. v. BPA*, 261 F.3d 843, 845 (9th Cir.2001). BPA does not receive annual appropriations, as is the case with most federal agencies. Rather, the revenue that BPA obtains from its sales and transmission of electricity is deposited in the Bonneville Power Administration fund ("BPA fund"). 16 U.S.C. § 838i(a). BPA then uses the fund to finance its operations. *Id.* § 838i(b).

As a self-financing power marketing agency, BPA must set its prices high enough to cover its costs. *Indus. Customers of Nw. Utilities v. BPA*, 408 F.3d 638, 641 (9th Cir.2005); *Ass'n of Public Agency Customers, Inc. v. BPA*, 126 F.3d 1158, 1164 (9th Cir.1997) [hereinafter *APAC*]. BPA must also sell power to consumers "at the lowest possible rates." 16 U.S.C. § 838g. At the same time, BPA must be environmentally conscious, supporting energy conservation and protecting the fish and wildlife of the Columbia River basin. *APAC*, 126 F.3d at 1164; *see, e.g.*, 16 U.S.C. § 839b(h)(10)-(11) (providing that BPA must use the BPA fund and its statutory authority in a manner that protects and enhances fish and wildlife).

In 1980, to assist BPA in balancing its responsibilities to provide low-cost energy while protecting fish and wildlife, Congress passed the Pacific Northwest Power Planning and Conservation Act ("Northwest Power Act" or "Act"), Pub.L. No. 96–501, 94 Stat. 2697 (1980) (codified at 16 U.S.C. §§ 839–839h). The Act authorized state governments to form what is now called the Northwest Power and Conservation Council ("Council"), an interstate compact agency<sup>2</sup> comprised of members from Idaho, Montana, Oregon, and Washington. 16 U.S.C. § 839b(a)(2)(B); *see Seattle Master Builders Ass'n v. Pac. Nw. Elec. Power & Conservation Council*, 786 F.2d 1359, 1366 (9th Cir.1986) (upholding the constitutionality of the Council). Each state has agreed to participate in the Council, *see Idaho Code* § 61–1201; *Mont.Code Ann.* § 90–4–401; *Or.Rev.Stat.* § 469.803; *Wash. Rev.Code Ann.* § 43.52A.010, and has enacted legislation authorizing its governor to appoint two members to the Council, *see Idaho Code* § 61–1202; *Mont.Code Ann.* § 90–4–402; *Or.Rev.Stat.* § 469.805; *Wash. Rev.Code Ann.* § 43.52A.030.

The Act charges the Council with two tasks fundamental to this case: (1) preparing and periodically reviewing a regional conservation and electric power plan to aid BPA in acquiring and developing power resources (“Power Plan” or “Plan”) and (2) preparing and periodically reviewing a program to protect, mitigate, and enhance fish and wildlife (“Fish and Wildlife Program” or “Program”). 16 U.S.C. § 839b(a)(1).

The current composition of the Council reflects the varied constituencies it serves. The Council is chaired by an expert in natural resource economics. Many Council members are former business persons or practicing attorneys. Indian tribes and \*674 fishing enthusiasts are also represented on the Council. Four of the eight current Council members have served as state senators or state representatives in the Pacific Northwest.<sup>3</sup>

The Council submits each project proposed for funding under its Fish and Wildlife Program for review by the Independent Scientific Review Panel, an eleven-member panel of independent scientists appointed by the Council from the recommendations of the National Academy of Scientists. *See id.* § 839b(h)(10)(D). The Act obliges BPA to consult with state fish and wildlife agencies and Indian tribes in carrying out its responsibilities under the Act. *See id.* § 839b(h)(11)(B). In short, the Act “establishes an innovative system of cooperative federalism under which the states, within limits provided in the Act, can represent their shared interests in the maintenance and development of a power supply in the Pacific Northwest and in related environmental concerns.” *Seattle Master Builders*, 786 F.2d at 1366.

## B

Section 839b(h)(10)(A) of the Act explains how the views of the Council guide BPA's actions. It provides:

The Administrator [of BPA] shall use the Bonneville Power Administration fund and the authorities available to the Administrator under this chapter and other laws administered by the Administrator to protect, mitigate, and enhance fish and wildlife to the extent affected by the development

and operation of any hydroelectric project of the Columbia River and its tributaries in a manner consistent with the plan, if in existence, the program adopted by the Council under this subsection, and the purposes of this chapter.

16 U.S.C. § 839b(h)(10)(A). In other words, the Act requires BPA's fish and wildlife protection, mitigation, and enhancement actions to be consistent with (1) the Council's Power Plan; (2) the Council's Fish and Wildlife Program; and (3) the purposes of the Act.<sup>4</sup> Section 839b(h)(10)(A) is thus referred to as the Act's “consistency requirement.”

The Council adopted its first Fish and Wildlife Program in 1982. Since 1982, the Council has reviewed and reformulated its Program five times. The current version of the Program was adopted in 2000 (“2000 Program”) and amended in 2003 by the Mainstem Amendments (“2003 Amendments”).

In preparing the 2000 Program, the Council consulted with the Pacific Northwest's fish and wildlife agencies, Indian tribes, and other interested members of the public, as required by the Act. *See id.* § 839b(g). After considering these parties' recommendations, the Council prepared \*675 a draft Program and conducted a public comment period before preparing the final version of the 2000 Program. The Program “expresses goals and objectives for the entire [Columbia River] basin based on a scientific foundation of ecological principles.” *Nw. Power & Conservation Council, Columbia River Basin Fish and Wildlife Program* 9 (2000) [hereinafter 2000 Program], available at <http://www.nwcouncil.org/library/2000/2000-19/FullReport.pdf>. These objectives apply to all fish and wildlife projects implemented in the basin. *Id.* The objectives crucial to this case include mitigating the adverse effects to salmon and steelhead caused by the Columbia River's hydropower system and ensuring sufficient populations of salmon and steelhead for both Indian tribal-trust and treaty-right fishing and non-tribal fishing. *Id.* at 16. A goal of the Program is to increase total adult salmon and steelhead runs on the Columbia River from about one million annually today to an average of five million annually by 2025. *Id.* at 7, 17.

C

The Fish Passage Center (“FPC”) has been a part of the Council's Fish and Wildlife Program since 1982. Originally called the Water Budget Center, it consisted of two managers who oversaw the annual water budget the Council adopted as part of the Program. The water budget provided for additional releases of water from federal dams each spring to facilitate the migration of juvenile salmon and steelhead to the Pacific Ocean. The Water Budget Center's two managers recommended to federal agencies how they could use the water budget to improve the survival rate of fish passing through the dams during their downstream migration. *See Pub. Utility Dist. No. 1 v. BPA*, 947 F.2d 386, 389 (9th Cir.1991) (discussing FPC's oversight of the annual water budget contained in the 1987 Program).

The FPC's responsibilities under the Program have expanded considerably since its days as the Water Budget Center. The Council's 1987 Program provided that BPA “shall fund the establishment and operation of a Fish Passage Center.” The Council envisioned that the FPC would assist the dams' fish passage managers in planning and implementing a smolt<sup>5</sup> monitoring program, developing and implementing flow and spill requests, and monitoring and analyzing research results to assist in implementing the water budget and spill planning.

The Council's 2000 Program “continues the operation of the Fish Passage Center.” 2000 Program, *supra*, at 28. The 2003 Amendments to the Program elaborate on the Council's vision of the FPC's role, stating that “[t]he mainstem plan calls for the continued operation of the Fish Passage Center,” and listing specific tasks the Council expects the FPC to perform in helping implement the water management measures in the Council's Fish and Wildlife Program. *Nw. Power & Conservation Council, Mainstem Amendments to the Columbia River Basin Fish and Wildlife Program 27* (2003) [hereinafter 2003 Amendments], available at <http://www.nwcouncil.org/library/2003/2003-11.pdf>.

The 2003 Amendments provide that “[t]he primary purpose of the [FPC] is to provide technical assistance and information to fish and wildlife agencies and [Indian] tribes in particular, and the public in general, on matters related to juvenile and \*676 adult salmon and steelhead

passage through the mainstem hydrosystem.” *Id.* The 2003 Amendments require the FPC to (1) plan and implement a smolt monitoring program; (2) gather, organize, analyze, store, and make widely-available monitoring and research information about fish passage and the implementation of water management and fish passage measures contained in the Council's Program; (3) provide technical information to assist fish and wildlife agencies and Indian tribes requesting the federal dams to spill water; and (4) provide technical assistance to ensure the recommendations for river operations avoid conflicts between anadromous<sup>6</sup> and resident fish. *Id.* at 27–28.

To carry out these responsibilities, the FPC monitors more than twenty dams and fish traps; collects data on chinook, steelhead, coho, shad, sockeye, pink salmon, and lamprey; and monitors river conditions, including temperature, dissolved gases, fish hatchery releases, and dam flows and spills. The FPC makes information it gathers available on its website. Fishery managers and Indian tribes use this information to make flow and spill requests to BPA and the operators of the dams, who, by controlling the water flow past the dams, can improve the survival rates of fish migrating downstream.<sup>7</sup>

From the administrative record it appears that the FPC operates independently of BPA and the Council. However, nothing in the record indicates that the FPC is a distinct legal entity. BPA funds the FPC through grants administered by master contracts with the Pacific States Marine Fisheries Commission (“Pacific States”). BPA specifies tasks for the FPC to perform in annual statements of work within BPA's master contract with Pacific States.

D

Conflict between environmental and energy interests in the Columbia River basin has on occasion played out in the courtroom, as shown in BPA-related cases decided by us. *See, e.g., Confederated Tribes of the Umatilla Indian Reservation v. BPA*, 342 F.3d 924 (9th Cir.2003); *Nw. Env'tl. Def. Ctr. v. BPA*, 117 F.3d 1520 (9th Cir.1997); *Nw. Res. Info. Ctr., Inc. v. Nw. Power Planning Council*, 35 F.3d 1371 (9th Cir.1994) [hereinafter, *NRIC*]; *Nw. Res. Info. Ctr., Inc. v. Nat'l Marine Fisheries Serv.*, 25 F.3d 872 (9th Cir.1994). In this case, however, an issue over how to balance fish survival and recovery with the inexpensive

production of hydropower was raised in the legislative committee process.

\*677 In June 2005, the United States Senate Appropriations Subcommittee on Energy and Water Development issued its report on House Resolution 2419, the resolution that would become the Energy and Water Development Appropriations Act of 2006 ("2006 Appropriations Act"). The subcommittee report stated that BPA "may make no new obligations from the Bonneville Power Administration Fund in support of the Fish Passage Center" because "there are universities in the Pacific Northwest that already collect fish data for the region" and can carry out the FPC's responsibilities "at a savings to the region's ratepayers." S.Rep. No. 109-84, at 179 (2005).

On November 19, 2005, Congress passed the 2006 Appropriations Act. Pub.L. No. 109-103, 119 Stat. 2247 (2005). The 2006 Appropriations Act makes no reference to the FPC. The Conference Committee Report of the Congress accompanying the Act, however, states that

The Bonneville Power Administration may make no new obligations in support of the Fish Passage Center. The conferees call upon Bonneville Power Administration and the Northwest Power and Conservation Council to ensure that an orderly transfer of the Fish Passage Center functions (warehouse of smolt monitoring data, routine data analysis and reporting and coordination of the smolt monitoring program) occurs within 120 days of enactment of this legislation. These functions shall be transferred to other existing and capable entities in the region in a manner that ensures seamless continuity of activities.

H.R.Rep. No. 109-275, at 174 (2005) (Conf.Rep.).

On December 8, 2005, in response to the committee reports, BPA issued a "Program Solicitation for Key Functions previously performed by the Fish Passage Center" ("Program Solicitation"). The Program Solicitation states that "[i]n November 2005, the U.S.

Congress passed legislation (House Report 109-275), which forbids BPA from making additional obligations in support of the Fish Passage Center." The Program Solicitation further states that "BPA has decided to implement this requirement thru [sic] the issuance of this Program Solicitation."

BPA received five responses to its Program Solicitation. On January 26, 2006, BPA announced, in a press release, its decision to award contracts for the functions formerly performed by the FPC to Battelle Pacific Northwest National Laboratory ("Battelle") and Pacific States.<sup>8</sup> The new model divides between Battelle and Pacific States a number of the functions that had been wholly the responsibility of the FPC. According to the press release, under this new model, Pacific States will "coordinate implementation of the Smolt Monitoring Program, manage the real-time database of the monitoring program and related data, and perform routine analysis and reporting of that data." On the other hand, Battelle will "serve a coordinating function, relying on experts in the field to provide in-depth analysis of the data." Battelle executed its contract with BPA on February 28, 2006, and Pacific States executed its contract on March 16, 2006.

## E

Northwest Environmental Defense Center, Public Employees for Environmental Responsibility, and Northwest Sports-fishing Industry Association (collectively, "NEDC") filed a petition for review with \*678 us on January 23, 2006 and an amended petition for review on February 6, 2006, challenging BPA's decision to transfer the functions of the FPC to Pacific States and Battelle, alleging that the transfer of the functions of the FPC ran afoul of BPA's duties under the Northwest Power Act. The Confederated Tribes and Bands of the Yakama Nation ("Yakama") filed a petition for review on March 3, 2006, also challenging BPA's decision to transfer the functions of the FPC.

On March 17, 2006, we granted the petitioners' request for a stay pending our review of BPA's action. We ordered BPA to "continue, pending resolution of [the petition for review] and/or further order of the court, its existing contractual arrangement to fund and support the Fish Passage Center under the existing terms and conditions."

On April 7, 2006, we consolidated NEDC's petition with the petition filed by Yakama.

The petitioners ask us to set aside BPA's decision to transfer the functions of the FPC and to use our equitable authority to order BPA to fund the FPC. Before we address the merits of their petitions for review, we must determine whether we have jurisdiction. *See Steel Co. v. Citizens for a Better Env't*, 523 U.S. 83, 94-95, 118 S.Ct. 1003, 140 L.Ed.2d 210 (1998).

## II

[1] BPA raises two challenges to our jurisdiction. First, BPA argues that we lack statutory jurisdiction to adjudicate the petitioners' challenge to BPA's decision to transfer the functions of the FPC because BPA's December 8, 2005 Program Solicitation is not a "final action" of BPA. *See* 16 U.S.C. § 839f(e)(5) (permitting judicial review of "final actions" of BPA and the Council). Second, BPA asserts that the petitioners do not have standing to challenge BPA's action in this case because a decision in favor of the petitioners will not be likely to redress the petitioners' injury, as required for us to exercise jurisdiction under Article III of the United States Constitution. We consider these challenges to our subject-matter jurisdiction de novo. *Indus. Customers of Nw. Utils.*, 408 F.3d at 644.

### A

[2] The Northwest Power Act vests us with original and exclusive subject-matter jurisdiction over challenges to "final actions and decisions taken pursuant to [the Act] by the Administrator [of BPA] or the Council, or the implementation of such final actions." 16 U.S.C. § 839f(e) (5). We have interpreted § 839f(e)(5)'s judicial review provision "with a broad view of this Court's jurisdiction." *Transmission Agency of N. Cal. v. Sierra Pac. Power Co.*, 295 F.3d 918, 925 (9th Cir.2002) (internal quotation omitted).

BPA argues that we lack jurisdiction over the petitioners' challenge to the December 8, 2005 Program Solicitation because the Program Solicitation was not a "final action." But in its brief BPA concedes that its January 26, 2006 decision, selecting the successors to the FPC, is a final

agency action subject to judicial review under § 839f(e) (5). While BPA's issuance of the Program Solicitation alone might not have been a final action subject to our review, BPA's initial decision to create a new model Fish Passage Center and to issue the Program Solicitation was part of the process BPA used to set its course, leading to what BPA concedes was its final action transferring the functions of the FPC to Pacific States and Battelle. Because both NEDC's and Yakama's petitions for review directly challenge the January 26, 2006 final action, and BPA's December 8, 2005 action was simply a part of the process that led to BPA's final action, \*679 we have statutory jurisdiction over both NEDC's and Yakama's petitions for review.

### B

[3] [4] BPA next argues that we lack Article III jurisdiction over these petitions for review. To have constitutional standing to challenge BPA's action, the petitioners must satisfy a familiar three-part test established by the Supreme Court. First, the petitioners must have suffered an "injury in fact" which is (a) concrete and particularized and (b) actual or imminent. *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560, 112 S.Ct. 2130, 119 L.Ed.2d 351 (1992). Second, the petitioners must show a causal connection between the injury and the conduct complained of. *Id.* Finally, "it must be likely, as opposed to merely speculative, that the injury will be redressed by a favorable decision." *Id.* at 561, 112 S.Ct. 2130 (internal quotations omitted). BPA argues that the petitioners have failed to satisfy the final element of the test, claiming that the remedy that the petitioners seek is beyond our authority.

The petitioners ask that we set aside BPA's final action transferring the functions of the FPC to Pacific States and Battelle and order BPA to continue the FPC's funding until it can reconsider, in accordance with any opinion of this court, its decision to transfer the functions of the FPC. BPA contends that we have no authority to order BPA to fund the FPC, making it impossible for us to redress any injury suffered by the petitioners and leaving the petitioners without standing. BPA points out that it funded the FPC through an annual grant that expired and was renewed every year. BPA argues that to order it to continue to fund the FPC requires us to force BPA to

contract against its will, an action beyond the authority of the judiciary.

[5] [6] The cases BPA relies on are cases stating the unremarkable proposition of contract law that a court will not create new obligations that do not exist within the four corners of a contract. *See Imperial Fire Ins. Co. of London v. Coos County*, 151 U.S. 452, 462, 14 S.Ct. 379, 38 L.Ed. 231 (1894) (rejecting jury instructions contrary to the unambiguous language of an insurance policy); *City of New Orleans v. New Orleans Waterworks Co.*, 142 U.S. 79, 91, 12 S.Ct. 142, 35 L.Ed. 943 (1891) (refusing to construe a decision of the Louisiana Supreme Court as creating a new contract between the parties); *Jaeger v. Canadian Bank of Commerce*, 327 F.2d 743, 745 (9th Cir.1964) (stating that courts have no power to make new contracts); *Peterson v. Noots*, 255 F. 875, 880 (9th Cir.1919) (refusing to read additional provision into a liquidated damages clause where the liquidated damages clause was unambiguous). In a contract case between two private parties, our remedial power is no doubt limited to enforcing the obligations to which the private parties agreed. *See* 25 Richard A. Lord, *Williston on Contracts* § 67:30 (4th ed.2006) (stating that a court, in granting equitable relief “is curtailed to the extent that it must generally act within the framework of the contract”).

[7] This case presents a different situation. Rather than asking us to remedy a violation of private law (e.g., a breach of contract), the petitioners ask us to remedy the violation of a public law—the Administrative Procedure Act (“APA”)<sup>9</sup>—by contending \*680 that BPA acted arbitrarily, capriciously, and contrary to law in transferring the functions of the FPC. *See* 5 U.S.C. § 706(2)(A); *see also* 16 U.S.C. § 839(f)(e)(2) (directing that courts review final actions of BPA under the APA). When a public law has been violated, we are not bound to stay within the terms of a private agreement negotiated by the parties, and may exercise our equitable powers to ensure compliance with the law. *See Nat'l Wildlife Fed'n v. Espy*, 45 F.3d 1337, 1343 (9th Cir.1995) (“The court's decision to grant or deny injunctive or declaratory relief under[the] APA is controlled by principles of equity.”).

[8] [9] Moreover, “[w]here the public interest is involved, ‘equitable powers assume an even broader and more flexible character than when only a private controversy is at stake.’” *United States v. Alisal Water Corp.*, 431 F.3d 643, 654 (9th Cir.2005) (quoting *Porter v.*

*Warner Holding Co.*, 328 U.S. 395, 398, 66 S.Ct. 1086, 90 L.Ed. 1332 (1946)). Unless Congress provides otherwise, “[c]ourts of equity may, and frequently do, go much farther both to give and withhold relief in furtherance of the public interest than they are accustomed to go when only private interests are involved.” *United States v. Coca-Cola Bottling Co. of L.A.*, 575 F.2d 222, 228 (9th Cir.1978) (quoting *United States v. First Nat'l City Bank*, 379 U.S. 378, 383, 85 S.Ct. 528, 13 L.Ed.2d 365 (1965)).

For example, in *FTC v. H.N. Singer, Inc.*, 668 F.2d 1107, 1109 (9th Cir.1982), the FTC sought a permanent injunction under the Federal Trade Commission Act. In comparing the scope of the equitable powers of federal courts in private law matters versus public law matters, we wrote:

“Unless otherwise provided by statute, all the inherent equitable powers of the District Court are available for the proper and complete exercise of [its] jurisdiction. And since the public interest is involved in a proceeding of this nature, those equitable powers assume an even broader and more flexible character than when only a private controversy is at stake. Power is thereby resident in the District Court, in exercising [its] jurisdiction, to do equity and to mould each decree to the necessities of the particular case.”

*Id.* at 1112 (quoting *Porter*, 328 U.S. at 398, 66 S.Ct. 1086) (citation and internal quotation omitted). We concluded that, in the absence of congressional directive, federal courts retain broad equitable powers in public law matters, including the “authority to grant any ancillary relief necessary to accomplish complete justice.” *Id.* at 1113. We thus affirmed the district court's injunction freezing the assets of certain defendants. *Id.*

[10] *Section 706(2) of the APA gives us the equitable power to “set aside” BPA's action transferring the functions of the FPC, if we determine that BPA's action was arbitrary, capricious, or contrary to law. See 5 U.S.C. § 706(2)(A); Tinoqui-Chalola Council of Kitanemuk & Yowlumne Tejon Indians v. U.S. Dep't of Energy*, 232 F.3d 1300, 1305 (9th Cir.2000) (holding that, under the APA, a

court has authority to order rescission of a contract for sale if the federal agency “acted in excess of statutory authority or without observance of the procedures required by law”). As shown by our prior order mandating that BPA continue to fund the FPC until we rule on the merits of the petitions for review, this court, as a court of equity conducting judicial review under the APA, has broad powers to order “mandatory \*681 affirmative relief.” <sup>10</sup> *Adams v. Witmer*, 271 F.2d 29, 38 (9th Cir.1958), if such relief is “necessary to accomplish complete justice.” *H.N. Singer, Inc.*, 668 F.2d at 1113. Stated another way, if we conclude that BPA violated the APA by acting arbitrarily, capriciously, or contrary to law, we have the ability and indeed the juristic duty to remedy BPA’s violation. Viewed in this light, we are confident that we retain the power to require BPA to fund the FPC, at least for a period of time in which BPA can reconsider its action in accordance with our opinion. Because we have the power to redress the injury suffered by the petitioners if they prevail on their legal theory, we hold that, under *Lujan*, the petitioners have standing to pursue their petitions for review.

### III

As we discussed above, the Northwest Power Act dictates that our review of BPA’s final agency action is governed by § 706 of the APA, 5 U.S.C. § 706, 16 U.S.C. § 839f(e)(2). Under the APA, we must set aside BPA’s action if it was “arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.” 5 U.S.C. § 706(2)(A); see *NRIC*, 35 F.3d at 1383. The petitioners contend that BPA violated the APA in two ways. First, the petitioners contend that BPA acted “not in accordance with law” by transferring the functions of the FPC based on its belief that language in a committee report had a binding legal effect on the agency. Second, the petitioners argue that BPA acted arbitrarily and capriciously because it did not employ a rational decision-making process in deciding to transfer the functions of the FPC to Pacific States and Battelle. We address those arguments in turn.

#### A

The petitioners first contend that BPA’s decision to transfer the functions of the FPC was “not in accordance with law,” 5 U.S.C. § 706(2), because BPA gave legally-binding effect to a passage of legislative history. BPA

counters by asserting that it engaged in the rational decision-making process that the APA requires by observing the language contained in the congressional committee reports regarding the 2006 Appropriations Act and implementing the directives in the reports.

1

Though the text of the 2006 Appropriations Act itself made no reference to the FPC, its accompanying conference committee report stated that “[t]he Bonneville Power Administration may make no new obligations in support of the Fish Passage Center.” H.R.Rep. No. 109–275, at 174 (2005) (Conf.Rep.). The committee report language also instructed BPA and the Council “to ensure an orderly transfer of the Fish Passage Center functions ... within 120 days of enactment of this legislation.” *Id.* The report issued by the Senate Appropriations Subcommittee on Energy and Water Development on House Resolution 2419, the resolution that would become the 2006 Appropriations Act, contained similar language, indicating that \*682 BPA “may make no new obligations from the Bonneville Power Administration Fund in support of the Fish Passage Center.” S.Rep. No. 109–84, at 179 (2005).

It is an understatement to say that BPA gave great weight to these reports; more accurate is the observation that BPA slavishly deferred to what it thought the reports commanded. As one example, BPA’s Program Solicitation states that “[i]n November 2005, the U.S. Congress passed legislation (House Report 109–275), which forbids BPA from making additional obligations in support of the Fish Passage Center.” A September 20, 2005 email written by a Vice President of BPA, Gregory K. Delwiche, also reflects BPA’s view of the importance of the Senate subcommittee report. Michelle DeHart, Manager of the FPC, had asked Delwiche his thoughts on the future of the FPC. After Delwiche responded that he would have to wait and see “how this is playing out in our nation’s capitol [sic],” DeHart replied, “I was really not thinking about talking about the language [in the subcommittee report] but in getting an idea from you as to what your thinking was on the Fish Passage Center in the future.” Delwiche responded:

“[T]he reason the language is important is that what my thinking

is on the Fish Passage Center really isn't relevant, what's relevant is what the direction from Wash DC [sic] is. We are merely the implementer of guidance from back there."

Delwiche again indicated his belief that BPA had no choice but to follow the committee report language in a declaration filed in our court, characterizing the language in the committee reports as "unambiguous Congressional direction." Delwiche explained BPA's decision to transfer the FPC by stating that "I did not think that, as an Executive Branch agency, accountable to Congress, BPA could ignore this unambiguous Congressional direction." Finally, in BPA's brief, BPA states that it interpreted the conference committee report as "the unambiguously expressed will of the Congress."

[11] In summary, BPA treated the committee report language as if the language placed a legal obligation on BPA to transfer the functions of the FPC. However, as we explain in the next section, committee report language unconnected to the text of an enacted statute has no binding legal import, and it was contrary to law for BPA to base its decision to transfer the FPC on its belief that "the U.S. Congress passed legislation (House Report 109–275) ... forbid[ding] BPA from making additional obligations in support of the Fish Passage Center."

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[12] [13] The APA empowers us to set aside an agency decision that is contrary to governing law. 5 U.S.C. § 706(2); see *Lands Council v. Powell*, 395 F.3d 1019, 1026 (9th Cir.2005). The case law of the Supreme Court and our court establishes that legislative history, untethered to text in an enacted statute, has no compulsive legal effect. It was thus contrary to law for BPA to conclude, from committee report language alone, that it was bound to transfer the functions of the FPC.

In *Shannon v. United States*, 512 U.S. 573, 579, 114 S.Ct. 2419, 129 L.Ed.2d 459 (1994), the petitioner, a criminal defendant, argued that the district court erred by failing to instruct the jury about the consequences of finding him not guilty by reason of insanity. The petitioner argued that Congress, in enacting the Insanity Defense Reform Act of 1984 ("IDRA"), intended to require that district

courts instruct the jury as to the consequences of \*683 an insanity acquittal. *Id.* at 583, 114 S.Ct. 2419. The text of IDRA was silent on the matter. *Id.* at 580, 114 S.Ct. 2419; see 18 U.S.C. § 4242(b) (stating that "the jury shall be instructed to find ... the defendant—(1) guilty; (2) not guilty; or (3) not guilty only by reason of insanity"). In support of his argument that IDRA required the district court to instruct the jury about the consequences of an insanity acquittal, the petitioner in *Shannon* pointed to language in the Senate Report on IDRA, which stated that "[t]he Committee endorses the procedure used in the District of Columbia whereby the jury, in a case in which the insanity defense has been raised, may be instructed on the effect of a verdict of not guilty by reason of insanity." *Shannon*, 512 U.S. at 583, 114 S.Ct. 2419 (internal quotation omitted).

[14] The United States Supreme Court refused to give weight to this passage of legislative history unattached to the text of IDRA: "We are not aware of any case ... in which we have given authoritative weight to a single passage of legislative history that is in no way anchored in the text of the statute." *Id.* The Court emphasized that the passage of legislative history Shannon identified "[did] not purport to explain or interpret any provision of the IDRA." *Id.* The Court concluded by stating that "'courts have no authority to enforce [a] principl[e] gleaned solely from legislative history that has no statutory reference point.'" *Id.* at 584, 114 S.Ct. 2419 (alterations in original) (quoting *Int'l Bhd. of Elec. Workers, Local Union No. 474 v. NLRB*, 814 F.2d 697, 712 (D.C.Cir.1987)); see also *Abrego v. Dow Chem. Co.*, 443 F.3d 676, 686 (9th Cir.2006) (per curiam) (holding that statutory silence, "coupled with a sentence in a legislative committee report untethered to any statutory language," did not bring about a change in governing law). The Supreme Court thus made clear that principles in legislative history that have no statutory reference point and do not purport to explain any part of an enacted law do not carry the force of law. As such, they do not bind *anyone*—administrative agencies included.

[15] [16] [17] *Shannon* is not the only case illustrating that it is contrary to law for an agency to conclude that it is legally bound by language in a congressional committee report. In *Cherokee Nation of Oklahoma v. Leavitt*, 543 U.S. 631, 646, 125 S.Ct. 1172, 161 L.Ed.2d 66 (2005), the Secretary of Health and Human Services argued that unambiguous statutory language, when paired with conflicting legislative history, rendered

a statute ambiguous. The Court held that the statute was not ambiguous, stating that “[t]he relevant case law makes clear that restrictive language contained in Committee Reports is not legally binding.” *Id.* at 646, 125 S.Ct. 1172 (citing *Lincoln v. Vigil*, 508 U.S. 182, 192, 113 S.Ct. 2024, 124 L.Ed.2d 101 (1993); *UAW v. Donovan*, 746 F.2d 855, 860–61 (D.C.Cir.1984) (Scalia, J.); *Blackhawk Heating & Plumbing Co. v. United States*, 224 Ct.Cl. 111, 622 F.2d 539, 552 & n. 9 (1980)); *see also Lincoln*, 508 U.S. at 192, 113 S.Ct. 2024 (“[I]ndicia in committee reports and other legislative history as to how ... funds should or are expected to be spent do not establish any legal requirements on [an] agency.” (internal quotation omitted)).<sup>11</sup>

\*684 [18] The principle that committee report language has no binding legal effect is grounded in the text of the Constitution and in the structure of separated powers the Constitution created. Article I, section 7, clause 2 of the Constitution is explicit about the manner in which Congress can take legally binding action.<sup>12</sup> Members of Congress cannot use committee report language to make an end run around the requirements of Article I. If Congress wishes to alter the legal duties of persons outside the legislative branch, including administrative agencies, it must use the process outlined in Article I. *See INS v. Chadha*, 462 U.S. 919, 952, 103 S.Ct. 2764, 77 L.Ed.2d 317 (1983); *see also Clinton v. City of New York*, 524 U.S. 417, 439–40, 118 S.Ct. 2091, 141 L.Ed.2d 393 (1998) (holding that “the power to enact statutes may only be exercised in accord with a single, finely wrought and exhaustively considered, procedure” outlined in Article I (internal quotation omitted)). BPA acted contrary to law by treating committee report language—language that was not subjected to the bicameralism and presentment requirements of Article I—as imposing upon BPA a legal duty to transfer the functions of the FPC. Because the committee reports in this case were not subject to the “finely wrought” process in Article I, BPA erred by giving the reports binding effect.

Treating legislative reports as binding law also undermines our constitutional structure of separated powers, because legislative reports do not come with the traditional and constitutionally-mandated political safeguards of legislation. As noted above, legislative reports are not acts of law satisfying the precise requirements of Article I, which were devised by the Framers to ensure separation of powers and a careful

legislative process. By contrast, legislative reports may in some cases be written by an individual legislator, congressional staffers, or even lobbyists.<sup>13</sup> \*685 Giving binding effect to passages in legislative reports may thus give binding legal effect to the unchecked will of a lone person, and that is not what our Constitution envisions.

The statements of BPA Vice President Delwiche illustrate how BPA's reliance on legislative history undermined separation of powers in this case. Delwiche said that BPA, the agency he led, was “an Executive Branch agency, accountable to Congress.” It is certainly true that Congress through legislation may direct how BPA shall operate. But an executive branch agency which views itself as subservient to a sentence in a legislative report undermines the distribution of authority in our federal government in which every exercise of political power is checked and balanced.

BPA's treatment of legislative history as binding law also frustrated the statutory design of the Northwest Power Act. Rather than adhering to the Act's carefully-tailored requirement that BPA take actions consistent with the guidance provided by the Plan and Program crafted by the Council as well as the purposes of the Act, BPA simply gave conclusive weight to what might have been the view of a lone legislator, staffer, or lobbyist. That the Council, and guidance from it, derives from political and expert representatives from four Pacific Northwest states, affected Indian tribes, and groups with interest in fisheries only intensifies BPA's error in relying so heavily on congressional report statements that might have been penned by a single legislator or single lobbyist, and that do not satisfy Article I's requirements and do not have force of law. The Act contemplates a participatory process in which the varied constituencies of the Pacific Northwest advise BPA on how it should exercise its discretion. By following congressional committee report language as if it were mandatory law, BPA ignored the opinions of those individuals and groups directly affected by its policy choices and circumvented the unique structure of cooperative federalism created by the Act.

Delwiche incorrectly believed that the dominant factors in his decision about the continued operation of the FPC were statements in legislative history, untied to the legislative commands of Congress, when, to the contrary, his agency's organic statute, the Northwest Power Act, states that one of its purposes is to allow

the States, local governments, and citizens of the Pacific Northwest (including fish and wildlife agencies and Indian tribes) to participate in the development of regional energy conservation plans, plans for renewable resources, and plans for environmental \*686 protection and enhancement. 16 U.S.C. § 839(3).<sup>14</sup>

The Act also requires BPA to exercise its authority in a manner consistent with the Council's Fish and Wildlife Program, *see id.* § 839b(h)(10)(A), the most recent version of which called for the continued operation of the FPC. Indeed, the Act makes no secret that BPA's actions "shall be consistent with the [Council's Fish and Wildlife] plan and any amendment thereto," *id.* § 839b(d)(2), as the Act recites the consistency requirement numerous times, *see id.* §§ 839b(h), 839c(d)(3), 839d(b)-(c). Possibly, BPA could exercise some discretion to depart from its prior practice of funding the FPC in accordance with the Council's Fish and Wildlife Program, if such a departure was necessary for BPA to comply with its statutory obligation to use its authority in a manner consistent with the Council's Power Plan or purposes of the Act. But no nice question of balancing potentially conflicting obligations is presented when BPA adopts a slavish adherence to a sentence in a legislative committee report.

[19] We may only sustain an agency's action on the grounds actually considered by the agency. As the Supreme Court explained in *SEC v. Chenery Corp.*, 318 U.S. 80, 95, 63 S.Ct. 454, 87 L.Ed. 626 (1943), "an administrative order cannot be upheld unless the grounds upon which the agency acted in exercising its powers were those upon which its action can be sustained." In other words, the APA obliges us to set BPA's action aside unless the record demonstrates that, because BPA considered some other basis for its action, BPA's decision to transfer the functions of the FPC was not arbitrary, capricious, or contrary to law. *See SEC v. Chenery Corp.*, 332 U.S. 194, 196, 67 S.Ct. 1575, 91 L.Ed. 1995 (1947) ("[A] reviewing court, in dealing with a determination or judgment which an administrative agency alone is authorized to make, must judge the propriety of such action solely by the grounds invoked by the agency. If those grounds are inadequate or improper, the court is powerless to affirm the administrative action by substituting what it considers to be a more adequate or proper basis.").

B

BPA argues that, even if language in the congressional committee reports did not provide a rational basis for its action transferring the functions of the FPC, its decision can be upheld as a reasonable application of the Act's requirement that it exercise its authority in a manner consistent with the Council's Fish and Wildlife Program. BPA contends that it carefully considered the issues before it and therefore we should let stand its decision to transfer the functions of the FPC. The petitioners contend, by contrast, that BPA never considered the consistency provision of the Act in deciding to transfer the functions of the FPC and insufficiently analyzed the issues before it. Thus, petitioners urge that BPA acted arbitrarily and capriciously.

1

[20] Before further evaluating BPA's decision to transfer the functions of the \*687 FPC to Pacific States and Battelle, we outline the principles governing the scope of our review under the arbitrary and capricious standard of § 706(2) of the APA. The Supreme Court has explained:

The scope of review under the "arbitrary and capricious" standard is narrow and a court is not to substitute its judgment for that of the agency. Nevertheless, the agency must examine the relevant data and articulate a satisfactory explanation for its action including a "rational connection between the facts found and the choice made."

*Motor Vehicle Mfgs. Ass'n v. State Farm Mutual Auto. Ins. Co.*, 463 U.S. 29, 43, 103 S.Ct. 2856, 77 L.Ed.2d 443 (1983) (quoting *Burlington Truck Lines v. United States*, 371 U.S. 156, 168, 83 S.Ct. 239, 9 L.Ed.2d 207 (1962)); *see Natural Res. Def. Council v. U.S. Forest Serv.*, 421 F.3d 797, 806 (9th Cir.2005). That is, an agency must "cogently explain why it has exercised its discretion in a given manner," and "[i]n reviewing that explanation, we must 'consider whether the decision was based on a consideration of the relevant factors and whether there has been a clear error of judgment.'" *State Farm*, 463 U.S. at 43, 48, 103 S.Ct. 2856 (quoting *Bowman Transp., Inc. v. Ark.-Best Freight Sys.*, 419 U.S. 281, 285, 95 S.Ct. 438, 42 L.Ed.2d 447 (1974)).

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[21] An agency decision is arbitrary and capricious “if the agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise.” *State Farm*, 463 U.S. at 43, 103 S.Ct. 2856.<sup>15</sup>

[22] In this case, BPA departed from its long-standing practice of funding a unitary Fish Passage Center and transferred the FPC's functions to two separate entities. An agency is entitled to change its course when its view of what is in the public's interest changes. However, “an agency changing its course must supply a reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored, and if an agency glosses over or swerves from prior precedents without discussion it may cross the line from the tolerably terse to the \*688 intolerably mute.” *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C.Cir.1970) (footnotes omitted), *quoted in State Farm*, 463 U.S. at 57, 103 S.Ct. 2856; *see also Atchison, Topeka & Santa Fe Ry. v. Wichita Bd. of Trade*, 412 U.S. 800, 808, 93 S.Ct. 2367, 37 L.Ed.2d 350 (1973) (plurality opinion) (“Whatever the ground for the [agency's] departure from prior norms, ... it must be clearly set forth so that the reviewing court may understand the basis of the agency's action and so may judge the consistency of that action with the agency's mandate.”); *W. States Petroleum Ass'n v. EPA*, 87 F.3d 280, 284 (9th Cir.1996) (stating that an agency “must clearly set forth the ground for its departure from prior norms”).

[23] Moreover, in reviewing BPA's action, we must look to BPA's reasoning in making its decision to transfer the functions of the FPC, and not to other reasons for its decision that BPA might marshal before us. As the Supreme Court has explained, we “may not accept appellate counsel's post hoc rationalizations for agency action,” *Burlington Truck Lines*, 371 U.S. at 168, 83 S.Ct. 239, and we “may not supply a reasoned basis for the agency's action that the agency itself has not given.” *Bowman Transp., Inc.*, 419 U.S. at 285–86, 95 S.Ct. 438 (citing *Chenery*, 332 U.S. at 196, 67 S.Ct. 1575).<sup>16</sup>

[24] In arguing that it sufficiently assessed the issues before it, BPA defends its decision as the outcome of “a public process within the confines of the 120–day transition period set by Congress.” However, the administrative record does not show that BPA, as required by *State Farm*, considered the relevant facts and used a rational process to decide to transfer the functions of the FPC to other entities. Apart from the evidence in the record reflecting BPA's incorrect belief that it was required to follow the congressional committee report language, there is no evidence showing how BPA decided to transfer the functions of the FPC and to issue the December 8, 2005 Program Solicitation. This failure presents itself in high relief in light of the Council's program calling for the continued operation of the FPC. So far as the record is concerned, we have no explanation for why BPA would abandon the FPC in the face of its inclusion in the Council's Program, beyond the mistaken belief of BPA that statements in legislative reports were mandatory and foreclosed the continued funding of the FPC.

As evidence of the decision-making process BPA used to decide to award the contract for the functions formerly performed by the FPC to Pacific States and Battelle, BPA points to a PowerPoint slide from a presentation dated January 26, 2006, the same day BPA issued a press release announcing that it decided to transfer the FPC's functions to Pacific States and Battelle. In the slide BPA \*689 prepared, each bidder received an “X” for each of eight specified tasks<sup>17</sup> BPA determined the bidder could satisfactorily perform. In other words, a bidder who BPA concluded could perform all eight tasks satisfactorily would receive eight Xs, a bidder who could perform four of the eight tasks satisfactorily would receive four Xs, and so on. But there is no evidence in the record of how BPA determined whether a bidder would get an X or be left blank for each specified task. And even if the PowerPoint presentation did contain evidence of a rational decision-making process, it is uncertain whether BPA actually relied on that process in making its decision to transfer the functions of the FPC to Pacific States and Battelle because the PowerPoint slide was prepared on January 26, 2006, the very same day BPA announced it decided to award Pacific States and Battelle the contracts to perform the functions formerly performed by the FPC.

As further purported evidence of the process which led BPA to decide to transfer the functions of the FPC to Pacific States and Battelle, BPA presents a memorandum

comparing the functions of the FPC with the functions of the new model. However, the memorandum giving this comparison was drafted on March 13, 2006, a month and a half after BPA awarded the contracts for the functions formerly performed by the FPC to two other entities. BPA thus could not have relied on this memorandum in deciding to transfer the functions of the FPC and in awarding the contracts to Pacific States and Battelle.

BPA also indicated, in a letter to the Yakama tribe and a similar letter to five members of the Pacific Northwest's congressional delegation, that it believed the Program Solicitation complied with its duty, under the Act, to "mitigate the impact on salmon and steelhead in a manner consistent with the Program." But again, the letter does not reflect any rational decision-making process that BPA relied upon to conclude that transferring the functions of the FPC was in accord with its statutory duty to use its authority in a manner consistent with the Council's Fish and Wildlife Program.

In *Confederated Tribes*, 342 F.3d at 933, we held that BPA provided a reasoned explanation for its decision that implementing certain biological opinions was consistent with BPA's statutory mandate to treat fish and wildlife equitably with power because the record elaborated BPA programs, decisions, and opinions reflecting how BPA gave equitable treatment to fish and wildlife. By contrast, in this case, the only reference in the administrative record to the Act's consistency requirement is the letter from BPA to Yakama and the similar letter from BPA to five members of the Pacific Northwest's congressional delegation baldly asserting that BPA is transferring the functions of the FPC to comply with its statutory mandate to protect fish and wildlife consistent with the Program. But the record does not show the process, if there was one, that BPA used to determine that its decision to transfer the functions of the FPC was consistent with BPA's statutory mandate to use its authority in a manner consistent with the Council's Fish and Wildlife Program. Because the 2003 Amendments to the Council's Program describe the functions \*690 the FPC should perform, BPA's record of decision should have shown reasons for its decision to transfer the FPC's functions elsewhere and how this would be consistent with the Council's Fish and Wildlife Program.

This case is more similar to *State Farm* than it is to *Confederated Tribes*. In *State Farm*, the Supreme

Court held that the National Highway Traffic Safety Administration's ("NHTSA") decision to rescind a rule requiring automobile manufacturers to include passive restraints in their cars was arbitrary and capricious because the NHTSA provided "no findings and no analysis here to justify the choice made, no indication of the basis on which the [agency] exercised its expert discretion." *State Farm*, 463 U.S. at 48, 103 S.Ct. 2856 (alteration in original) (quoting *Burlington Truck Lines*, 371 U.S. at 167, 83 S.Ct. 239). Just as the NHTSA had the authority to use its discretion to rescind the passive restraint rule in *State Farm*, so too BPA possibly may have the ability rationally to conclude that the continued operation of the FPC in its present state was no longer in the public interest, after giving due weight to the Act's requirement that its actions be consistent with what the Council said in the Program and Plan, and the purposes of the Northwest Power Act. "But an agency changing its course must supply a reasoned analysis...." *Id.* at 57, 103 S.Ct. 2856 (internal quotation omitted). BPA has not cogently explained its decision to transfer the functions of the FPC, and the record does not indicate that that decision was the output of a rational decision-making process. Instead, BPA departed from its two-decade-old precedent without supplying a reasoned analysis for its change of course.<sup>18</sup> BPA's decision to transfer the functions of the FPC was arbitrary and capricious.<sup>19</sup>

#### \*691 IV

The United States Supreme Court has declared that we must require that an agency "cogently explain why it has exercised its discretion in a given manner." *State Farm*, 463 U.S. at 48, 103 S.Ct. 2856. The only explanation shown in BPA's record for why it transferred the functions of the FPC was that it was responding to congressional committee report language that BPA believed created a binding obligation on it. That is not a cogent explanation because BPA acted contrary to law in concluding that congressional committee report language carried the force of law and bound BPA to transfer the functions of the FPC. Because BPA has not shown a rational basis for its decision to transfer the functions of the FPC to Pacific States and Battelle, we grant the petition for review. We hold that BPA's decision to transfer the functions of the FPC to Pacific States and Battelle was arbitrary, capricious, and contrary to law. We set aside BPA's decision to transfer the functions of the FPC to Pacific

States and Battelle and order that BPA continue its existing contractual arrangement to fund and support the FPC unless and until it has established a proper basis for displacing the FPC.

#### All Citations

477 F.3d 668, 07 Cal. Daily Op. Serv. 858, 2007 Daily Journal D.A.R. 1109

#### PETITION FOR REVIEW GRANTED.

#### Footnotes

- 1 A steelhead is a rainbow trout which has spent part of its life at sea. Alaska Dep't of Fish & Game, *Steelhead Trout*, <http://www.adfg.state.ak.us/pubs/notebook/fish/steelhd.php> (last visited Jan. 17, 2007).
- 2 For a landmark discussion of the use of the Compact Clause, article I, section 10, clause 3 of the Constitution, to permit agreements by states on a regional basis, including the need to do so to promote sound development of electrical power and conservation of natural resources, see Felix Frankfurter & James M. Landis, *The Compact Clause of the Constitution—A Study In Interstate Adjustments*, 34 Yale L.J. 685 (1925).
- 3 For biographical information on the Council's current members, see Council Members, <http://www.nwcouncil.org/contact/members.asp> (last visited Jan. 17, 2007).
- 4 In 16 U.S.C. § 839, Congress listed the purposes of the Act: (1) to encourage electricity conservation and the development of renewable resources in the Pacific Northwest; (2) "to assure the Pacific Northwest of an adequate, efficient, economical, and reliable power supply"; (3) to allow the States, local governments, and citizens of the Pacific Northwest (including fish and wildlife agencies and Indian tribes) to participate in the development of regional energy conservation plans, plans for renewable resources, and plans for environmental protection and enhancement; (4) to ensure that BPA's customers cover the costs necessary to meet the region's electricity needs; (5) to ensure that non-federal entities continue to regulate, plan, conserve, supply, and distribute electricity; and (6) "to protect, mitigate and enhance the fish and wildlife ... of the Columbia River and its tributaries."
- 5 A smolt is a juvenile salmon in the stage where it becomes covered with silvery scales and first embarks on its journey to salt water. See John V. Byrne, *Salmon Is King—Or Is It?*, 16 *Env'tl. L.* 343, 352–53 (1986).
- 6 An anadromous fish lives in the sea but breeds in freshwater. See 50 C.F.R. § 401.2(g) (defining anadromous fish as "[a]quatic, gill breathing, vertebrate animals bearing paired fins which migrate to and spawn in fresh water, but which spend part of their life in an oceanic environment"); see also Convention for the Conservation of Anadromous Stocks of the North Pacific Ocean, art. II.1, annex pt. I, Feb. 11, 1992, T.I.A.S. No. 11,465 (classifying the following species as anadromous fish: chum salmon, coho salmon, pink salmon, sockeye salmon, chinook salmon, cherry salmon, and steelhead trout); 16 U.S.C. §§ 5001–12 (implementing the Convention).
- 7 Fish migrating down the stream of a dammed river encounter a series of dangers. The fish must navigate the reservoir of standing water maintained behind the dam. The standing water slows the migration of the fish and exposes the fish to predators. After navigating the reservoir, the fish must then pass the dam safely. Fish may pass a dam by being spilled over the dam, by passing through the turbines of the dam, or by being transported around the dam. See *Nat'l Wildlife Fed'n v. Nat'l Marine Fisheries Serv.*, 422 F.3d 782, 788–89 (9th Cir.2005). The data gathered by the FPC is used to measure the success that fish have passing dams.
- 8 Pacific States is the entity that now contracts with BPA to receive the grants that Pacific States in turn uses to fund the operations of the FPC. See *supra* at 677.
- 9 Public law is the body of law regulating relations between private parties and the government and regulating the structure and operation of the government itself. See *Black's Law Dictionary* 1267 (8th ed.2004). Public law consists of the fields of constitutional law, criminal law, and administrative law. *Id.*
- 10 In *Norton v. Southern Utah Wilderness Alliance*, 542 U.S. 55, 64, 124 S.Ct. 2373, 159 L.Ed.2d 137 (2004), the Supreme Court held that, when a party seeks redress because an agency has failed to act, a court may only require the agency to perform non-discretionary actions that the agency is required by law to undertake. *Norton* is distinguishable from the instant case because *Norton* dealt with the power of courts to "compel agency action unlawfully withheld" under 5 U.S.C. § 706(1). The petitioners here do not seek redress for agency inaction under § 706(1), but rather challenge a final agency action under the § 706(2) and the Northwest Power Act.
- 11 The utility of legislative history stands on a different footing when it is tied directly to statutory language and that language is ambiguous. In such a case, the legislative history may permissibly inform judgment about interpreting ambiguous

statutory terms. For example, in *Northwest Forest Resource Council v. Glickman*, we stated, “a congressional conference report is recognized as the most reliable evidence of congressional intent because it ‘represents the final statement of the terms agreed to by both houses.’ ” 82 F.3d 825, 835 (9th Cir.1996) (quoting *Dept of Health & Welfare v. Block*, 784 F.2d 895, 901 (9th Cir.1986)). However, in that case, the statutory language was not silent on the relevant issue. See *id.* Here, by contrast, the passage of legislative history in question is unrelated to any provision of the statute that Congress has enacted. When legislative history is not tied to any statutory text, we properly should give it no weight. See *Abrego*, 443 F.3d at 683 (“[C]onsideration of legislative history is appropriate where statutory language is ambiguous. Ambiguity, however, is at least a necessary condition. In this instance, the statute is not ambiguous. Instead, it is entirely silent as to the burden of proof on removal.” (citations omitted))

12 Article I, section 7, clause 2 of the United States Constitution provides:

Every bill which shall have passed the House of Representatives and the Senate shall, before it become a law, be presented to the President of the United States; if he approve; he shall sign it; but if not, he shall return it, with his objections, to that House in which it shall have originated, who shall enter the objections at large on their journal, and proceed to reconsider it. If after such reconsideration two thirds of that House shall agree to pass the bill, it shall be sent, together with the objections, to the other House, by which it shall likewise be reconsidered, and if approved by two thirds of that House, it shall become a law. But in all such cases the votes of both Houses shall be determined by yeas and nays, and the names of the persons voting for and against the bill shall be entered on the journal of each House respectively. If any bill shall not be returned by the President within ten days (Sundays excepted) after it shall have been presented to him, the same shall be a law in like manner as if he had signed it, unless the Congress by their adjournment prevent its return, in which case it shall not be a law.

13 The Supreme Court has cautioned:

[L]egislative materials like committee reports, which are not themselves subject to the requirements of Article I, may give unrepresentative committee members—or, worse yet, unelected staffers and lobbyists—both the power and the incentive to attempt strategic manipulations of legislative history to secure results they were unable to achieve through the statutory text.

*Exxon Mobil Corp. v. Allapattah Servs., Inc.*, 545 U.S. 546, —, 125 S.Ct. 2611, 2626, 162 L.Ed.2d 502 (2005).

Judge Kozinski has likewise observed:

Reports are usually written by staff or lobbyists, not legislators; few if any legislators read the reports; they are not voted on by the committee whose views they supposedly represent, much less by the full Senate or House of Representatives; they cannot be amended or modified on the floor by legislators who may disagree with the views expressed therein.

*Wallace v. Christensen*, 802 F.2d 1539, 1560 (9th Cir.1986) (en banc) (Kozinski, J., concurring).

Committee reports often contain “what some committee members wanted in the bill, but did not get,” and are often written before the bill is drafted, *Puerta v. United States*, 121 F.3d 1338, 1344 (9th Cir.1997), or after a bill is passed, *Lao v. Wickes Furniture Co., Inc.*, 455 F.Supp.2d 1045, 1051 (C.D.Cal.2006) (refusing to give weight to committee report issued ten days after the passage of a law).

14 In *NRIC*, 35 F.3d at 1388, we recognized that the Council must give “due weight” to views of fishery managers, state and federal wildlife agencies, and Indian tribes in formulating the Fish and Wildlife Program. See 16 U.S.C. § 839b(h)(7). It follows with stronger logic that when the final Fish and Wildlife Program, the product of a collaborative process, calls for the continued operation of the FPC, BPA cannot then disregard the Council’s view without giving the Council’s view due weight. The Northwest Power Act requires BPA to act in a manner *consistent* with the Fish and Wildlife Program. *Id.* § 839b(h)(10)(A).

15 “Some courts have held that agency action is arbitrary and capricious if ‘the agency has not really taken a “hard look” at the salient problems and has not genuinely engaged in reasoned decision-making.’ ” *Riverbend Farms, Inc. v. Madigan*, 958 F.2d 1479, 1488 (9th Cir.1992) (quoting *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 851 (D.C.Cir.1970)). Accordingly, some commentators have suggested that our task in reviewing agency action under § 706(2) of the APA is to “look[ ] closely at whether the agency has taken a hard look at the question” before it, 33 Charles Alan Wright & Charles H. Koch, Jr., *Federal Practice and Procedure* § 8335 (2006) (emphasis omitted), though other commentators decline to adopt the “hard look” phraseology, see 2 Richard J. Pierce, Jr., *Administrative Law Treatise* § 11.4 (4th ed. 2002) (“In order to avoid judicial reversal of its action as arbitrary and capricious, an agency must engage in ‘reasoned decisionmaking,’ defined to include an explanation of how the agency proceeded from its findings to the action it has taken.”). Because the Supreme Court has never explicitly embraced the “hard look” approach to judicial review under the arbitrary and capricious standard of the APA, cf. *Indus. Union Dep’t, AFL–CIO v. Am. Petroleum Inst.*, 448 U.S. 607, 695

n. 9, 100 S.Ct. 2844, 65 L.Ed.2d 1010 (1980) (Marshall, J., dissenting) (stating that the arbitrary and capricious "inquiry is designed to require the agency to take a 'hard look' " at the issues before it), we adhere to the Supreme Court's explicit guidance in *State Farm* that an agency must cogently explain its actions and demonstrate a rational connection between the facts it found and the choice it made.

- 16 BPA argues that its interpretation of the Northwest Power Act and its decision to transfer the functions of the FPC are entitled to substantial deference under *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842–45, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984), *Aluminum Co. of America v. Central Lincoln Peoples' Utility District*, 467 U.S. 380, 389, 104 S.Ct. 2472, 81 L.Ed.2d 301 (1984), and their progeny in our court, see, e.g., *APAC*, 126 F.3d at 1164. Perhaps BPA might be entitled to deference in this case if it was actually interpreting the Act, one of its organic statutes. However, as we discuss in the next section, there is scant evidence in the record that BPA, in deciding to transfer the functions of the FPC, was interpreting the Act's provision that it exercise its authority in a manner consistent with the Council's Fish and Wildlife Program, see 16 U.S.C. § 839b(h)(10)(A), or was interpreting any other provision of the Act.
- 17 The specified tasks were: database management; routine analysis and reporting; coordination of the smolt monitoring program; miscellaneous additional technical tasks; expanded, non-routine analysis; independent technical review; policy oversight and guidance; and coordination with other contractors.
- 18 In its brief, BPA argues that it consulted with various fishery managers, one scientist, and the public in making its decision to transfer the functions of the FPC. BPA asserts that, in deciding which proposals to accept, it "consulted with tribal, state and federal fisheries managers"; "provided a forum in which to hold public discussion and debate on this issue"; "considered and largely followed the recommendations" of a group of Indian tribes and an association of fisheries; ensured that the Program Solicitation complied with the 2003 Amendments to the Fish and Wildlife Program; "followed the general principles from the U.S. National Academies scientific reporting process" in preparing the technical services agreement with the entities replacing the FPC; obtained "expert scientific review of the proposals" from the former executive director of the Columbia Basin Fish and Wildlife Authority; and "relied on the advice provided in letters from members of the Northwest congressional delegation, as well as the report language and the Program amendments." However, as we discussed, it does not appear from the record that BPA actually relied upon any of these rationales in deciding to transfer the functions of the FPC, and BPA may not justify its decision to our court based on these post-hoc rationalizations for its action. See *Burlington Truck Lines*, 371 U.S. at 168, 83 S.Ct. 239.
- 19 BPA argues that its decision to transfer the functions of the FPC complies with its substantive obligation to exercise its authority "in a manner consistent with the plan, ... the program adopted by the Council ..., and the purposes of [the Northwest Power Act]," 16 U.S.C. § 839b(h)(10)(A), even though the 2000 Program and the 2003 Amendments "call [ ] for the continued operation of the Fish Passage Center." 2003 Amendments, *supra*, at 27. Because we hold that BPA's decision to transfer the functions of the FPC was not the output of a reasoned decision-making process, as the APA requires, we need not determine whether, on a proper record with factual determinations and an adequate explanation of a rational connection between facts determined and action taken, a decision of BPA to transfer the functions of the FPC is consistent with the Council's Fish and Wildlife Program and with the Plan and the objectives of the Northwest Power Act.

305 Ga.App. 734

Court of Appeals of Georgia.

PARRIS PROPERTIES, LLC et al.

v.

NICHOLS et al. (two cases).

Nichols et al.

v.

Parris Properties, LLC et al.

Nos. A10A1029, A10A1030, A10A1031.

|  
Aug. 30, 2010.

|  
Certiorari Denied Feb. 7, 2011.

### Synopsis

**Background:** Landowners of servient estate brought action against adjacent landowner, which held dominant estate of underground sewer-line easement, to prevent it from replacing existing sewer pipe with a larger one. Dominant estate owner counterclaimed for conversion based upon disposal by servient estate owners of its construction materials. Following a jury trial in which jury found that the larger diameter pipe would not constitute a substantial change in the easement, the Clarke Superior Court, Sweat, J., entered judgment prohibiting dominant estate owners from making any permanent changes to surface of servient estate owners' property in replacing the pipe, and holding servient estate owners liable for conversion. Both parties appealed.

**Holdings:** The Court of Appeals, McMurray, Senior Appellate Judge, held that:

[1] easement unambiguously authorized replacement of sewer line;

[2] replacement of four-inch cement sewer pipe with six- or eight-inch polyvinyl chloride (PVC) sewer pipe would not be unilateral alteration of physical boundaries of easement;

[3] issue of whether replacement would constitute substantial change in manner, frequency, and intensity of use of easement was for jury;

[4] dominant owner had implied right to place surface structures on servient estate as required by city ordinance;

[5] servient owners exercised dominion and control over dominant owner's pipe fixtures as required for conversion; and

[6] remand was required to determine whether dominant owner or servient estate owners were prevailing parties.

Affirmed in part, reversed in part, vacated in part, and remanded with directions.

West Headnotes (28)

### [1] Appeal and Error

~ Extent of Review Dependent on Nature of Decision Appealed from

#### Appeal and Error

~ Appeal from ruling on motion to direct verdict

#### Appeal and Error

~ Effect of evidence and inferences therefrom on direction of verdict

#### Appeal and Error

~ Judgment

30 Appeal and Error

30XVI Review

30XVI(A) Scope, Standards, and Extent, in General

30k862 Extent of Review Dependent on Nature of Decision Appealed from

30k863 In general

30 Appeal and Error

30XVI Review

30XVI(A) Scope, Standards, and Extent, in General

30k862 Extent of Review Dependent on Nature of Decision Appealed from

30k866 On Appeal from Decision on Motion for Dismissal or Nonsuit or Direction of Verdict

30k866(3) Appeal from ruling on motion to direct verdict

30 Appeal and Error

30XVI Review

30XVI(G) Presumptions

## KC REPLY APPENDIX 62

30k927 Dismissal, Nonsuit, Demurrer to Evidence, or Direction of Verdict  
30k927(7) Effect of evidence and inferences therefrom on direction of verdict  
30 Appeal and Error  
30XVI Review  
30XVI(G) Presumptions  
30k934 Judgment  
30k934(1) In general

On appeal from the denial of a motion for a directed verdict or for judgment notwithstanding the verdict (JNOV), appellate courts construe the evidence in the light most favorable to the party opposing the motion, and the standard of review is whether there is any evidence to support the jury's verdict.

4 Cases that cite this headnote

**[2] Appeal and Error**

- - Cases Triable in Appellate Court

30 Appeal and Error  
30XVI Review  
30XVI(F) Trial De Novo  
30k892 Trial De Novo  
30k893 Cases Triable in Appellate Court  
30k893(1) In general

Construction, interpretation and legal effect of a contract such as an easement is an issue of law, which is subject to de novo review.

3 Cases that cite this headnote

**[3] Easements**

- - Maintenance and repair

141 Easements  
141II Extent of Right, Use, and Obstruction  
141k53 Maintenance and repair  
"Maintenance" of sewer line included removal and replacement of a malfunctioning or worn-out sewer pipeline, and, thus, easement which permitted construction, repair, and maintenance of sewer line unambiguously authorized replacement of cement sewer line which was more than 50 years old; sewer pipe was becoming increasingly brittle and crushed easily, rendering the entire sewer line in need of replacement with new polyvinyl chloride (PVC) pipe.

Cases that cite this headnote

**[4] Easements**

- - By express grant or reservation

141 Easements  
141II Extent of Right, Use, and Obstruction  
141k39 Extent of Right  
141k42 By express grant or reservation

In construing the language of an express easement, courts apply the rules of contract construction.

3 Cases that cite this headnote

**[5] Contracts**

- - Intention of Parties

**Contracts**

- - Language of contract

95 Contracts  
95II Construction and Operation  
95II(A) General Rules of Construction  
95k147 Intention of Parties  
95k147(1) In general  
95 Contracts  
95II Construction and Operation  
95II(A) General Rules of Construction  
95k147 Intention of Parties  
95k147(2) Language of contract

Cardinal rule of contract construction is to ascertain the parties' intent, and where the contract terms are clear and unambiguous, the court will look to that alone to find the true intent of the parties.

4 Cases that cite this headnote

**[6] Contracts**

- - Ambiguity in general

95 Contracts  
95II Construction and Operation  
95II(A) General Rules of Construction  
95k176 Questions for Jury  
95k176(2) Ambiguity in general

Absent an ambiguity that cannot be resolved by the rules of construction, the interpretation of contractual terms is a question of law for the court.

4 Cases that cite this headnote

**[7] Easements**

~ Alteration

141 Easements

14111 Extent of Right, Use, and Obstruction

141k54 Alteration

Replacement of four-inch cement sewer pipe with six- or eight-inch polyvinyl chloride (PVC) sewer pipe would not be unilateral alteration of physical boundaries of sewer line easement; easement did not specify exact dimensions of the land granted for running the sewer pipeline, and there was evidence that replacement would not expand the physical boundaries of the easement because six-inch replacement pipe would have same outer dimensions as old pipe, and eight-inch pipe would not occupy appreciably more space.

1 Cases that cite this headnote

**[8] Easements**

~ Practical location by parties

141 Easements

14111 Extent of Right, Use, and Obstruction

141k46 Location

141k48 Ways

141k48(5) Practical location by parties

Path of sewer line easement was defined and became fixed according to the original construction and placement of the pipeline.

Cases that cite this headnote

**[9] Easements**

~ Change of location

**Easements**

~ Deviation from way

141 Easements

14111 Extent of Right, Use, and Obstruction

141k46 Location

141k48 Ways

141k48(6) Change of location

141 Easements

14111 Extent of Right, Use, and Obstruction

141k46 Location

141k49 Deviation from way

Once the path of sewer line easement became fixed, the path could not be unilaterally relocated or widened by either of the parties.

1 Cases that cite this headnote

**[10] Easements**

~ Mode of use

**Easements**

~ Alteration

141 Easements

14111 Extent of Right, Use, and Obstruction

141k50 Mode of use

141 Easements

14111 Extent of Right, Use, and Obstruction

141k54 Alteration

Change in the manner, frequency, and intensity of use of the easement within the physical boundaries of the existing easement is permitted without the consent of the other party, so long as the change is not so substantial as to cause unreasonable damage to the servient estate or unreasonably interfere with its enjoyment.

3 Cases that cite this headnote

**[11] Easements**

~ Extent of way

141 Easements

14111 Extent of Right, Use, and Obstruction

141k39 Extent of Right

141k44 Ways

141k44(2) Extent of way

Physical boundaries of a sewer line easement are not limited to such space as was actually occupied by the specific pipe laid at the inception of the easement; rather, easement includes the general area occupied by the existing pipeline, that is, the basic trench path within which the existing pipe was placed.

Cases that cite this headnote

**[12] Easements**

~ Trial

141 Easements

14111 Extent of Right, Use, and Obstruction

## KC REPLY APPENDIX 64

141k61 Actions for Establishment and Protection of Easements

141k61(9.5) Trial

Issue of whether replacement of the sewer pipeline would constitute a substantial change in manner, frequency, and intensity of use of sewer line easement was for jury in action to prevent dominant estate owner from replacing existing sewer pipe with a larger one.

2 Cases that cite this headnote

**[13] Easements**

~ Alteration

141 Easements

14111 Extent of Right, Use, and Obstruction

141k54 Alteration

Dominant estate owner had implied right under sewer line easement to place surface structures on the servient estate as required by city ordinance; inability to do so would frustrate its express rights granted in the easement to repair and maintain the sewer pipeline.

Cases that cite this headnote

**[14] Easements**

~ By express grant or reservation

141 Easements

14111 Extent of Right, Use, and Obstruction

141k39 Extent of Right

141k42 By express grant or reservation

Grant of an easement impliedly includes the authority to do those things which are reasonably necessary for the enjoyment of the things granted.

2 Cases that cite this headnote

**[15] Easements**

~ By express grant or reservation

**Property**

~ Nature of right of property and acquisition in general

141 Easements

14111 Extent of Right, Use, and Obstruction

141k39 Extent of Right

141k42 By express grant or reservation

315 Property

315k1 Nature of right of property and acquisition in general

When one grants a thing, he is deemed also to grant that which is within his ownership without which the grant itself will be of no effect.

Cases that cite this headnote

**[16] Easements**

~ By express grant or reservation

141 Easements

14111 Extent of Right, Use, and Obstruction

141k39 Extent of Right

141k42 By express grant or reservation

Grantees of an easement also have an implied right in the easement to take the action required of them to comply with government rules and regulations.

Cases that cite this headnote

**[17] Appeal and Error**

~ Sufficiency and scope of motion

30 Appeal and Error

30V Presentation and Reservation in Lower Court of Grounds of Review

30V(B) Objections and Motions, and Rulings Thereon

30k234 Necessity of Motion Presenting Objection

30k241 Sufficiency and scope of motion

Grounds raised in a motion for judgment notwithstanding the verdict (JNOV) that were not raised in the motion for directed verdict will not be considered on appeal.

3 Cases that cite this headnote

**[18] Conversion and Civil Theft**

~ Assertion of ownership or control in general

**Conversion and Civil Theft**

~ Use or disposition of property

97C Conversion and Civil Theft

97CI Acts Constituting and Liability Therefor

97Ck108 Assertion of ownership or control in general

(Formerly 389k4 Trover and Conversion)  
97C Conversion and Civil Theft  
97C1 Acts Constituting and Liability Therefor  
97Ck115 Use or disposition of property

(Formerly 389k10 Trover and Conversion)  
Servient estate owners exercised “dominion and control” over dominant estate owner's pipe fixtures as required for dominant owner's conversion claim by having them removed from their property and disposed of at a landfill, even if dominant estate owners acted wrongfully by depositing and storing them on servient owners' land; there was evidence that servient owners failed to exercise due care in removing them by having them dumped, with no consideration given as to their ultimate fate, and temporary restraining order designated that dominant owners were to remove them.

Cases that cite this headnote

**[19] Conversion and Civil Theft**

~ In general:nature and elements  
97C Conversion and Civil Theft  
97C1 Acts Constituting and Liability Therefor  
97Ck100 In general:nature and elements  
(Formerly 389k1 Trover and Conversion)  
“Conversion” consists of an unauthorized assumption and exercise of the right of ownership over personal property belonging to another, in hostility to his rights, an act of dominion over the personal property of another inconsistent with his rights, or an unauthorized appropriation; thus, any distinct act of dominion and control wrongfully asserted over another's personal property, in denial of his right or inconsistent with his right, is a conversion of such property.

4 Cases that cite this headnote

**[20] Conversion and Civil Theft**

~ Use or disposition of property  
97C Conversion and Civil Theft  
97C1 Acts Constituting and Liability Therefor  
97Ck115 Use or disposition of property  
(Formerly 389k10 Trover and Conversion)

Unauthorized removal and disposal of personal property can constitute “conversion.”

1 Cases that cite this headnote

**[21] Conversion and Civil Theft**

~ Assertion of ownership or control in general  
97C Conversion and Civil Theft  
97C1 Acts Constituting and Liability Therefor  
97Ck108 Assertion of ownership or control in general  
(Formerly 389k4 Trover and Conversion)  
Exercise of dominion and control over property in violation of a court order or judgment is “conversion.”

4 Cases that cite this headnote

**[22] Conversion and Civil Theft**

~ Verdict and findings  
97C Conversion and Civil Theft  
97C11 Actions  
97C11(E) Trial  
97Ck235 Verdict and findings  
(Formerly 389k68 Trover and Conversion)  
Jury verdict in favor of dominant estate owner on conversion claim, which was based on servient estate owners dumping expensive pipe fixtures at landfill, was not inconsistent with verdict in favor of servient owners on nuisance claim, which was based upon dominant owner placing pipe fixtures and construction equipment on servient owners' land; jury could have predicated verdict on nuisance claim on items other than pipe fixtures.

Cases that cite this headnote

**[23] Easements**

~ Pleading  
**Judgment**  
~ Relief awarded in general  
141 Easements  
14111 Extent of Right, Use, and Obstruction  
141k61 Actions for Establishment and Protection of Easements

141k61(8) Pleading  
228 Judgment  
228VIII Amendment, Correction, and Review  
in Same Court  
228k313 Relief awarded in general  
Court did not err by declining to amend  
judgment to include the additional finding  
that the servient estate owner could not make  
any permanent changes to the surface of the  
sewer line easement until installation of the  
new sewer pipe by dominant estate owner;  
issue of servient owners' construction plans  
which would have resulted in changes to the  
surface were not included in the pre-trial order  
as matters for determination, and dominant  
estate owners had not previously requested  
any declaratory or injunctive relief pertaining  
to this issue prior to the entry of judgment.  
West's Ga.Code Ann. § 9–11–52(c).

Cases that cite this headnote

**[24] Appeal and Error**

-~ Insufficient discussion of objections  
30 Appeal and Error  
30XVI Review  
30XVI(K) Error Waived in Appellate Court  
30k1079 Insufficient discussion of objections  
Appellant's enumeration of error which  
lacked legal argument or citation to authority  
in support was abandoned. Court of Appeals  
Rule 25(a)(3), (c)(2).

Cases that cite this headnote

**[25] Judgment**

-~ Nature and scope of remedy  
**Trial**  
-~ Additional findings  
228 Judgment  
228VIII Amendment, Correction, and Review  
in Same Court  
228k294 Nature and scope of remedy  
388 Trial  
388X Trial by Court  
388X(B) Findings of Fact and Conclusions of  
Law  
388k401 Additional findings  
Motion for the trial court to amend the  
judgment to make additional findings is not a

procedural device for injecting new issues into  
the case. West's Ga.Code Ann. § 9–11–52(c).

Cases that cite this headnote

**[26] Judgment**

-~ Conformity to Pleadings and Proofs  
228 Judgment  
228VI On Trial of Issues  
228VI(C) Conformity to Process, Pleadings,  
Proofs, and Verdict or Findings  
228k247 Conformity to Pleadings and Proofs  
228k248 In general  
Party cannot request and obtain relief where  
the propriety of that relief was never litigated  
and the opposing party was never given an  
opportunity to assert defenses to the relief.  
West's Ga.Code Ann. § 9–11–54(c)(1).

Cases that cite this headnote

**[27] Appeal and Error**

-~ Ordering New Trial, and Directing  
Further Proceedings in Lower Court  
30 Appeal and Error  
30XVII Determination and Disposition of  
Cause  
30XVII(D) Reversal  
30k1178 Ordering New Trial, and Directing  
Further Proceedings in Lower Court  
30k1178(1) In general  
Remand was required to determine whether  
dominant estate owner or servient estate  
owners were prevailing parties and entitled to  
costs, where jury found in favor of dominant  
owners on some claims and in favor of servient  
owners on others. West's Ga.Code Ann. § 9–  
11–54(d).

Cases that cite this headnote

**[28] Costs**

-~ Who is prevailing party in general  
102 Costs  
1021 Nature, Grounds, and Extent of Right in  
General  
102k32 Prevailing or Successful Party in  
General  
102k32(2) Who is prevailing party in general

Trial court is afforded discretion in assessing costs because sometimes it is not so clear who the prevailing party is, as one party may win on some issues and claims and the other on other issues and claims. West's Ga.Code Ann. § 9–11–54(d).

Cases that cite this headnote

### Attorneys and Law Firms

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Gibson, Deal, Fletcher & Durham, James B. Deal, Michael R. Dunham, Norcross, for appellees.

### Opinion

McMURRAY, Senior Appellate Judge.

**\*734** Kathy and Dennis Nichols own property that is burdened by an underground sewer line easement that benefits the adjacent property owned by Parris Properties, LLC. The Nicholse brought this action against Parris Properties and its principal, Kenneth Parris (collectively, the “Parris Defendants”), to prevent the Parris Defendants from replacing the existing sewer pipe with a larger one. The Parris Defendants answered and counterclaimed for conversion based upon the Nicholse's disposal of certain construction materials owned by Parris Properties.

The case was tried before a jury which found, among other things, that replacement of the existing sewer pipeline with a larger diameter pipe would not constitute a substantial change in the easement, and that the Nicholse were liable for conversion. The trial court subsequently entered its “Final Judgment, Declaratory **\*735** Judgment, and Order on Permanent Injunction” that included a provision prohibiting the Parris Defendants from making any permanent changes to the surface of the Nicholse's property in replacing the sewer pipe. The trial court also declined to award costs to the Parris Defendants. The Parris Defendants then filed a motion requesting that the trial court amend the final judgment to remove the provision prohibiting surface alteration and to make additional findings related to the easement, which the trial court denied.

In Case No. A10A1031, the Nicholse contend that the trial court erred by denying their motions for a directed verdict and for judgment notwithstanding the verdict (“j.n.o.v.”) pertaining to the scope of the easement and the Parris Defendants' counterclaim for conversion. In Case Nos. A10A1029 and A10A1030, the Parris Defendants contend that the trial court erred by including the provision prohibiting surface alteration in the judgment, and erred by declining to amend the judgment or award them court costs as the prevailing parties.

For the reasons discussed below, we affirm the trial court's denial of the Nicholse's motions for a directed verdict and for j.n.o.v.; reverse the judgment to the extent it prohibits surface alteration; reverse in part the trial court's denial of the Parris Defendants' motion to amend the judgment; vacate the trial court's order declining to award costs to the Parris Defendants; and remand for further action consistent with this opinion.

### Case No. A10A1031

**[1] [2]** 1. The Nicholse contend that the trial court erred in denying their motions for a directed verdict and for j.n.o.v. pertaining to whether enlargement of the sewer pipe fell within the scope of the easement. On appeal from the denial of a motion for a directed **\*\*852** verdict or for j.n.o.v., we construe the evidence in the light most favorable to the party opposing the motion, and the standard of review is whether there is any evidence to support the jury's verdict. See *McClung v. Atlanta Real Estate Acquisitions, LLC*, 282 Ga.App. 759, 759–760, 639 S.E.2d 331 (2006). However, “[t]he construction, interpretation and legal effect of a contract such as an easement is an issue of law,” which is subject to de novo review. (Footnote omitted.) *Savannah Jaycees Foundation v. Gottlieb*, 273 Ga.App. 374, 376(1), 615 S.E.2d 226 (2005). See *Reynolds Properties v. Bickelmann*, 300 Ga.App. 484, 487, 685 S.E.2d 450 (2009). Guided by these principles, we turn to the record in the present case.

*The Sewer Line Easement.* At the heart of these companion appeals is an express easement originally executed and recorded in 1952 by C.L. Bradford, as grantor, and William R. Bentley, as **\*736** grantee. It is undisputed that the Nicholse are the successors in title to Bradford, and that Parris Properties is the successor in title to Bentley.

The easement provides in relevant part:

That the said C.L. Bradford does give, grant and convey to William R. Bentley a permanent easement for the construction of a sewer from the property of William R. Bentley to the trunk sewer on Vermont Road. The said sewer is to be constructed along the Southeastern line of the said C.L. Bradford and is to run along the hedge of said Southeastern line of C.L. Bradford one hundred and forty[-]seven and six-tenths (147.6) feet from the property of the said William R. Bentley to Vermont Road.

The said William R. Bentley agrees that he will bear the total cost of the construction of the said sewer and any cost of the maintenance and repair of the same, for which he binds himself, his heirs and assigns, and that the said sewer will be placed beneath the surface of the said property of C.L. Bradford, and that the said William R. Bentley will fill in and restore the property of the said C.L. Bradford to its present condition and will do no damage to the said property of the said C.L. Bradford.

The property burdened by the sewer line easement has a single family residence on it and is part of a neighborhood listed on the National Register of Historic Homes. The Nicholoses acquired the property and currently live in the residence.

The property that benefits from the sewer line easement is adjacent to the Nicholoses' property and has three rental homes located on it. The property has dual zoning: the front portion of the property is zoned multifamily, and the rear portion is zoned single family. Parris Properties acquired the property and wishes to develop it by building a number of townhomes.

*Installation of the Sewer Pipeline.* At or about the time the easement was granted in 1952, a sewer pipe was placed in the ground of what is now the Nicholoses' property. It was a concrete pipe with an inside diameter of four inches and an outside diameter of six inches. At the time the sewer pipe was placed in the ground, the City of Atlanta did not require that the pipeline have any surface structures installed as part of the line, and so the pipeline could be located wholly beneath the surface of the property.

A four-inch sewer pipe is typical of a service connection for a \*737 single family residence.<sup>1</sup> In contrast, the City of Atlanta generally requires an eight-inch sewer pipe for multifamily residential units, such as townhomes, although in some circumstances a six-inch sewer pipe may be permitted. The City of Atlanta now requires installation of a manhole to provide access to eight-inch sewer pipes and installation of a cleanout to provide access to six-inch sewer pipes. As explained by the Director of Watershed Management for the City of Atlanta, a cleanout is "a place where you can insert what plumbers call a snake into the line, which is a long wire or a cable[ ] ... that can turn and push and cut things that might plug up the pipe." Manholes and cleanouts run from the pipeline to the surface and are "visible from the ground."

**\*\*853** *The Proposed Replacement of the Sewer Pipeline.* In 2005, the Nicholoses began a project for the renovation and expansion of their home, and a subcontractor working on the project damaged a segment of the existing four-inch concrete sewer pipe. The Nicholoses replaced the segment with PVC pipe of the same size. As required by the City of Atlanta, the Nicholoses had a cleanout installed on the surface of their property as part of the repair work.

That same year, Parris Properties hired a structural engineer to devise plans for replacing the entire existing sewer pipeline with either a six-inch or eight-inch PVC pipe in order to accommodate the multifamily residential units that Parris Properties wanted to construct on its property. Pursuant to City of Atlanta requirements, replacement with a six-inch pipe would necessitate the installation of a cleanout with a six-inch diameter on the Nicholoses' property; replacement with an eight-inch pipe would necessitate the installation of a manhole on their property.

Parris Properties sought and obtained building permits from the City of Atlanta to replace the existing sewer pipeline with an eight-inch pipe. Before the replacement project began, however, the Nicholoses filed the present action against the Parris Defendants to prevent the project from happening.<sup>2</sup>

A jury trial ensued in which the central issue was whether increasing the size of the sewer pipeline to a six-inch or eight-inch pipe would constitute a substantial change in the easement requiring the Nicholoses' consent. The Nicholoses moved for a directed verdict on the ground that

replacement with a larger diameter pipe was beyond the scope of the easement as a matter of law, which the trial court denied. The jury thereafter found that replacement of the sewer \*738 pipeline with either a six-inch or eight-inch pipe would not constitute a substantial change. The Nicholse moved for j.n.o.v., which the trial court denied.

[3] (a) The Nicholse contend that they were entitled to judgment as a matter of law because the unambiguous language of the easement does not authorize Parris Properties to replace a functioning sewer pipeline. The Nicholse emphasize that the easement provides for the “construction,” “repair,” and “maintenance” of the sewer line easement, words they contend do not encompass the “replacement” of the existing sewer pipeline, which they maintain is functioning properly. We are unpersuaded.

[4] [5] [6] In construing the language of an express easement, we apply the rules of contract construction. See *Municipal Elec. Auth. of Ga. v. Gold-Arrow Farms, Inc.*, 276 Ga.App. 862, 866(1), 625 S.E.2d 57 (2005). The cardinal rule of contract construction is to ascertain the parties' intent, and “[w]here the contract terms are clear and unambiguous, the court will look to that alone to find the true intent of the parties.” (Citation and punctuation omitted.) *Id.* Absent an ambiguity that cannot be resolved by the rules of construction, the interpretation of contractual terms is a question of law for the court. *Id.*

Applying these principles to the construction of the easement at issue, we conclude that the easement unambiguously authorizes the removal and replacement of a malfunctioning or worn-out sewer pipeline. The right to remove and replace such a sewer pipe falls within the ambit of “repair” and “maintenance.” “The common definition of ‘repair’ is very broad in scope and includes in its meaning ‘to make good’ ” by replacing a structure in poor condition. (Citation and punctuation omitted.) *Carpet Central v. Johnson*, 222 Ga.App. 26, 27(1), 473 S.E.2d 569 (1996) (physical precedent only). See also Merriam–Webster's Online Dictionary, <http://www.merriam-webster.com/dictionary/repair> (“repair” means “to restore by replacing a part or putting together what is torn or broken,” “to restore to a sound or healthy state,” or “to make good” or “remedy”). Furthermore, to “maintain” equipment means to “preserve [it] from failure or decline,” see Merriam–Webster's Online Dictionary, \*\*854 <http://www.merriam-webster.com/>

dictionary/maintain, and a sewer cannot be properly maintained if the pipe cannot be replaced when it no longer functions properly or wears out.

The Parris Defendants presented evidence that the existing sewer pipe, which is over a half century old, is in such a condition. According to a plumbing contractor who had previously worked on the sewer pipe, the existing concrete pipe is becoming increasingly brittle and crushes easily, rendering the entire sewer line in need of replacement with new PVC pipe. A former City of Atlanta sewer \*739 engineer also testified that the existing sewer line, as modified by the repairs made by the Nicholse in 2005, is graded improperly and is virtually guaranteed to create future problems with sewage clogging and backing up in the line. Kenneth Parris further testified that the existing sewer pipe has an issue with “slow draining” in a shower, sink, and tub of one of the rental homes on the property owned by Parris Properties.

Because there was some evidence that the existing sewer pipe is not functioning properly and is worn out, and because the terms of the easement permit replacement of a pipe in that condition, the trial court properly denied the Nicholse's motions for a directed verdict and for j.n.o.v. on the asserted ground.

[7] (b) The Nicholse next contend that they were entitled to judgment as a matter of law because enlarging the dimensions of the sewer pipe would impermissibly expand the scope of the easement. According to the Nicholse, a six-inch or eight-inch pipe would occupy more land than the existing sewer pipeline and thus would constitute a unilateral alteration in the physical boundaries of the easement if installed by Parris Properties. We disagree.

[8] [9] [10] The easement in the present case does not specify the exact dimensions of the land granted for running the sewer pipeline. Hence, under Georgia law the path of the easement was defined and became fixed according to the original construction and placement of the pipeline. See *Sloan v. Sarah Rhodes, LLC*, 274 Ga. 879, 880, 560 S.E.2d 653 (2002) (“[W]here the parties have established the actual location and dimensions of an easement, that determination is the controlling factor under Georgia law.”). Once the path of the easement became fixed, the path could not be unilaterally relocated or widened by either of the parties. See *id.* at 879–880, 560 S.E.2d 653; *Herren v. Pettengill*, 273 Ga. 122, 123–124(2),

538 S.E.2d 735 (2000); *Thomason v. Kern & Co.*, 259 Ga. 119, 120, 376 S.E.2d 872 (1989); *Martin v. Seaboard Air Line R.*, 139 Ga. 807, 809(1), 77 S.E. 1060 (1913); *Jackson Elec. Membership Corp. v. Echols*, 84 Ga.App. 610, 611–612, 66 S.E.2d 770 (1951). In contrast, a change in “the manner, frequency, and intensity of use” of the easement *within the physical boundaries of the existing easement* is permitted without the consent of the other party, so long as the change is not so substantial as to “cause unreasonable damage to the servient estate or unreasonably interfere with its enjoyment.” (Punctuation omitted.) *Municipal Elec. Auth. of Ga.*, 276 Ga.App. at 869(2), 625 S.E.2d 57, quoting Restatement (Third) of Property: Servitudes § 4.10 cmt. f. See also *Faulkner v. Ga. Power Co.*, 243 Ga. 649, 649–650, 256 S.E.2d 339 (1979); *Humphries v. Ga. Power Co.*, 224 Ga. 128, 129–130(3), 160 S.E.2d 351 (1968); *Kerlin v. Southern Bell Tel., etc. Co.* 191 Ga. 663, 667–668(2), 13 S.E.2d 790 (1941).

\*740 Here, there was evidence that the removal of the existing sewer pipe and replacement with either a six-inch or eight-inch PVC pipe would not expand the physical boundaries of the easement. As to a new six-inch PVC pipe, there was testimony at trial that PVC pipe is thinner than concrete pipe, such that the old concrete pipe with a four-inch inner diameter and a new PVC pipe with a six-inch inner diameter would actually have the same *outer* diameter. A new six-inch PVC pipe thus would occupy the equivalent amount of land as the existing pipe.

[11] As to a new eight-inch PVC pipe, it is true that the pipe itself would occupy a greater amount of space than the existing pipe, although not appreciably so. But the physical boundaries of a sewer line easement are not “limited to such space as was actually occupied by [the] specific [pipe]” laid at the inception of the easement. \*\*855 *Kerlin*, 191 Ga. at 667(2), 13 S.E.2d 790 (utility easement not “limited to such space as was actually occupied by [the] specific poles and wires” originally installed). See also *Humphries*, 224 Ga. at 129–130(3), 160 S.E.2d 351. Rather, the easement includes the general area occupied by the existing pipeline, that is, the basic trench path within which the existing pipe was placed.<sup>3</sup> See *Reid v. Washington Gas Light Co.*, 232 Md. 545, 194 A.2d 636, 639 (1963) (replacement of existing pipe with larger one along same trench path did not constitute a relocation or alteration of the boundaries of the easement); *Knox v. Pioneer Natural Gas Co.*, 321 S.W.2d 596, 601 (Tex.Civ.App.1959); 61 AmJur 2d Pipelines § 36

(“Replacement of a small gas line with a larger one, using the same trench, is permitted where the increased capacity of the line results in no decrease in safety to the landowner and no substantial increase in the burden of the servient estate.”).<sup>4</sup>

\*741 The Nicholoses do not contend that Parris Properties intends to relocate the trench path in removing and replacing the existing sewer pipeline. Furthermore, Parris Properties’ structural engineer testified that the eight-inch sewer pipeline would “go straight within the same alignment of where the existing sewer line was.” And the “Sewer Extension Drawings” developed by the structural engineer, which included diagrams of how the existing sewer pipeline would be replaced, also constituted some evidence that the new pipe would be installed along the same basic trench path as the existing pipeline. Accordingly, even though an eight-inch PVC pipe has a slightly larger outer diameter than the existing sewer pipe, there was evidence that the new pipe would “not encroach upon any space which is beyond or without” the same “general area” now being occupied by the sewer line easement, and thus is “permissible as territorially within the easement.” *Kerlin*, 191 Ga. at 667–668(2), 13 S.E.2d 790.

Under these circumstances, there was evidence reflecting that the removal of the existing sewer pipe and replacement with either a six-inch or eight-inch PVC pipe would not expand the physical boundaries of the easement, and so the Nicholoses were not entitled to judgment as a matter of law on that issue. Rather, the replacement with the new pipe would constitute a change in the manner, frequency, and intensity of use of the easement, meaning that Parris Properties could unilaterally make the replacement as long as the change would not be so substantial as to cause unreasonable damage to the servient estate or unreasonably interfere with its enjoyment. See *Municipal Elec. Auth. of Ga.*, 276 Ga.App. at 869(2), 625 S.E.2d 57.

[12] (c) The Nicholoses further contend that they were entitled to judgment as a matter of law because the uncontroverted evidence showed that increasing the size of the sewer pipeline would constitute a substantial change in the manner, frequency, and intensity of use of the easement. We do \*\*856 not agree because there was conflicting evidence over whether replacement of the

sewer pipeline would constitute a substantial change, creating a jury question on the issue.

While there was testimony from the Director of Watershed Management for the City of Atlanta that a new sewer pipe with a six-inch or eight-inch diameter would increase the amount of wastewater flowing through the sewer pipeline, he also testified that a pipe of larger diameter is much less likely to get clogged than a smaller diameter pipe. There was testimony, moreover, that a new larger pipe would be more durable than the old one because it would be made of PVC rather than concrete. Additionally, Mr. Nichols testified that the sewer pipeline for his home does not tie into the sewer pipeline occupying the easement, and so any clog or problem in the latter pipeline would not affect the operation of his own sewer or risk any damage to his home.

\*742 In light of this testimony, there was evidence from which the jury could find that increasing the size of the sewer pipe would not cause unreasonable damage to the Nicholoses' property or unreasonably interfere with its enjoyment. See generally *Faulkner*, 243 Ga. at 649–650, 256 S.E.2d 339; *Humphries*, 224 Ga. at 129–130(3), 160 S.E.2d 351; *Kerlin*, 191 Ga. at 667–668(2), 13 S.E.2d 790; *Municipal Elec. Auth. of Ga.*, 276 Ga.App. at 869(2), 625 S.E.2d 57; Restatement (Third) of Property: Servitudes § 4.10 cmt. f. The issue of whether the replacement of the sewer pipe would constitute a substantial change in the easement, therefore, was properly submitted to the jury.

[13] (d) Lastly, the Nicholoses contend that they were entitled to judgment as a matter of law because replacement of the existing sewer pipe requires installation of surface structures (a manhole or cleanout) which they contend are not authorized or contemplated by the easement. They point out that the easement states that the sewer pipeline will be placed “beneath the surface” and that the surface of the land will be “restore[d] ... to its present condition.” Consequently, the Nicholoses argue that the easement does not permit Parris Properties to make any permanent alterations to the surface of their property as part of the installation of a new pipeline. Again, we disagree.

The evidence at trial reflected that unlike when the easement was first created, the City of Atlanta currently requires installation of a cleanout to provide access to a six-inch sewer pipe and of a manhole to provide access to

an eight-inch sewer pipe for repair and maintenance of the pipeline. Indeed, it is undisputed that replacement of the existing four-inch sewer pipe with a pipe of the same inner diameter likewise would require installation of a cleanout. Moreover, even when an old pipeline is not replaced in its entirety, a cleanout must be installed when a portion of the pipe is repaired or replaced near the City of Atlanta's right-of-way.

[14] [15] [16] This evidence shows that Parris Properties cannot exercise its rights under the easement to repair and maintain the sewer pipeline by replacing a malfunctioning or worn-out pipe if it cannot install any surface structures on the Nicholoses' property. “The grant of an easement impliedly includes the authority to do those things which are reasonably necessary for the enjoyment of the things granted.” *Jakobsen v. Colonial Pipeline Co.*, 260 Ga. 565, 566(2), 397 S.E.2d 435 (1990) (pipeline easement included implied right to side-cut timber encroaching upon the right-of-way so that an inspection of the pipeline could be made). See also *Avery v. Colonial Pipeline Co.*, 213 Ga.App. 388, 389–390(1), 444 S.E.2d 363 (1994). Moreover, “[w]hen one grants a thing, he is deemed also to grant that within his ownership without which the grant itself will be of no effect.” (Citation and punctuation omitted.) \*743 *Roberts v. Roberts*, 206 Ga.App. 423, 424(2), 425 S.E.2d 414 (1992). See also *Massey v. Britt*, 224 Ga. 762, 164 S.E.2d 721 (1968). Grantees of an easement also have an implied right in the easement to take the action required of them to comply with government rules and regulations. See *Avery*, 213 Ga.App. at 390(1), 444 S.E.2d 363 (pipeline easement included implied right to remove trees and vegetation from the right-of-way in order to comply with federal safety regulations). In light of these principles, Parris Properties has an implied right under \*\*857 the easement to place surface structures on the Nicholoses' property where, as here, the inability to do so would frustrate its express rights granted in the easement to repair and maintain the sewer pipeline.

For the combined reasons set forth in subdivisions (a)–(d), the trial court properly denied the Nicholoses' motions for a directed verdict and for j.n.o.v. regarding whether enlargement of the existing sewer pipe fell within the scope of the easement. Parris Properties is authorized to remove the existing sewer pipeline and replace it with a six-inch or eight-inch PVC pipe along the same basic trench path, and to install a manhole or cleanouts on the surface of the

Nicholses' property to the extent required by the City of Atlanta.

[17] 2. The Nicholses also contend that the trial court erred in denying their motions for a directed verdict and for j.n.o.v. on the Parris Defendants' counterclaim for conversion predicated on the Nicholses' disposal of pipe fixtures owned by Parris Properties. According to the Nicholses, they never attempted to assert dominion over the pipe fixtures and never interfered with Parris Properties' ability to remove the materials.<sup>5</sup> In addition, the Nicholses maintain that they were entitled to remove the pipe fixtures because Parris Properties had no right to deposit the fixtures on their property in the first instance. Finally, the Nicholses assert that the jury's verdicts on their claim for nuisance and the Parris Defendants' counterclaim for conversion were inconsistent.

Construed in favor of the jury's verdict, the relevant facts pertaining to the conversion counterclaim are as follows. This case was originally filed by the Nicholses in the Superior Court of Fulton County but was transferred to the Superior Court of Clarke County. In an order entered on March 10, 2006, the Superior Court of Fulton \*744 County recited that Parris Properties had agreed "to refrain from any construction" until the transfer had been completed and the case had been assigned to a new judge.

On or about April 28, 2006, before the transfer of the case had been effectuated, Parris Properties deposited construction equipment and materials, including pipe fixtures for constructing a manhole, on the Nicholses' property. Thereafter, on May 4, 2006, in the order formally transferring the case to the Superior Court of Clarke County, the Superior Court of Fulton County directed all parties "to refrain from commencing to build, construct, or renovate anything on the property that is subject to the alleged easement."

On May 9, 2006, following the transfer and reassignment of the case, the Superior Court of Clarke County entered a temporary restraining order ("TRO") providing that the construction equipment and materials were to be removed from the Nicholses' property by Parris Properties, but did not specify a time frame within which the items had to be removed. Some of the items were removed from the property by Parris Properties, but not the pipe fixtures, which were the subject of negotiations between the parties

concerning the time frame for removal. Subsequently, on June 6, 2006, after receiving proposed orders for interlocutory relief from both parties, the trial court entered its order on interlocutory injunction in which the Parris Defendants were "ordered to remove any equipment or materials placed on the Nichol[ses]' property within ten days of the date of this order, if not already removed."

It later became clear, however, that in the interim between entry of the TRO and the order on interlocutory injunction, the Nicholses had made the unilateral decision to have a contractor remove the pipe fixtures from their property and dump them at a \*\*858 landfill. According to Mr. Parris, the pipe fixtures were worth over \$4,000.

In the ensuing litigation, the Nicholses sought damages for nuisance based upon the depositing of the construction equipment and materials on their property, and the Parris Defendants sought damages for conversion based upon the Nicholses' removal and disposal of the pipe fixtures. The jury found in favor of the Nicholses on their nuisance claim and in favor of the Parris Defendants on their conversion counterclaim.

[18] [19] [20] [21] We conclude that the evidence adduced at trial was sufficient to support the Parris Defendants' counterclaim for conversion against the Nicholses.

[C]onversion consists of an unauthorized assumption and exercise of the right of ownership over personal property belonging to another, in hostility to his rights; an act of dominion over the personal property of another inconsistent \*745 with his rights; or an unauthorized appropriation. Thus, any distinct act of dominion and control wrongfully asserted over another's personal property, in denial of his right or inconsistent with his right, is a conversion of such property.

(Citations, punctuation and footnotes omitted.) *Williams v. Nat. Auto Sales*, 287 Ga.App. 283, 285(1), 651 S.E.2d 194 (2007). See OCGA § 51-10-1. The unauthorized removal and disposal of personal property can constitute

conversion. See *Washington v. Harrison*, 299 Ga.App. 335, 339(1), 682 S.E.2d 679 (2009) (unauthorized removal of personal property from land by salvage crew at behest of landlord “with no consideration given as to its ultimate fate,” and in violation of dispossessionary statute, constituted conversion); *Thakkar v. St. Ives Country Club*, 250 Ga.App. 893, 896(5), 553 S.E.2d 181 (2001) (conversion could be found based upon unauthorized removal of trees from land and placement in “trash heap”). Furthermore, the exercise of dominion and control over property in violation of a court order or judgment constitutes conversion. See *Blevins v. Brown*, 267 Ga.App. 665, 668(2), 600 S.E.2d 739 (2004) (former husband's exercise of dominion and control over truck that had been awarded to former wife in divorce action constituted conversion).

The Nicholoses exercised dominion and control over the pipe fixtures by having them removed from their property and disposed of at the landfill. And while a landowner may have the common law right to remove the personal property of others left on his land without his consent, the landowner still must use due care in removing the property. See *Reinertsen v. Porter*, 242 Ga. 624, 628(1), 250 S.E.2d 475 (1978); *Grier v. Ward*, 23 Ga. 145 (1857). Here, even if Parris Properties acted wrongfully by depositing and storing the pipe fixtures on the Nicholoses' property,<sup>6</sup> there was evidence that the Nicholoses failed to exercise due care in removing the expensive fixtures by having them dumped at a landfill “with no consideration given as to [their] ultimate fate.” *Washington*, 299 Ga.App. at 339(1), 682 S.E.2d 679. Furthermore, this case is unique because the method for the removal of the pipe fixtures from the Nicholoses' property was designated by court order: Parris Properties was to remove the fixtures under the terms of the TRO. Nevertheless, the Nicholoses chose to exercise self-help and remove and dispose of the pipe \*746 fixtures themselves when Parris Properties did not remove the fixtures as quickly as the Nicholoses desired, and while the issue of the time frame for removal was still pending before the trial court for resolution. Under these circumstances, the jury was entitled to find that the Nicholoses converted the pipe fixtures through their unauthorized removal and destruction of the fixtures in violation of a court order. See, e.g., *Washington*, 299 Ga.App. at 339(1), 682 S.E.2d 679; *Blevins*, 267 Ga.App. at 668(2), 600 S.E.2d 739; *Thakkar*, 250 Ga.App. at 896(5), 553 S.E.2d 181.

[22] Nor was the jury's verdict on the conversion counterclaim inconsistent with the verdict in favor of the Nicholoses on their nuisance claim. As previously noted, there \*\*859 was construction equipment and materials deposited on the Nicholoses' property other than the pipe fixtures, and those other items were not removed and dumped at the landfill. The jury could have predicated its verdict on the nuisance claim on those other items and its verdict on the conversion counterclaim on the pipe fixtures, and, therefore, the verdicts on the two claims were not inconsistent.<sup>7</sup>

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3. The Parris Defendants contend that the trial court erred by including a provision in the judgment that prohibited them from making any permanent alterations to the surface of the Nicholoses' property as part of the installation of a new sewer pipe. The Parris Defendants further contend that the trial court erred by denying their motion to amend the judgment to allow for the installation of surface structures, such as a manhole or cleanouts, on the Nicholoses' property. We agree. For the reasons discussed supra in Division 1(d), the Parris Defendants are entitled to alter the surface of the Nicholoses' property by installing a manhole or cleanouts to the extent required by the City of Atlanta. Accordingly, the trial court's judgment is reversed to the extent it prohibits surface alteration, and the case is remanded for reentry of a judgment consistent with this opinion.

[23] [24] 4. The Parris Defendants contend that the trial court erred in declining to amend the judgment to include the additional finding that the Nicholoses could not make any permanent changes to the surface of the easement until installation of the new sewer pipe.<sup>8</sup> In moving to amend the judgment pursuant to OCGA § 9-11-52(c), the \*747 Parris Defendants claimed that the Nicholoses planned to construct a new concrete driveway and a retaining wall over portions of the sewer line easement as part of the renovation and remodeling of their home, and that these changes to the surface of the easement would materially interfere with the installation of the new sewer pipe. They requested that the Nicholoses not be permitted to proceed with any such construction “for six months from the date of a ruling on this [m]otion to [a]mend, or six months from the date an appellate court rules on this case, if an appeal is filed.”

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[25] [26] The issue of the Nicholoses' planned construction and any potential claims related thereto were not included in the pre-trial order as matters for determination, and the Parris Defendants had not previously requested any declaratory or injunctive relief pertaining to this issue prior to the entry of judgment. A motion for the trial court to amend the judgment to make additional findings under OCGA § 9–11–52(c) is not a procedural device for injecting new issues into the case. See *Truststreet Properties v. Burdick*, 287 Ga.App. 565, 568, 652 S.E.2d 197 (2007) (motion to amend judgment properly denied where party sought to inject into the case a new methodology for calculation of damages to replace the one used at trial). Moreover, a party cannot request and obtain relief where the propriety of that relief was never litigated and the opposing party was never given an opportunity to assert defenses to the relief. See OCGA § 9–11–54(c) (1); *Church v. Darch*, 268 Ga. 237, 238(2), 486 S.E.2d 344 (1997). The trial court thus did not err in declining to amend the judgment in the manner requested by the Parris Defendants.

[27] [28] 5. Lastly, the Parris Defendants contend that the trial court erred in failing to award court costs to them as the prevailing parties. Under OCGA § 9–11–54(d), “costs shall be allowed as a matter of course to the prevailing party unless the court otherwise directs.” The trial court is afforded discretion in assessing costs because “[s]ometimes it is not so clear who the prevailing party is, as one party may win on some issues and claims and the other on other issues and claims.” (Citation and punctuation omitted.) *Dacosta v. Allstate Ins. Co.*, 199 Ga.App. 292, 294(2), 404 S.E.2d 627 (1991).

In the present case, the jury found in favor of the Nicholoses on their claim for nuisance, but not on their additional claims for trespass and punitive damages. The jury found in favor of the Parris Defendants on the issue of whether replacement with a six-inch or eight-inch pipe would constitute a substantial change and on their \*748 counterclaim for conversion, but not on their additional counterclaims for trespass and punitive damages.

As discussed supra in Division 3, the trial court erred by including a provision in the judgment prohibiting the Parris Defendants from making any permanent alterations to the surface of the Nicholoses' property as part of the installation of a new sewer pipe. The trial court's erroneous ruling on that issue may have affected its assessment of whether the Parris Defendants should be treated as the prevailing parties. Consequently, without expressing any opinion on the issue, we vacate the trial court's order declining to award costs and remand for reconsideration in light of this opinion.

*Judgment affirmed in part, reversed in part, and vacated in part, and case remanded with direction in Case Nos. A10A1029 and A10A1030. Judgment affirmed in Case No. A10A1031.*

BARNES, P.J., and Senior Appellate Judge G. ALAN BLACKBURN concur.

#### All Citations

305 Ga.App. 734, 700 S.E.2d 848, 10 FCDR 2886

#### Footnotes

- 1 Unless otherwise noted, references to the diameter of a pipe are to its inside diameter.
- 2 The City of Atlanta also was a named defendant in the original lawsuit, but the trial court granted the City's motion to dismiss. That ruling has not been appealed, and the City is not a party to any of these companion appeals.
- 3 Our holding in this case is not inconsistent with *Nodvin v. Plantation Pipe Line Co.*, 204 Ga.App. 606, 612(4), 420 S.E.2d 322 (1992), abrogated in part on other grounds, *Yaali, Ltd. v. Barnes & Noble*, 269 Ga. 695, 696(2), 506 S.E.2d 116 (1998). In *Nodvin*, we rejected the contention that the pipeline easement was void for being vague and indefinite, noting that the location and size of a pipeline becomes certain once the pipe is placed in the ground and used with the acquiescence of both the grantor and grantee. *Nodvin*, 204 Ga.App. at 612(4), 420 S.E.2d 322. *Nodvin* addressed the validity of the easement in the first instance, not whether the subsequent replacement of the existing pipeline with a larger one would impermissibly expand the physical boundaries of the easement.
- 4 We have similarly held that with respect to overhead transmission lines, the stringing of new wires within the general area marked by the original poles, wires, and appurtenances was a “change in degree only, and not in kind,” and thus was “a reasonable and normal incident of the existing [easement] right.” *Kerlin*, 191 Ga. at 668(3), 13 S.E.2d 790. See also

*Faulkner*, 243 Ga. at 649–650, 256 S.E.2d 339 (installation of new, higher voltage transmission wire in same easement right of way did not exceed the scope of the existing easement); *Humphries*, 224 Ga. at 129–130(3), 160 S.E.2d 351 (power company authorized to enter right-of-way and replace existing transmission poles and wires with new, larger equipment to accommodate higher voltages); *Municipal Elec. Auth. of Ga.*, 276 Ga.App. at 869(2), 625 S.E.2d 57 (addition of fiber optic line to existing electronic transmission system of towers and poles was a change in the degree of use rather than the kind of use, and thus fell within the scope of the original utility easement).

- 5 The Nicholsons further argue that they were entitled to judgment as a matter of law because they disclaimed title and tendered the pipe fixtures to Parris Properties so as to discharge and release them from a conversion claim under OCGA § 44–12–153. While the Nicholsons raised this argument in their motion for j.n.o.v., they did not raise it in their motion for a directed verdict. “[G]rounds raised in a motion for judgment notwithstanding the verdict that were not raised in the motion for directed verdict will not be considered on appeal.” (Citation omitted.) *Southern Land Title, Inc. v. North Ga. Title*, 270 Ga.App. 4, 7(2), 606 S.E.2d 43 (2004). See also *Fertility Technology Resources v. Lifetek Med., Inc.*, 282 Ga.App. 148, 153(2), 637 S.E.2d 844 (2006).
- 6 We need not resolve where or to what extent Parris Properties was entitled to deposit and store the construction equipment and materials on the Nicholsons' property as part of its right to repair and maintain the sewer pipeline. Nor must we resolve whether Parris Properties violated the March 10, 2006 order by depositing and storing the items on the property.
- 7 The Parris Defendants do not challenge the jury's verdict on the Nicholsons' nuisance claim.
- 8 The Parris Defendants also enumerate as error the trial court's denial of their motion to amend the judgment to include an additional finding that the City of Atlanta is authorized to issue new building permits for the replacement of the existing sewer pipeline. However, they provide no legal argument or citation to authority in support of this enumeration, as required by Court of Appeals Rule 25(a)(3). The enumeration of error, therefore, is deemed abandoned. See Court of Appeals Rule 25(c)(2).

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION  
COMMISSION

In the Matter of )  
Adopting and Repealing Rules in ) DOCKET NO. UE-990473  
 )  
Chapter 480-100 WAC ) GENERAL ORDER NO. R-495  
 )  
Relating to Rules establishing ) ORDER ADOPTING AND  
requirements for electric companies ) REPEALING RULES  
 ) PERMANENTLY  
..... )

1     **STATUTORY OR OTHER AUTHORITY:** The Washington Utilities and  
Transportation Commission takes this action under Notice WSR #01-11-147, filed  
with the Code Reviser on May 23, 2001. The Commission brings this proceeding  
pursuant to RCW 80.01.040 and RCW 80.04.160.

2     **STATEMENT OF COMPLIANCE:** This proceeding complies with the Open  
Public Meetings Act (chapter 42.30 RCW), the Administrative Procedure Act  
(chapter 34.05 RCW), the State Register Act (chapter 34.08 RCW), the State  
Environmental Policy Act of 1971 (chapter 43.21C RCW), and the Regulatory  
Fairness Act (chapter 19.85 RCW).

3     **DATE OF ADOPTION:** The Commission adopts this rule on the date that this  
Order is entered.

4     **CONCISE STATEMENT OF PURPOSE AND EFFECT OF THE RULE:** RCW  
34.05.325 requires that the Commission prepare and provide to commenters a concise  
explanatory statement about an adopted rule. The statement must include the  
identification of the reasons for adopting the rule, a summary of the comments  
received regarding the proposed rule, and responses reflecting the Commission’s  
consideration of the comments.

5     The Commission often includes a discussion of those matters in its rule adoption  
order. In addition, most rulemaking proceedings involve extensive work by  
Commission Staff that includes summaries in memoranda of stakeholder comments,  
Commission decisions, and Staff recommendations in each of those areas.

6     In this docket, to avoid unnecessary duplication, the Commission designates the  
discussion in this Order as its concise explanatory statement, supplemented where not  
inconsistent by the Staff memoranda presented at the adoption hearing and at the  
open meetings where the Commission considered whether to begin this rulemaking  
and whether to adopt the specific language proposed by Staff. Together, the  
documents provide a complete but concise explanation of the agency’s actions and  
the agency’s reasons for taking those actions.

7 **REFERENCE TO AFFECTED RULES:** This Order repeals and adopts the following sections of the Washington Administrative Code:

**WAC 480-100-056 Refusal of service.**

*Repealed, subject addressed in WAC 480-100-123.*

**WAC 480-100-116 Responsibility for delinquent accounts.**

*Repealed, subject addressed in WAC 480-100-123.*

**WAC 480-100-123 Refusal of service.**

*New section that combines WAC 480-100-056 and WAC 480-100-116.*

8 **PREPROPOSAL STATEMENT OF INQUIRY:** The Commission filed a Preproposal Statement of Inquiry (CR-101) on April 7, 1999, at WSR #99-08-105.

9 **ADDITIONAL NOTICE AND ACTIVITY PURSUANT TO PREPROPOSAL STATEMENT:** The Preproposal Statement of Inquiry advised interested persons that the Commission was considering entering a rulemaking on rules relating to electric companies to review them for content and readability pursuant to Executive Order 97-02, with attention to the rules' need, effectiveness and efficiency, clarity, intent and statutory authority, coordination, cost, and fairness. The review included consideration of whether substantive changes or additions were required.

10 The Commission also informed persons of the inquiry into this matter by providing notice of the subject and the CR-101 to all persons on the Commission's list of persons requesting such information pursuant to RCW 34.05.320(3) or who appeared on lists of interested persons in Docket No. UE-990473. Pursuant to the notice, the Commission:

- Held four interested person/stakeholder meetings.
- Created inter-institutional discussion and drafting subgroups to prepare initial rules drafts.
- Developed draft rules using the information gathered from stakeholders.
- Circulated three working drafts to stakeholders for comment.
- Updated drafts to incorporate comments received.

11 **NOTICE OF PROPOSED RULEMAKING:** The Commission filed a supplemental notice of Proposed Rulemaking (Supplemental CR-102) on May 23, 2001, at WSR #01-11-147.

12 **MEETINGS OR WORKSHOPS; ORAL COMMENTS:** Before filing the notice of Proposed Rulemaking, the Commission held four workshops at its headquarters in Olympia on June 3, June 24, October 14-15, 1999, and May 25, 2000. Representatives from the following companies, agencies and organizations attended all or some of the workshops: Avista Utilities (Avista), Puget Sound Energy (PSE),

Northwest Natural Gas (NW Natural), Office of Public Counsel (Public Counsel), PacifiCorp, Cascade Natural Gas (Cascade), The Energy Project, Energy Advocates, Cost Management Services, the Energy Office of the Department of Community, Trade, and Economic Development, International Brotherhood of Electric Workers, and the Washington State Building Code Council. During the workshops, attendees provided oral comments about all the sections under review. Most of the discussions focused on consumer related issues, including refusal of service, prior obligation, and disclosure of private information. The Commission incorporated in its rules many of the suggestions offered by various stakeholders.

- 13*     **COMMENTERS (WRITTEN COMMENTS):** The Commission received written comments, and in some cases, several rounds of written comments from Avista, Cascade, Mr. Jay Lei, Northwest Industrial Gas Users (NWIGU), NW Natural, PacifiCorp, Public Counsel, PSE, The Boeing Company (Boeing), The Energy Project, TrizecHahn Office Properties, Ltd., and Washington Health Care Association. The Commission accepted many of the proposals contained in these written comments.
- 14*     **RULEMAKING HEARINGS:** The Commission originally scheduled this matter for oral comment and adoption under Notice WSR #01-11-147 at 9:30 a.m., at a rulemaking hearing scheduled during the Commission's regularly scheduled open public meeting on Wednesday, June 27, 2001, at the Commission's offices in Olympia, Washington. The Notice also provided interested persons an opportunity to submit written comments to the Commission. The Commission continued the rule adoption hearing on June 27, July 11, July 25, and August 8, 2001. On September 12, 2001, Chairwoman Marilyn Showalter, Commissioner Richard Hemstad, and Commissioner Patrick J. Oshie considered the rule proposal for adoption, pursuant to notice during the Commission's regularly scheduled open public meeting. The Commission heard oral comments from representatives of PSE, Boeing, Public Counsel, NWIGU, Avista, and Htech.
- 15*     **SUGGESTIONS FOR CHANGE THAT ARE REJECTED:** The Commission rejected PSE's and PacifiCorp's proposals to include language in WAC 480-100-123 regarding "economic feasibility" and "adverse impacts" from WAC 480-100-056 as reasons for refusal of service, or to provide examples of economic feasibility and adverse impacts. The Commission does not believe that the rule language should contain specific examples of reasons to refuse service. The language should be left flexible and open, consistent with the language in RCW 80.28.110. Instead the Commission includes conditions in subsections (1) and (2) under which a utility may refuse to provide service, and provides a "catch all" in subsection (5) that would require a utility to file for Commission approval if the utility proposes to refuse service to a customer for reasons other than those listed in subsections (1) and (2).
- 16*     The Commission also rejected the proposals of Cascade, NW Natural, and PacifiCorp to eliminate or specify the number of prior obligations a residential customer or applicant can incur in one calendar year before a utility may refuse

service. The Commission believes that more accurate data about the use and consequences of prior obligation is needed to support a substantial change to this rule.

17 **COMMISSION ACTION:** After considering all of the information regarding this proposal, the Commission repealed and adopted the rules as proposed in the Supplemental CR-102 at WSR #01-11-147 with the changes described below.

18 **CHANGES FROM PROPOSAL:** The Commission adopted the proposal with the following changes from the text noticed at WSR #01-11-147:

19 **Subsection (2)(d).** The Commission revised this subsection and made it more general to include all possibilities in response to PacifiCorp's concern that the proposed language implied that the utility is responsible for securing all rights-of-way, easements, and other permits. Most utilities' line extension tariffs address the responsibility of the applicant to obtain the necessary rights-of-way and easements. It is not the Commission's intent to make the utility responsible for actually obtaining, paying for, or holding all rights-of-way, easements, approvals, and permits. up to the customer's point of attachment. The rule simply recognizes that if all necessary rights-of-way, easements, approvals, and permits are not in place, after reasonable efforts to secure them, the utility may not be required to provide service.

20 **Subsection (3).** Based on the comments of Public Counsel and The Energy Project concerning prior obligations, the Commission determined that for the present it will restate the existing rule, which does not limit the number of prior obligations a residential customer or applicant can incur before a utility may refuse service. The Commission believes that more accurate data about the use and consequences of prior obligation is needed to support a substantial change to this rule.

21 Subsection (4). The Commission revised this subsection to address NWIGU's request that the Commission extend the applicability of this subsection beyond residential applicants and customers. In NWIGU's opinion, to limit this subsection to residential applicants or customers only creates an inequitable obligation on all other customers. The Commission agrees that this subsection should not be restricted to residential applicants or customers and extends the applicability of subsection (4) to all applicants and customers.

22 **Subsection (5).** The Commission replaced the existing subsection (3) with this subsection to address the concerns expressed by TrizecHahn Office Properties, Ltd. and Boeing's request that the Commission repeal this subsection's original language that permitted a utility to refuse new or additional service if "such service will adversely affect service being rendered to other customers" or if to provide service would be "economically unfeasible," in order to preclude a utility from having discretion to refuse service with no effective recourse for the potential customer.

23 Boeing suggested that revision of the existing rule was needed for two reasons. First, revision was necessary for the continued vitality of the economy in Washington.

Boeing commented that the obligation of electric utilities to serve has been critical to economic development in the state because it has contributed to the region's dependable supply of low-cost electric power. According to Boeing, if utilities are permitted to refuse new or additional service, this source of economic strength would be imperiled. Second, Boeing believes that the current Refusal of Service rule is inconsistent with the statutory and common law obligation of an electric utility to provide service: RCW 80.28.010(2); *National Union Insurance Co. v. Puget Sound Power & Light Co.*, 94 Wn. App. 163; 972 P.2d 481 (1999). Boeing commented that the Commission has jurisdiction to require an electric utility to provide service. *In re Tanner Elec. Co.* 1991 Wash. UTC LEXIS 17 (WUTC 1991). Contrary to these principles, according to Boeing, the current rule could give a utility untrammelled discretion to refuse service with no opportunity for Commission oversight and no redress for a customer denied service.

- 24 Boeing asserts that the obligation to serve is a well established principle in utility regulation. The utility has the opportunity to earn a reasonable rate of return and, in exchange, it has the obligation to serve. The presumption should be that the utility has the obligation to serve unless there are reasonable exceptions. The exceptions included in the revised rule fall in the zone of reasonableness.
- 25 The Commission observes that existing language in the rule permits a utility to refuse new or additional service if "such service will adversely affect service being rendered to other customers" or if to provide service would be "economically unfeasible." These terms are too general and vague to be useful. Commission resolution of obligation to serve issues is likely to be based on fact-specific analysis. So resolution of such issues is not amenable to the prescriptive language of a rule. Obligation to serve issues, when they arise and cannot be resolved otherwise, should be brought to the Commission for resolution.
- 26 The Commission has removed the original subsection (3) language that permitted a utility to refuse new or additional service if "such service will adversely affect service being rendered to other customers" or if to provide service would be "economically unfeasible." The revised rule includes conditions in subsections (1) and (2) under which a utility may refuse to provide service, and provides a "catch all" in subsection (5) that would require a utility to file for Commission approval if the utility proposes to refuse service to a customer for reasons other than those listed in subsections (1) and (2).
- 27 The Commission also revised subsection (5) and added subsection (6) to address the process issues raised by Public Counsel, PSE, TrizecHahn Office Properties, Ltd., Boeing, and Mr. Jay Lei. Subsection (5) requires the utility to work with the customer requesting service to resolve the issues before coming to the Commission. Subsection (6) informs applicants and customers about options available under Chapter 480-09 WAC, the Commission's procedural rules.

28 **STATEMENT OF ACTION; STATEMENT OF EFFECTIVE DATE:** In reviewing the entire record, the Commission determines that WAC 480-100-056 and WAC 480-100-116 should be repealed, and WAC 480-100-123 should be adopted to read as set forth in Appendix A, as a rule of the Washington Utilities and Transportation Commission, to take effect pursuant to RCW 34.05.380(2) on the thirty-first day after filing with the Code Reviser.

**ORDER**

29 THE COMMISSION ORDERS That:

30 WAC 480-100-056 and WAC 480-100-116 are repealed, and WAC 480-100-123 is adopted to read as set forth in Appendix A, as a rule of the Washington Utilities and Transportation Commission, to take effect on the thirty-first day after the date of filing with the Code Reviser pursuant to RCW 34.05.380(2).

31 This Order and the rules set out below, after being recorded in the register of the Washington Utilities and Transportation Commission, shall be forwarded to the Code Reviser for filing pursuant to chapters 80.01 and 34.05 RCW and chapter 1-21 WAC.

DATED at Olympia, Washington, this 3rd day of December, 2001.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

RICHARD HEMSTAD, Commissioner

PATRICK J. OSHIE, Commissioner

32 MARILYN SHOWALTER, Dissenting:

- 33 I cannot agree with the majority's decision to adopt the so-called "prior obligation rule," WAC 480-100-123(3). Under this rule, a residential customer who has been disconnected for failing to pay prior bills (i.e., who has a "prior obligation") is entitled to be reconnected and to receive electric service upon payment of a deposit and reconnection fee. The underlying amounts owed for prior service need never be paid to receive future service. The rule applies to any residential customer regardless of income or other circumstances. Further, the rule allows an unlimited number of prior defaults and disconnections over an unlimited number of months or years with unlimited amounts owing.
- 34 The most basic principle underlying all commerce is that people must pay for the goods or services they receive, and cannot expect to continue to receive those goods or services if they have not paid their bills. This universal principle is as important to the operation of public service companies as it is in the broader world. Utilities are obligated to provide service in return for compensation from customers that is fair, just, reasonable and sufficient. In short, the company must serve, but in return, the customer must pay--or at least, that is what our general rule *should* provide.
- 35 Not surprisingly, there appear to be no other jurisdictions with a rule like the one being adopted. Some jurisdictions require the prior obligation to be paid in full before the utility must reconnect (e.g., Seattle City Light, Snohomish Public Utility District, Tacoma Power, Clark Public Utility District). Others allow thirty days (e.g., the state of Oregon, but only once—after a second disconnection for nonpayment, all overdue obligations must be paid in full before reconnection is required). Others allow a longer period for full payment, but these provisions are limited to low-income customers and/or seasonally related to allow winter service to continue pending full payment. All jurisdictions, as far as I know, ultimately require full payment of prior amounts owed as a condition of the right to receive continued service.
- 36 An entirely valid concern is the plight of low-income customers who have difficulty paying their energy bills. The rule adopted by the majority, however, is not tailored to them (since it has no means test) and even appears to discriminate against them, as I will discuss shortly.
- 37 There are several programs devoted to low-income needs, all of which I support. Most broadly, there are state and federal income-assistance (welfare) programs. More specifically, there are state and federal programs that provide money to help low-income customers pay their electric and gas bills. These programs are outside the direct purview of this commission.
- 38 There are two state statutes, however, that relate more directly to our regulatory authority to address the needs of low-income customers. RCW 80.28.010, the "winter moratorium" law, prohibits defaulting low-income customers from being disconnected during the winter months (November 15 through March 15) if they agree to pay their bills in full by the following October 15. This law only makes

sense if it is premised (reasonably) on the existence of a general requirement to pay one's bills in order to continue to receive service, to which the law provides a circumscribed exception. The rule being adopted, however, negates this premise. As a result, the winter moratorium law is far more demanding of participating low-income customers (they must ultimately pay their bills) than the adopted rule is for all customers (who need never pay their bills). Moreover, the rule actually excludes from its protection anyone who defaults while participating in the winter moratorium program, so it actually discriminates against those low-income customers who are naïve enough but also responsible enough to agree to pay their bills under that program.

39 A second law, RCW 80.28.068, allows public service companies to propose, and the Commission to approve, discounted rates for low-income customers. The costs of the discount are borne by the other ratepayers. The Commission is not authorized to order a discounted rate on its own initiative; it can only respond to a proposal by the company. This law, too, only makes sense if the legislature assumes (reasonably) that without it, all ratepayers, including low-income ratepayers, will otherwise be paying a uniform residential rate. But the rule being adopted has no income test and allows unlimited amounts to go unpaid--in effect creating a much deeper discount than would ever be achieved under the low-income discount law.

40 The rule raises other fairness questions. Those who take advantage of the rule receive its "discount," but those in identical (or worse) circumstances who do manage to pay their bills will not. The majority says it wants more data to evaluate the effects of the rule. But the data being collected will not tell us the income levels or personal circumstances of those who use the rule. Nor will the data tell us the income levels or personal circumstances of those who do *not* use the rule.

41 Of course, in one sense the rule is "fair" in that all residential ratepayers are entitled to take advantage of it. But if large numbers of people were to stop paying their bills and yet continue to receive service, the resulting costs would cut into the revenue requirements of the utility and drive up costs for the rest of the ratepayers. So the rule is not sustainable if used on a broad basis. Regardless of whether the current, similar rule has been broadly or sparingly used, a rule like the one being adopted poses too much risk of misuse or broad use, especially in the absence of any well-articulated purpose. I believe in programs and policies that focus clearly on the needs of those who are unable to pay their energy bills, but the rule adopted here has a much more diffuse focus and potentially more diffuse and unsound effects.

42 The general principle that one is obligated to pay for the services one receives is deeply understood and fundamental to a functioning economy. Instead of abandoning and undermining this principle, our rules should reinforce it, and carve out exceptions to it carefully and fairly.

43 For these reasons, I respectfully dissent.

MARILYN SHOWALTER, Chairwoman

*Note: The following is added at Code Reviser request for statistical purposes:*

Number of Sections Adopted in Order to Comply with Federal Statute: New 0, amended 0, repealed 0; Federal Rules or Standards: New 0, amended 0, repealed 0; or Recently Enacted State Statutes: New 0, amended 0, repealed 0.

Number of Sections Adopted at Request of a Nongovernmental Entity: New 0, amended 0, repealed 0.

Number of Sections Adopted on the Agency's own Initiative: New 1, amended 0, repealed 2.

Number of Sections Adopted in Order to Clarify, Streamline, or Reform Agency Procedures: New 1, amended 0, repealed 2.

Number of Sections Adopted using Negotiated Rule Making: New 0, amended 0, repealed 0; Pilot Rule Making: New 0, amended 0, repealed 0; or Other Alternative Rule Making: New 0, amended 0, repealed 0.

2003 WL 24122603 (Wash.U.T.C.)  
Slip Copy

In the Matter of the Petition of VERIZON NORTHWEST INC., For Waiver of WAC 480-120-071(2)(a).

UT-011439

Washington Utilities and Transportation Commission

April, 2003

TWELFTH SUPPLEMENTAL ORDER

***Synopsis:** The Commission grants Verizon's petition for a waiver of WAC 480-120-071(2)(a) of the requirement to extend service to two locations in Verizon's Bridgeport exchange. The Commission affirms its orders joining Qwest and RCC as parties but now dismisses Qwest and RCC as parties to the proceeding. The Commission finds moot Qwest's motion to strike portions of Staff's Response Brief.*

**ORDER GRANTING VERIZON PETITION FOR WAIVER OF WAC 480-120-071(2)  
(A) AND DISMISSING QWEST AND RCC AS PARTIES TO THE PROCEEDING**

**\*1 Nature of the Proceeding:** Docket No. UT-011439 is a petition by Verizon Northwest Inc. (Verizon), seeking a waiver of the requirement to extend wireline service under WAC 480-120-071<sup>1</sup> to the Taylor location and the Timm Ranch, located in Verizon's Bridgeport exchange in Douglas and Okanogan counties respectively.

**Procedural history:** The matter was heard upon due and proper notice to all interested parties before the Commissioners and Administrative Law Judge Theodora Mace on January 22 to 24, 2003.

**Appearances:** Judith Endejan, Attorney, Graham & Dunn, Seattle, Washington, represents Verizon. Gregory Trautman, Assistant Attorney General, Olympia, Washington, represents staff of the Washington Utilities and Transportation Commission (Commission Staff or Staff). Douglas N. Owens, attorney, Seattle, Washington, represents Qwest Corporation (Qwest). Brooks Harlow, attorney, Seattle, Washington, Miller Nash LLP, represents RCC Minnesota, Inc. (RCC).

**I. PROCEDURAL HISTORY**

Verizon is a telecommunications carrier that provides wireline telecommunications services in the State of Washington, subject to the jurisdiction of the Washington Utilities and Transportation Commission. Regulated intrastate telecommunications carriers such as Verizon are obligated to extend service pursuant to the provisions of WAC 480-120-071 ("line extension rule")<sup>2</sup>. The rule in its current form went into effect January 1, 2000.<sup>3</sup> This is the first contested case to test the waiver provisions of the new line extension rule.

On January 22, 2002, the Commission convened a prehearing conference in this docket at Olympia. The parties agreed to a schedule of proceedings that allowed them to address the question of whether or not Qwest should be made a party, as well as a schedule for evidentiary hearings.

On May 31, 2002, the Commission entered its Third Supplemental Order granting Commission Staff's motion to join Qwest as a party to the proceeding and establishing a revised schedule for hearing.

**KC REPLY APPENDIX 86**

\*2 On July 10, 2002, the Commission granted Qwest's motion to join RCC as a party and further revised the schedule of proceedings.

Evidentiary hearings took place before Chairwoman Marilyn Showalter, Commissioner Richard Hemstad, Commissioner Patrick J. Oshie and Administrative Law Judge Theodora M. Mace in Olympia on January 22, 23, and 24, 2003.

Verizon, Qwest, RCC and Commission Staff filed opening briefs on March 6, 2003. Commission Staff, Qwest and RCC filed response briefs on March 27, 2003. Verizon filed its response brief on March 28, 2003. Qwest and RCC filed reply briefs on April 3, 2003.

On April 3, 2003, Qwest also filed a Motion to Strike Portions of Staff's Response Brief. On April 10, 2003, Staff filed its response to the Motion.

## II. MEMORANDUM

**Background.** The issues now before the Commission are: 1) whether Verizon should be granted a waiver of the requirement to extend service to the Timm Ranch and the Taylor location; 2) whether Qwest and RCC should remain parties; and 3) if Qwest and RCC remain parties and Verizon is granted a waiver, whether either Qwest or RCC should be required to extend service.

WAC 480-120-071(2)(b) states that telecommunications companies that file tariffs with the Commission must extend service, upon application, to occupied premises. Verizon's waiver application requests that the company be relieved from providing service extensions to two different locations within its service territory, citing WAC 480-120-071(7)(a). This subsection of the rule provides that the Commission may determine whether an exchange company should be relieved of the obligation to provide service.

In its post-hearing Reply Brief, Verizon asserts that the Commission also has authority to grant the company a waiver of the extension requirement under the provisions of WAC 480-120-015(1). That provision addresses general exemptions from rules included in chapter 480-120 WAC.

**Discussion.** The first location for which Verizon seeks a waiver is called the Taylor location on the record.<sup>4</sup> At the Taylor location, in Verizon's Bridgeport Exchange in Douglas County, the applicants, including Mrs. Kay Taylor, live in three houses along Hayes Road, in a box canyon, approximately 14 miles from the town of Bridgeport. Mrs. Taylor requested service from Verizon on December 7, 2001. Other applicants in the canyon are Wendy Shomler and Ann Nichols. Three additional households located in the canyon have not, to date, requested service. Verizon asserts it would have to construct over 17 miles of new facilities to provide service to this location.

The second location, the Timm Ranch, consists of five residences along Timm Road on the Timm Ranch, in the portion of the Bridgeport exchange located in Okanogan County, bordering on the Columbia River. Mr. Ike Nelson initiated the first service request from this location on June 15, 2002. Verizon has received four other service requests from Billie Timm, Robert Timm, Brad Derting and Darrell Shannon. *Exhibit 171D at 9; Exhibit 121 T at 3-4*. Mr. Nelson is also constructing a new house on the ranch for himself. One of his sons will live in the old house. *Exhibit 171D at 13*. Mr. Nelson's family owns Timm Brothers Inc., which for 50 years has operated the 10,000-acre cattle ranch. The family also rents up to 100,000 acres for ranch purposes. *Exhibit 121 T at 4*. Verizon states it would have to construct approximately 30 miles of fiber cable to serve this location.

**A. SHOULD VERIZON'S REQUEST FOR A WAIVER OF THE LINE EXTENSION RULE BE GRANTED?**

\*3 Subsection (7)(a)<sup>5</sup> of the line extension rule gives the Commission authority to determine “whether any applicant for service is not reasonably entitled to service.” In determining “reasonable entitlement,” the Commission may consider the seven factors listed in subsection (7)(b)(ii) and “such other information that it may consider necessary to a proper determination.” The seven factors are:

- The total direct cost of the extension;
- The number of customers to be served;
- The comparative price and capabilities of radio communications service or other alternatives available to customers;
- Technological difficulties and physical barriers presented by the requested extensions;
- The effect on the individuals and communities involved;
- The effect on the public switched network;
- The effect on the company.

As is evident from the language of subsection (7)(a), this list is non-exclusive and non-mandatory. It is a list of factors likely to be at issue in a line extension, but not all of these factors will be significant in every case, and there may be other factors, not listed, that will be relevant in a particular case. The fundamental task before the Commission is to consider and weigh all relevant factors, in order to determine, under the rule and under RCW 80.36.090, whether an applicant is “reasonably entitled” to service from the local exchange company. We begin by considering the listed factors, as they apply to each location.

**1. The total direct cost of the extension.**

The line extension rule defines an extension of service as an extension of distribution plant to a location outside any municipal boundary and where no distribution plant of the extending company exists at the time an extension is requested. The extension must be constructed at the request of one or more applicants, and extend more than 1/10 of a mile. *WAC 480-120-071(1)*.

The rule further defines the “cost of service extension” as “the direct and indirect costs of the material and labor to plan and construct the facilities including, but not limited to, drop wire, permitting fees, rights-of-way fees, and payments to subcontractors, and does not include the cost of reinforcement, network upgrade or similar costs.” *WAC 480-120-071(1)*.

The rule contains no definition of the cost of reinforcement, but Commission Staff defines the cost as the expenditure required to shore up existing facilities in order to allow the company to construct an extension. *Exhibit 131T at 13*.

\*4 Verizon explains that, historically, line extension construction costs were allocated between the company and the customer so that the customer requesting an extension would bear a significant share of the costs. This allocation reflected a desire to avoid subsidies to individual customers by other existing customers. Under the new line extension rule, customers pay maximum initial and final payments of no more than 20 times their basic monthly service rate. *WAC 480-120-071(3)*. The company shoulders the rest of the cost but, under the rule, can request recovery of its direct and

indirect costs by means of filing a tariff to include a service-extension element on terminating access charges. *WAC 480-120-071(4)*.

**a. Timm Ranch.** Verizon states that it would have to extend its facilities 30 miles to reach the Timm Ranch, requiring installation of fiber optic cable and signal boosters. *Exhibit 1T at 7*. Approximately 23 miles of the construction would be along a dirt road and would constitute the longest loop in Verizon's Washington service territory with no other customers. *Id. at 10*. Verizon estimated the cost to build these facilities at \$881,497 or a per-customer cost of \$176,299.<sup>6</sup> *Id. at 5*. The facilities would serve the residences of each of the five applicants.

Staff estimates that the total direct cost to Verizon for building the Timm Ranch extension would be \$737,612, which Staff derives by excluding \$143,825 in reinforcement costs from Verizon's cost estimate. *Exhibit 131T at 14*. Staff calculates the per-customer cost for the Timm Ranch to be approximately \$123,000, based on the five current applications, plus the potential for service to the house soon to be built by Ike Nelson.

**b. Taylor Location.** Verizon estimates that it would cost \$329,839 to extend service to the Taylor location or a per-customer cost of approximately \$110,000.<sup>7</sup> *Exhibit 1T at 3, 5; Exhibit 3*. The company would have to lay copper cable for 15 miles along Highway 17 and two miles along Hayes Road in the canyon. Verizon contends that actual costs may be higher than the estimate because of the basalt rock in the area that might require the use of a backhoe or rock saw. *Exhibit 1T at 5-6*.

Staff estimates that it would cost Verizon \$165,015 to construct service to the Taylor location, derived by excluding \$164,824 from Verizon's cost estimate for reinforcement costs. Staff's per-customer cost is \$27,500, based on the fact that Verizon sized its estimate to accommodate six potential customers.

**\*5 c. Total Cost and Cost Considerations.** Verizon's estimate of the total cost to serve the two locations is \$1.2 million, or, \$150,000 per-customer. Staff estimates the total cost at \$902,687, or \$75,228 per-customer.

Verizon contends that its estimated cost is disproportionately high by any measure. Although Staff disputes the inclusion of reinforcement costs in deciding what is the appropriate direct cost, Verizon points out that Staff does not dispute the accuracy of the cost estimate itself. *T 618*. Verizon further complains that no Staff witness provided any guidance to the Commission as to what cost level would be too high, though clearly the line extension rule contemplates that some limit might be appropriate.

Verizon presented the testimony of Dr. Carl Danner to identify the overarching cost considerations that would help in determining the appropriate cost ceiling to be applied in line extension requests. Dr. Danner testified that the cost to society as a whole for these extensions is far greater than any offsetting benefit to the individual subscribers. Building such extensions uses up resources that could be used to provide service to a greater number of customers. It is economically reasonable, according to Dr. Danner, to expend such resources only when the product is more valuable than what is achieved by consuming them. *Exhibit 30T at 6, 12*. Dr. Danner also testified that the value of adding these customers to the network, also termed the "externality value," would be small compared to the cost of adding them. *Id. at 8-9; T 262-263*. Dr. Danner suggested that even a \$15,000-20,000 limit would be too high a cost for such extensions.

Verizon states that evidence of the low value of wireline service to these applicants is demonstrated by the fact that, ten years ago, when the applicants originally expressed an interest in obtaining wireline service, they were not willing to pay the costs of construction, which, at that time, were between \$23,000 and \$40,000. *Exhibits 565 and 566; Exhibits 171D at 13 and 172D at 16*. Verizon argues that nothing in the record allows a determination that the extensions would create \$150,000 of value for each applicant in this case.

Verizon compares the per-customer costs of these extensions to the average cost-per-customer of extensions built so far under the new rule -- \$10,000. *T 193*. The average length of line extensions built under the new line extension rule is 7,500 feet. *Exhibit 7T at 9*. The length of the Timm extension is 142,300 feet. The length of the Taylor extension is 42,600 feet. *Exhibit 4*. Verizon claims that the total cost of the extensions in this case equals 40% of its 2002 construction budget for the Wenatchee District.<sup>8</sup> *Exhibit 1T at 9*. The sheer length of the circuits involved invites higher maintenance costs. *Id. at 12-14*. When the facilities wear out, replacement costs will also be extremely costly. Moreover, Verizon is concerned that if demand for service at these locations lessens or disappears, all or part of the \$1.2 million in construction costs would be stranded investment.

\*6 Verizon further argues that the Commission should consider the total cost of construction, including reinforcement costs, because these would be the actual costs incurred by the company. Verizon disputes the Staff's position that reinforcement costs must be excluded from that consideration.

Verizon argues that it has not received any recovery in basic rates for reinforcement costs for line extensions such as those at issue in this case. Basic rates are intended to recover the costs of "normal reinforcement" related to typical extensions. Verizon estimates that the \$309,000 in reinforcement that Staff excludes could build 30 average line extensions. *Verizon Opening Brief at 18*.

Commission Staff points out that Verizon's calculation of cost-per-customer at these locations is overstated because Verizon undercounts the number of customers or potential customers. Staff believes it appropriate to divide the cost by the number of households that would be able to take service. *Staff Response Brief at 3*. On that basis the customer count would be six at each location. Staff further asserts that the proper cost estimates per-customer -- \$27,500 at the Taylor location and \$123,000 at the Timm Ranch -- are either below or on a par with the per-customer costs of other line extensions Verizon has constructed under the rule, such as the Cedar Ponds extension in the Sultan exchange. *Exhibit 214C*;<sup>9</sup> *Exhibit 215: Staff Opening Brief at 28*.

Commission Staff also defends the exclusion of reinforcement costs from the Verizon cost estimates. Staff argues that Order R-474 adopting the new line extension rule provided the context for concluding that reinforcement costs should not be considered in the waiver factors. *Order R-474 at ¶22*. According to Staff, the order indicated that each local exchange carrier must maintain, reinforce, and improve its network and that it receives funding for these efforts in its authorized rates. *Id. at ¶27*. If cost recovery for performance of these activities is inadequate, the carrier can request a rate increase. Staff asserts that reinforcement costs are considered a part of the company's ongoing business operations. *Id. at ¶43*.

Commission Staff contends that Verizon has failed to forecast growth at the Taylor and Timm locations and has failed to adequately reinforce its network in north central Washington. An example of this is the difficulty of customers in that area to obtain second lines from Verizon. *Exhibit 545 ¶2.1*. Staff further points out that Verizon says its facilities west of Foster Creek Ranch, near the Taylor location, are "at exhaust," or 100% in use. Thus, Verizon would have to reinforce up to Foster Creek in order either to construct a line extension or to serve one more applicant at Foster Creek Ranch.

\*7 Staff claims that Verizon does not state that it lacks funds for reinforcement. *T169*. Staff contends that Verizon believes the money it has received from ratepayers for reinforcement would be a loss to shareholders if invested in reinforcement. Staff argues that the Commission rejected the claim that a carrier should only be required to serve where it has an existing plan to add additional capacity in the near future or where it makes business sense to do so.<sup>10</sup>

Staff also argues that, in addition to reinforcement dollars Verizon receives in rates, Verizon also receives high-cost, or universal service, funding on a per-access-line basis in high-cost areas. Customers in high-cost areas receive supported service because the federal and state governments have determined that below-cost service should be provided in order to enhance universal service.<sup>11</sup> This funding includes a "fill" factor to allow for spare capacity to meet current demand

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plus an additional allowance for growth. *Docket No. UT-980311(a) Tenth Supplemental Order at ¶257*. Staff claims that Verizon receives such support based on the number of inhabited households served by Verizon at the time the Commission entered the Tenth Supplemental Order in that case. *Id. at 26-28; Exhibit 131T at 14*. Because households at the Taylor location and the Timm Ranch were inhabited at the time of the Tenth Supplemental Order in Docket No. UT-980311(a), Staff claims Verizon receives high-cost support specifically for extending service to the Taylor location and the Timm Ranch. Staff argues that to allow Verizon to recover reinforcement costs under these circumstances would constitute allowing the company a double recovery.

Staff disputes the effect of the Taylor and Timm Ranch extensions on the Wenatchee District construction budget. Staff maintains that Verizon has sufficient flexibility in its budgeting process to allow construction of the extensions, since for 2000 it overspent its budget by \$19 million. *Exhibit 111T at 2*. Moreover, Verizon would be able to recoup its construction costs, less reinforcement, within one year under the rule.

Finally, Staff contends that because Verizon requested a line extension rule waiver under subsection (7)(a), rather than under subsection (7)(b), the Commission should not give primary weight to the cost of a line extension in deciding this case. Staff suggests that a waiver under (7)(a) means that applicants are not reasonably entitled to service whether they pay any or all of the cost of service. Under (7)(b), construction would still be required but Verizon could charge an applicant the direct cost if the Commission found it unreasonable to recover the cost from ratepayers under subsection (4) of the rule. Staff claims that a waiver under (7)(a) might deny service to future purchasers of property. The total direct cost and the number of customers served plays a far more important role in considering the seven waiver factors under (7)(b) than under (7)(a) because the issue is who should bear the cost of what is built.

\*8 Verizon contends that the reinforcement costs Staff excludes would only arise because of the Timm Ranch and Taylor location line extensions. *T 199-202*. Verizon points out that Staff states it would allow Qwest to recover reinforcement costs if Qwest built the Timm Ranch extension, because Qwest could not have planned to serve that location. However, Verizon asserts that neither did Verizon plan to serve that location. Also, with regard to the capacity of Verizon's facilities to the Foster Creek Ranch, Verizon contends it has technologies available, when actual cable is at exhaust, to allow it to expand capacity without reinforcement if there is plant within a certain distance of a central office. Foster Creek is within the required distance; the Taylor location is not. Thus, Verizon would need to expend money for reinforcement to extend service to the Taylor location that would not be required to expand existing service to Foster Creek.

Verizon claims that the requested line extensions would not serve "normal demand," because they represent applications that arose as a result of the new line extension rule. The new rule resulted in increased demand and increased costs for such construction. In 2001 Verizon built 85 projects under the new rule. *T 192*. These increased costs could not have been factored into ratemaking that occurred prior to the new rule. *T 266*. Verizon argues that rates set in 1999 to recover the revenue requirement at that time could not have taken into account the effect of the new rule which became effective in 2000. Verizon further argues that the cost models used and rates set in the universal service docket, UT-980311(a), merely constituted a reallocation of existing revenue levels that were established based on embedded costs, and did not create any new money for network improvement or extension. *Exhibit 32T at 17-19*. Verizon argues it would not obtain any additional universal service recovery as a result of the new line extensions. *T 453*.

Verizon rejects Staff's contention that the company should construct these extensions because it has already built more-expensive line extensions such as Cedar Ponds, for which Verizon sought recovery under the new rule. Verizon asserts that the company built the Cedar Ponds extension prior to the new rule, and under pressure from Staff. Verizon only requested recovery for Cedar Ponds under section (4) of the new rule because Staff suggested it do so. Verizon also notes that its experience with the Pontiac Ridge extension demonstrates that Staff's method of counting customers at each location in this case is suspect. Verizon built the Pontiac Ridge extension based on 44 applications for service, but now serves only 37 lines there. *Exhibit 7T at 15*.

**2. Number of customers to be served.**

As discussed above, Verizon and Staff have divergent views about the proper method of counting number of customers to be served at each location. Verizon counts only the number of actual applications—eight—for the two locations. Staff counts twelve—the number of potential customers at both locations.

**3. The comparative prices and capabilities of radio communications service or other alternatives.**

\*9 Verizon argues that both the Timm Ranch and the Taylor location applicants have access to wireless or radio communications services. The availability of such services makes the provision of wireline service, if not superfluous, certainly not as urgent a need as Staff portrays. At the Timm Ranch, Ike Nelson has radiophone service at his residence which functions like a wireline phone. He extends a line to a residence across the Columbia River, which gives him a dial tone from Qwest's Coulee Dam exchange. *Exhibit 1T at 5; Exhibit 171D at 25*. All of the applicants at the Timm Ranch have Verizon Wireless service but they are unable to receive signal at their homes. They have to drive some 2-3 miles to get a signal. *Exhibit 171D at 23*. Mr. Nelson pays \$65 per month for the two wireless phones he has from Verizon Wireless. *Id. at 24*.

At the Taylor location, the Taylor residence has stationary cell service from Americell Communications, which provides a connection to emergency services. *Exhibit 172D at 22*. Mrs. Taylor also has wireless service from AT&T, which she uses in conjunction with her business. The Taylors pay \$8,000 per year for their wireless service, which includes business use. *Id. at 41-42*. Mrs. Taylor co-owns a janitorial service in Grand Coulee, 28 miles from her home. The Taylors also have DirecTV satellite service available to them at \$79 per month. *Id. at 5-13*.

RCC has installed phone cell<sup>12</sup> service at both the Taylor residence and the Nelson residence on a trial basis. RCC's tests showed that both the Taylor and Shomler residences receive phone cell signal through RCC at the Taylor location. The Ike Nelson and Bob Timm residences receive signal at the Timm Ranch. Although RCC installed the service gratis at the Taylor and Nelson residences for purposes of testing it for this case, it normally costs \$1,200 to install. *Exhibit 91T at 11; T 307-308; Exhibit 171D at 15*.

Staff contends that the wireless alternatives available to the applicants do not provide "reasonably comparable service at a reasonably comparable price compared to wireline in the area." *WAC 480-120-071(2)(c)*. None of the wireless services used by the applicants is as reliable as landline. The Timm Ranch applicants cannot obtain wireless signal at their residences. The radiophone at the Nelson residence is subject to the risk of lightning damage. Mr. Nelson must make a 140-mile trip to troubleshoot problems with the line. *Exhibit 131T at 20; 171D at 25*. The Taylors' wireless service suffers from static on the line. *Exhibit 172D at 22, 33*. Staff asserts that the quality of their wireless service may have been an issue in the death of Mrs. Taylor's father-in-law when she failed initially to reach 911 by using her wireless phones. *Exhibit 140T*.

\*10 Staff points out that RCC phone cell service would not be adequate because it would not serve all the applicants at each location. *Exhibits 91T at 8-9; 101T at 5*. Also, the industry standard for the RCC service is more lenient than wireline. *Exhibit 91T at 3*. For example, at the Timm Ranch, there has been sporadic trouble and static on the line. *Exhibit 309*. Staff also mentions that none of the applicants have requested service from RCC.

Verizon responds that it is a myth that existing wireless service is not a reasonable substitute for wireline. There is no evidence that either Mrs. Taylor or Mr. Nelson would give up their wireless service if wireline were installed. In fact, at the ranch, wireless would be beneficial for calling while out on the ranch property, whereas wireline cannot serve that function. Nor was there any evidence that any of the applicants could not afford the wireless service they purchased.

Finally, comparing the price of wireline with the price of wireless presents difficulties due to the variability of wireless calling plans, which often include the ability to make unlimited long distance calls for a flat monthly fee.

**4. Technological difficulties and barriers presented by the requested extensions.**

Verizon contends that the distances involved and the nature of the terrain in the areas to be served present various technological difficulties and barriers. Verizon predicts that it would require 4,300 man-hours of work to construct the extensions due to these conditions. *Exhibit 1T at 11-13*. The existence of basalt rock would make excavation difficult, and possibly more expensive than original estimates. The presence of the Columbia River would require Verizon to serve the Timm Ranch out of the Brewster exchange, even though the ranch is in the Bridgeport exchange. *T 132, Exhibit 1T at 7*. The residences at the ranch are situated along a dirt country road not maintained in winter. Lack of winter maintenance would increase the personnel required to detect problems. There are potential hazards from bad weather, vandalism, wildfire, mechanical breakdown, damage from wild animals and livestock. Even though these types of conditions exist throughout the Wenatchee district, most extensions are not as lengthy as the ones proposed here.

Staff says that Verizon has not shown that there are any barriers different from those commonly faced in the Wenatchee district. *T 130-132*. Staff notes that Verizon complains about unplowed roads, yet the company places cross-country wire at various locations in Washington. *131T at 26*. Staff contends that a new rule, WAC 480-120-440, which will become effective July 1, 2003, will give telephone companies more time to repair outages and will alleviate some of the pressure on Verizon regarding maintenance of the extensions in this case. Finally, Staff claims that although the proposed Timm Ranch loop would be 23 miles long without other customers, there are thousands of loops in Washington that are 20 to 40 miles in length. *Exhibit 111T at 3; T470*. On cross examination, however, Staff witness Shirley indicated that he knew of no other loops in Washington which stretched for 23 miles without any customers. *T 563*.

**5. The effect on individuals and communities involved.**

\*11 Verizon suggests that one effect of building line extensions for the applicants in this case is that they will experience a financial windfall and their property values will increase significantly. Verizon contends the Taylors have lived at their current location for 28 years without wireline. The evidence shows that their wireless service enables them to maintain contact with their community of interest, Grand Coulee, where Mrs. Taylor has her business.

Verizon claims that wireline would provide an additional benefit to Timm Bros. Inc., because the primary use of the line extension would be for ranch business. *Exhibit 171D at 26*. Verizon notes that the line extension rule definition of "premises" includes farmhouses, but does not include predominantly commercial or industrial structures. *WAC 480-120-071(1)*. Verizon contends that a line extension to the Timm Ranch would create a subsidy to the already substantial commercial cattle operation located there. Furthermore, a grant of the waiver would not have a negative effect—the ranch has been successful with the type of telecommunications service it has procured to date. Several individuals have lived there for some time and all built and retained their connections to communities nearby and to the larger world of cattle ranching. *Exhibit 171D at 24*.

Finally, Verizon observes that the nearby Nespelem Valley Electrical Cooperative provides a \$1,500 credit towards extension of an electrical line. After that, the customer must pay \$7 per foot toward the construction costs.

Staff responds that just because the Taylor and Timm Ranch applicants have been without wireline service for many years does not mean they would not benefit from that service. To say that they moved to a rural area with no expectation of having wireline service is true of everyone who applies for an extension. Mrs. Taylor would benefit by a more reliable connection to 911 because she frequently cares for her grandchildren. Her current service was unable to provide her with a timely connection to 911 when her father-in-law died. *Exhibit 172D at 29-30; T 568*.

As for Mr. Nelson, wireline would help him both personally and in his business; would provide access to the internet; would allow him contact with his children in college. *Exhibit 171D at 25-26*. He would be able to participate more fully in the community. *Exhibit 590; T 717*. The line extension definition of "premises" deliberately includes farmhouses because they are to some extent both business premises and residences. As Staff witness Duft pointed out, the location of a ranch or farm is dictated by the nature of its activities and the blending of business and personal is required.

Verizon contends that ratepayers and Verizon should not subsidize a large-scale agricultural operation like the Timm Ranch on the basis that it can't be located in a populous or urban area. Verizon points out that numerous commercial enterprises are place-bound and still would not be eligible for subsidized line extensions.

#### **6. The effect on the public switched network.**

\*12 Verizon argues that eight new customers would add only a de minimus value to other subscribers on the network at a disproportionately high cost. *T 262-263*. The extraordinary costs involved would deplete resources to maintain the existing network and to expand the network in response to projected demand and growth. *T 201*.

Staff questions whether this criterion refers to the proper use of funds to maintain and build the network, or to technical interference in the network caused by an extension of service. If the latter, Verizon has offered no evidence to indicate that the extensions should not be built. Staff argues that the marginal cost of adding an individual customer will often be greater than the marginal benefit. The state and federal government have recognized the need for subsidized service in high cost areas.

#### **7. The effect on the company.**

Verizon states that it has complied with the new line extension rule as evidenced by its construction of 85 line extensions since the rule became effective. Verizon points out that prior to the new rule, Verizon constructed one or two line extensions per year. *T 192*. Although the new rule has increased the number of extensions, Verizon has kept pace. However, Verizon contends that the extraordinary cost of the requested extensions in this case caused it to file for a waiver, due to the potential adverse effect of the projects on ratepayers and the company.

As noted above, Verizon objects to the fact that 40% of its Wenatchee District construction budget for 2002 would be absorbed by the projects. Verizon further objects to the exclusion of \$309,000 in what Staff terms reinforcement costs from the amount it would recover under the rule. *T 200-201; Exhibit 217C; Exhibit 7T at 7-8*. Verizon argues that it would not recover these reinforcement costs in basic rates or through universal service funding. *Bench Request Exhibit 800*.<sup>13</sup> If the potential customers at the Taylor or Timm Ranch location drop their wireline service, or fail to make applications in the numbers Staff predicts, Verizon will end up with stranded investment. Verizon claims it is making less than a 2% rate of return currently and cannot afford to absorb either the reinforcement costs proposed by Staff or the stranded investment that may result from these projects.

Staff reiterates its arguments that Verizon's reinforcement costs, as Staff defines them, should not be considered as a factor in whether to grant a waiver. Verizon chose not to invest in developing facilities in north central Washington, making reinforcement a necessity in order to extend service to the two locations at issue here. The Commission has rejected past requests by carriers to be relieved of the duty to extend service based on "business reasons." *Docket No. UT-961638*. Verizon already receives in base rates cost recovery for reinforcement expenses. *Exhibit 131T at 13*. Verizon also receives \$33 million in high-cost funding that includes support for the construction of these two specific projects. *UT-980311(a); Exhibit 131T at 14*.

## **8. Discussion and Decision.**

\*13 Based on its review of all relevant factors, the Commission grants Verizon's request for a waiver. Relative to the number of customers, the cost of each project, including future maintenance costs, is extraordinarily high. The Commission does not adopt Staff's view that the company's reinforcement costs must be ignored in coming to a final decision. Subsection (7)(a) of the rule permits the Commission to consider other matters necessary to reach a decision about granting a waiver. In this case, Verizon would be required to make significant expenditures to improve its existing facilities so as to make them capable of accommodating the proposed line extensions. Absent the line extension requests, there is no evidence Verizon would need to make such expenditures.

Verizon witness Danner's testimony convincingly calls into question the value of adding so small a number of customers to the network, whether it be Staff's count of twelve or Verizon's count of eight, compared to the cost in money and resources that would be expended, and in light of available alternatives. Staff's argument that Verizon and Qwest have both constructed similarly costly extensions under the new rule begs the question whether extensions of such high cost should be permitted under the rule. The provisions of the rule clearly contemplate that, in conjunction with other factors, some cost level might prove too high. Staff's refusal to acknowledge any realistic figure that might be "too high" is inconsistent with the "reasonableness test" of RCW 80.36.090 and WAC 480-120-071(7).

Commission Staff's argument that Verizon's waiver request under Subsection (7)(a) precludes giving substantial weight to the cost of a project is unpersuasive. Subsection (7)(a) clearly anticipates Commission discretion to consider cost and to give cost the weight proper to achieve a balance of all the factors involved in reaching a decision.

The Commission is also persuaded that the comparative price and capabilities of the available alternative technologies dictate in the direction of a waiver in this case. Commission Staff's argument that wireless service cannot be considered unless it provides "reasonably comparable services at reasonably comparable prices" compared to wireline is incorrect. The requirement Staff cites is derived from section (2) of the line extension rule and pertains to the circumstance of a company required to extend service that undertakes to provide that service through a service or financial agreement with a wireless company. The language of the section (7) waiver provision only indicates the Commission may consider the comparative price and capabilities of wireless or other alternatives in deciding whether to grant a waiver. Staff's view here begs the question of what is reasonable in the first instance. There is no provision of federal or state law that prescribes that every location and every potential customer, no matter how remote or expensive to reach by wireline, is entitled to wireline service. We do not read the "reasonableness" test of our state law, RCW 80.36.090, to be inconsistent with a requirement for "reasonably comparable services at reasonably comparable prices."

\*14 Considering the effects of a waiver on the individuals involved, it is of course true that wireline would give them an additional mode of communication. But in view of the communications alternatives available to them, and the comparative costs discussed above, we find that the advantages of wireline do not outweigh other, counterbalancing factors. Nor do we think the nearest communities will be significantly affected.

However, the Commission is persuaded that there would be a potentially significant adverse effect on the company and other ratepayers if a waiver is not granted. A denial of the waiver would send the signal that extraordinarily costly line extensions to serve few customers are warranted under the new rule. This in turn would make it increasingly difficult for carriers to devote resources to their existing network and would create an unreasonable increase in the subsidies paid by other ratepayers. It would increase maintenance costs and burdens for which carriers either would not obtain cost recovery or would have to seek recovery from other ratepayers. It would increase the possibility of stranded investment if other alternative technologies, such as wireless, erode wireline business.

Nothing in the language of this subsection, or of the rule as a whole, would preclude later applications for service from residents at the Taylor location or the Timm Ranch if circumstances change from those presented in this case. If

circumstances change, for example, more residents move into the area, or cost-saving innovations develop, a future line extension may prove to be appropriate. For now, however, taking into consideration and carefully balancing all relevant factors, we find that Verizon's waiver request is appropriate.

Accordingly, we grant Verizon's request to waive WAC 480-120-071(2)(a), with respect to both the Taylor and Timm Ranch locations.

**B. SHOULD VERIZON BE GRANTED A WAIVER OF THE  
LINE EXTENSION REQUIREMENT UNDER WAC 480-120-015?**

In light of the Commission's determination to grant Verizon a waiver under the more specific waiver provision relating to line extensions, the Commission need not address Verizon's request for relief under the general waiver provision.

**C. SHOULD THE COMMISSION DISMISS QWEST AS A PARTY TO THE PROCEEDING?  
SHOULD THE COMMISSION REQUIRE QWEST TO SERVE THE TIMM RANCH?**

Commission Staff initially sought to join Qwest because Staff viewed Qwest as a potential alternative provider of service to the Timm Ranch. Staff argued that Qwest's facilities are nearer the Timm Ranch than Verizon's facilities. In the event Verizon were granted a waiver, Staff asserted that, if Qwest were a party, the Commission could examine whether Qwest might serve the Timm Ranch, which would involve redrawing the exchange boundaries between Verizon and Qwest.

Over Qwest's objection in this case, the Commission granted Staff's motion and joined Qwest as a party to the proceeding, noting that:

\*15 While it is not clear whether and how this authority should be invoked in this proceeding, Qwest has a significant stake in the outcome since it bears a common exchange boundary with Verizon near the Timm Ranch, its facilities are closer to the Timm Ranch than Verizon's and Staff alleges that Qwest's costs to extend service to the Timm Ranch would be less than Verizon's. Thus, to protect its interests under Civil Rule 19, *supra*, Qwest is properly made a party to this proceeding. *Third Supplemental Order at 7.*

In Commission Staff's original motion to join Qwest, Staff stated that: "Staff may ultimately recommend that the Commission adjust the Qwest and Verizon exchange area boundaries...and may also recommend that the Commission require Qwest to provide service to the Nelson property." *Motion of Staff to Join Qwest as a Party Respondent at 2.* However, no formal motion was made by any party to redraw the boundaries. In light of the evidence amassed thus far, we decline, on our own motion, to initiate a boundary revision, as Qwest's costs appear to be on the same order of magnitude as Verizon's. For purposes of evaluating Verizon's request for waiver, it was necessary and appropriate for Qwest to be joined and provide evidence. For that reason, we re-affirm our decision to join Qwest and deny Qwest's motion to vacate the Third Supplemental Order. Qwest has no further obligations in this docket, however, and we now dismiss Qwest from the proceeding.

**D. SHOULD THE COMMISSION DISMISS RCC AS A PARTY TO  
THIS PROCEEDING AND FUTURE SIMILAR PROCEEDINGS?**

Similar to Qwest, RCC was a necessary party at the outset of and during this hearing. Just as Qwest did, RCC provided valuable information and arguments regarding the issues in this case of first impression and was an integral part of the proceeding. However, no party, nor the Commission, seeks any further action be taken by RCC. Therefore, RCC is now dismissed from the proceeding. It is premature to take any action on RCC's request that it not be joined to future proceedings under the line extension rule's waiver provisions.

**E. SHOULD THE COMMISSION GRANT QWEST'S MOTION  
TO STRIKE PORTIONS OF STAFF'S RESPONSE BRIEF?**

Since Qwest has been dismissed from the case, Staff's Response Brief (even considering the contested portions) with respect to Qwest is moot, as is Qwest's motion to strike.

**III. FINDINGS OF FACT**

Having discussed in detail both the oral and documentary evidence concerning all material matters inquired into, and having previously stated findings and conclusions based thereon, the Commission now makes the following summary of the facts. The portions of the preceding detailed findings and the discussion pertaining to the ultimate facts are incorporated herein by this reference.

(1) The Washington Utilities and Transportation Commission is an agency of the State of Washington vested by statute with the authority to regulate rates, rules, regulations, practices, accounts, securities, and transfers of public service companies, including telecommunications companies that have reached the appropriate jurisdictional threshold.

\*16 (2) On January 1, 2000, WAC 480-120-071, the Commission's current rule relating to service extensions, became effective.

(3) WAC 480-120-071(7) gives the Commission the authority to waive the requirement that a service extension be constructed.

(4) WAC 480-120-015 gives the Commission authority to grant exemptions from any rule in the chapter based on a showing of undue hardship.

(5) Verizon is a public service company subject to the jurisdiction of the Commission.

(6) Qwest is a public service company subject to the jurisdiction of the Commission.

(7) On May 31, 2002, the Commission joined Qwest as a party to the proceeding.

(8) RCC is a Commercial Mobile Radio Service (CMRS) provider authorized by the Commission on August 14, 2002 to be an Eligible Telecommunications Carrier (ETC) serving the exchange areas material to this case.

(9) On July 10, 2002, the Commission joined RCC as a party to the proceeding.

(10) Verizon is the local exchange carrier whose exchange boundaries currently include both the Timm Ranch and the Taylor location.

(11) Qwest's current exchange boundaries do not encompass either the Timm Ranch or the Taylor location.

(12) The Commission's authority to prescribe exchange boundaries for telecommunications companies under its jurisdiction is contained in RCW 80.36.230.

(13) On December 7, 2001, Kay Taylor requested that Verizon extend wireline service to her residence on Hayes Road in Verizon's Bridgeport Exchange.

**KC REPLY APPENDIX 97**

- (14) Since December 7, 2001, two additional residents on Hayes Road have requested that Verizon extend service to them.
- (15) On June 15, 2002, Ike Nelson requested that Verizon extend wireline service to his residence at the Timm Ranch in Verizon's Bridgeport Exchange.
- (16) Since June 15, 2002, four other applicants have requested that Verizon extend service to them at the Timm Ranch.
- (17) The total cost estimate for a Verizon extension of wireline service to the Taylor location on Hayes Road is \$329,839.
- (18) Verizon would have to install 17 miles of copper cable to extend service to the Taylor location.
- (19) The total cost estimate for a Verizon extension of wireline service to the Timm Ranch applicants is \$881,497.
- (20) Verizon would have to install 30 miles of facilities to extend service to the Timm Ranch.
- (21) The per-customer cost for Verizon's Taylor location extension is \$27,500.
- (22) The per-customer cost for the Timm Ranch extension is \$123,000.
- (23) The total cost estimate for Qwest to provide service to the Timm Ranch applicants is \$811,920.
- (24) The average cost of new line extensions built by Verizon under WAC 480-120-071 is \$10,000.
- (25) The cost estimate for RCC to build additional communications towers to serve both locations is between \$400,000 and \$1.5 million.
- \*17 (26) Verizon and Qwest would each be able to recover part of their costs of construction by means of a temporary access charge tariff pursuant to provisions of WAC 480-120-071.
- (27) RCC, since it is not a wireline carrier, would not be able to recover any of its cost of construction pursuant to the new line extension rule.
- (28) Wireless telephone service is available at both the Taylor location and the Timm Ranch.
- (29) Kay Taylor pays approximately \$8,000 per year for wireless phone service from two different wireless companies and part of that cost is associated with her business use of the phone.
- (30) Ike Nelson pays approximately \$65 per month for the wireless phone service he receives.
- (31) Both Mrs. Taylor and Mr. Nelson have access to emergency services through use of their current wireless phone alternatives.
- (32) RCC installed phone cell devices at both the Taylor residence and the Nelson residence.
- (33) RCC phone cell service costs approximately \$1,200 per installation.
- (34) RCC phone cell devices receive a signal acceptable in the CMRS industry at two residences in the Taylor location and at two residences on the Timm Ranch.

## KC REPLY APPENDIX 98

(35) Verizon and Qwest would each experience increased maintenance expenses to service the line extensions to each location.

(36) Verizon's extension to the Timm Ranch would involve building a 23-mile loop, which would have no other customers, the longest of its kind in Washington.

(37) The construction costs that Verizon or Qwest could not recover under the new rule represent funds that could potentially be used to connect a larger number of customers to the network.

(38) The construction costs to build extensions to the Taylor location and the Timm Ranch will deplete Verizon's ability to provide maintenance service and network upgrades for other customers.

(39) Taking into consideration all the factors identified in the line extension rule waiver provisions, the Taylor location applicants and the Timm Ranch applicants are not, at this time, reasonably entitled to Verizon wireline service.

(40) No party requests that the Commission order RCC to build new facilities to provide service to the applicants in this case.

#### IV. CONCLUSIONS OF LAW

Having discussed above in detail all matters material to this decision, and having stated general findings and conclusions, the following provides summary conclusions of law. Those portions of the preceding detailed discussion that state conclusions pertaining to the ultimate decisions of the Order are incorporated by this reference.

(1) The Washington Utilities and Transportation Commission has jurisdiction over the parties to, and subject matter of, this proceeding.

(2) The Commission has authority to grant a waiver of the requirement that a telecommunications company extend service to an applicant.

(3) Verizon's request for a waiver under WAC 480-120-015 is moot.

\*18 (4) The eight applicants in this case are not reasonably entitled to service from Verizon. The Commission should grant Verizon's waiver request.

(5) Qwest should be dismissed as a party to this proceeding.

(6) RCC should be dismissed as a party to this proceeding.

(7) The Commission should retain jurisdiction over the subject matter of and the parties to the proceeding to effectuate the provisions of this Order.

#### V. ORDER

Based on the above findings of fact and conclusions of law, the Commission enters the following Order.

(1) The Commission has jurisdiction over the subject matter of and the parties to this proceeding.

## KC REPLY APPENDIX 99

(2) Verizon's petition for a waiver under WAC 480-120-071(2)(a) is granted.

(3) Qwest's motion to vacate the Commission's Third Supplemental Order and Fifth Supplemental Orders is denied.

(4) Qwest is dismissed as a party to this proceeding.

(5) RCC is dismissed as a party to this proceeding.

Dated at Olympia, Washington, and effective this \_\_\_\_ day of April, 2003.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

MARILYN SHOWALTER, Chairwoman

RICHARD HEMSTAD, Commissioner

PATRICK J. OSHIE, Commissioner

**NOTICE TO PARTIES: This is a final order of the Commission. In addition to judicial review, administrative relief may be available through a petition for reconsideration, filed within 10 days of the service of this order pursuant to RCW 34.05.470 and WAC 480-09-810, or a petition for rehearing pursuant to RCW 80.04.200 or RCW 81.04.200 and WAC 480-09-820(1).**

#### APPENDIX B

##### UT-011439 Analysis of Cost Estimates

Party Proposing	Taylor	Timm Ranch	Total
Verizon/Ruosch	\$329,839	\$881,497	\$1.2 million
March 2, 2002 at 5 (Verizon costs)	(17 miles) 3 customers	(30 miles) 5 customers	
	\$110,000/customer	\$176,000/customer	\$150,000/customer
Qwest/Hubbard		\$811,920	\$811,920
July 5, 2002 at 5 (Qwest's costs)			
RCC/Huskey	\$150,000-	\$250,000	
91T at 10-11 (RCC's costs)	\$1 million	\$500,000	\$1.5 million
Staff (Verizon)	\$165,015	\$737,672	\$902,687
131T at 14	(excl. \$164,824 reinf.)	(excl. \$143,825 reinf.)	

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(Verizon's costs)	6 customers	6 customers	
	\$27,500/customer	\$123,000/customer	
Staff		\$435,365	\$435,365
(Qwest's costs)		(excl. \$376,556 reinf.)	

Other Cost Analysis

**Danner Threshold:** **\$10,000-15,000**

**Cost per mile of construction:**

1) Verizon historic ave. cost of construction/buried cable	\$31,710 per mile
2) Timm Ranch buried cable line extension cost	\$29,383 per mile
3) Historic cost for aerial line	\$25,805 per mile
4) Nelson aerial line cost estimate	\$19,402 per mile

Footnotes

- 1 A copy of WAC 480-120-071 is attached to this Order as Appendix A.
- 2 WAC 480-120-071 requires companies to extend service to "reasonably entitled" applicants within 18 months of a request. Under the rule, an "extension of service" is an extension of distribution plant beyond the company's existing distribution plant. The rule provides for voluntary cross-boundary extensions of service; allocation of construction costs between applicant and company; a means by which the company may recover some of its share of construction costs from other ratepayers; and a provision allowing companies to request a waiver of the requirement to extend service.
- 3 *Order Amending and Adopting Rule Permanently*, General Order No. R-474, Docket No. UT-991737 ("Order R-474").
- 4 Commission Staff also refers to this as the Hayes Road location.
- 5 Subsection (7)(a) allows for a waiver of the subsection (2)(b) requirement that service be extended to occupied premises. Subsection (7)(b) permits petitions for waiver of subsection (3)(a) and allows a company to build an extension but charge the applicants for all or part of it, if shifting the cost to other ratepayers is found unreasonable.
- 6 Appendix B to this Order is a chart summarizing the cost testimony in the record. Verizon contends there are only five applicants at the Timm Ranch.
- 7 Verizon argues that there are only three actual applicants for service at the Taylor location. Verizon's cost estimates include facilities that could potentially serve six households in the canyon. *T 130*.
- 8 Verizon's Wenatchee District covers approximately 4,500 square miles in north central Washington, extending from Wenatchee to the Canadian border. The District consists of twenty exchanges with a total of approximately 78,000 access lines. *Exhibit 1T at 1*.
- 9 During the hearing, Verizon stated that the numbers in the "Total" column on the last page of Exhibit 214C were not confidential. *T 149*.
- 10 *WUTC v. U S West Communication, Inc.*, Docket No. UT-961638, Fourth Supplemental Order Rejecting Tariff Filing, January 16, 1998 at 15-21. ("*Fourth Supplemental Order*").
- 11 47 USC 254; RCW 80.36.300; *WITA v. WUTC* (Wash. Sup. Ct.) (March 6, 2003 Slip Opinion).
- 12 A phone cell is a "hybrid cellular system packaged with a dial tone emulator. It uses a base station that receives the cellular signal like a typical cell phone, then converts that signal into a noncellular signal like a standard telephone line." *Exhibit 91T at 6*.
- 13 Bench Requests 800 and 801 are admitted in evidence.

**BEFORE THE WASHINGTON STATE  
UTILITIES AND TRANSPORTATION COMMISSION**

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION,	)	DOCKETS UE-090134 and UG-090135 (consolidated)
Complainant,	)	
	)	
v.	)	ORDER 10
	)	
AVISTA CORPORATION, d/b/a AVISTA UTILITIES,	)	
Respondent.	)	
	)	
.....	)	
	)	
In the Matter of the Petition of	)	DOCKET UG-060518 (consolidated)
	)	
AVISTA CORPORATION, d/b/a AVISTA UTILITIES,	)	ORDER 10
	)	
For an Order Authorizing Implementation of a Natural Gas Decoupling Mechanism and to Record Accounting Entries Associated With the Mechanism.	)	FINAL ORDER REJECTING TARIFF FILING; APPROVING AND ADOPTING MULTI-PARTY PARTIAL SETTLEMENT STIPULATION; DEFERRING LANCASTER COSTS; EXTENDING DECOUPLING MECHANISM; AUTHORIZING TARIFF FILING; AND REQUIRING COMPLIANCE FILING
	)	
.....	)	

1 ***Synopsis:** The Commission rejects revised tariff sheets Avista Corporation (Avista) filed on January 23, 2009, but authorizes and requires the Company to file tariff sheets that will result in increases of about 2.8 percent for electric rates and 0.25 percent for natural gas rates, which are found on the record of this proceeding to be fair, just, reasonable and sufficient. In approving these rate increases, the Commission approves and adopts a Multi-Party Partial Settlement Stipulation filed by the parties to this general rate case that resolves the overall cost of capital, the majority of power supply costs, and various other issues. Among several contested*

*issues, the Commission denies the Company's proposed pro forma adjustments that are not demonstrated to be known and measurable and not offset by other factors, but accepts many proposed by Commission Staff. Further, the Commission authorizes Avista to defer its costs associated with the Lancaster power purchase agreement for possible later recovery, determining that Avista failed to make various factual and other showings that are prerequisite to immediate inclusion of such power costs in rates. These include failure to make the requisite showing of a binding agreement to purchase the power from the Lancaster plant, failure to make the required affiliated interest filing in compliance with RCW 80.16, and failure to demonstrate that this new power purchase agreement complies with the greenhouse gas emissions limits in RCW 80.80. Accordingly, the Commission will consider the recovery of the Lancaster costs in a later proceeding once those prerequisite showings have been made. In addition, we decline the Company's request to prematurely terminate the energy recovery mechanism (ERM) surcharge. Finally, the Commission approves a continuation of Avista's decoupling mechanism, with modifications including a lower maximum deferral rate of recovery for lost margins.*

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SUMMARY

2 **PROCEEDINGS:** On January 23, 2009, Avista Corporation d/b/a Avista Utilities (Avista or Company) filed with the Washington Utilities and Transportation Commission (Commission) revisions to its currently effective Tariff WN U-28, Electric Service in Docket UE-090134, and revisions to its currently effective Tariff WN U-29, Gas Service in Docket UG-090135. The revisions proposed a general rate increase of \$69.8 million, or 16.0 percent, for electric service and \$4.9 million, or 2.4 percent, for gas service. Avista also proposed to decrease the current Energy Recovery Mechanism surcharge by \$32.4 million, or 7.4 percent, resulting in an overall net increase of 8.6 percent for electric rates. The Company also sought to increase its overall rate of return from 8.22 percent to 8.68 percent. The Commission suspended the filings on February 3, 2009, prior to their stated effective date of February 23, 2009, and set the matter for hearing in October 2009. *Order 01* and *Order 02*.

3 On April 30, 2009, Avista filed a petition to consolidate Docket UG-060518, which addresses its pilot natural gas decoupling mechanism, with the rate case proceedings. As part of its petition, the Company asked the Commission to extend the pilot program beyond its scheduled termination date of June 30, 2009. On May 15, 2009, the Commission consolidated the decoupling issue into the general rate cases. *Order 06*. Shortly thereafter, on June 30, 2009, the Commission granted an interim extension of Avista's existing pilot decoupling mechanism but deferred a full evaluation of the program until the October 2009 evidentiary hearings. *Order 07*.

4 On August 17, 2009, Commission Staff, the Public Counsel Section of the Washington Office of Attorney General (Public Counsel) and the intervening parties filed their respective response testimonies.<sup>1</sup> Staff opposed a number of the Company's restating and pro forma adjustments as well as the Company's proposed

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<sup>1</sup> In formal proceedings, such as this, the Commission's regulatory staff participates like any other party, while the Commissioners make the decision. To assure fairness, the Commissioners, the presiding administrative law judge, and the Commissioners' policy and accounting advisors do not discuss the merits of this proceeding with the regulatory staff, or any other party, without giving notice and opportunity for all parties to participate. *See RCW 34.05.455*.

rate of return. Staff recommended smaller increases in annual revenues: \$20.1 million for annual electric revenue and \$281,000 for annual natural gas revenue. Public Counsel opposed many of the same adjustments criticized by Staff and also opposed Avista's proposed inclusion in rates of the costs of a power purchase agreement (PPA) to acquire the power from the existing Lancaster Generation Facility, a combined-cycle natural gas-fired power plant located near Rathdrum, Idaho.<sup>2</sup> Further, Public Counsel and the Industrial Customers of Northwest Utilities (ICNU) jointly opposed the Company's proposed rate of return. Public Counsel recommended a \$12.8 million reduction from currently approved annual electric revenue and a \$431,000 increase for annual natural gas revenue. The Energy Project's response case sought to ensure that Avista's Low Income Residential Assistance Program (LIRAP) was increased by the same percentage as any increase authorized for the Company's revenue requirement.

5 On September 4, 2009, the parties filed a Partial Settlement Stipulation; the Northwest Energy Coalition (NWEC or Coalition) did not join in the proposed settlement, but does not oppose its terms. The Partial Settlement Stipulation proposed to resolve issues relating to cost of capital and rate of return, power costs (excepting the Lancaster contracts), pro forma adjustment of power generation operation and maintenance (O&M) costs, electric rate spread and rate design, natural gas rate spread, and low-income ratepayer assistance. As a result, the Company revised downward its revenue requirement requests to \$38.61 million for electric and \$3.14 million for natural gas. On September 17, 2009, the settling parties filed their Joint Testimony in Support of Partial Settlement Stipulation.

6 On rebuttal, filed September 11, 2009, Avista further reduced its asserted revenue deficiencies to \$37.5 million for electric and \$2.8 million for natural gas, taking into account updated cost figures. Table 1 (below) summarizes the final levels of adjustment to annual revenue proposed by the three parties who put on full revenue requirement cases.

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<sup>2</sup> Public Counsel also opposed the inclusion in rates of agreements related to the Lancaster facility for natural gas capacity and electric transmission rights.

**TABLE 1**  
**Proposed Total Adjustments to Annual Base Rates**  
**Revenue Requirement Relative to Current Rates**

	As-Filed	Response	Rebuttal/Cross Answer
<b>Electric:</b>			
Avista	\$69,800,000		\$37,500,000
Staff		\$20,100,000	\$22,800,000
Public Counsel		(\$12,800,000)	\$4,300,000
<b>Natural Gas:</b>			
Avista	\$4,919,000		\$2,849,000
Staff		\$281,000	\$568,000
Public Counsel		\$431,000	\$690,000

- 7 The Commission conducted evidentiary hearings in Olympia, Washington, on October 6-9, 2009. The parties filed simultaneous Post-Hearing Briefs on November 10, 2009.
- 8 **PARTY REPRESENTATIVES:** David J. Meyer, Vice President and Chief Counsel for Regulatory and Governmental Affairs, Spokane, Washington, represents Avista. Simon ffitich, Assistant Attorney General, Seattle, Washington, represents Public Counsel. Greg Trautman, Assistant Attorney General, Olympia, Washington, represents the Commission's regulatory staff (Commission Staff or Staff). S. Bradley Van Cleve and Irion Sanger, Davison Van Cleve, P.C., Portland, Oregon, represents ICNU. Chad M. Stokes and Tommy Brooks, Cable Huston Benedict Haagensen & Lloyd LLP, Portland, Oregon, represent Northwest Industrial Gas Users (NWIGU). David Johnson, Seattle, Washington, represents NWEC. Ronald Roseman, Seattle, Washington, represents The Energy Project.
- 9 **COMMISSION DETERMINATIONS:** The Commission suspended and set for hearing the rates Avista originally proposed. The Company, as summarized above, revised its as-filed proposal downward during the pendency of these proceedings. Accordingly, the Commission must determine fair, just, reasonable and sufficient

rates based on the record before us.<sup>3</sup> In this order, we evaluate Avista's final revised rate request and resolve a number of contested issues that separate the parties by several million dollars. We also resolve several important policy issues relating to the standards and guidelines for evaluating and approving pro forma adjustments and reiterate the requirements for addressing transactions with affiliated interests. We summarize our determinations in Tables 4 and 5 (below).

10 The Commission finds on the basis of the evidence presented that Avista requires rate relief and therefore determines that the Company should be authorized and required to file rates in compliance with our decisions, as summarized here and discussed in detail below. When implemented via the compliance filing we require the Company to make, the resulting rates will be fair, just, reasonable and sufficient, and neither unduly discriminatory nor preferential. Because we require Avista to rerun its AURORA power cost model based on the removal of the Lancaster contracts, we will determine the Company's exact revenue deficiency for electric service after its compliance filing.<sup>4</sup> We find a revenue deficiency of \$557,000 for natural gas and authorize Avista to file rates to recover additional revenue in this amount. The Company's new rates will be effective no earlier than January 1, 2010. Finally, the Commission approves a continuation of Avista's decoupling mechanism, with modifications including a lower maximum deferral rate of recovery for lost margins.

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<sup>3</sup> RCW 80.28.020.

<sup>4</sup> Reviewing the evidence available to us at this time, we estimate a revenue deficiency of \$12.1 million for electric.

**MEMORANDUM**

**I. Background and Procedural History**

- 11 On January 23, 2009, Avista filed revisions to its currently effective Tariff WN U-28, Electric Service, and revisions to its currently effective Tariff WN U-29, Natural Gas Service. The proposed tariff revisions bore an effective date of February 23, 2009. Avista proposed a general rate increase of 16.0 percent for the electric tariffs and 2.4 percent for the gas tariffs. The Commission suspended the proposed tariff revisions on February 3, 2009, consolidated the two dockets, and set the matters for hearing.
- 12 Avista's initial request was based on a test year ending September 30, 2008, with pro forma adjustments into 2010. The filing also included proposals for the following:
- An overall rate of return of 8.68 percent.
  - A rate of return on common equity of 11.0 percent.
  - A capital structure consisting of 47.51 percent equity and 52.49 percent debt.
  - Inclusion of the Lancaster power purchase agreement (PPA) in electric rates, beginning on January 1, 2010.

The Company's direct testimony accompanied its filing, as required by law.

- 13 The Commission conducted a prehearing conference on February 24, 2009, before Administrative Law Judge Adam E. Torem. On February 27, 2009, the Commission entered Order 02, granting various petitions to intervene, authorizing formal discovery, and establishing a procedural schedule.
- 14 The parties prefiled extensive testimony and numerous exhibits sponsored by 36 witnesses, including 19 for Avista, 6 for Public Counsel, 8 for Staff, and 3 for the various intervenors. On September 4, 2009, all parties except NWECA filed a Partial Settlement Stipulation resolving cost of capital, rate spread, and several other issues. NWECA does not oppose the terms of this proposed settlement.

- 15 The Commission held separate public comment hearings in both Spokane Valley, Washington, and Spokane, Washington, on September 30, 2009, and conducted evidentiary hearings in Olympia, Washington, on October 6-9, 2009. Chairman Jeffrey D. Goltz, Commissioner Patrick J. Oshie and Commissioner Philip B. Jones were assisted at the bench by presiding Administrative Law Judge Adam E. Torem. Altogether, the record includes more than 300 hundred exhibits entered during four days of evidentiary proceedings. The transcript of these proceedings exceeds 1300 pages in length.
- 16 The parties filed simultaneous Post-Hearing Briefs on November 10, 2009. The Commission here enters its Final Order resolving the disputed issues, approving certain uncontested adjustments, and granting appropriate relief considering the full record of proceedings and the parties' arguments based on that record.

## II. Discussion and Decisions

### A. Introduction

- 17 The Commission has a statutory duty to determine and set rates that are fair, just, reasonable, and sufficient.<sup>5</sup> As set forth in more detail below in the context of some contested issues, to strike this balance between company and ratepayer interests, the Commission follows long-established and judicially recognized rate-making principles.<sup>6</sup> The rates must not only be reasonable to consumers, but they must be "sufficient" for the company in that they "enable the company to operate successfully, to maintain its financial integrity, to attract capital, and to compensate its investors for the risks assumed . . . ."<sup>7</sup>
- 18 Pursuant to these principles and historic Commission practice, the Commission determines appropriate levels of prudently incurred expenses the company will incur,

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<sup>5</sup> RCW 80.28.020.

<sup>6</sup> See *People's Organization for Washington Energy Resources v. Washington Utilities & Transportation Comm'n*, 104 Wn.2d 798, 807-13, 711 P.2d 319 (1985) (describing ratemaking principles and process) [Hereinafter *POWER*].

<sup>7</sup> *Id.* at 812, quoting *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. 591, 605, 64 S.Ct. 281, 88 L.Ed. 333 (1944).

and allows recovery of those expenses. In addition, the Commission determines the company's "rate base" and determines an appropriate rate of return to be applied to that rate base to determine the authorized return. The two figures – expenses and return – constitute the company's revenue requirement which is to be recovered in rates.<sup>8</sup> The Washington Supreme Court explained the rate-making formula:

In order to control aggregate revenue and set maximum rates, regulatory commissions such as the WUTC commonly use and apply the following equation:

$$R = O + B(r)$$

In this equation,

R is the utility's allowed revenue requirements;  
O is its operating expenses;  
B is its rate base; and  
r is the rate of return allowed on its rate base.

Although regulatory agencies, courts and text writers may vary these symbols and notations somewhat, this basic equation is the one which has evolved over the past century of public utility regulation in this country and is the one commonly accepted and used.<sup>9</sup>

<sup>19</sup> In this case, the parties propose a settlement on a number of the issues in the rate-making equation. We first address that proposed settlement and then address the contested issues.

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<sup>8</sup> *POWER*, 104 Wn.2d at 807-09.

<sup>9</sup> *Id.* at 809.

**B. Partial Settlement Stipulation**

20 *Background.* On September 4, the Company filed a Partial Settlement Stipulation on behalf of all the parties that had contested electric revenue and rate design issues. The Partial Settlement Stipulation proposes resolution of the following contested issues:

- Cost of Capital, Capital Structure and Rate of Return;
- Power Costs (excepting the effect of the Lancaster Contracts);
- *Pro Forma* Adjustment of Power Generation O&M; and
- Rate Spread (electric and natural gas) and Rate Design (electric only).

In this section, we set out the regulatory requirements for our consideration of such agreements. We then summarize the parties' Partial Settlement Stipulation, which is attached to and made a part of this Order by reference (Appendix A). If any inconsistency is perceived between our summary and the Partial Settlement Stipulation, the express terms of the Partial Settlement Stipulation control.

21 WAC 480-07-750(1) states in part: "The commission will approve settlements when doing so is lawful, the settlement terms are supported by an appropriate record, and when the result is consistent with the public interest in light of all the information available to the commission." Thus, the Commission considers the individual components of the Partial Settlement Stipulation under a three-part inquiry. We ask:

- Whether any aspect of the proposal is contrary to law.
- Whether any aspect of the proposal offends public policy.
- Whether the evidence supports the proposed elements of the Settlement Agreement as a reasonable resolution of the issue(s) at hand.

22 The Commission must determine one of three possible results:

- Approve the proposed settlement without condition.
- Approve the proposed settlement subject to conditions.
- Reject the proposed settlement.

23 As discussed below, we find the Partial Settlement Stipulation terms proposed by the parties to be consistent with law and policy, and to reasonably resolve several

significant issues in this proceeding. The parties made concessions relative to their respective litigation positions to arrive at end results that are supported by the evidence in the record. When combined with the Commission's other determinations in these proceedings, the parties' compromises result in rates that are "fair, just, reasonable and sufficient," as required by law.<sup>10</sup>

24 *Cost of Capital, Capital Structure and Rate of Return – Electric and Natural Gas.*

The settling parties proposed a resolution of all cost of capital issues, including capital structure and cost rates for common equity and debt. They agreed to a 10.2 percent return on equity (ROE),<sup>11</sup> with a 46.5 percent common equity ratio, and the Company's originally proposed average debt cost of 6.57 percent. Under these agreed figures, the Company will have the opportunity to earn an overall Rate of Return (ROR) of 8.25 percent, slightly higher than its currently approved ROR of 8.22 percent.

25 The agreed ROE falls within the range of recommendations from the Company, Staff, Public Counsel and ICNU.<sup>12</sup> Further, it is the same ROE we approved for the Company in its past two rate orders.<sup>13</sup> Finally, these parties support the use of the

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<sup>10</sup> RCW 80.28.010(1); RCW 80.28.020.

<sup>11</sup> Public Counsel and ICNU reserved the right to advocate for a lower ROE in the event the Commission approves decoupling or another risk reduction mechanism for the Company. *See* Joint Testimony, Exh. JT-1T at 9:15-17 and 18:3-9 (characterizing the 10.2 percent ROE as a "cap" which could be reduced if Avista's decoupling mechanism is continued). As further explained below in our determination to approve a continuation of a decoupling mechanism, we decline to modify the Company's ROE.

<sup>12</sup> Staff's expert witness, Mr. David Parcell, estimated a range for ROE between 9.5 to 10.5 percent. Joint Testimony, Exh. JT-1T at 16:5-11; *see also* Parcell, Exh. DP-1T at 4:9-12. Public Counsel's and ICNU's expert witness, Mr. Michael P. Gorman, estimated a range for ROE between 9.7 to 10.5 percent. Joint Testimony, Exh. JT-1T at 17:17 to 18:2; *see also* Gorman, Exh. MPG-1T at 2:3-10.

<sup>13</sup> *See* Dockets UE-080416 and UG-080417 (approving a settlement with an ROE of 10.2 percent) and Dockets UE-070804 and UG-070805 (approving a settlement with an ROE of 10.2 percent). However, we recognize that in this case there was substantial disagreement about the impact of the current economic recession on the ROE appropriate for setting rates. Public Counsel argued that the current economic situation should accommodate a lower ROE (Gorman, Exh. MPG-1T at 9-13), while the Company argued otherwise (Avera, Exh. WEA-1T at 7-17). Because this was

46.5 percent equity ratio as a reasonable compromise between the Company's actual year-end 2008 equity ratio of 45.4 percent and its projection of 47.51 percent by the end of 2009.<sup>14</sup>

26 We find that the proposed cost of capital falls within the range of outcomes supported by the evidence of record. Therefore, we conclude that the 10.2 percent ROE and resulting 8.25 percent overall ROR are reasonable and we approve this portion of the Partial Settlement Stipulation.

27 *Power Costs.* The settling parties agreed to an \$11.1 million increase in the Company's currently approved revenue requirement associated with net power costs.<sup>15</sup> Relative to the Company's original revenue request, the settling parties agree to the following six separate but interrelated adjustments:

- 1) *Natural Gas Fuel Costs.* Adjust natural gas fuel costs to be \$5.61 per dekatherm (at Stanfield) for the unhedged portion of 2010 power generation. This adjustment includes the actual 2010 calendar-year wholesale electric and natural gas transactions entered into through July 3, 2009. This adjustment reduces the Company's as-filed revenue requirement by \$18.1 million.
- 2) *Hydro-filtering.* Adjust power supply expense to remove the effects of months when hydro-generation was either higher or lower by more than one standard deviation from the 50-year average for that month. This reduces the Company's as-filed revenue requirement by \$729,000.
- 3) *Retail Load Adjustment.* Adjust rate-year system load used for calculating pro forma power expense (calendar 2010) by 3 percentage points from 5.1 percent to 2.1 percent. The effect of this adjustment is to reduce the Company's as-filed revenue requirement by \$9.1 million.

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settled, we need not resolve the dispute regarding the impact of the economy on establishing appropriate ROE in this proceeding.

<sup>14</sup> Joint Testimony, Exh. JT-1T at 16:11-14 and 18:10-14.

<sup>15</sup> Partial Settlement Stipulation, Exh. B-1 at 4, and Attachment A at 1.

- 4) *Colstrip Availability*. The parties agree to use the Company's proposed 5-year average for the period ended December 31, 2007, to represent the equivalent availability factor for Colstrip.
- 5) *WNP-3 Contract*. The parties agree to use the level of WNP-3 operations and maintenance cost approved by the Commission in Cause No. U-86-99, as reflected in the Company's original filing.
- 6) *Kettle Falls Fuel Availability*. Adjust Kettle Falls generation to reflect a reduction in fuel availability. The effect of this adjustment is to increase the Company's as-filed revenue requirement by \$383,000.

In sum, the agreed power cost adjustments reduce the Company's originally filed request in this matter by \$27.5 million.<sup>16</sup>

28 The parties' agreement allows the Company to recover additional costs related to power supply, while recognizing the significant reduction in natural gas fuel costs.<sup>17</sup> We view the fuel-related adjustments as balancing the interests of the parties (and ratepayers), while considering the impacts of recent conditions in the relevant fuel markets. Further, the agreement reflects the retail load and hydro-filtering adjustments jointly proposed by Staff and ICNU.<sup>18</sup> We conclude that the settlement's treatment of the power cost issues enumerated above is reasonable and supported by the evidence presented. Therefore, we approve these power cost adjustments. However, to the extent the power cost modeling supporting the settlement includes the costs and benefits of the Lancaster contracts, we direct later in this Order that the power cost model be revised to produce the net power cost adjustments excluding the Lancaster contracts.

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<sup>16</sup> Public Counsel seeks a further adjustment to net power costs by removing 2010 expenses related to the Lancaster Power Purchase Agreement (PPA) and associated contracts. We address the Lancaster matter below, beginning at ¶ 175.

<sup>17</sup> Joint Testimony, Exh. JT-1T at 15:5-6.

<sup>18</sup> *Id.* at 16:15-22.

29 *Power Generation O&M.* The settling parties agree to reduce the Company's original filed adjustment for generating plant operation and maintenance costs by \$2.4 million. The evidence of record regarding this adjustment is contained in the Company's original proposal to include these costs in rates<sup>19</sup> and Staff's analysis offered in support of reversing this adjustment.<sup>20</sup> The agreed upon adjustment is a compromise of as-filed positions supported by all parties which we therefore accept and approve.

30 *Electric Rate Spread and Rate Design.* The settling parties propose to apply an equal percentage increase to all electric service schedules for purposes of recovering the Company's revenue requirement.<sup>21</sup> With regard to electric rate design, the settling parties agree to the Company's initial proposal as contained in the original filing for all schedules except for Extra Large General Service Schedule 25.<sup>22</sup> The Extra Large General Service Schedule 25 will be altered so:

- the minimum charge will be increased from \$10,000 to \$11,000 per month (ten percent);
- the excess demand charge will be increased from \$3.00 to \$3.50 per kVa;
- the voltage discount for over 60kV will be increased to \$1.00/kVa and for over 115kV to \$1.20/kVa; and
- a uniform percentage increase will be applied to the first two energy block rates, and the increase to the third energy block rate will be equal to one half the percentage increase applied to the first two blocks.<sup>23</sup>

For residential service, the parties propose to increase the basic charge from \$5.75 per month to \$6.00 per month.<sup>24</sup>

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<sup>19</sup> Storro, Exh. RLS-1T at 23:16 – 24:3.

<sup>20</sup> LaRue, Exh. AMCL-1T at 14:1 – 15:22.

<sup>21</sup> Partial Settlement Stipulation, Exh. B-1 at 5.

<sup>22</sup> *Id.* at 5-6. Schedule 25 includes the Company's large commercial electric customers.

<sup>23</sup> *Id.*

<sup>24</sup> Partial Settlement Stipulation, Exh. B-1 at 5.

- 31 In accordance with the Settlement Agreement we approved in Dockets UE-070804 and UG-070805, Avista is expected to complete a new cost and load study in 2010.<sup>25</sup> Therefore, we agree with ICNU<sup>26</sup> that in this proceeding it remains appropriate to assign each class the same percentage increase. This approach preserves the status quo and allows time for parties to review and analyze the new study before embarking on a more complex shifting of costs to move the various ratepayer classes along toward parity. We also concur with Public Counsel's assessment that the 25 cent increase to the electric customer basic charge is acceptable.<sup>27</sup>
- 32 The record includes evidence sufficient to support the electric rate spread and rate design proposal made by the settling parties. Commission Staff supported a very similar approach to that adopted by the settling parties.<sup>28</sup> Therefore, we approve this portion of the settling parties' proposal.
- 33 *Natural Gas Rate Spread and Rate Design.* The settling parties also propose to apply an equal percentage increase to all natural gas service schedules, excepting Schedule 146 (Transportation), which will receive two-thirds of an equal margin increase, with the residual one-third allocated proportionately (based on margin) to the other schedules.<sup>29</sup> With regard to natural gas rate design, the settling parties agree to the Company's original proposal to increase the rates within Schedules 111 and 112 to maintain the existing break-even usage level between Schedules 101 and 111, aiming to minimize future customer schedule shifting. Although the Partial Settlement Stipulation does not resolve Schedule 101 gas rate design issues (including customer charges), the settling parties agree that design of rates under Schedule 101 will not be

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<sup>25</sup> Knox, Exh. TLK-1T at 14:4 – 15:2.

<sup>26</sup> Joint Testimony, Exh. JT-1T at 19:6-15. Public Counsel's expert witness, Glenn A. Watkins, also concurred with the across-the-board equal percentage increase in base rates by class. *Id.* at 21:18 – 22:2; *see also* Watkins, Exh. GAW-1T at 3-8.

<sup>27</sup> Joint Testimony, Exh. JT-1T at 22:3-7; *see also* Watkins, Exh. GAW-1T at 9.

<sup>28</sup> Joint Testimony, Exh. JT-1T at 17:3-4.

<sup>29</sup> Partial Settlement Stipulation, Exh. B-1 at 6.

conditioned or dependent upon the rates in Schedules 111 and 112.<sup>30</sup> Finally, the settling parties agree that Schedule 146 rates (including the customer charge) will be increased on an equal percentage basis.<sup>31</sup>

34 The Partial Settlement Stipulation provides consensus around nearly all issues regarding rate spread and rate design; due to the disputes over the fate of Avista's decoupling mechanism, only the natural gas basic charge issue could not be resolved.<sup>32</sup> We concur with NWIGU that the proposed spread of the gas rate increase was accomplished in a manner consistent with the available cost of service analyses.<sup>33</sup> In addition, Public Counsel and the Energy Project confirm that the proposal follows the status quo on rate spread established in the Company's most recent rate case.<sup>34</sup>

35 We find that the record contains sufficient evidence to support the natural gas rate spread and rate design recommendations of the settling parties. Therefore, we also approve this portion of the settling parties' proposal.

36 *Low-Income Ratepayer Assistance Program (LIRAP) – Electric and Natural Gas.* The Partial Settlement Stipulation also addresses the low income bill assistance funding issues through an agreement to increase rates for the Low Income Ratepayer Assistance Program (LIRAP) portion of the tariff riders (Schedules 91 and 191) by the *greater* of the overall percentage increase in base revenue approved for each schedule or, for electric, 9 percent, and for natural gas, 1.75 percent.<sup>35</sup>

37 Commission Staff endorsed the augmented LIRAP funding, noting that while the electric increase is a larger percentage of revenue than comparable company programs, the natural gas increase is within the range of those adopted by other

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<sup>30</sup> *Id.* at 6-7.

<sup>31</sup> *Id.*

<sup>32</sup> Joint Testimony, Exh. JT-1T at 15:7-11.

<sup>33</sup> *Id.* at 20:18-21; *see also* Schoenbeck, Exh. DWS-5T at 3-8.

<sup>34</sup> Joint Testimony, Exh. JT-1T at 21:18 – 22:2.

<sup>35</sup> Partial Settlement Stipulation, Exh. B-1 at 7.

natural gas companies.<sup>36</sup> We agree with Public Counsel and the Energy Project that establishing an increase for LIRAP funding guaranteed to keep pace with or possibly exceed any approved rate increase is in the public interest. The current economic recession has placed increased pressure on low income households and resulted in the creation of more low income households. Though even this increased level of LIRAP funding may not be adequate to meet all the needs of all low income households, the proposed approach to LIRAP funding is consistent with RCW 80.28.068 and will have minimal impact on the bulk of other ratepayers.<sup>37</sup>

38 This portion of the Partial Settlement Stipulation advances established public policy goals in Washington, and the record contains sufficient supporting evidence. Therefore, we approve the settling parties' proposal to increase LIRAP funding.

39 *Overall Approval of Partial Settlement Stipulation.* In sum, the Partial Settlement Stipulation's provisions reach agreement on an overall rate of return within the ranges advocated by the parties, make appropriate adjustments to the Company's power costs, and adopt a common-sense approach to rate spread and rate design. The settlement also ensures that funding for Avista's LIRAP program keeps pace with any rate increases we approve for the Company. The compromises reached by the settling parties comply with the law, are consistent with state policy and are in the public interest. Therefore, we adopt the Partial Settlement Stipulation in its entirety.

### C. Pro Forma Adjustments

#### 1. General Principles of Utility Rate Setting Applied to Pro Forma Adjustments

40 As part of its obligation to determine rates that are fair, just, reasonable, and sufficient, pursuant to RCW 80.28.020, and order them into effect prospectively, the Commission must base its decision on the record provided by the Company and the other parties.

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<sup>36</sup> Joint Testimony, Exh. JT-1T at 17:9-15.

<sup>37</sup> *Id.* at 22:17 – 23:6.

41 The Commission's long-established and well-understood ratemaking practice requires companies filing for revised rates to start with an historical test year. There is a fundamental reason for this starting point: costs, revenues, loads, and all other pertinent factors are known and can be measured with a high degree of certainty because they have, in fact, occurred. The practical value of the historical test year is that the cost, revenue and plant data are available for audit, and the test year captures the complex relationships among the various aspects of utility costs, revenue, load, and other factors over a uniform period of time.

42 The Commission recognizes that the test year is a snapshot in time. The typical test year is the twelve month period preceding the rate filing, ended as of the most recent auditable results of operations.<sup>38</sup> A utility, however, continues to operate, incur costs (including capital additions), achieve savings, and receive revenues during the pendency of its rate review subsequent to the test year that would carry over into the year in which the rates would be effective (known as the "rate year") and beyond. The theory, well supported by ratemaking theory and past commission practice,<sup>39</sup> is that once the relationship is set, it will continue to provide appropriate income to the company in the future. If the utility hooks up new customers, the revenues and expenses will increase in the same proportion as existed in the test year. If new facilities are put into service to serve those customers, then the resulting revenues would not only cover the company's added expenses, but also effectively provide a return on that new investment.

43 However, our past decisions, and our rules, recognize that there are some expenses or investments that do not take place in the test year that, nevertheless, should be included in the rate-making formula. Thus, subject to important conditions, a company's rate filing may include restating and pro forma adjustments.<sup>40</sup> These are

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<sup>38</sup> The test year is a period of company operations for which the Commission conducts a careful audit and review prior to authorizing any change in rates. See 1 Leonard S. Goodman, *The Process of Ratemaking* 141 (1998).

<sup>39</sup> See Charles F. Phillips, Jr., *The Regulation of Public Utilities* 196 (1993).

<sup>40</sup> WAC 480-07-510 (3)(e)(ii) and (iii) provide as follows:

(ii) "Restating actual adjustments" adjust the booked operating results for any defects or infirmities in actual recorded results that can distort test period earnings. Restating actual adjustments are also used to adjust from an as-recorded basis to a

allowed to revise or update expenses, revenues, and rate base so long as there is a mechanism ensuring, and evidence establishing, that these adjustments do not disturb test year relationships.

44 In order to ensure that the Commission has proper information on which to base test year expenses and investments, and any adjustments to those expenses and investments, the Commission has rules that require certain threshold information that all parties must include in their rate filings. With regard to accounting adjustments, work papers must

contain a detailed portrayal of restating actual and pro forma adjustments that the company uses to support its filing or that another party uses to support its litigation position, specifying all relevant assumptions, and including specific references to charts of accounts, financial reports, studies, and all similar records relied on by the company in preparing its filing, and by all parties in preparing their testimony and exhibits. All work papers must include support for, and calculations showing, the derivation of each input number used in the detailed portrayal and for each subsequent level of detail. The derivation of all interstate and multiservice allocation factors must be provided in the work papers.<sup>41</sup>

To be approved, a pro forma adjustment to test year operations must comport with the three key principles expressed above, two of which are embodied in the Commission's regulations and the third in statute.

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basis that is acceptable for rate making. Examples of restating actual adjustments are adjustments to remove prior period amounts, to eliminate below-the-line items that were recorded as operating expenses in error, to adjust from book estimates to actual amounts, and to eliminate or to normalize extraordinary items recorded during the test period.

(iii) "Pro forma adjustments" give effect for the test period to all known and measurable changes that are not offset by other factors. The work papers must identify dollar values and underlying reasons for each proposed pro forma adjustment.

<sup>41</sup> WAC 480-07-510(3)(e).

45 First, the adjustment must be known and measurable. The known and measurable concept requires that an event that causes a change in revenue, expense or rate base must be *known* to have occurred during or after the historical 12 months of actual results of operations.<sup>42</sup> It must also be demonstrated (*i.e., known*) that the effect of the event will be in place during the 12-month period when rates will likely be in effect.<sup>43</sup> The actual amount of the change must be *measurable*. This means the amount cannot be an estimate, a projection, the product of a budget forecast, or some similar exercise of judgment—even informed judgment—concerning future revenue, expense or rate base. Costs that are documented by actual expenditure, invoice, contract, or other specific obligation usually meet this test. Costs that are the product of forecasts, projections, or budgets generally will not qualify. There are exceptions, and we will discuss those below.

46 Second, for rate base, and for expense or revenue items, pro forma adjustments must be matched with offsetting factors. Offsetting factors, as the term suggests, diminish the impact of the known and measurable event. A mismatch would be created if offsetting factors are not taken into account.<sup>44</sup> That is, the known and measurable change will be overstated or understated, distorting the test year relationships among revenues, expenses, and rate base.

47 The less certainty with which actual utility costs and offsetting factors are known and measurable, the greater is the risk that an adjustment would disturb test year relationships and the less appropriate is the pro forma adjustment. The Commission must assess the certainty with which costs and offsetting factors are known when it balances the competing pressure to change test year values to reflect newer information with the objective of preserving the integrity of test year relationships.<sup>45</sup>

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<sup>42</sup> This is also known as the “test year,” “test period” or “historical test year.”

<sup>43</sup> This is also known as the “rate year.”

<sup>44</sup> For example, a pro forma adjustment that incorporates the addition of new plant in service would be offset by an adjustment to test year O & M expenditures that reflect the aged condition of the plant replaced.

<sup>45</sup> The farther a proposed adjustment is removed in time from the test year, and the less time that supporting evidence is available for examination, discovery, and testing by our staff and other

- 48 Third, if the pro forma adjustment is to add new plant, pursuant to statute it must be shown that the new plant will be used and useful to serve Washington customers.<sup>46</sup> With very limited exceptions the plant must be in service by no later than the end of the rate proceeding if it is to be allowed in rate base.<sup>47</sup> Typically, this means the plant will be in service before the suspension date, which generally marks the beginning of the “rate year.”
- 49 Certain rate-making mechanisms have been developed to allow prospective changes for inclusion in rates by “building in” adjustments that ensure that the matching principle is maintained. The power cost models used to measure net power costs under average and otherwise expected conditions of load, weather, and market conditions are such a mechanism, allowing for exception to strict application of the above three principles. Power cost models yield expected net power costs by rigorously matching costs and revenues. While these models employ assumptions, estimates, and forecasts as inputs, the modeled results are generally acceptable if the model inputs are reasonable and the modeling is comparable in analytical rigor to what is brought to bear in making normalizing adjustments.
- 50 The production plant cost adjustment factor (known sometimes in this rate case as a “production property adjustment”) is another rate making mechanism that preserves test year relationships between costs and revenues. It does so in appropriate

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parties, the greater is the Company’s burden to demonstrate that the requirements guiding adjustment to test year data have been met.

<sup>46</sup> The Commission also examines whether the new plant has been prudently built or acquired. To answer the prudence question, the Commission examines many factors, including whether the costs asserted are reasonable compared to other alternatives the Company considered at the time the decision to build or acquire was made. The Company must support its decision with sufficient evidence. See *UTC v. Puget Sound Power & Light Company*, Docket Nos. UE-920433, UE-920499, & UE-921262 (consolidated), 11<sup>th</sup> Supplemental Order, at 18-24 (Sept. 21, 1993) and 19<sup>th</sup> Supplemental Order (Sept. 27, 1994).

<sup>47</sup> In accordance with RCW 80.04.250, the Commission is empowered “to ascertain and determine the fair value for rate making purposes of the property of any public service company used and useful for service in this state and shall exercise such power whenever it shall deem such valuation or determination necessary or proper under any of the provisions of this title. In determining what property is used and useful for providing electric, gas, or water service, the commission may include the reasonable costs of construction work in progress to the extent that the commission finds that inclusion is in the public interest.”

circumstances by adjusting rate year costs to match test-year loads. We emphasize that pro forma adjustments to costs that are not included in such well-established mechanisms must be accompanied by thorough and specific analyses of their offsetting factors.

51 As articulated below, in this case, for a number of proposed pro forma adjustments, Avista fell short of meeting its obligations under the relevant Commission rules. Rather than present evidence of costs for new capital additions or for new expenses, Avista provided estimates. Also, rather than carefully analyzing savings or other offsetting factors that should be included in any pro forma analysis, the Company sometimes ignored such factors or addressed them in a minimal fashion. Accordingly, as detailed below, we did not accept a number of the Company's proposed pro forma adjustments.

52 In each instance, our decision does not preclude recovery of the cost of capital additions in a future proceeding where new plant additions are shown to be in service and the costs and offsetting benefits are reflected in test year data or are thoroughly analyzed in support of a pro forma adjustment.

## **2. Uncontested Adjustments to Test Year Results of Operations**

53 The parties agree on a number of restating and pro forma adjustments to the Company's results of operations for the test year. We summarize these in Table 2A for electric and Table 2B for natural gas on the following pages.

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**TABLE 2A**  
**Uncontested Restating & Pro Forma Adjustments – Electric (\$000)**

	NOI	Rate Base
<b>Test Year Results of Operations</b>	<b>68,538</b>	<b>1,053,828</b>
<b>UNCONTESTED ADJUSTMENTS</b>		
Deferred FIT Rate Base	-	(142,713)
Deferred Gain on Office Building	-	(126)
Colstrip 3 AFUDC	202	(1,956)
Colstrip Common AFUDC	-	436
Kettle Falls Disallowance	(56)	(854)
Customer Advances	-	(231)
Depreciation True-up	39	-
Settlement Exchange Power	-	18,422
Eliminate B&O Tax	(22)	-
Uncollectable Expense	70	-
Regulatory Expense	(52)	-
FIT	(1,751)	-
Eliminate WA Power Cost Deferral	(8,844)	-
Nez Perce Settlement Adj.	(6)	-
Eliminate A&R Expense	335	-
Office Space Charges to Subsidiary	5	-
Restate Excise Taxes	(20)	-
Net Gain/Losses	79	-
Revenue Normalization	23,394	-
Miscellaneous Restating (1)	113	-
Restate Debt Interest	697	-
Transmission Rev/Exp	(51)	-
Spokane River Relicense	(2,549)	22,530
Montana Lease	(2,285)	2,859
O&M Plant Expense	-	-
Employee Benefits	(2,920)	-
Colstrip Mercury(2)	(630)	-
Clark Fork PM&E	(426)	-
<b>Total Uncontested Adjustments</b>	<b>5,322</b>	<b>(101,633)</b>

(1) Includes Company's correction to transfer Edison Electric Institute dues from natural gas to electric books per EMA-8(11).

(2) Andrews, TR. 532:7-25, confirms agreement on this adjustment.

**TABLE 2B**  
**Uncontested Restating & Pro Forma Adjustments – Natural Gas (\$000)**

	NOI	Rate Base
<b>Per Books</b>	<b>12,004</b>	<b>178,717</b>
<b>UNCONTESTED ADJUSTMENTS</b>		
Deferred FIT Rate Base	-	(27,674)
Deferred Gain on Office Building	-	(42)
Gas Inventory	-	11,064
Weatherization & DSM	-	-
Customer Advances	-	(52)
Depreciation True-up	54	-
Revenue Normalization	3,648	-
Eliminate B&O Tax	(4)	-
Uncollectable Expense	93	-
Regulatory Expense	(9)	-
FIT	(10)	-
Net Gain/Losses	8	-
Eliminate A&R Expense	55	-
Office Space Charges to Subsidiary	1	-
Restate Excise Taxes	(51)	-
Miscellaneous Restating (1)	97	-
Restate Debt Interest	80	-
Employee Benefits	(771)	-
AGA Dues(2)	-	-
JP Storage	(1,778)	8,922
<b>Total Uncontested Adjustments</b>	<b>1,413</b>	<b>(7,782)</b>

(1) Includes Company's correction to transfer Edison Electric Institute dues from natural gas to electric books per EMA-8(11).

(2) Adjustment to AGA Dues is included in adjustment to miscellaneous restatements per EMA-8(11).

54 We accept these uncontested adjustments as appropriate without the necessity for detailed discussion. However, we must now review each of the contested adjustments, considering in detail the record evidence and the key principles previously described.

### 3. Contested Pro Forma Adjustments to Rate Base

#### a. Introduction

55 The rate base represents the net book value of assets which are used and useful in providing utility service to ratepayers within our state. Typically, it is determined for the test year (and therefore for rate-making purposes) by determining the average net book value for each month of the test year and then averaging those figures. This “average of monthly averages” method has long been the method of determining rate base by this commission.<sup>48</sup>

#### b. Pro Forma Rate Base – Capital Additions – Electric

56 *Positions of the Parties.* Avista proposes “to include in retail rates the costs associated with utility plant that is in service, and will be used to provide energy service to our customers during the 2010 pro forma rate year.” According to the Company, its proposal is “consistent with prior ratemaking practice in the state of Washington.”<sup>49</sup>

57 Explaining the factors driving its need to make new plant investments, Avista points to the need to strengthen the Company’s transmission and distribution systems, aging infrastructure, physical degradation, and to meet the costs of municipal compliance including street relocations. The Company asserts that these necessary plant investments are increasingly expensive and exceed depreciation revenue due to

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<sup>48</sup> See *UTC v. Washington Water Power*, Cause No. U-76-8, Second Supplemental Order Rejecting Revisions to Tariff WN U-23 But Authorizing Refiling Under Conditions Stated, at 6-7 (Dec. 23, 1976) (stating Commission opinion “that an historical test year properly restated and proformed, using an average-of-monthly-averages in calculating rate base continues to be a reliable and consistent basis for establishing rates in electric and other utility cases.”); see also *UTC v. Washington Water Power*, Cause No. U-82-10 & U-82-11(consolidated), Second Supplemental Order, at 9 (Dec. 29, 1982) (noting average-of-monthly-averages as historically preferred method for determining proper rate base); see also *UTC v. Puget Sound Power and Light*, Cause No. 85-53, Second Supplemental Order, at 27-28 (May 16, 1986) (adopting average-of-monthly-averages approach to depreciation expense adjustment as best means to properly match revenues and expenses).

<sup>49</sup> DeFelice, Exh. DBD-1T at 2:7-11.

increased cost of construction materials in the range of 55 percent to 170 percent since 2003.<sup>50</sup>

58 The Company proposes three adjustments to electric rate base to incorporate capital additions made, or planned to be made, subsequent to the September 30, 2008, end of the test-year.<sup>51</sup>

- The Company's first contested adjustment would add \$21.4 million to net rate base and reduce net operating income (NOI) by \$473,000 for capital projects completed during the last three months of calendar year 2008 and annualizes plant-in service balances to a December 31, 2008, end-of-period balance.<sup>52</sup>
- The Company's second contested adjustment would add \$22.9 million to net rate base and reduce NOI by \$2.9 million for plant additions and expenses for projects completed or planned to be completed in 2009 and annualizes plant-in service balances to a December 31, 2009, end-of-period balance.<sup>53</sup>
- The Company's third contested adjustment would add \$5.4 million to net rate base and reduce NOI by \$156,000 for plant additions planned to be completed on unit 3 of the Noxon generating station in early 2010. The Noxon plant is a hydroelectric generating station located on the Clark Fork River in western Montana. According to the Company, the cost of the new turbine and mechanical overhaul should be included in the production rate base because they are scheduled to be completed by March 2010 and have been included in the power cost dispatch model used to calculate pro forma net power costs.<sup>54</sup>

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<sup>50</sup> *Id.* at 6:18-9:13.

<sup>51</sup> These adjustments are designated in the Company's testimony as PF-6, PF-7, and PF-8.

<sup>52</sup> Andrews, Exh. EMA-6 at 10 (column PF-6). "End-of-period" balance denotes that account totals reflect the actual balance in December, as opposed to an average balance over the 12 month period ending in December.

<sup>53</sup> *Id.* at 10 (column PF-7).

<sup>54</sup> Andrews, Exh. EMA-1T at 26:1-7.

In combination, the Company's 2008 and 2009 adjustments (first two bullets above) reflect some 230 individual projects categorized as electric generation, electric transmission, electric distribution, general plant and equipment, vehicles and technology systems.<sup>55</sup> Table 3 shows that the total of all three adjustments proposed by the Company is an increase to net rate base of \$49,767,000 and decrease to NOI of \$3,535,000.<sup>56</sup>

59 Staff opposes the first two of these as improper pro forma adjustments, citing to the Commission rule governing pro forma adjustments that requires such adjustments to be "known and measurable" and "not offset by other factors."<sup>57</sup> Staff says the Company's proposed adjustments violate the matching principle of ratemaking because they simply "provide for a wholesale inclusion of all plant in service . . . [and do] not address the corresponding changes in customer count, expenses, and revenues."<sup>58</sup> In addition, Staff objects to the Company's proposal to depart from average-of-monthly-averages rate base and to instead measure rate base at a point in time three months after the close of the test year.<sup>59</sup>

60 Staff notes that in some limited instances the Commission has allowed out-of-period expenses and plant additions to be included in rates, but these instances have been narrowly justified.<sup>60</sup> Considering these past decisions, Staff proposes an alternative adjustment to include some out-of-period 2008 and 2009 expenses and plant

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<sup>55</sup> A description of the projects can be found at: DeFelice, Exh. DBD-1T at 10:16 – 16:15, and Kermode, Exh. DPK-1T at 28:12-15.

<sup>56</sup> Net operating income is the income after tax that is available to the utility for return on invested capital. Net operating income and revenue requirement move in opposite directions. An adjustment that reflects a decrease to net operating income produces an increase in necessary revenue requirement.

<sup>57</sup> Parvinen, Exh. MPP-1T at 4:17-18.

<sup>58</sup> Kermode, Exh. DPK-1T at 32:12-18 (emphasis in original).

<sup>59</sup> *Id.* at 31:21-32.

<sup>60</sup> Staff points to the Coyote Springs generating plant and Noxon Dam upgrades as examples allowed because of materiality of the resource and inclusion of the projects in the power cost model. Staff also cites certain transmission investment undertaken to improve reliability. Parvinen, Exh. MPP-1T at 9:10-20.

investments.<sup>61</sup> Staff would limit the proposed adjustments to those expenses and costs that are incurred, in service, and auditable by June 30, 2009, and:

- Required by laws, regulations, or directives from regulatory bodies, or
- Transmission investments related to reliability, or
- Generating plant investment and expenses that are included in the power cost calculation and that are adjusted to match the test-year loads by the production property adjustment.

Staff identifies projects originally included in the Company's 2008 and 2009 adjustments<sup>62</sup> that meet the criteria above and adjusts the plant amounts to the 2010 rate year average-of-monthly-averages rate base balances, including related depreciation and deferred taxes.<sup>63</sup> The result of Staff's adjustment for 2008 and 2009 capital additions is to increase net rate base by \$21,252,000, and decrease NOI by \$599,000.<sup>64</sup>

61 Public Counsel shares Staff's view that the Company's proposed adjustments "violate the ratemaking principle of matching revenues, expenses, and capital costs."<sup>65</sup> Public Counsel recommends that any adjustment to address 2008 and 2009 additions be limited to production plant that is reflected in power supply modeling. According to Public Counsel, the power supply model captures the costs and benefits of new power resources.<sup>66</sup> Public Counsel recommends an adjustment to increase net electric rate base by \$3,039,000 and decrease NOI by \$39,000.

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<sup>61</sup> *Id.* at 36:4-38:3.

<sup>62</sup> Note that the Staff removes the Noxon 1 generator upgrade originally included in the Company's PF-7 (2009) adjustment and includes it instead in Staff's PF-8 (2010) adjustment.

<sup>63</sup> Kermode, Exh. DPK-1T at 38:21-23 and Exh. B-10.

<sup>64</sup> Exh. DPK-2 at 9 (column PF-7). These figures and all others representing the level of adjustments proposed by all parties in this proceeding are relative to the Company's test period of operations (i.e., relative to "per books").

<sup>65</sup> Larkin, Exh. HL-1T at 14:1-10.

<sup>66</sup> *Id.* at 14:12-23.

62 The Company counters that Commission precedent treats many costs as known and measurable for purposes of pro forma adjustment even though they are estimates and not precisely known. It cites examples including modeled power costs, estimated generation for PURPA projects, average injuries and damages, average transmission wheeling revenues, and the unopposed inclusion of the Noxon No. 3 upgrade costs in this proceeding.<sup>67</sup> For specific precedent, the Company points to a 2002 order of the Commission in a water case that describes pro forma adjustments as those that “will occur prospectively to best estimate the relationship between the Company’s costs and revenues.”<sup>68</sup> According to the Company, its actual capital program expenditures have comported closely with planned expenditures for 2005 through 2008.<sup>69</sup>

63 The Company says that Staff’s proposal to include only a subset of its 2008 and 2009 rate base additions by using a cut-off date of June 30, 2009, would preclude it from including \$14.2 million of investments in rate base and preclude it from recovering \$6.5 million of related annual revenue even though “ratepayers will receive the benefit of these assets that are used and useful at December 31, 2009, for the entire 2010 rate year.”<sup>70</sup>

64 Without abandoning its preferred proposal, the Company offers an alternative approach based generally on Staff’s proposal. Avista would modify Staff’s method in two ways. First, it would include all costs through the end of 2009 associated with the subset of projects Staff identifies. Second, the Company would add to Staff’s set of projects some additional projects that were completed and in service by the end of July 2009. These two modifications add \$33.8 million of net rate base to Staff’s proposed \$21.2 million.<sup>71</sup> When compared to its original proposal of \$11.3 million,

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<sup>67</sup> Norwood, Exh. KON-1T at 8:8 – 11:4. We note that these examples generally involve normalizing the test year level of costs based on an average of known historical costs.

<sup>68</sup> *Id.* at 11:7-19, citing *UTC v. Rainier View Water Company, Inc.*, Docket UW-010877, Sixth Supplemental Order, Final Order Rejecting Tariff Filing; Ordering Refiling, ¶ 29 (July 12, 2002) [hereinafter *Rainier View Water Order*].

<sup>69</sup> *Id.* at 12:9-23.

<sup>70</sup> DeFelice, Exh. DBD-4T at 4:16-5:2.

<sup>71</sup> *Id.* at 11:18 – 15:20.

Avista's alternative proposal yields a combined revenue requirement of \$11.4 million for all three adjustments.

- 65 The Company contends that Public Counsel's recommendations remove from rate base \$41.3 million for assets that are used and useful by December 31, 2009, with a consequent reduction in revenue requirement of \$10.8 million.<sup>72</sup> Noting that Public Counsel's recommendation allows generating assets to be included in pro forma rate base, the Company contends that Public Counsel's calculation is nonetheless faulty and not reliable because it creates a mismatch between net plant additions and total plant depreciation.<sup>73</sup>
- 66 Both Staff and Public Counsel generally agree that an adjustment to include the cost of the Noxon No. 3 turbine upgrade is appropriate. For its part, Staff testifies that it believes the project will be completed on time, is prudent and will be used and useful in the rate year.<sup>74</sup> Staff modifies the Company's 2010 Noxon No. 3 adjustment to also include the investment and expense related to the Noxon No. 1 turbine. Staff explains that the Noxon No. 1 upgrades were completed in April 2009 and plant amounts had originally been included in the Company's adjusted 2009 capital additions. According to Staff, both the Noxon No. 1 and Noxon No. 3 projects were included in the power cost dispatch model and are therefore appropriate to include in the rate year rate base that will be adjusted to test-period loads with the production property adjustment.<sup>75</sup> Staff further adjusts the Noxon No. 3 plant amounts to reflect that the facility will be in service for only 9 months of the rate year.<sup>76</sup>
- 67 The Company objects to Staff's recommendation to limit the Noxon No. 3 costs to remove 25 percent of the total, arguing that 100 percent of the benefits of the upgrade are included in the power cost model. Staff disagrees, contending that the power cost

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<sup>72</sup> *Id.* at 10:10-20.

<sup>73</sup> *Id.* at 8:17 – 9:18.

<sup>74</sup> Kermode, Exh. DPK-1T at 40:2-16.

<sup>75</sup> *Id.* at 40:8-16.

<sup>76</sup> *Id.* at 40:14-16.

model's inclusion of the full year of Noxon No. 3 operations does not determine what cost-recovery should be allowed.<sup>77</sup>

68 The following table summarizes the final pro forma adjustments for electric capital additions proposed by the Company, Staff, and Public Counsel.

**Table 3. Comparison of Electric Plant Addition Adjustments \$(000)**

	Company <sup>78</sup>			Staff <sup>79</sup>			Public Counsel <sup>80</sup>		
	RB	NOI	RR	RB	NOI	RR	RB	NOI	RR
2008	21,445	(473)	3,605	0	0	0	2,254	(10)	315
2009	22,936	(2,906)	7,715	21,252	(599)	3,782	785	(29)	151
2010	5,386	(156)	965	14,592	(434)	2,633	5,386	(156)	965
<b>TOTAL</b>	<b>49,767</b>	<b>(3,535)</b>	<b>12,285</b>	<b>35,844</b>	<b>(1,033)</b>	<b>6,415</b>	<b>8,425</b>	<b>(195)</b>	<b>1,431</b>

Note – Revenue Requirement (RR) is calculated at settlement-proposed return of 8.25 percent and revenue conversion factor of .621953.<sup>81</sup>

69 *Commission Decision.* We have previously discussed and emphasized the important principles governing pro forma adjustments. The post-test-year capital addition adjustments the Company and parties propose are adjustments to rate base accounts and related expenses and must comport with all three of the important principles guiding the use of pro forma adjustments. Our analysis of the evidence and arguments regarding electric plant additions leads us to conclude that, of the various approaches, Staff's adjustment is most appropriate and consistent with these guiding principles.

70 Staff's adjustment allows recovery for plant investments made subsequent to the end of the test year so long as they are known to be completed and in service. Staff

<sup>77</sup> Kermode, TR. 739:12 – 740:16.

<sup>78</sup> Andrews, EMA-6 at 10.

<sup>79</sup> Kermode, Exh. DPK-2 at 9.

<sup>80</sup> Exh. B-5, Electric Results of Operations, Tab A-1 Columns AM, AN and AO.

<sup>81</sup> The revenue conversion factor translates net operating income (which is after tax) to revenue requirement (which includes income tax and other revenue sensitive taxes).

concludes that, based on careful auditing and analysis, those projects that it could confirm are in service and unlikely to have offsetting factors are appropriate to include in a pro forma adjustment. Staff's adjustment strikes a fair balance preserving the integrity of the test year, while at the same time allowing for recovery of significant capital expenditures that have occurred subsequent to September 30, 2008, the end of the test year.

71 First, Staff is correct to focus on audited results to ensure that the costs it proposes to include in rates comply with both the known and measurable principle and the used and useful principle.<sup>82</sup> Budgeted figures representing the Company's projected and planned costs for capital programs may prove to be inaccurate. While we do not question the rigor of the Company's management and planning processes, planned expenditures are not certain expenditures. For costs of new plant to be recovered in customer rates, the investment must have indeed occurred and the new facilities must be providing service to customers. As required by statute, the facilities must be "used and useful." Staff's adjustment includes those projects documented to be actually completed and put in service in the last quarter of 2008 and the first half of calendar year 2009.

72 Second, when adjustments are made to rate base outside of the test year, Staff is correct to be concerned about potential injury to the matching principle. Staff is correct to note that, while not perfect protection against mismatches caused by out-of-period adjustments, the operation of the production property adjustment will reasonably accomplish matching of its proposed increases to rate year production plant and related expenses to test year circumstances.

73 The Company's initial proposed adjustments and its alternative adjustments both suffer from the same related flaws: they include costs that are not shown, on this record, to be known and they also include projects that are not supported, on this record, to be in service.

74 The Company's assertions that its pro forma adjustments to electric rate base are consistent with Commission practice miss the mark. It points to two Commission

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<sup>82</sup> By auditing such costs, Staff also determines whether these costs have been prudently incurred.

orders for the proposition that adjustments to test year data must necessarily include “estimates.” It cites our order in Docket UW-010877, and excerpts the following quote:<sup>83</sup>

These adjustments are . . . for known and measurable events that will occur prospectively (pro forma adjustments), to best estimate the relationship between the Company’s costs and revenues and thus establish rates that are fair, just, and reasonable and allow the Company the opportunity to earn a fair rate of return. (emphasis added)

The Company stretches the meaning of our sentence. The sentence means that once an event is determined to be known and measurable, it can then be used to best estimate the relationship between revenues and costs. The sentence does not stand for the proposition that all estimates of costs satisfy the known and measurable criteria.

75 The Company also points to our order in Docket U-85-36 for the proposition that all plant that is used and useful to serve customers during the rate year must be included in rates in order for rates to be “just, reasonable and sufficient.”<sup>84</sup> Our order stated:

. . . the rate base shown on the books is adjusted to take into account known and measurable changes which will occur during the period rates will be in effect. Such pro forma adjustments correct what would otherwise cause a miscalculation of the value of property that is used and useful for service.

Our statement made in 1985 remains correct in 2009, but it does not mean that any capital projected to be completed and serving customers qualifies as a known and measurable change, regardless of whether its actual costs are known or its actual completion and in service status can be confirmed.

76 In addition to these flaws, the Company’s initial proposal relies on a significant departure from the standard measurement of rate base. Except in rare circumstances, rate base is measured as an average over the test year. The Company proposes an

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<sup>83</sup> Norwood, Exh. KON-1T at 11:7-19 citing *Rainier View Water Order*, ¶ 29.

<sup>84</sup> DeFelice, Exh. DBD-4T at 3:3-7, citing *UTC v. Washington Water Power Company*, Cause No. U-85-36, Third Supplemental Order at 29-30 (April 4, 1986) [hereinafter *1986 Washington Water Power Order*].

end-of-period measurement of rate base calculated at a point in time three months *after* the end of the test year. While we could consider departing from the conventional method for measuring rate base if presented with good justification and additional steps to conform other test period data to the end-of-period point in time, we are not persuaded on this record that the significant departure the Company proposes is justified.<sup>85</sup> We share Staff's concern that the Company's method would disrupt test period matching of rate base with all other costs, revenues and cost of service components. Consequently, we reject the Company's initial adjustments as flawed in method.

77 The Company characterizes its alternative proposal as merely an extension of the Staff's adjustment. This characterization misses the point: the heart of Staff's adjustment is based on audited and verified information. The Company's alternative proposal includes projects planned to be completed in the second half of 2009 that are not demonstrated on this record to be in service and for which costs have not been audited and confirmed.

78 We recognize that the Company's capital investment continued beyond June 30, 2009, the date when Staff completed its audit, and that new plant not included in Staff's proposed adjustment may be in service during the rate year. But this fact is not sufficient to override the requirement that rates be set based on actual costs and that adjustments to test period cost data must comport with the regulatory requirements governing pro forma adjustments. The Company's proposal to include all planned 2009 capital additions is tantamount to requiring either a continuous audit during the pendency of a rate proceeding or acceptance of budgeted or forecast data as known and measurable. Staff correctly points out that for it to verify that costs are sufficiently documented and appropriate to include in rates, the dictates of practicality require its audit must conclude at some point in time before the conclusion of the rate review.

79 Public Counsel's proposed adjustments allow for no pro forma additions to rate base unless the project is included in the power cost model. This allows for no adjustments for transmission investment or other non-power-generating plant outside the test year even if it is possible to audit and confirm that projects are completed and in service

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<sup>85</sup> See, *infra*, n.48.

subsequent to the test year. We find this approach to be unnecessarily rigid. It fails to recognize the practical fact that capital investment is not confined to the test year and that rate regulation can and should have the flexibility to include out-of-period costs, so long as the important principles guiding pro forma adjustments are not violated.

80 With regard to the Noxon No. 3 upgrade, we also agree with Staff that it is appropriate to include the upgrade costs and related expenses in the rates we approve in this proceeding. Staff's adjustment to net rate base appropriately reflects that the Noxon No. 3 upgrade will be in service for only 9 months of the rate year.

81 The Noxon No. 3 adjustment is notable and unusual because, as all the parties agree, the project upgrade will not be completed until March of 2010. All parties also agree that the project costs can be included in rates in this proceeding because they are sufficiently well established and certain that the project can be included in the power cost model that yields net power costs for the rate year. By approving the Staff's recommendation, we are knowingly making an exception to strict application of the principles guiding pro forma adjustments. The Noxon No. 3 upgrade is not yet in service. The agreement among all parties that the Noxon No. 3 costs are appropriate to include, together with the importance of the project and Staff's testimony that the plant will be completed on time and is a prudent project, allows us to make an exception in this limited case and in these circumstances. Our decision here should not be taken as precedent for other capital additions that present different facts and circumstances.

82 Based on the foregoing analysis and discussion, we find appropriate an adjustment to increase net electric rate base by \$35,844,000 and decrease associated NOI by \$1,033,000.

**c. Pro Forma Rate Base – Capital Additions – Natural Gas**

83 *Positions of the Parties.* The Company proposes two pro forma adjustments to natural gas rate base. The Company's first adjustment parallels its proposed adjustment to electric rate base. It adds capital projects for the final calendar quarter of 2008 and calculates net rate base as end-of-period rather than average-of-monthly-averages. The Company uses end of calendar year 2008 as the point of measurement for its end-of-period net rate base.<sup>86</sup> By this adjustment, it proposes to increase net rate base by \$1,234,000, increase NOI by \$294,000 and *decrease* revenue requirement by \$309,000.<sup>87</sup>

84 The Company's second adjustment also parallels its proposed adjustment to electric rate base to include all capital projects budgeted for calendar year 2009.<sup>88</sup> The Company uses end of calendar year 2009 as the point of measurement for its end-of-period net rate base. By this adjustment, the Company proposes to increase natural gas net rate base by \$6,094,000, decrease NOI by \$596,000, and *increase* revenue requirement by \$1,766,000.<sup>89</sup>

85 The combined effect of these two adjustments to plant accounts and related expenses is to increase rate base by \$7,328,000, decrease NOI by \$302,000, and increase revenue requirement by \$1,457,000.

86 The Company's rationale for these adjustments is the same as its rationale for the proposed capital addition adjustments to electric rate base. It asserts that its

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<sup>86</sup> DeFelice, Exh. DBD-1T at 19:1 – 22:11.

<sup>87</sup> Andrews, Exh. EMA-1T at 46:1-8.

<sup>88</sup> In combination, the 2008 and 2009 projects at issue include enhancements to the Jackson Prairie gas storage facility and projects to enhance or replace various components of the natural gas distribution system. DeFelice, Exh. DBD-1T at 16:17 – 17:35.

<sup>89</sup> Andrews, Exh. EMA-1T at 46:9-19.

adjustments are necessary to reflect plant investment that will be in service providing benefit to customers during the rate year.<sup>90</sup>

87 Staff and Public Counsel object to these adjustments as improper pro forma adjustments that are not known and measurable, are not shown to be in service and used and useful, and violate the matching principle. Staff also objects to the Company's end-of-period method for measuring rate base accounts.<sup>91</sup> Staff and Public Counsel recommend that the Commission reject both the Company's 2008 and 2009 adjustments.<sup>92</sup>

88 The Company objects that Staff's and Public Counsel's recommendations will deprive it of \$7.3 million of rate base and \$1.5 million in annual revenue for projects that it asserts are known and measurable, that have minimal or no offsetting factors, and that will be used and useful for customer benefit in the rate year.<sup>93</sup> According to the Company, it excluded capital projects used to connect new customers and new revenue, and only included projects that do not produce new revenue.<sup>94</sup>

89 As an alternative to its preferred proposal, the Company offers another approach for calculating adjustments to include plant additions for 2008 and 2009, similar to the Staff approach and the Company's alternative approach for the electric rate base adjustment. In the Company's rebuttal case, Mr. Howell describes three natural gas distribution projects he says were completed and put in service between October 2008 and July 31, 2009: "Qualchan Reinforcement", "Nine Mile Gate Station", and "Gas Distribution Minor Blanket." He also provides estimates of offsetting factors for these projects. The net investment for these three projects is \$4,373,358.<sup>95</sup>

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<sup>90</sup> DeFelice, Exh. DBD-1T at 2:7 – 3:7.

<sup>91</sup> Kermode, Exh. DPK-1T at 31:21 – 32:8.

<sup>92</sup> *Id.* at 32:12-18 and 35:12-23; *see also* Larkin, Exh. HL-1T at 14:19 – 15:13.

<sup>93</sup> DeFelice, Exh. DBD-4T at 5:5-19 and 11:1-13.

<sup>94</sup> Howell, Exh. DRH-1T at 3:14-19.

<sup>95</sup> *Id.* at 5:4 – 8:2.

- 90 Also in the Company's rebuttal case, Mr. DeFelice describes a fourth natural gas distribution project that was completed and put in service between October 2008 and July 31, 2009: "Replace Gas ERTs with Batteries Older than 10 Years". He provides an estimate of offsetting operation and maintenance costs and says that, net of estimated offsetting operation and maintenance cost savings, investment in this gas distribution project was \$733,000.<sup>96</sup> Mr. DeFelice also describes three "general plant" projects he says were completed and in service by July 31, 2009, for a net investment of another \$980,063.<sup>97</sup>
- 91 The Company proposes to pro form the above described four natural gas projects, and the portion of three additional general plant projects allocated to natural gas operations, that were completed and in service by July 31, 2009, totaling \$5,516,000 in rate base, net of accumulated depreciation and deferred taxes through calendar year 2010. The effect of the Company's rebuttal case alternative is to reduce net operating income by \$168,951 and increase revenue requirement by \$894,000. The latter figure compares to the Company's original total request for \$1,313,000 million of new revenue related to its 2008 and 2009 capital additions.<sup>98</sup>
- 92 *Commission Decision.* As post-test-year adjustments to rate base accounts, the Company's proposed natural gas capital additions adjustments must comport with all three of the principles guiding pro forma adjustment that we have previously discussed. We focus our analysis on the Company's alternative proposal. The adjustment the Company initially proposes involves a significant departure from measuring rate base as an average during the test-year. By proposing an end-of-period measurement (indeed, an end point three months *after* the end of the test-period) the Company eliminates the test year benefit of matching all cost of service elements. Moreover, the Company has taken no additional steps to cure the mismatch created by the end-of-period method by measuring historical revenues and other elements at the same point in time. As we noted in our discussion of the electric rate base adjustments, under exceptional circumstances we could accept a departure from

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<sup>96</sup> DeFelice, Exh. DBD-4T at 17:15-26.

<sup>97</sup> *Id.* at 18:1-36. Note that a portion of these general plant projects is also included in the Company's alternative electric capital addition adjustment.

<sup>98</sup> *Id.* at 16:1 – 17:2.

the convention of measuring rate base as a test year average, but the Company has not provided sufficient cause for us to do so here. Consequently, we reject the Company's initial proposed adjustment as flawed in method.

93 Turning to the rebuttal proposal, the Company provides evidence, in the form of a table (Exh. DBD-10), that purports to show the projects it seeks to add to rate base accounts were put in service by the middle of 2009. However, in contrast to the evidence of record on the electric plant additions, we have no Staff audit or testimony demonstrating the costs reported and the project completion dates. Lacking such demonstration, the post-test-year data contained in Exh. DBD-10 is not of the same quality as the audited data we rely upon in our analysis regarding the adjustments to electric rate base.<sup>99</sup>

94 With regard to the principle of matching, the Company asserts that the set of projects it seeks to include does not include projects undertaken to add new customers or to provide additional revenues. The Company provides estimates of the revenue or cost savings it believes could be attributable to each of the projects during the rate year. While these estimates may be accurate, this approach misconstrues the principle of matching. It implies that the necessary matching is limited solely to offsetting factors caused by the project in question. The principle of matching requires that all cost of service components – revenue, investment, expenses and cost of capital – be evaluated at a similar point in time. Staff is correct to point out that this requires consideration of all of the Company's costs and revenues.<sup>100</sup>

95 In ratemaking for the electric side of the Company's operations, the production property adjustment is a method applied broadly to rate year production plant, costs and revenues to scale them to test period loads. While this method does not provide a perfect replica of test year matching, it is superior to a project-by-project approach. There is no production property adjustment employed on the natural gas side, so the protections against injury to the matching principle afforded by that method are not present in the Company's case or generally in natural gas ratemaking.

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<sup>99</sup> We reiterate our previous cautions that data introduced late in a proceeding does not carry the benefit of full examination by our staff and the parties and therefore is accorded less reliability and weight.

<sup>100</sup> Staff Brief, ¶¶ 49-51.

96 Considering the lack of audited evidence regarding the actual amount of plant investment and the project completion dates, and the absence of a ratemaking mechanism to preserve against injury to the matching principle, we conclude that the Company's proposed pro forma adjustments to test period natural gas rate base are not appropriate and should be disallowed. Our decision again does not preclude recovery of the capital additions in a future proceeding where costs and offsetting benefits are reflected in test year data, or otherwise thoroughly documented consistent with the principles governing pro forma adjustments reiterated here.

**d. Other Contested Pro Forma Adjustments**

**(1) Production Property Adjustment**

97 *Positions of the Parties.* The Company makes a pro forma adjustment to both electric rate base and electric net operating income to reflect the ratios of test year retail load divided by the pro forma period and the projected rate period loads.<sup>101</sup> After reflecting the agreements in the Partial Settlement, the Company's adjustment reduces rate year adjusted net rate base by \$5,926,000 and increases NOI by \$2,014,000.<sup>102</sup>

98 The purpose of a production property adjustment is to adjust pro formed rate year production costs to comport with test year loads.<sup>103</sup> In this case, no party opposes the application of a production property adjustment; instead, the parties dispute the appropriate methodology. All parties also agree that, regardless of the methodology used, the final production property adjustment will depend on resolution of all production and transmission related adjustments. The adjustment, therefore, will require updating to reflect final decisions regarding these adjustments.<sup>104</sup>

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<sup>101</sup> Andrews, Exh. EMA-1T at 21:21 – 22:13.

<sup>102</sup> Andrews, Exh. EMA-6 at 9.

<sup>103</sup> See Kermode, Exh. DPK-1T at 24:14-20; *see also* Staff Brief, at 14-16.

<sup>104</sup> Knox, Exh. TLK-8T at 3:6-14.

99 The Company proposes a new method for calculating this adjustment that relies on separate production factors for 2009 and 2010, and application of these production factors only to pro formed costs, not to production costs already included in test year results. The Company asserts that only pro formed costs need be matched to test year loads and that unadjusted production costs do not require an adjustment to test year loads because they are already matched with test year billing determinants.<sup>105</sup> It claims that the method advocated by Staff, which applies the production factor to all rate year production plant and related costs, will cause the Company to under-recover its costs in the rate year.<sup>106</sup> Based on all of its proposed pro forma adjustments for capital additions, and after application of the revenue conversion factor, the Company's adjustment reduces the Company's revenue requirement by \$4,024,000.

100 Staff argues for continued reliance on the established method for calculating the production property adjustment. According to Staff, the established method ensures proper matching of all production rate base, including pro forma plant additions, and production related expenses with the test year rate loads. Staff asserts that the purpose of the adjustment is to "bring the pro formed rate year costs, on a unit basis, back to the historical test year for proper matching and comparability of all costs used in the revenue requirement determination."<sup>107</sup> Staff says that its method allows the Company to recover its test year costs at rate year loads, which is the objective of this type of adjustment.<sup>108</sup> Based on its adjustments to capital additions, Staff's adjustment reduces rate year adjusted net rate base by \$11,360,000 and increases NOI by \$2,464,000.<sup>109</sup> After application of the revenue conversion factor, the net effect is to reduce the Company's revenue requirement by \$5,469,000.

101 Public Counsel also proposes a production property adjustment. Public Counsel objects to the Company's adjustment because it includes the Company's projected capital additions for 2008 and 2009 as well as projected increases in property tax,

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<sup>105</sup> *Id.* at 2:17 – 3:3.

<sup>106</sup> *Id.* at 3:16 – 6:14.

<sup>107</sup> Kermode, Exh. DPK-1T at 25:4-7.

<sup>108</sup> Staff Brief, ¶ 39.

<sup>109</sup> Kermode, Exh. DPK-2, at 26:16-19.

operating and maintenance expense and other expenses with which it does not agree. In calculating its adjustment, Public Counsel uses two production factors. One is applied to test period production plant and the other is applied to Public Counsel's proposed pro forma adjustments to electric rate base and power costs for the rate year. Public Counsel's method differs from the Staff method and the Company method.<sup>110</sup>

102 The Company confirmed that Staff's method in this proceeding is the one used by the Company and approved by the Commission in Avista's last two general rate cases.<sup>111</sup> However, the Company points out a number of errors in the spreadsheet Staff used to implement the method and derive its adjustment.<sup>112</sup> Staff corrected these errors in a revised exhibit.<sup>113</sup>

103 *Commission Decision.* We noted earlier that the production property adjustment is an important mechanism for ensuring that pro forma adjustments to production plant and net power costs are properly matched to test period data. We are satisfied with Staff's representation that the method it advocates, and that the Company has used in the past, properly accomplishes the objective of the matching principle. Indeed, even Mr. Norwood, for the Company, describes application of the production property adjustment in a manner identical to the method used by Staff.<sup>114</sup> Staff's method recognizes that the whole of the pro formed production rate base will be used to accomplish service to customers in the rate year. Staff's method using a single, rather than multiple production factors, also recognizes that it is only the rate year costs that

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<sup>110</sup> Larkin, Exh. HL-1T at 10:12 – 11:12; Larkin, Exh. HL-3 at 10.

<sup>111</sup> Knox, TR. 692:23 – 693:1. See *UTC v. Avista Corporation*, Dockets UE-070804, UG-070805, and UE-070311 (*consolidated*), Order 05, Final Order Rejecting Tariff Sheets; Approving and Adopting Settlement Stipulation; Requiring Compliance Filing (Dec. 19, 2007) [hereinafter *2007 Avista Rate Case Order*]; *UTC v. Avista Corporation*, Dockets UE-080416 and UG-080417 (*consolidated*), Order 8, Final Order Approving and Adopting Multi-Party Settlement Stipulation and Requiring Compliance Filing (Dec. 29, 2008) [hereinafter *2008 Avista Rate Case Order*].

<sup>112</sup> Knox, Exh. TLK-8T at 8:5 – 11:5.

<sup>113</sup> Kermode, Exh. DPK-6 (revised October 5, 2009).

<sup>114</sup> Norwood, Exh. KON-1T at 20:26 – 22:4 (“Because retail rates are set using the lower number of customers and lower customer kWh sales for the 2008 test year, to preserve the matching principle, *the pro forma adjusted rate base* for the 2010 rate year is adjusted back to the 2008 test year through the production property adjustment.” (underline in original, italics added)).

are in need of adjustment to accomplish matching to the test year. Consequently, we are not persuaded to adopt a different production property adjustment method than that used and approved in multiple recent rate cases. We approve the method Staff proposed.

104 As Staff and the Company agree, the exact magnitude of this adjustment will require revision to reflect the disposition of all related adjustments in this case. We therefore require the Company to recalculate the Production Property Adjustment using the method shown in Exhibit DPK-6 as part of its compliance filing.

**(2) Labor – Executive and Non-Executive**

105 *Positions of the Parties.* The Company proposed pro forma adjustments to electric and natural gas test year results to reflect labor expense increases for 2008, 2009, and 2010.<sup>115</sup> Staff and Public Counsel generally agree that known and measurable company obligations, such as union wage increases resulting from collective bargaining agreements or non-union wage increases approved by the board of directors, are proper adjustments.<sup>116</sup> Staff says that the Company's 2008 and 2009 labor adjustments, revised to reflect actual salaries, meet this standard.<sup>117</sup>

106 Public Counsel agrees that the actual salaries for 2008 and 2009 meet the standard of known and measurable. However, Public Counsel recommends adjusting the 2008 salaries paid to executives to the same annualized increase received by administrative employees.<sup>118</sup>

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<sup>115</sup> Andrews, Exh. EMA-4T-C at 6:14 – 8:11.

<sup>116</sup> LaRue, Exh. AMCL-1T at 5, Larkin, Exh. HL-1T at 11-13; *see also* LaRue, TR. 685:5-11. Public Counsel's approach differs slightly from Staff's due to the methodology utilized for annualizing 2008 wage increases.

<sup>117</sup> LaRue, Exh. AMCL-1T at 6:2-5.

<sup>118</sup> Larkin, Exh. HL-1T at 11:23 – 12:19.

- 107 The Company objects to Public Counsel's adjustment to 2008 executive salaries contending that its data represents actual salaries paid to officers in 2008, not an estimate.<sup>119</sup>
- 108 Both Staff and Public Counsel dispute any adjustment that includes future wage levels to which the Company has not obligated itself, such as the proposed adjustment for 2010 wage increases.<sup>120</sup>
- 109 Originally, the Company pro formed expected 2010 salary increases of 3.8 percent for administrative, union, and executive employees. On rebuttal, the Company re-aligned its predictions about 2010 salary increases to be consistent with industry projections as of September 2009. The Company argues that its projections based on industry studies and the likely outcome of union negotiations are a reliable forecast of labor cost increases in the rate year; further, the Company asserts that it has regularly granted wage increases in March.<sup>121</sup>
- 110 *Commission Decision.* Labor costs are undeniably an ongoing expense incurred by the Company. Where there is clear documentation that labor expenses will increase because of known and certain increases in salaries, it becomes easier for us to justify this sort of pro forma adjustment. However, the Company's argument that its proposed 2010 wage increases are known and measurable is not persuasive. As noted in our discussion of basic principles, budget projections and estimates do not meet this regulatory standard. The Company's updates to its wage figures during the pendency of this proceeding counter any argument that next year's salary increases, if any, are known and measurable.<sup>122</sup> Past practice may demonstrate that the Company traditionally grants salary increases every year in March, but in this record the amount

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<sup>119</sup> Andrews, Exh. EMA-4T-C at 11:5-8.

<sup>120</sup> Staff Brief, ¶¶ 14-16 and 18; Public Counsel Brief, ¶ 163.

<sup>121</sup> Andrews, Exh. EMA-4T-C at 9:20 – 12:14.

<sup>122</sup> We encourage the Company to refine its data when it can, but in recommending pro forma adjustments, we are limited to approving those where the effect is known and measurable. As an example of how updated data can convert projections into known and measurable changes, see our discussion of the property tax adjustment, below.

for 2010 is simply not known.<sup>123</sup> Forecasts and estimates are, by their nature, uncertain. Here, the evidence is clear that the Company is not yet obligated to pay any specific level of wage increase in 2010. The Company's witness, Ms. Andrews, confirmed that the Board has not yet approved any increases for 2010 and that the Company is not obligated by contract other than the collective bargaining agreement to pay any wage increase in March 2010.<sup>124</sup>

111 Turning to Public Counsel's recommendation to annualize the 2008 executive salaries based on the increase granted administrative employees, we find there is no justification to make this adjustment. The Company has revised its salary data to represent what was actually paid to officers. Public Counsel provides no compelling reason to depart from this actual data.

112 We find reasonable Staff's recommendation to include 2008 and 2009 wage levels that are approved and already in effect and adopt the pro forma adjustments to electric and natural gas shown in Table 4 and Table 5.

### (3) Asset Management Program

113 *Positions of the Parties.* The Company's Asset Management Program (AMP) is a consolidated maintenance program for managing key components of Avista's transmission and distribution systems by modeling when to inspect and when to replace its wood poles, as well as evaluating downtown Spokane network and vegetation management programs.<sup>125</sup> Avista made pro forma adjustments to both its electric and natural gas results of operations to reflect its claim that AMP expenses have increased over 6 percent per year for labor, fuel and equipment costs. According

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<sup>123</sup> In these difficult economic times, it may be particularly hard to predict with any accuracy what an appropriate wage increase, if any, might be for Avista's employees and executive officers.

<sup>124</sup> Andrews, TR. 591:25 – 593:1.

<sup>125</sup> Kinney, Exh. SJK-1T at 17-28. Avista initiated the AMP in March 2004. Since at least early 2007, the AMP has included annual line patrols for all of the Company's 230 kV and some of the Company's 115 kV transmission corridors to ensure compliance with NERC Reliability Standard FAC-003-1. *Id.* at 15:37-38. The AMP also covers the Company's plans to perform vegetation management on a five year cycle for nearly 200 miles of its high pressure gas pipeline rights-of-way, in compliance with CFR 49 and WAC 480-93-188. *Id.* at 25:19 – 26:2.

to the Company, the three factors driving AMP costs higher than in the test period are the contract with Asplundh for vegetation management; special use permits and restrictions on road access by the U.S. Forest Service; and inflation of 6 percent based on the Asplundh contract.<sup>126</sup> The Company also asserts that our prior orders in Dockets UE-050482 and UE-070804 require it to increase its vegetation management and wood pole inspection programs, respectively.<sup>127</sup>

114 Commission Staff opposes this adjustment because it says the expenses proposed to be included are not known and measurable, but only management's estimates of future expenses. Further, there are no offsetting amounts for increased revenue or clear decreases in test year costs. Public Counsel also opposes these adjustments as not known and measurable and not offset with resultant cost savings or benefits, as was found to be the case in a recent proceeding in Idaho.<sup>128</sup>

115 On rebuttal, the Company asserted that its AMP expenses are not "merely budgeted costs" as Public Counsel contended, but based on "sound, historical experience" combined with a comprehensive asset management model that "maximizes the value of these capital assets" by "determining the future failure rates."<sup>129</sup> Even so, the Company conceded the absence of offsetting factors through 2010, but predicted there

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<sup>126</sup> Kinney, TR. 650:16 - 654:1.

<sup>127</sup> *UTC v. Avista Corporation*, Dockets UE-050482 & UG-050483 (consolidated), Order 5, Approving and Adopting Settlement Agreement with Conditions, ¶ 15 (Dec. 21, 2005) [hereinafter *2005 Avista Rate Case Order*] (Requiring the Company to spend approximately \$2.8 million annually on electric and natural gas vegetation management programs); *2007 Avista Rate Case Order* (Line 9 of Appendix 1 to Appendix 8 of the Settlement Stipulation requires the Company to establish a one-way balancing account and report to the Commission on the level of wood pole capital and expenses).

<sup>128</sup> Larkin, Exh. HL-1T at 16-17.

<sup>129</sup> Andrews, Exh. EMA-4T-C at 19-23.

would be O&M savings in later years.<sup>130</sup> The Company included estimates of offsetting factors for some of the program components.<sup>131</sup>

116 *Commission Decision.* The Company's ongoing effort to implement a comprehensive and efficient program to manage maintenance, facility upgrades, and capital replacements in its transmission and distribution systems is commendable. This activity promises to maximize the value of Avista's facilities, minimize operations and maintenance costs, and demonstrates prudent management. However, this expectation alone is not sufficient to justify a pro forma adjustment. Here, the tests of whether a pro forma adjustment to expense for the AMP is appropriate are two-fold: (a) whether the Company has proven that expenses have increased by known and measurable amounts over test year levels, and (b) whether any increased known and measurable expenses are net of offsetting factors.

117 The Company's evidence for increased transmission level expenses driven in part by increased regulatory requirements is unavailing; the North American Electric Reliability Corporation (NERC) standards, which the Company claims are a key driver of increased costs, were actually in place prior to the test year.<sup>132</sup> Consequently, these requirements are not new and the test year values must reflect some level of compliance costs. Although the Company's historical experience with this ongoing program may demonstrate that costs are generally rising, our record contains no specific evidence of the costs (or increased costs) contained in the Asplundh contract, whether from a new requirement for U.S. Forest Service road access permits or from a contract escalator clause regarding inflation. Further, our orders in prior dockets do not require the Company to increase its expenditures for

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<sup>130</sup> *Id.* at 20:13-16.

<sup>131</sup> The Company's offsetting factors included benefits associated with components of the program for distribution, transmission, substation, and network expense. *See* Andrews, Exh. EMA-4T-C at 21:11 – 23:11.

<sup>132</sup> NERC adopted its NERC Reliability Standard FAC-003-1 on February 7, 2006, with an effective date of April 7, 2006. By its terms, companies are required to comply with this standard by February 7, 2007. Mr. Kinney testifies that all NERC reliability standards became mandatory in June 2007. SJK-1T at 15:37-38. Consequently, Avista's requirements under this standard were in effect during the test year.

either vegetation management<sup>133</sup> or wood pole inspections.<sup>134</sup> Even if we had mandated some escalation in Company expenditures in a previous order, the Company must carry the burden of proving those increases are known and measurable and that they are not offset by other factors; the Company fails to so in this docket.<sup>135</sup> While we appreciate that the Company has offered some estimates of offsetting factors, these amount to estimates of benefits which are used to offset estimates of costs. In short, we are left with budget estimates rather than known and measurable values. Therefore, we adopt Staff's and Public Counsel's recommendation to disallow the AMP adjustments to the electric and natural gas test years.

#### (4) Information Systems

118 *Positions of the Parties.* The Company makes pro forma adjustments to both electric and natural gas test year results for labor and non-labor informational services costs planned for 2010 that exceed test year costs.<sup>136</sup> Its proposed adjustments would increase revenue requirement by \$1,114,000 on the electric side and increase revenue requirement by \$287,000 on the natural gas side.<sup>137</sup> The Company says these increased expenses are for additional labor costs to support software, mobile dispatch and outage management systems, non-labor costs for various software license and maintenance fees, and non-labor costs associated with replacing certain hardware and software.<sup>138</sup>

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<sup>133</sup> See *infra*, n.127, 2005 Avista Rate Case Order, ¶ 15. Our order did not compel that more than \$2.8 million be spent on vegetation management, nor did we address how an increase in cost for this purpose should be treated in future cases.

<sup>134</sup> *Id.*, 2007 Avista Rate Case Order. Our order did not compel any increase in expenditures nor did we address how any increase in costs should be treated in future proceedings.

<sup>135</sup> According to Company witness Scott Kinney, the net overall effect of the Company's increased electric AMP spending on O&M costs is an approximately \$100,000 increase over the test period for 2010. See Kinney, Exh. SJK-4T at 14:13 – 15:11.

<sup>136</sup> Andrews, Exh. EMA-1T at 26:12-15.

<sup>137</sup> Andrews, Exh. EMA-4T-C at 25:3-5.

<sup>138</sup> Kopczynski, Exh. DFK-1T at 7:22 – 8:7.

119 Staff again asserts that these expenses are “planned,” not known and measurable, and that the Company’s adjustment does not adequately quantify any offsetting benefits of the pro formed costs.<sup>139</sup> Public Counsel raises similar concerns.<sup>140</sup> Staff cites the paucity of information in the Company work papers, noting that the Company appears to “shift to Staff the responsibility to build detailed support for the proposed Company adjustments, through audits or data requests.”<sup>141</sup>

120 The Company responds that the costs proposed to be pro formed are known and measurable because they are associated with existing technology and labor that are already employed. It argues that many of the increased expenses do not provide offsetting benefits because they are associated with “compliance purposes” such as disaster recovery, business continuity, and maintaining a secure cyber and data environment.<sup>142</sup> The Company’s witness, Mr. Kensock, provides a list of 16 projects for which he identifies cost and offset estimates and an explanation of each project. He explains that the offsets he calculates represent savings in the information services department, rather than savings in the “operating areas in which these services are being utilized.” He asserts that savings offsets in other operating areas are already represented in the test year for applications initiated prior to, or during the test year. For three of the projects – Mobile Dispatch, Outage Management, and Web Applications – Mr. Kensock explains that new full-time employees are being hired and the labor expensed rather than capitalized in project development. For another project (Technology and Electronic Payment Service Providers) the Company estimates a 100 percent offset in costs and for one project the Company has delayed implementation until 2010. Mr. Kensock removes the cost for these two projects in revising the Company’s adjustment on rebuttal. For the remainder of the projects, he asserts that the costs have already been incurred since the close of the test year or are predictable based on license fees for new employees.<sup>143</sup> He concedes that the cost and

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<sup>139</sup> Kermode, Exh. DPK-1T at 43-44.

<sup>140</sup> Larkin, Exh. HL-1T at 17.

<sup>141</sup> Kermode, Exh. DPK-1T at 43:18 – 44:4.

<sup>142</sup> Kensock, Exh. JMK-1T at 3:9-13.

<sup>143</sup> *Id.* at 4:1 – 10:7.

offset figures he provides are estimates and that the two projects for which he removed the costs in revising for rebuttal the Company's originally filed adjustment were characterized as known and measurable in the original filing.<sup>144</sup>

121 *Commission Decision.* We encourage and support utility efforts to apply new technologies, including information processing systems, which may have the end result of benefiting customers. The Company's efforts in this regard are not questioned by Staff or Public Counsel, nor do we question them here. The Company claims that a majority of the costs it says have increased have been, or are being, incurred and that it has attempted to quantify offsetting benefits – at least within the information services department.

122 While our record contains summary tables of expenses, it does not contain invoices or other detailed evidence documenting actual expenditures, invoices, contracts, or other specific obligations to demonstrate that costs have increased beyond what is included in test year data. Nor does our record include details of the Company's calculation of estimates of offsetting savings. On the other hand, our record does show changes in what the Company initially characterized as known and measurable as the Company's plans have changed during the pendency of our review. This alone casts suspicion on the validity of the Company's proposed pro forma adjustment. Finally, the Company's estimates of offsetting benefits measure only the effect on costs incurred within the information services department, and not more broadly across Company operations. We understand that the Company claims that savings for existing applications are already represented in the test year, but given that three of the projects involve shifting labor from a capital to an operating expense, it is not reasonable to conclude that there are no effects at all realized in the rest of the Company's operations.

123 We conclude that the Company's pro forma adjustments for information services are not sufficiently supported because they lack specific cost documentation and lack a complete analysis of offsetting factors. Our rules require comprehensive and detailed work papers to support proposed pro forma adjustments. The Company's electric and natural gas pro forma adjustments are not supported as required and are not accepted.

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<sup>144</sup> Kensock, TR. 688:11 – 690:15.

(5) Incentive Program

124 *Positions of the Parties.* Avista makes incentive payments to officers and employees based on the Company achieving customer satisfaction and reliability targets. The actual incentive amounts paid are based on savings in utility operation and maintenance costs. In this case, the Company makes pro forma adjustments to both electric and natural gas test year results for its incentive program expenses to the level it expects to pay in 2009. In addition, the Company proposes to “normalize” recovery of incentive payment amounts in rates to a six year average based on payouts made from 2003 through 2009.<sup>145</sup> The Company’s proposed adjustments would increase electric revenue requirement by \$574,000 and natural gas revenue requirement by \$159,000.

125 Staff argues that the Company has not demonstrated any rationale explaining why the 2009 incentive payments are not normal and thus fails to provide any justification for using a normalizing average rather than actual test year costs.<sup>146</sup> Staff recommends eliminating the six year averaging and the use of the Consumer Price Index to convert all dollars to 2008. It proposes an adjustment to reduce test year expense producing a reduction in electric revenue requirement of \$18,202 and a reduction in gas revenue requirement of \$5,029.<sup>147</sup>

126 Public Counsel also opposes the Company’s use of the six-year average, arguing that incentive payout levels have been declining and that no increase is likely during 2009 due to the current economic conditions, making the known 2008 level an adequate representation.<sup>148</sup> Public Counsel argues that no pro forma adjustment is appropriate for either electric or natural gas operations.

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<sup>145</sup> Andrews, Exh. EMA-1T at 29:14 – 30:18.

<sup>146</sup> LaRue, Exh. AMCL-1T at 10-12.

<sup>147</sup> *Id.* at 11:13 – 12:2.

<sup>148</sup> Larkin, Exh. HL-1T at 19-20.

127 On rebuttal, the Company notes that Staff relied on an average for incentive pay in the Company's 2007 rate case when it served to reduce revenue requirements.<sup>149</sup> Further, the Company disagrees with Public Counsel's argument regarding economic conditions stating that its incentive program triggers are independent of the health of the economy. At hearing, Company witness Ms. Andrews testified that incentives are paid only if a target based on operation and maintenance cost per customer is achieved.<sup>150</sup>

128 *Commission Decision.* We last thoroughly analyzed Avista's incentive program in its 1999 general rate case. In that proceeding we disallowed certain costs tied to financial performance and found that the program was not tied to ratepayer benefit. The Commission nevertheless approved the program subject to correction of those problems.<sup>151</sup> The four Avista general rate cases since 1999 were resolved, at least in part, by settlement, and none specifically raised the treatment of an incentive program as a topic of interest.<sup>152</sup> In this proceeding, the issue of the incentive program is, for the first time in nine years, presented as a litigated matter for Commission review and decision. However, the record in this proceeding is insufficient to allow a comprehensive review or justify deviation from test year results.

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<sup>149</sup> Andrews, Exh. EMA-4T-C at 29-31.

<sup>150</sup> Andrews, TR. 607:12 – 610:24. Ms. Andrews also confirmed that ratepayers, not shareholders, pay both the incentive payments and the operation and maintenance costs upon which the incentive program is based. *See* Andrews, TR. 617:1-18.

<sup>151</sup> *See UTC v. Avista Corporation*, Dockets UE-991606 & UG-991607 Third Supplemental Order, at ¶¶ 271-273 (Sept. 29, 2000) [hereinafter *1999 Avista Rate Case Order*]. Since the 1999 rate case, Avista's incentive program has been tied to reduction in O&M costs. *See* Andrews, Exh. EMA-4T-C at 17:3-6.

<sup>152</sup> *See UTC v. Avista Corporation*, Docket UE-011595, Fifth Supplemental Order (June 18, 2002) [hereinafter *2001 Avista Rate Case Order*] (adopting a settlement stipulation which did not specifically address the incentive program); *2005 Avista Rate Case Order* (approving and adopting a settlement stipulation which did not specifically address the incentive program); *2007 Avista Rate Case Order* (approving and adopting a settlement stipulation that did not specifically address the matter of incentive programs, although the stipulated results of gas and electric adjusted results of operations did include restated incentive amounts); *2008 Avista Rate Case Order* (approving and adopting a multi-party settlement that includes the provision "adjust incentives to actual" in the appended summary table of agreed adjustments).

129 Thus, we reject both the Staff and Company adjustments and leave the Company's incentive program costs for electric and natural gas operations at the test year level. We direct the Company and all interested parties to review the program for a more thorough evaluation of how the incremental cost of employee incentives should be treated in rates. Based on such discussions and review, we direct that the Company address in its next rate case whether ratepayers should pay the incremental cost of incentives to achieve O&M savings when ratepayers are already paying the full costs of O&M. Further, if the cost of incentives is appropriate to include in rates, parties should also explain whether these costs should be normalized.

### (6) Insurance

130 *Positions of the Parties.* The Company adjusts insurance expense for general liability, directors and officers (D&O) liability, and property to the actual cost of insurance policies in effect in 2009.<sup>153</sup> Its adjustments increase electricity and natural gas revenue requirement by approximately \$228,000 and \$63,000, respectively.<sup>154</sup>

131 Staff and Public Counsel agree with the Company that insurance costs should be updated to reflect actual premiums paid for 2009. Staff agrees with the Company's proposed allocation of some of the cost to subsidiaries, and with the allocation of costs between electric and gas operations. Public Counsel argues Avista is allocating all of the D&O insurance premium to the utility and advocates that a portion be allocated to subsidiaries.

132 Staff and Public Counsel also argue that D&O insurance should be allocated 50/50 between ratepayers and shareholders because it provides benefits to both shareholders and ratepayers.<sup>155</sup> Staff proposes adjustments that *reduce* electricity and natural gas

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<sup>153</sup> Andrews, Exh. EMA-1T at 34.

<sup>154</sup> Andrews, Exh. EMA-6 at 12 and Exh. EMA-7 at 9.

<sup>155</sup> LaRue, Exh. AMCL-1T at 16-18. Staff also notes that California, Arkansas, and Connecticut share the D&O insurance cost 50/50, with Connecticut recently increasing shareholder responsibilities to 75 percent. *Id.* at 17:10 – 18:6. At hearing, Staff witness Ann Larue testified that her research showed that shareholders file the bulk of lawsuits against directors. *See* LaRue, TR. 682:18 – 683:5.

revenue requirement by approximately \$148,000 and \$19,000, respectively. Public Counsel's proposed adjustments to insurance and its separate adjustment to D&O insurance *reduce* electric and natural gas revenue requirements by approximately \$198,000 and \$51,000.<sup>156</sup>

133 The Company disagrees with the recommendation for a 50/50 sharing of the cost of D&O insurance between ratepayers and shareholders. The Company argues that without D&O insurance it would be unable to retain qualified directors who are vital to the fundamental governance of the Company. According to Company, the purpose of D&O insurance, like other insurance the Company secures, is to transfer risk to third-parties and reduce volatility in utility expenses and exposure to catastrophic financial losses.<sup>157</sup>

134 As an alternative position, if the Commission chooses to require that shareholders bear some part of the D&O insurance premium, the Company recommends a 90/10 split between ratepayers and shareholders. This is based on the formula currently used to allocate officer compensation between ratepayers and shareholders. The Company says this split would "equate to a revenue requirement reduction of \$72,000 electric and \$20,000 gas" from its adjustment.<sup>158</sup> Subtracting these figures from the Company's adjustment yields an overall insurance adjustment that increases electric and natural gas revenue requirements by \$156,000 and \$43,000, respectively.

135 *Commission Decision.* Aside from an error the Company points out in Public Counsel's adjustment,<sup>159</sup> the dispute about this adjustment centers on whether the cost

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<sup>156</sup> Larkin, Exh. HL-1T at 21-23. *See also* Exh. HL-5 at 4, column C-10, and Exh. HL-6 at 3, column C-5.

<sup>157</sup> *See* Andrews, TR. 525:25-526:21. Ms. Andrews also testified that risk is a factor in determining insurance coverage and that Avista has few subsidiaries that impose risks for which insurance coverage is secured. *Id.* at 581:1 – 584:2. According to Ms. Andrews, the cost of D&O insurance has declined since Avista sold Avista Energy. In 2007, prior to this sale, the 66 percent allocation to utility operations amounted to \$787,000; in comparison, in 2009, the 98 percent allocated to utility operations totaled \$721,000. Andrews, Exh. EMA-4T-C at 28:1-10.

<sup>158</sup> Andrews, Exh. EMA-4T-C at 31:2-4.

<sup>159</sup> In addition to opposing the 50/50 split, the Company objected to the level of Public Counsel's proposed D&O adjustment because it does not reflect the updated insurance premium information

of D&O insurance premiums should be split between customers and shareholders and, if so, by what percentages. There is no dispute about whether D&O insurance is a necessary expense for a publicly owned company, or whether the level of insurance coverage and premium amount paid by Avista is appropriate. The Company's argument that without insurance protection it would be unable to attract and retain qualified directors is persuasive. The Company's suggestion, however, that the shareholders do not benefit from the protection insurance provides the directors does not persuade us.<sup>160</sup> Clearly the shareholders have an interest in a well-managed company and attracting good directors promotes good management and benefits all involved, as they ultimately bear the responsibility of ensuring the Company is properly managed.<sup>161</sup>

136 We find that a company's directors benefit both shareholders and ratepayers. Shared benefit justifies some level of shared responsibility to pay the cost of D&O insurance. Staff and Public Counsel point us to decisions in other jurisdictions that require the cost of D&O insurance to be shared 50/50 between shareholders and ratepayers, but fail to establish how those decisions are relevant here and not simply illustrative of what has been done elsewhere.

137 We find on the basis of our limited record here that D&O insurance is a benefit that is part of the compensation package offered to attract and retain qualified officers and directors. Accordingly, it makes sense to split the costs in the same manner we require other elements of their compensation to be shared. Based on the formula currently used to allocate officer compensation between ratepayers and shareholders, this results in 90 percent of the costs being included for recovery in rates. After accepting the Company's revised overall insurance adjustment filed on rebuttal, our

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that has otherwise been agreed to among the Company, Staff, and Public Counsel. Andrews, Exh. EMA-4T-C at 27:6-14.

<sup>160</sup> Andrews, TR. 525:5-7.

<sup>161</sup> We note that Avista's directors owe a fiduciary duty to the corporation's shareholders to oversee with diligence and reasonable care the actions of the corporation. Simply stated, the directors must act *affirmatively and in good faith*, to protect the interests of the Company and its stockholders, and to refrain from doing anything that would injure the Company or deprive the Company of profit or an advantage that might properly be brought to the Company for it to pursue. The directors owe no fiduciary duty to protect the interests of the ratepayers.

approved 90/10 split results in an additional revenue requirement of \$156,000 for electric and \$43,000 for natural gas.<sup>162</sup>

**(7) Director Fees & Board Meetings**

138 *Positions of the Parties.* Avista included \$45,229 and \$12,501 (electric and gas) in test year cost from Board of Director meetings,<sup>163</sup> and \$544,333 and \$150,542 (electric and gas) in test year costs for Board of Directors fees.<sup>164</sup> Staff agrees that Board of Director meetings are a necessary cost of doing business and contends that the meetings benefit both ratepayers and shareholders. Therefore, Staff recommends adjusting the Company's expenses to reflect a 50/50 sharing of the meeting costs.<sup>165</sup> Staff does not address or propose an adjustment to Directors' fees.

139 Public Counsel recommends a 50/50 split between ratepayers and shareholders for all expenses incurred for Directors' meetings and Directors' fees. According to Public Counsel, the Board is the Company's ultimate governing authority, overseeing all company activities, and its primary responsibility is to protect shareholders' assets. Therefore, Public Counsel contends that it is not unreasonable to ask shareholders to bear half of the cost of the Board's meetings as well as half the cost of paying an attendance stipend to directors who are working part-time on behalf of the Company's shareholders.<sup>166</sup>

140 The Company disagrees with the arguments made by both Staff and Public Counsel, noting that Board of Directors expenses are a necessary expense of doing business to support financing the company and maintain access to capital markets.<sup>167</sup> According

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<sup>162</sup> We recognize that these figures may appear to be of modest consequence in this proceeding, but the question of shareholders and ratepayers equitably sharing the costs of mutually beneficial Company obligations is an important principle.

<sup>163</sup> Larkin, Exh. HL-1T at 23:20-24:2.

<sup>164</sup> *Id.* at 25:5-9.

<sup>165</sup> Kermode, Exh. DPK-1T at 20:5-21.

<sup>166</sup> Larkin, Exh. HL-1T at 23-25; Kermode, Exh. DPK-1T at 20.

<sup>167</sup> Andrews, Exh. EMA-4T-C at 31-33.

to Company witness Ms. Andrews, recruitment and retention of qualified directors who provide overall guidance for the utility “inures to the benefit of ratepayers.”<sup>168</sup> However, Ms. Andrews acknowledged that shareholders nominate and elect the Directors, not ratepayers. Ms. Andrews also confirmed that the Directors act on shareholder proposals, oversee both utility and non-utility activities of the corporation, and receive part of their compensation in the form of common stock.<sup>169</sup> As with the D&O insurance expense, the Company proposes a compromise of 90/10 sharing between ratepayers and shareholders if the Commission determines any sharing is necessary.<sup>170</sup>

141 *Commission Decision.* This disputed issue is similar in some respects to the disagreement over D&O insurance adjustments. The evidence of record regarding Directors’ fees and Directors’ meetings also supports the conclusion that the activities of the Board are essential to the function of the utility and its access to capital markets and therefore serve to benefit both shareholders and ratepayers. Both Staff and Public Counsel agree with the Company that the Board is necessary and that its expenses are a necessary cost of doing business.

142 The Company asserts that all of these costs should be borne by ratepayers or that, at most, there should be a 90/10 sharing. In our analysis of D&O insurance costs, we focused on the point that it is part of the officers’ and directors’ compensation package, necessary to attract and retain qualified management. In contrast, our focus here is on Board activities and expenses incurred during the year, many of which are shown by the record to not provide ratepayer benefit.<sup>171</sup> The record supports a finding

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<sup>168</sup> *Id.* at 32:5 – 33:2. At hearing, Ms. Andrews testified that shareholders benefit from a well-run company, but that “customers are the major benefit of the activities that are done by the board.” See Andrews, TR. 526:9-21.

<sup>169</sup> *Id.* at 561:18 – 569:8.

<sup>170</sup> *Id.* at 32:5-11. According to Ms. Andrews’ calculations, a 90/10 split would reduce revenue requirement for meetings by \$5,000 and \$1,000 (electric and natural gas), respectively.

<sup>171</sup> At hearing, Company witness Ms. Andrews confirmed a number of extravagances associated with Board of Director meetings, to include expensive hotels, meals, cruises, museum visits, Directors’ gifts, first class air fare, and entertainment. Ms. Andrews made some corrections to several thousand dollars in meeting cost items that should have been charged to non-utility

that the Board of Directors provides services that benefit shareholders to the same extent those activities benefit ratepayers. Therefore, we determine Directors' Fees and Meetings costs should be shared equally between shareholders and ratepayers. The effect of adopting this adjustment is to increase electric and natural gas net operating income by \$192,000 and \$53,000, and reduce revenue requirement by \$309,000 and \$85,000, respectively.<sup>172</sup>

### (8) Injuries & Damages

143 *Positions of the Parties.* The Company included a restating adjustment to replace the "accrual with actuals to obtain the six-year rolling average to injuries and damages not covered by insurance." The effect of the proposed adjustment is to decrease net operating income by \$56,000 and \$42,000 for electric and natural gas, respectively.<sup>173</sup> The revenue requirement impacts are an increase of \$90,000 for electricity and a decrease of \$68,000 for natural gas.

144 Staff does not oppose the Company's adjustment. Public Counsel does not object to the proposed adjustment, but argues that the Injuries and Damages reserve balance should be deducted from rate base. Public Counsel argues that to properly match the rate base with the expenses charged to ratepayers for injuries, the injuries and damages reserve liability must be deducted from rate base. Public Counsel's recommended adjustment to rate base removes the reserve balances and reflects the

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accounts and confirmed that first class air fare would no longer be booked to utility cost. *See* Andrews, TR. 570:5–575:17. These sorts of expenses, particularly in an era of belt tightening and cutbacks, do not cast the Company in the best light, particularly when seeking ratepayer dollars for such expenses. In any future rate proceedings, we expect that the Company will sort out those expenses related to Board of Directors' meetings that do not have any benefit to ratepayers and make the appropriate restating adjustment at the outset. The Company should not expect Public Counsel or Commission Staff to perform that review function.

<sup>172</sup> In essence, we adopt the end result of Public Counsel's proposed adjustment, though we reach that conclusion by a different analysis.

<sup>173</sup> Andrews, EMA-1T at 17:14-19 and 42:3-8.

effects on deferred taxes; as corrected at hearing, it would reduce electric rate base by \$107,000 and natural gas rate base by \$57,000.<sup>174</sup>

145 The Company opposed Public Counsel’s methodology, even with corrections to calculations; because “only actual claims that have been paid are included in the utility’s costs of service” and “the Company has not otherwise collected from ratepayers the reserve that has been recorded for financial purposes only.”<sup>175</sup>

146 *Commission Decision.* We conclude that Public Counsel’s proposed modification to the Company’s adjustment is flawed. Such an adjustment is not consistent with the standard accounting practice that we have previously approved for the Company’s injuries and damages reserve. The Company adequately explained its rationale and methodology for this adjustment as originally proposed. Therefore, we approve the Company’s proposal.

### (9) Customer Deposits

147 *Positions of the Parties.* Staff recommends adjustments to deduct from electric and natural gas rate base the average of monthly averages of customer deposits held by the Company. Staff argues that these deposits are a source of capital to the Company supplied by ratepayers, not by investors, and therefore should not be included in the Company’s rate base. According to Staff, this capital is less expensive than the Company’s cost of capital since the customer deposits earn interest at 0.42 percent.<sup>176</sup> The effect of Staff’s proposed adjustment on the electric side is to reduce rate base by \$2,473,256 and reduce net operating income by \$6,752, for a revenue requirement

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<sup>174</sup> See Larkin, Exh. HL-1T at 29:9 – 30:24 for original calculations proposing a \$7.7 million reduction in electric rate base and a \$1.2 million reduction in natural gas rate base. See Larkin, TR. 694:15 – 695:8 and Exh. B-5 for corrected calculations.

<sup>175</sup> Andrews, Exh. EMA-4T-C at 38:5 – 39:16. See also Avista’s Post-Hearing Brief, ¶ 121, nn.48 and 49.

<sup>176</sup> Staff also adjusts the Company’s net operating income to reflect payment of interest on the deposits.

decrease of \$334,000. On the gas side, this will reduce rate base by \$1,353,000 and net operating income by \$3,861 for a revenue requirement decrease of \$173,000.<sup>177</sup>

148 The Company opposes the concept of treating customer deposits as a form of financing. The Company asserts that it uses customer deposits to manage costs associated with its uncollectable accounts receivable, a short-term function. Thus, according to the Company, Staff's method effectively deprives the Company of its full return on the deducted rate base in exchange for compensation at the short-term interest rate the deposits actually receive. The Commission's rules and Company's implementing tariff make clear that the deposits must be returned, with interest, to customers after 12 months of solid payment history. Therefore, the Company interprets the rule and tariff language to mean that "customer deposits are simply a tool for the management of accounts receivable write-offs."<sup>178</sup>

149 *Commission Decision.* We have established the exclusion of customer deposits from rate base as our standard practice.<sup>179</sup> The Company does not deny that it holds a balance of customer deposits and does not argue that these deposits are somehow separated from its other working capital. The Company merely points to the rule and tariff language governing the charging and interest on deposits, but fails to explain how this language limits its use of the deposit money to "managing uncollectables." Requiring a utility to hold and then return a customer's deposit at a future time certain does not limit the Company's use of those funds to a single use during the interim holding period. We find the Company's assertions unpersuasive and adopt Staff's adjustments to electric and natural gas rate base.

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<sup>177</sup> Kermode, Exh. DPK-1T at 17:18 – 19:19 and Exh. DPK-2 at 4 (both exhibits revised November 6, 2009). We note that Public Counsel proposed a similar adjustment, but originally recommended a different calculation for the interest expense. At hearing, Public Counsel adopted Staff's calculation and now proposes an adjustment identical to Staff's. See Exh. B-5.

<sup>178</sup> Andrews, Exh. EMA-4T-C at 34:18 – 37:29.

<sup>179</sup> In regulating Puget Sound Energy, this has been the norm for approximately 25 years. Kermode, Exh. DPK-1T at 19:2-10. We recently approved this same treatment for PacifiCorp in an uncontested adjustment in that utility's 2006 general rate case. *UTC v. PacifiCorp*, Dockets UE-061546 & UE-060817 (consolidated), Order 8, Final Order Rejecting Tariff Sheets; Authorizing and Requiring Compliance Filing, ¶ 59 (June 21, 2007).

(10) Property Taxes

150 *Positions of the Parties.* The Company included a restating adjustment in its original filing to update property taxes to what was then (in January 2009) the most current information and to eliminate adjustments made “in the prior year.” This adjustment included property taxes now imposed by Oregon authorities on the Coyote Springs generating plant.<sup>180</sup> The Company’s initial restating adjustment decreased electric net operating income by \$939,000 and increased natural gas net operating income by \$193,000.

151 Public Counsel opposed the adjustment for electric operations because the Company’s adjustment based its calculations on projected taxes, which were therefore not known and measurable and not matched to test-year rate base at September 30, 2008. Public Counsel agreed with the natural gas adjustment to decrease property taxes.<sup>181</sup>

152 Staff recommended a property tax adjustment, but relied on actual tax assessments for 2009, rather than the projections used by the Company. Staff’s adjustment decreases net operating income for the electric side by \$127,000 and increases net operating income for the natural gas side by \$486,000. The related changes to revenue requirement are an increase of \$205,000 for electricity and a decrease of \$781,000 for natural gas.<sup>182</sup>

153 *Commission Decision.* The Company agrees with Staff’s electric and natural gas adjustments reflecting actual 2009 property tax rates and assessments.<sup>183</sup> Public Counsel’s selective handling of the proposed electric and natural gas property tax adjustments seems arbitrary and we reject it.

154 This pro forma adjustment illustrates the basic principles we discussed earlier in this order. Property taxes are an annual expense that is consistently known and must be

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<sup>180</sup> Andrews, Exh. EMA-1T at 16:21 – 17:5.

<sup>181</sup> Larkin, Exh. HL-1T at 8:16 – 9:24.

<sup>182</sup> Kermode, Exh. DPK-1T at 16:11 – 17:12.

<sup>183</sup> Andrews, Exh. EMA-4T-C at 33:17 – 34:11.

planned for every year. However, the exact amount of these taxes remains unmeasurable until the taxing authorities announce rates and property valuations for any given tax year. It is wholly appropriate to pro form new tax rates and assessments once they become measurable. Therefore, we approve the adjustments agreed to by Staff and the Company and reject Public Counsel's proposed adjustments. The effect is to decrease net operating income for the electric side by \$127,000 and increases net operating income for the natural gas side by \$486,000. The related changes to revenue requirement are an increase of \$205,000 for electricity and a decrease of \$781,000 for natural gas.

### (11) Coeur d'Alene Settlement

155 *Positions of the Parties.* In its 2008 electric general rate case in Docket UE-080416, Avista sought recovery of costs associated with the settlement of the Coeur d'Alene Tribe's (Tribe) claim for damages related to the operation of Avista's Spokane River Hydroelectric Project (Project), including its Post Falls hydroelectric facility located on the Spokane River downstream of Lake Coeur d'Alene.<sup>184</sup> Avista began operating the Project under Idaho state authority in 1907 and in 1972 requested a FERC license for its continued operation, but the Coeur d'Alene Tribe objected and intervened, claiming title to the lake.<sup>185</sup>

156 In 2001, after years of litigation in a number of forums, the United States Supreme Court ultimately determined that the United States holds, in trust for the Tribe, those portions of the lake within the boundaries of the Coeur d'Alene Reservation.<sup>186</sup> The Court's ruling did not settle the Tribe's dispute with Avista related to the historic and future use of the lake to benefit Project operations, including compensatory claims founded in Section 10(e) of the Federal Power Act for inundating reservation lands.<sup>187</sup> However, in 2008, Avista and the Tribe reached a comprehensive settlement whereby

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<sup>184</sup> 2008 Avista Rate Case Order, ¶ 67.

<sup>185</sup> *Id.*, ¶ 68.

<sup>186</sup> *Id.*

<sup>187</sup> *Id.*

Avista agreed to compensate the Tribe for past damages and future use of the lake to serve the Project.<sup>188</sup>

157 In approving the Settlement proposed in Docket UE-080416, the Commission allowed Avista to defer its Washington share of the 2008 and 2009 payments to the Tribe, totaling \$35.4 million, as a regulatory asset (CDA Asset), deferring recovery in rates spread over the remaining life of the project.<sup>189</sup> The Commission's approval of the Settlement in that docket resolved the accounting for the regulatory asset, but did not actually include recovery of the asset amortization in rates.

158 Public Counsel and other joint parties opposed the Settlement terms arguing that Avista's payments to the Tribe should be disallowed as imprudent because Avista "admitted to past trespass."<sup>190</sup> They also asserted that the settlement with the Tribe would require current customers to pay for past misconduct and usage charges resulting in retroactive ratemaking in violation of RCW 80.28.020, which requires the Commission to set rates prospectively.<sup>191</sup> The joint parties argued that the past Section 10(e) usage costs and past trespass damages are costs that should have been included in ratemaking for previous periods.<sup>192</sup>

159 The Commission rejected the joint parties' argument that Avista's operation of the Project or its actions in response to the Tribe's claim were imprudent, finding instead that "Avista operated the Project with authority from the entity it reasonably believed was the lawful owner, the State of Idaho, and, when challenged, it defended its right to operate it pursuant to the authority granted." The Commission also found that "without further legal recourse, Avista acted prudently to settle its dispute with the

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<sup>188</sup> *Id.*, ¶ 69. As compensation for past trespass and Section 10(e) water storage claims, Avista agreed to pay the Tribe \$25 million in 2008, \$10 million in 2009, and \$4 million in 2010. Future Section 10(e) compensation consists of flat annual payments of \$400,000 for the first 20 years of the license and \$700,000 flat annual payments for the remaining 30 years of the license.

<sup>189</sup> *Id.*, ¶ 70. For details on the resulting *pro forma* adjustments, see ¶ 71.

<sup>190</sup> *Id.*, ¶ 72.

<sup>191</sup> *Id.*

<sup>192</sup> *Id.*

Tribe and wrap the Project's relicensing issues into a comprehensive agreement ensuring long-term availability of valuable hydroelectric resources for the benefit of Avista's current and future ratepayers."<sup>193</sup>

- 160 The Commission also disagreed with the joint parties' assertion that the settlement constituted retroactive ratemaking, determining instead that "retroactive ratemaking involves the *current* collection, through rates, of *past* obligations," and noting that "until Avista reached a settlement earlier this year, it had no obligation to the Tribe."<sup>194</sup>
- 161 Public Counsel appealed the Commission's decision in Dockets UE-080416 and UG-080417 to the Thurston County Superior Court.
- 162 Avista now proposes to give effect to the cost-recovery terms approved in Docket UE-080416 through a pro forma adjustment adding \$16.8 million to electric rate base, decreasing NOI by \$539,000 and increasing revenue requirement by \$3.1 million at the Partial Settlement rate of return.<sup>195</sup> The adjustment includes one year of amortization based on an asset life of 45 years as well as the annual payment for 2009 agreed under the Tribal Settlement for use of the Tribe's property.
- 163 In this proceeding, Public Counsel points to its pending appeal and opposes the Company's adjustment. Public Counsel apparently accepts a pro forma adjustment to include the annual payment made under the agreement for use of Tribal property, but proposes to exclude amortization of the deferred asset and principal balance of \$16.8 million.<sup>196</sup> Public Counsel's proposed adjustment decreases NOI by \$168,000, increases revenue requirement by \$270,000 and allows no adjustment to rate base.
- 164 The Company acknowledges that the matter is under appeal, but argues that the Commission's Order in Docket UE-080416 is still in effect. The Company contends

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<sup>193</sup> *Id.*, ¶ 77.

<sup>194</sup> *Id.*, ¶ 78.

<sup>195</sup> Andrews, Exh. EMA-1T at 28:3-19.

<sup>196</sup> Larkin, Exh. HL-1T at 17:23 – 18:12.

that its adjustment is consistent with that order and that Public Counsel's adjustment should be rejected.<sup>197</sup>

165 *Commission Decision.* Public Counsel's appeal of our order in Dockets UE-080416 & UG-080417 (*consolidated*) is still pending before the court.<sup>198</sup> The Company is correct that unless and until the court orders otherwise, the provisions of our order are still in effect. The Company's pro forma adjustments in this proceeding are consistent with our prior order and are approved.

### (12) ERM Surcharge

166 *Positions of the Parties.* Schedule 93 is the Power Cost Surcharge added to base electricity rates to recover deferral balances generated by the Energy Recovery Mechanism (ERM) approved by the Commission in Docket UE-011595.<sup>199</sup> According to the Company, the deferral balance was \$15.7 million as of September 2009 and projected to decline to \$4.3 million by the end of December 2009.<sup>200</sup>

167 The Company proposes to eliminate the current Schedule 93 surcharge at the time the general rate increase is implemented, and to carry any remaining deferral balance forward for recovery in a future period.<sup>201</sup>

168 The Company says that the current ERM surcharge is 7.4 percent, based on currently charged base rates.<sup>202</sup> It projects that the balance will reach zero in February 2010,

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<sup>197</sup> Andrews, Exh. EMA-4T-C at 43:5-15.

<sup>198</sup> We understand that on Friday, December 18, 2009, the Thurston County Superior Court issued an oral decision that would uphold the Commission's Order in this matter.

<sup>199</sup> 2001 *Avista Rate Case Order*; Settlement at 7.

<sup>200</sup> Docket UE-011595, Monthly Power Cost Deferral Report, September 2009 (filed October 14, 2009).

<sup>201</sup> Morris, SLM-1T at 3:3-5 and Norwood, KON-1T at 30:18-20. The Company did not file a proposed change to Schedule 93 with the tariffs in this case. Schedule 93 is not under suspension. Mr. Hirschorn testifies that it "would file Schedule 93 with its tariff compliance filing in this case to reduce the present surcharge rate(s) to zero." Hirschorn, BJH-1T at 6:1-3.

<sup>202</sup> Hirschorn, BJH-1T at 2:27-29.

and contends that eliminating the surcharge would “partially offset the rate impact on customers and eliminate the number of rate of rate impacts experienced by customers in a short period of time, especially during the winter months.”<sup>203</sup>

169 Staff opposes eliminating the surcharge before the ERM deferral balance goes to zero. Staff argues that it is appropriate for customers to see the surcharge reduced to zero “on its own merits.” Staff contends that if the deferral balance reaches zero in January or February 2010, customers will see a surcharge go away that had been in place on their bills since October 2001.<sup>204</sup>

170 Responding to Staff, the Company modified its proposal. Instead of eliminating the surcharge, it proposes to reduce the surcharge to a level adequate to eliminate the deferral balance over 12 months. This change would be implemented at the conclusion of this case. The Company estimates that the surcharge would be reduced to approximately one percent.<sup>205</sup>

171 Public Counsel, does not oppose the Company’s proposal, but says that elimination of the surcharge should not be considered “as a component of the overall revenue request.”<sup>206</sup>

172 ICNU favors the Company’s modified proposal and says that the ERM surcharge should be reduced on the effective date of the new rates approved in this proceeding “in the interests of rate stability.”<sup>207</sup>

173 *Commission Decision.* The Company has not filed a change to the Schedule 93 tariff as a part of this rate proceeding. Consequently, the tariff is not suspended and is not at issue in this general rate case. The Schedule 93 surcharge is required to be “zeroed

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<sup>203</sup> Norwood, KON-1T at 30:13-14.

<sup>204</sup> Parvinen, MPP-1T at 14:15 – 15:2.

<sup>205</sup> Norwood, KON-1T at 30:20 – 31:10.

<sup>206</sup> Woodruff, KDW-1T at 5:3-7.

<sup>207</sup> ICNU Brief, ¶ 4.

out” when the deferral balance is eliminated.<sup>208</sup> We note that this is expected to happen in the next several months. Reducing the level of the surcharge prior to that point in time would offer rate relief during this difficult winter, in return for extending the surcharge at a lower level for some period of time.

174 We see value in the Company providing its customers with rate relief when it can, and we are sympathetic to ICNU’s preference for one modification to rates this winter, rather than two. Nevertheless, the Schedule 93 tariff is not properly before us in this proceeding and the matter of the ERM surcharge is not relevant to the question of whether the tariffs that are before us yield rates that are fair, just, reasonable and sufficient. The Company can choose its own time for filing a modification to Schedule 93, consistent with requirements of our order initially approving the tariff.

#### **D. Contested Issues – Lancaster Generation Facility**

##### **1. Positions of the Parties**

175 *The Company’s Proposal.* The Company seeks to recover in rates the costs associated with operation of the Lancaster Generating Facility, which is a 245 MW natural gas-fired combined-cycle combustion turbine (CCCT) plant located in Rathdrum, Idaho. Although the Company does not have an executed agreement regarding the plant’s operation, it intends to obtain the rights to operate this facility under a “tolling agreement” with Avista Turbine Power (Avista Turbine), a wholly-owned subsidiary of Avista Corporation. The Company affirms that the power supply expense included in the Partial Settlement Stipulation (which decreases test year NOI by \$6,904,000 and increases revenue requirement by \$11,101,000) includes the Lancaster generation plant expenses and revenues.<sup>209</sup> The Company also requests that we find prudent its arrangement with Avista Turbine.<sup>210</sup>

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<sup>208</sup> *2001 Avista Rate Case Order*; Settlement at 7-8 (“At the point in time when the Energy Cost Deferral Balance reaches zero, the Schedule 93 surcharge tariff will be eliminated. . .”).

<sup>209</sup> Johnson, TR. 922:1-9. *See also* Exh. RLS-6 at 13, which discusses the impact of the Lancaster contracts on the Company’s revenue requirement. According to Table 10, there is a \$12.9 million impact on revenue requirement for the 2010 rate year.

<sup>210</sup> Storro, Exh. RLS-1T at 8:13 – 9:8 and 16:13-26. *See also* Exh. RLS-3 for a map of the Lancaster Generating Facility’s location and a picture of the plant.

176 The Company's understanding with Avista Turbine for the control of the Lancaster facility requires review of the existing contracts between Avista Turbine and Coral Energy. These contracts consist of the Lancaster power purchase agreement (PPA), two transmission contracts, and three agreements for gas transportation from two delivery points, Alberta and Malin. By way of the power cost element of the Partial Settlement Stipulation discussed above, the Company also requests recovery of the cost of natural gas to be purchased as fuel for the Lancaster plant.

177 Avista explains that under the anticipated Lancaster PPA, it would have rights to dispatch Lancaster beginning January 1, 2010, and retain those rights through October 31, 2026.<sup>211</sup> As part of the transaction in which Avista Utilities would obtain control of the plant's output, the Company would be responsible for procuring and arranging transport of natural gas fuel to the plant and arranging the subsequent transmission of electric power from the plant.<sup>212</sup>

178 The Lancaster plant is currently interconnected to the Bonneville Power Administration (BPA) transmission system.<sup>213</sup> Avista Corporation now holds (in the name of Avista Energy) two transmission agreements for a total of 250 MW of long-term firm transmission capacity from the Lancaster plant to BPA facilities at the John Day dam. These agreements are temporarily assigned to Coral Energy, and would be permanently assigned to Avista Utilities after January 1, 2010.<sup>214</sup> Avista Corporation expressed its intent to rely on these transmission rights while evaluating a direct interconnection between the Lancaster plant and the Company's own transmission system.<sup>215</sup> The Company says it is in the process of jointly studying with BPA the

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<sup>211</sup> Storro, Exh. RLS-1T at 10:4-6.

<sup>212</sup> *Id.* at 10:6-9.

<sup>213</sup> *Id.* at 10:19-20.

<sup>214</sup> *Id.* at 10:20 – 11:2.

<sup>215</sup> *Id.* at 11:2-3. *See also* Storro, TR. 775:14-16 (observing that the plant is within 300 feet of Avista Corporation's own transmission network).

prospect of interconnecting its transmission to BPA's Lancaster substation and this process is expected to take a minimum of two years.<sup>216</sup>

179 The Lancaster plant is also interconnected to the Gas Transmission Northwest (GTN) pipeline system.<sup>217</sup> On January 1, 2010, Avista Utilities would receive permanent assignment of firm natural gas transport rights on the TransCanada Alberta and TransCanada B.C. systems and temporary assignment of firm gas transport rights on the GTN system. These contracts provide access to three different natural gas hubs: AECO (via TransCanada) and Malin or Stanfield (via GTN),<sup>218</sup> but terminate on October 31, 2017.<sup>219</sup>

180 The Company relies on a White Paper<sup>220</sup> and two studies to support its assertion that utility acquisition of the Lancaster contracts would be prudent:<sup>221</sup>

- Lancaster Generating Facility Power Purchase Agreement Evaluation Overview (Evaluation Overview Study) completed on April 11, 2007, and
- Thorndike Landing Study (TL Study) performed by an independent evaluator and completed on October 30, 2007.

181 The Company's own Evaluation Overview Study concludes that the Lancaster contracts were more cost-effective than building a new "greenfield" plant and also a better option than a "brownfield" project.<sup>222</sup> According to the Company, the

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<sup>216</sup> Lafferty, Exh. RJL-1T at 4.

<sup>217</sup> Storro, Exh. RLS-1T at 10:10-11.

<sup>218</sup> *Id.* at 10:15-18.

<sup>219</sup> *Id.* at 10:11-18.

<sup>220</sup> The White Paper, completed on November 2, 2007, summarizes two other studies completed earlier in 2007 and described more fully below. The White Paper is contained in Exh. RLS-6.

<sup>221</sup> Storro, Exh. RLS-1T at 11:4 – 14:10 and 15:8 – 17:2; the Company's internal Evaluation Overview Study is contained in Exh. RLS-4. Thorndike Landing's "Independent Valuation of Lancaster Facility Tolling Agreement" is contained in Exh. RLS-5.

<sup>222</sup> Storro, Exh. RLS-1T at 12:3-8. The Company indicates it has not been able to identify any brownfield projects with a cost approximating \$550 per installed kW.

independent TL Study used several different valuation methods and concluded that the Lancaster PPA was financially favorable relative to other natural gas fired options in the Northwest.<sup>223</sup>

182 Based on these studies, subsequent observations of market transactions and the need for capacity referenced in its 2007 IRP, the Company asserts that acquisition of the Lancaster PPA and the associated transmission and gas transport contracts by Avista Utilities would be prudent.<sup>224</sup>

183 *Public Counsel's Opposition.* Public Counsel opposes the Company's request to include the Lancaster contracts in 2010 rates and advances three separate arguments.<sup>225</sup> First, Public Counsel contends that the Company's decision to assign the Lancaster contracts to Avista Utilities did not comply with the various prudence and other criteria established by the Commission.<sup>226</sup> Second, Public Counsel argues the Commission should reject assignment of any of the Lancaster contracts to Avista Utilities for calendar year 2010 because the Company has not shown a capacity need for the plant in that year, and short term energy purchases may be less expensive.<sup>227</sup> Third, Public Counsel recommends the Commission either entirely reject the Lancaster contracts or only allow assignment of the Lancaster PPA to Avista Utilities beginning in 2011, along with 80 percent of the gas transportation contract's cost and capacity, rejecting as unnecessary for the Company's needs the assignment of the BPA transmission contracts and the remaining 20 percent of the gas transportation contracts.<sup>228</sup> Public Counsel points out that the Company's own studies show that the

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<sup>223</sup> *Id.* at 12:20 – 16:12. The TL Study assumed that the output from Lancaster could be interconnected to the Avista transmission system and that the BPA transmission rights would be remarketed or otherwise optimized. *Id.* at 13:3-4.

<sup>224</sup> *Id.* at 16:13-17.

<sup>225</sup> Woodruff, Exh. KDW-1T at 3:1-13 and 5:14 – 35:11.

<sup>226</sup> *Id.* at 8:8 – 12:13. Public Counsel takes the position that each of the three Lancaster contracts is severable and should have been separately valued by the Company. *See* Public Counsel Brief, ¶ 98.

<sup>227</sup> Woodruff, Exh. KDW-1T at 12:14 – 16:10 and 33:13 – 34:11.

<sup>228</sup> *Id.* at 16:11 – 17:12 and 28:12 – 33:12. *See also* Public Counsel Brief, ¶ 148.

Lancaster Contracts would increase power cost expense by approximately \$18 million on a system basis in 2010.<sup>229</sup>

184 Public Counsel also asserts that in the settlement stipulation establishing Avista's Energy Recovery Mechanism (ERM),<sup>230</sup> the Company agreed not to enter into electric or natural gas commodity transactions with Avista Energy until the Energy Cost Deferral Balance (ECDB) falls to zero or Avista obtains agreement from all settling parties in relevant prior dockets.<sup>231</sup> Public Counsel contends that the Lancaster PPA transaction is a "commodity transaction" under any reasonable interpretation of that term as used in the ERM Settlement agreement.<sup>232</sup>

185 In addition, Public Counsel points out that assignment of the Lancaster contracts from Avista Turbine to Avista Utilities would be an affiliate transaction and Avista did not cite any affiliate transaction rules as applicable to this proposal.<sup>233</sup> It asserts that without a "market test" to determine what other resources were available to the Company, the Commission does not have sufficient information to draw conclusions regarding the reasonableness or prudence of the Lancaster contracts.<sup>234</sup> Further, Public Counsel contends that Avista's failure to issue a request for proposals (RFP) to

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<sup>229</sup> Public Counsel Brief, ¶ 122.

<sup>230</sup> See *2001 Avista Rate Case Order*, Appendix B. At page 7 of the Settlement, Section 4.e states: "Transactions with Avista Energy: The Company agrees that it will not enter into any electric or natural gas commodity transactions with Avista Energy related to Avista Utilities' electric operations until the Energy Cost Deferral Balance carries a net credit balance. This provision does not preclude transactions between the two companies related to Avista Utilities' natural gas distribution business."

<sup>231</sup> Woodruff, Exh. KDW-1T at 11:3-22. See also Public Counsel Brief, ¶¶ 108-114. ICNU did not file testimony on the Lancaster contracts, but it raises an identical concern in its Brief at ¶ 14.

<sup>232</sup> Public Counsel Brief, ¶ 110.

<sup>233</sup> Woodruff, Exh. KDW-1T at 5:16 – 7:16 and 10:10-24. See also Public Counsel Brief, ¶¶ 105-106 and ICNU Brief, ¶ 11.

<sup>234</sup> Woodruff, Exh. KDW-1T at 12:1-3; Public Counsel cites to the "lower of cost or market" standard set out in the Commission's decision in *UTC v. Avista Corporation*, Docket No. UG-021584, Sixth Supplemental Order Rejecting Benchmark Mechanism Tariff, ¶ 32 (Feb. 13, 2004).

meet the power capacity need identified in its 2007 Integrated Resource Plan (IRP) appears to violate the requirements of WAC 480-107.<sup>235</sup>

186 Noting that the pro forma power supply adjustment agreed to in the Partial Settlement Stipulation includes Lancaster costs, Public Counsel recommends a further adjustment to remove costs associated with the Lancaster contracts from the rate year. Public Counsel's recommended adjustment to power cost increases NOI by \$779,000.<sup>236</sup>

187 *Company Response to Public Counsel.* In reaction to Public Counsel's challenges, the Company asserts that the Lancaster contracts are not above-market and provides a table of levelized costs of comparable Northwest CCCTs that recently have been sold.<sup>237</sup> The Company also disagrees with Public Counsel's claim that the Lancaster contracts were acquired too early, countering that resources are often "lumpy" and rarely come into service on a schedule that perfectly meets a Company's needs.<sup>238</sup> Further, the Company disagrees with Public Counsel's assertion that an RFP was required because it interprets the rule to mandate issuance of an RFP only if a resource deficit is projected to occur within three years of the publication of the IRP.<sup>239</sup>

188 The Company also opposes Public Counsel's adjustment to remove the cost of the Lancaster PPA for the year 2010, claiming that the plant is cost-effective over the life of the plant.<sup>240</sup> Asserting that a prudence determination should be based on information available at the time of the decision, the Company also asserts that the

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<sup>235</sup> Woodruff, Exh. KDW-1T at 12:9-13. *See also* Public Counsel Brief, ¶ 107.

<sup>236</sup> Exh. B-5, Electric Schedules, Revised (Oct. 19, 2009), at Tab A-1, column AH.

<sup>237</sup> Kalich, Exh. CGK-4T at 2:7-10.

<sup>238</sup> *Id.* at 3:1-5.

<sup>239</sup> *Id.* at 8:16-20.

<sup>240</sup> *Id.* at 1:21 – 4:21.

average post-Lancaster project costs are more than twice the cost of Lancaster if other plant costs are adjusted to 2010 dollars.<sup>241</sup>

189 The Company opposes Public Counsel's proposed adjustment to remove the costs of the BPA transmission contracts for the year 2010 asserting instead that they are essential for the Lancaster plant.<sup>242</sup> It points out that the assumption as to remarketing three-quarters of its transmission capacity was based on the long-term operation of the plant.<sup>243</sup> The Company describes the recovery of transmission costs as an assumption entered into the financial models.<sup>244</sup> As a result, its projected revenues for the remarketing of BPA transmission reflected in the power cost rates in the Partial Settlement are also assumptions.<sup>245</sup> Although Lancaster has been operated by Avista Turbine since 1999,<sup>246</sup> it has just begun the process of interconnecting the plant to Avista's transmission system.<sup>247</sup>

190 The Company also opposes Public Counsel's adjustment to remove 20 percent of the costs of the gas transport contracts asserting that the extra capacity would be used to help meet the utility's peak needs when it runs the Lancaster and Coyote Springs 2 plants simultaneously.<sup>248</sup> The Company reveals that it does not have enough long-term firm gas transport capacity to operate both plants at full capacity and will have to

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<sup>241</sup> *Id.* at 12:5-12.

<sup>242</sup> The Company describes the Lancaster contracts as having two BPA transmission contracts: one that can be terminated on two years notice and one that cannot be terminated. The Company also indicates the two BPA contracts are insufficient to deliver the Lancaster plant's full output capacity and that the Company will purchase non-firm transmission to deliver the additional output above 250 MW. *See* Lafferty, Exh. RJL-1T at 2:10-12 and 3:1-3.

<sup>243</sup> Storro, Exh. RLS-4T at 3.

<sup>244</sup> Storro, TR. 780:5-21.

<sup>245</sup> *Id.* at 868:2-8.

<sup>246</sup> *Id.* at 797:16-17.

<sup>247</sup> Lafferty, TR. 905:11 – 906:3; *see also* Exh. RJL-2-X.

<sup>248</sup> Lafferty, Exh. RJL-1T at 6:1-4.

buy additional capacity.<sup>249</sup> It asserts that were the Commission to disallow all or a portion of the costs associated with the transmission or gas transport contracts as suggested by Public Counsel, the Company would need to examine other alternatives for Lancaster, rather than dedicating it for the benefit of its ratepayers.<sup>250</sup>

191 As to the circumstances Avista Corporation faced when it secured the facility and transferred its rights to Avista Turbine, Avista Utilities emphasizes the very limited window of opportunity within which Avista Corporation could act, given the pending sale of Avista Energy.<sup>251</sup> It states that there was neither time nor the requirement to obtain a formal RFP.<sup>252</sup> It argues further that the Lancaster contracts were the lowest cost resources at the time of the decision, April of 2007,<sup>253</sup> and without Lancaster it would need to build a CCCT plant to serve its load at a cost premium of 50 percent or more, which would not be in its customers' long-term interests.<sup>254</sup>

192 At hearing the Company revealed under questioning from the bench that Avista Turbine holds the long-term rights to the Lancaster contracts and that there is no written agreement between Avista Utilities and Avista Turbine regarding the transfer, sale or assignment of the Lancaster contracts.<sup>255</sup> Nor, according to the Company, would there be such a transfer should the Commission reject the Company's proposed rate treatment. During the proceeding and in written testimony, it insisted that Lancaster would only be transferred to the utility when and if the Commission

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<sup>249</sup> *Id.*

<sup>250</sup> Kalich, Exh. CGK-4T at 16:9-11.

<sup>251</sup> Avista Brief, ¶ 37 [emphasis in original].

<sup>252</sup> *Id.*

<sup>253</sup> *Id.*, ¶ 48.

<sup>254</sup> Kalich, Exh. CGK-4T at 18:11-13.

<sup>255</sup> Storro, TR. 817:22-24. While the Company testified that the transaction was between two affiliated corporations, it was only after the evidentiary hearing that it conceded that the proposed transaction constitutes an affiliated transaction and is therefore governed by the Commission's principle that the costs of affiliated interest transactions are reflected in rates at the lower of market or cost. *See* Avista Brief, ¶ 45, n.15.

approves recovery of its future costs.<sup>256</sup> If the Commission did not allow all Lancaster costs into rates, then Avista Turbine would explore other transfer or sale opportunities that better reward the shareholders of Avista Corporation.<sup>257</sup>

193 *Position of Staff at Hearing.* Staff did not pre-file responsive testimony regarding the Lancaster contracts. At hearing, however, Staff voiced its support for a finding of prudence for the Lancaster contracts.<sup>258</sup> Staff opined that acquisition of the Lancaster tolling agreement would not violate the ERM settlement agreement because the tolling agreement is not a commodity.<sup>259</sup> However, Staff agreed that the Lancaster contracts are affiliate transactions.<sup>260</sup> Staff witness Alan Buckley indicates that the fact that Lancaster was a low-cost resource compared to other natural gas plants in the region “overrode” in his mind the considerations of the affiliate interest statute that are designed to protect the ratepayer.<sup>261</sup> Staff testified that it believes the issuing of an RFP to compare the Lancaster contracts to bids from an RFP would not have changed Staff’s ultimate conclusion.<sup>262</sup>

194 Staff based its opinion regarding prudence on (1) a balance of interests between the Company’s shareholders and ratepayers, (2) the long-term effect on rates rather than the effect today, (3) the administrative burden of analyzing market transactions to meet resource needs versus long term contracts (4) the qualitative comparison of other similar transactions in the market place and (5) analysis of the cost and attributes of other similar natural gas plants reviewed recently by the Commission.<sup>263</sup> However,

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<sup>256</sup> The “regulatory out clause” became a repetitive theme for the Company. See Avista Brief, ¶¶ 22, 32, 37, 42 (twice), ¶ 43 (four times), ¶ 44 (twice), ¶ 45, and ¶ 55. See also Kalich, CGK-4T at 16:9-11 and Storro, TR. 815:23 – 818:18.

<sup>257</sup> Storro, TR. 777:1 – 778:24.

<sup>258</sup> Buckley, TR. 939:24-25.

<sup>259</sup> *Id.* at 942:5-17.

<sup>260</sup> *Id.* at 945:9-13.

<sup>261</sup> *Id.* at 945:19 – 946:9.

<sup>262</sup> *Id.* at 957:20-23.

<sup>263</sup> *Id.* at 948:3 – 950:14; Staff Brief, ¶ 74.

Staff testified it was a surprise to discover that there was no contract between Avista Utilities and Avista Turbine to transfer the Lancaster contracts.<sup>264</sup>

195 Staff reiterates its position in support of the prudence of the Lancaster contracts on briefing.<sup>265</sup> Staff concludes that the presence or absence of a contract between Avista Utilities and Avista Turbine is not determinative because Avista Corporation, the parent corporation, has a duty to both its ratepayers and its shareholders and there is no guarantee that the Corporation would hold off on perhaps dealing with another utility in order to save the Lancaster contracts for Avista Utilities in 2011.<sup>266</sup> Staff explains its position on the ERM settlement prohibition on “commodity transactions” as applying to hourly, secondary market purchases, not to the acquisition of the full operating rights of a large power plant.<sup>267</sup> Staff also agrees with the Company that the acquisition “should” meet the affiliate transaction standard of lower of cost or market and cites to five pages of Company testimony in support of its conclusion.<sup>268</sup>

196 *ICNU*. *ICNU* recommends that the Commission should adopt a result on Lancaster that provides the most benefits to customers, while sending a message to Avista that ignoring the rules applicable to affiliate transactions will not be tolerated.<sup>269</sup>

197 *ICNU* asserts that when Avista knew in 2007 it intended to assign the Lancaster tolling agreement to Avista Utilities, it should have filed an affiliate interest application with the Commission seeking approval of the transfer pursuant to RCW 80.16.020. *ICNU* describes a similar incident in a 1999 rate case in which Avista failed to file for approval of an affiliate interest transaction and instead filed

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<sup>264</sup> Buckley, TR. 946:6-15.

<sup>265</sup> *Id.*, ¶ 73.

<sup>266</sup> *Id.*, ¶ 75.

<sup>267</sup> *Id.*, ¶ 76.

<sup>268</sup> *Id.*, ¶ 77.

<sup>269</sup> *ICNU* Brief, ¶ 15.

for recovery in a general rate case without ever acknowledging the affiliate nature of the transaction.<sup>270</sup>

198 ICNU also notes that there is no evidence of record that Avista Utilities tried to negotiate a later start date of 2011 for the Lancaster contracts.<sup>271</sup>

## 2. Compliance with Emissions Performance Standard

199 In response to questions posed from the Bench during and subsequent to the evidentiary hearing, the Company says it believes that the Lancaster PPA must comply with the Greenhouse Gases Emissions Performance Standard (EPS) established in RCW 80.80.<sup>272</sup> In further response to our questions, and despite the fact that it filed no request in its direct or rebuttal cases, it seeks our determination in this proceeding that the Lancaster arrangement will comply with the EPS.<sup>273</sup> The Company points to elements of evidence here and there in our record that it asserts will carry its burden to demonstrate compliance with the standard. This evidence includes an air permit issued by the state of Idaho the Company offers subsequent to the evidentiary hearing as an attachment to our bench request.<sup>274</sup> Avista asserts that evidence of record demonstrates that the greenhouse gas emissions related to the Lancaster PPA are 810 pounds of CO<sub>2</sub> per MWH, well below the standard of 1,100 pounds.<sup>275</sup>

200 Staff argues that the EPS standard does not apply because the requirements imposed by RCW 80.80 only apply to power supply contracts entered into after June 30, 2008. According to Staff, the record shows that “Avista Utilities, through its affiliates (subsidiaries), has continuously held the capacity and electric rights under the

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<sup>270</sup> *Id.*, ¶¶ 12, 13.

<sup>271</sup> *Id.*, ¶ 13.

<sup>272</sup> Norwood, TR. 1083:10 – 1086:8.

<sup>273</sup> Exh. B-13 (supplemental response, October 15, 2009) and Avista Brief, ¶ 31.

<sup>274</sup> Exh. B-14 (response to Bench Request No. 13, October 13, 2009).

<sup>275</sup> Avista Brief, ¶ 31.

Lancaster PPA since 1998, with the exception of the limited term when those rights were assigned to Coral, with reversionary rights to Avista Utilities (through Avista Turbine) in 2010.”<sup>276</sup>

201 Public Counsel and the Northwest Energy Coalition say that the provisions of RCW 80.80 do apply to the Lancaster PPA. Public Counsel contends that prior to July 1, 2008, the Lancaster PPA was held by an unregulated subsidiary and that the “utility does not acquire the rights to the power, if at all, until January 1, 2010.”<sup>277</sup>

202 Avista argues that the information it points to in the record is sufficient and that the “sensible” approach is for the Commission to make the determination it requests in this proceeding.<sup>278</sup>

### 3. Commission Decision

203 The Lancaster matter is extraordinary. Our record contains evidence and argument that demonstrate sharp disagreement regarding whether the Lancaster contracts are a prudent and cost-effective resource to include in customer rates. However, those issues of fact and perspective are not what make the matter extraordinary. Lancaster is extraordinary for what is *not* in our record, and for the unique way in which the Company presented the matter to us.<sup>279</sup>

204 The Company seeks a prudence determination and recovery in customer rates for a power contract that it has not provided to the Commission for the record in this case.

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<sup>276</sup> Exh. B-16 (response to Bench Request No. 12, October 14, 2009).

<sup>277</sup> Exh. B-15 (NWEC response to Bench Request No. 12, October 14, 2009) and Exh. B-18 (Public Counsel response to Bench Request No. 12, October 15, 2009).

<sup>278</sup> Avista Brief, ¶ 31.

<sup>279</sup> A utility’s initial filing in a general rate case must contain the maximum amount of information then available to the company. Staff, Public Counsel, and intervening parties cannot always thoroughly investigate and vet new information and figures submitted later in the proceeding. We recognize that some data and figures will be subject to updating or supplementation, but the evidentiary crucible of the rate case proceeding is deprived of its effectiveness if key facts and positions are not contained in the initial filing.

Indeed, during the hearing, it conceded that the contract had not been executed.<sup>280</sup>

The Company concedes that the PPA that has been anticipated since 2007 would be a transaction with an affiliated interest,<sup>281</sup> yet our record contains no affiliated interest filing with which to determine compliance with the requirements of RCW 80.16.020 and our rule, WAC 480-100-245, regarding such transactions.

205 Further, the Company concedes that the anticipated power purchase arrangement must comply with the greenhouse gases emissions performance standards set out in RCW 80.80 and our rules at WAC 480-100-405 through -435, yet it filed no request for a determination in its direct or rebuttal cases.<sup>282</sup> It requests our approval without having filed a comprehensive presentation of evidence adequate for the parties to examine and for us ultimately to determine whether the standard applies and, if it does, if the anticipated PPA would comply.

206 Finally, the Company presents us with the proposed PPA as an ultimatum – it will execute the agreement only if we approve the ratemaking treatment requested as a condition precedent.

207 These are not mere technical deficiencies in the Company's case. They constitute failure on the part of the Company to bring a matter properly before us. Accordingly, we need not (indeed, cannot) reach the related issues of whether the Lancaster PPA acquisition is prudent and whether its associated costs can be put in rates because the issues are not properly before us. Furthermore, the Company's tone is troublesome. In effect, the Company suggests we take a "trust us" approach. However, we require more than trust to support a rate filing. Regulated utilities carry the burden of

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<sup>280</sup> Storro, TR. 817:22-24. Subsequent to the hearing, and after the close of the record and the completion of briefing, the Company provided a copy of an agreement dated December 7, 2009, for the sale of the output of the Lancaster facility. From the face of the cover letter, it was unclear whether the Company intended to file the contract in this rate case docket or in a new docket seeking approval of an affiliated interest arrangement. Accordingly, the Commission sought clarification through a letter from the Executive Director and Secretary of the Commission. The Company responded on December 11, 2009, that it did *not* intend to file the contract in this rate case docket, but only in a new affiliated interest proceeding.

<sup>281</sup> Storro, TR. 810: 2-16; Avista Brief, ¶ 45, n.15.

<sup>282</sup> Exh. B-13.

demonstrating that the rates they propose will be fair, just, reasonable and sufficient.<sup>283</sup> The Legislature enacted these various requirements for sound policy reasons and required us to enforce them. We do so here. We cannot approve the Company's request to find the Lancaster contracts prudent and the associated costs put into rates for the following three reasons.

208 First, although there is no dispute that the Company has consistently stated its intent to acquire rights to control and operate the Lancaster plant, the fact remains that there is no contract before us.<sup>284</sup> Avista made this decision in early April 2007, following an internal evaluation, but prior to the public announcement regarding the sale of Avista Energy.<sup>285</sup> Shortly thereafter, Avista communicated this decision to its investors via its 2007 Annual Report.<sup>286</sup> Nevertheless, the Company did *not* file a contract reflecting this intent with the Commission at any time during 2007 or 2008. Further, the Company never submitted an executed contract between Avista Utilities and Avista Turbine as part of its filings in this proceeding.<sup>287</sup>

209 In its brief, the Company characterizes the lack of a contract for the transfer of the Lancaster contracts as a matter of "housekeeping" and easily cured by its own internal "ministerial act."<sup>288</sup> In a self-serving statement regarding the significance of the fact that there is no contract in the record regarding any commitment between Avista

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<sup>283</sup> RCW 80.28.020.

<sup>284</sup> Avista Brief, ¶ 42.

<sup>285</sup> See Exh. RLS-4; Avista Brief, ¶¶ 32 and 37; and Exh. RLS-19-X.

<sup>286</sup> See Exh. KDW-7, at 2-3 (corresponding to pages 14-15 of the Annual Report). We note that Avista stated not only its firm intent for Avista Energy to contract for the Lancaster PPA from 2010 through 2026, but also its recognition that the rights associated with the PPA could not be transferred to the regulated utility until it obtained future approval from this Commission and the Idaho Public Utilities Commission.

<sup>287</sup> See Exh. RLS-22-X (response acknowledges the lack of written documentation regarding the Company's obligations to purchase power from the Lancaster plant). To the best of our knowledge, the Company's only filing with the Commission of a Lancaster contract occurred on Tuesday, December 8, 2009. On Friday, December 11, 2009, the Company clarified that its filing was intended as a new affiliated interest proceeding, not as a supplement to these dockets.

<sup>288</sup> Avista Brief, ¶ 43.

Turbine and the Company regarding the Lancaster plant, the Company's Brief provides that "the short answer to Chairman Goltz's question is that the absence of such a contract to reassign the PPA to Avista Utilities does not matter."<sup>289</sup> We disagree. Moreover, we are surprised that the Company apparently fails to recognize the importance of providing the Commission with the executed terms and conditions of a contract it asks us to approve. Without the contract, the Company cannot carry its burden of proof. In other words, the contract *does* matter.

210 Second, RCW 80.16.020 requires the Company to file with the Commission a copy of nearly any contract or arrangement it enters with an affiliated interest. The language is expansive:

Every public service company shall file with the commission a verified copy, or a verified summary if unwritten, of a contract or arrangement providing for the furnishing of management, supervisory[,] construction, engineering, accounting, legal, financial, or similar services, or any contract or arrangement for the purchase, sale, lease, or exchange of any property, right, or thing, or for the furnishing of any service, property, right, or thing, other than those enumerated in this section, hereafter made or entered into between a public service company and any affiliated interest as defined in this chapter . . . .

211 The filing must be made prior to the effective date of the contract and thereafter the Commission is empowered to investigate and disapprove the contract if the Company fails to prove the contract is reasonable and consistent with the public interest.

212 There is no dispute that Avista Turbine is an affiliated interest of Avista Utilities. Further, there is no dispute that the Company had settled on its arrangement to obtain dispatch control of and power from the Lancaster plant approximately 2 ½ years in advance of the desired January 1, 2010, effective date of a contract. The Company has made clear that it understood its obligations to make an affiliated interest filing with regard to the Lancaster contracts.<sup>290</sup> Nonetheless, no such filing is part of our

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<sup>289</sup> Avista Brief, ¶ 44 (emphasis added); *see also* ¶ 41 referencing Chairman Goltz's question posed at hearing.

<sup>290</sup> *See* Avista Brief, ¶ 45, n.15.

record. As a result, we see no regulatory route or method that would enable us to satisfy our statutory duties to evaluate this affiliated transaction.<sup>291</sup>

213 If the Company's original filing in January 2009 had included the required affiliated interest submissions, we have no doubt that the parties to this case would have created a sufficient record on which we could enter our determination. For reasons not explained, the Company failed to timely make the required filing that might have allowed us to grant the relief it seeks.

214 This is particularly puzzling given that this is not Avista's first experience handling an affiliated interest filing. In 1999, the Company failed to provide notice in its case in chief of an affiliated transaction with Spokane Energy, LLC, one of its subsidiaries. In that matter, the Company repeatedly asserted that it was not required to file or even notify the Commission of its arrangements with an affiliated interest. Although we ordered the Company to promptly make the required filing, we refrained from penalizing the Company for its omissions.<sup>292</sup> Accordingly, because of the lack of any affiliated interest approval, we cannot reach the issues Avista seeks to put before us.

215 Third, we cannot approve the costs of the Lancaster facility in Avista's rates because we need to make a decision whether it complies with RCW 80.80, and we cannot do so on this record.

216 All baseload electric resources built or acquired by utilities after June 30, 2008, and all baseload power purchase agreements of longer than five year duration entered into by utilities after June 30, 2008, must comply with the greenhouse gases emissions

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<sup>291</sup> The Company not only failed to present us with the actual terms and conditions of its agreement; it also failed to support its representations as to the potential agreement's costs. Again, we are asked to take it on faith that the unspecified terms will reflect the costs actually paid by Avista Turbine. Furthermore, the Company did not support its market analysis with other PPAs that may be available to it for the same period. Instead, its market analysis relied solely on the cost of power plants sold in the region with full ownership rights. While not quite an "apples to oranges" comparison, the difference between a tolling agreement and actual ownership could have a significant impact on costs.

<sup>292</sup> 1999 Avista Rate Case Order, ¶¶ 67-70.

performance standard of 1,100 pounds per MWH set out in RCW 80.80.<sup>293</sup> The statute imposes on us the responsibility to ensure that new electrical company power supply resources comply with this standard.<sup>294</sup>

217 This statute requires the Commission to first determine whether a new power resource is “baseload electric generation” – defined by statute as a resource that operates with a capacity factor of no less than 60 percent.<sup>295</sup> If the resource is not baseload electric generation, the requirements of RCW 80.80 do not apply and electrical companies do not receive certain special rights regarding cost deferral granted by the statute.<sup>296</sup> Our responsibility in this area is a new one, and we take it very seriously. We are especially mindful of the first cases we are obligated to address under this statute in order to ensure that a deliberate and thorough process is established for future cases.

218 The Commission shares the responsibility for regulating compliance with the EPS with the Department of Ecology (WDOE) and the Energy Facility Site Evaluation Council (EFSEC) for power plants located within the borders of Washington, to the degree these agencies must condition permits under their jurisdiction on compliance with the standard.<sup>297</sup> But, in the instance of an out-of-state power plant (or contract for power supply from an out-of-state power plant), we are the sole agency with EPS enforcement authority over electrical companies because the EFSEC and WDOE have no permitting jurisdiction over out-of-state facilities. This fact underscores the importance we place on our responsibility in these circumstances. The proposed Lancaster PPA is just such a circumstance.

219 If a new power resource is “baseload electric generation,” then the statute describes two alternate methods by which the Commission may approve any “long-term financial commitment” for such a resource. The relevant portions of RCW 80.80.060 are as follows:

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<sup>293</sup> RCW 80.80.040.

<sup>294</sup> RCW 80.80.060(2).

<sup>295</sup> RCW 80.80.060(3).

<sup>296</sup> RCW 80.80.060(6).

<sup>297</sup> RCW 80.80.040(13).

(1) No electrical company may enter into a long-term financial commitment unless the baseload electric generation supplied under such a long-term financial commitment complies with the greenhouse gases [gas] emissions performance standard established under RCW 80.80.040.

(2) In order to enforce the requirements of this chapter, the commission shall review in a general rate case or as provided in subsection (5) of this section any long-term financial commitment entered into by an electrical company after June 30, 2008, to determine whether the baseload electric generation to be supplied under that long-term financial commitment complies with the greenhouse gases [gas] emissions performance standard established under RCW 80.80.040.

(5) Upon application by an electrical company, the commission shall determine whether the company's proposed decision to acquire electric generation or enter into a power purchase agreement for electricity complies with the greenhouse gases [gas] emissions performance standard established under RCW 80.80.040. The commission shall not decide in a proceeding under this subsection (5) issues involving the actual costs to construct and operate the selected resource, cost recovery, or other issues reserved by the commission for decision in a general rate case or other proceeding for recovery of the resource or contract costs.

220 The first of the two methods is discussed in subsection (2), quoted above. That allows the Commission to review “in a general rate case” a “long-term financial commitment entered into” by the Company after June 30, 2008. Because the Lancaster PPA was not entered into prior to the rate case, subsection (2) cannot apply. The second way is discussed in subsection (5). That allows review by the Commission of a “proposed decision” to “enter into a power purchase agreement.” But if that statutory route is chosen, the statute prohibits the Commission from deciding in that proceeding “issues involving the actual costs to construct and operate the selected resource, cost recovery, or other issues reserved by the commission for decision in a general rate case.” So, neither option works for Avista. Indeed, the statute simply prohibits the Commission from considering the matter of a *proposed* agreement in this case.

221 In this proceeding we are presented by Avista with an eleventh hour request that we in effect “mine the record,” in lieu of the Company making its own organized presentation, to satisfy ourselves that sufficient information is present for us to find that its proposed Lancaster acquisition would comply with the EPS. As we consider this unusual request, we are mindful of three important points. First, WAC 480-100 clearly places the burden on the Company to demonstrate that a new power acquisition complies with the EPS.<sup>298</sup> Second, while the Company points us to elements of evidence scattered through our record that it claims satisfy the requirements of our rules, our staff and the other Parties have not had the opportunity to examine and test this evidence for the purpose to which it is now put by the Company. Third, the Company is asking us to exercise for the first time an important and new responsibility regarding contracts for out-of-state power supply in a last minute and ad hoc manner.

222 We contrast this situation with our recent proceeding regarding PacifiCorp’s acquisition of a new in-state power resource, the Chehalis generating plant.<sup>299</sup> In that proceeding, we considered an organized company presentation and a thorough Staff analysis before making an EPS determination. In this proceeding we have neither, yet the Company urges us to act because it says to do so would be “sensible.”

223 Our record evidence, in the unorganized and ad hoc manner the Company has presented it, leaves us unable to conclude that the EPS even applies in this instance. This is a threshold issue. The Company has not demonstrated and we are not able to conclude with certainty from our own evaluation that the proposed Lancaster PPA qualifies as “baseload electric generation.” Moreover, Staff has raised legitimate questions about the application of RCW 80.80 in the context of serial ownership and a complicated transaction with an affiliate of the electrical company. Finally, as to compliance with the EPS, if it applies at all, the heat-rate data and Idaho air permit data the Company commend to our attention is useful, but insufficient without

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<sup>298</sup> WAC 480-100-405, “Electrical companies bear the burden to prove compliance with the greenhouse gases emissions performance standard under the requirements of WAC 480-100-415 or as part of a general rate case.”

<sup>299</sup> *UTC v. PacifiCorp*, Docket UE-090205, Order 09, *Final Order Approving and Adopting Settlement Stipulation* (Dec 16, 2009).

supporting analysis and corroborating engineering testimony. In general, technical data, such as this, must be presented or supported by an expert witness and subject to cross-examination before we can find it to be relevant and reliable. Accordingly, we cannot approve at this time Avista's request under RCW 80.80.

- 224 *The Company's Ultimatum is Tantamount to Making the Commission a Contract Party.* We are also concerned with the framing of the issue in the form of an ultimatum to the Commission: if you do not approve this arrangement that you do not have before you and for which there have been no affiliated interest or RCW 80.80 filings, we will not enter into the agreement even though it is of great benefit to the ratepayers.
- 225 The Commission considered a "regulatory out clause" in a 2004 proceeding involving Puget Sound Energy's contract for purchase of a power plant from a third party.<sup>300</sup> In that matter, given the facts of the transaction in question, we concluded that the contract was not contrary to the public interest. However the case before us presents significantly different facts. First, the arrangement at issue here is a contract with an affiliated interest, not a third party. The contracting parties are in a practical sense representing the same interest. Second, the "regulatory out clause" in our prior case was bilateral, optional, and related only to our approval of the power plant acquisition, not any specific ratemaking treatment. In the present case, the Company says it intends to enter a contract that can be "unwound" if the "appropriate ratemaking treatment" is not approved.<sup>301</sup> We do not have to reach a decision about the appropriateness of the "regulatory out" language in the contract, as it is not even in the record, and, as described above, there are other prerequisites as well.
- 226 In sum, in this case, we do not authorize the Company to recover in rates any costs associated with the Lancaster facility. We conclude that the Lancaster contracts cannot be included in 2010 rates and must be removed from the Company's power

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<sup>300</sup> *UTC v. Puget Sound Energy, Inc.*, Docket No. UE-031725, Order 12, *Granting Regulatory Approvals for Frederickson I Acquisition; Resolving Disputed Gas Price Issue* (April 7, 2004).

<sup>301</sup> Avista Brief, ¶ 43. The Company's claim that following any undesirable ratemaking treatment from the Commission it would simply "unwind" any contract it makes with its affiliate Avista Turbine Power raises the question of why such a contract wasn't signed long ago.

costs included in the Settlement Agreement. We adopt Public Counsel's adjustment to pro forma power supply that increases test period NOI by \$779,000 to accomplish this result. We require the adjustment to be revised by the compliance we require. Avista must make a compliance filing to revise the pro forma power supply adjustment by rerunning its power supply model with all aspects of Lancaster removed and all other assumptions and inputs equivalent to those used to calculate power supply for the Partial Settlement Stipulation.<sup>302</sup>

227 Our decision here does nothing to prevent the Company from seeking recovery of Lancaster costs or deferred balances in the future. Without having the Company's detailed filings before us, we decline to permanently disallow the 2010 Lancaster costs or find the entire contract imprudent for its full term. We acknowledge that the Company's IRP identifies a need for new cost-effective energy and capacity resources over the next decade. Staff and the Company both represent that taking a long-term view of the Lancaster contracts suggests they may be beneficial to ratepayers. However, we cannot reach that issue and make such a conclusion at this time.

228 Notwithstanding the discussion above, because of the uniqueness of the confluence of facts and law on the Lancaster issue, we will allow the Company to defer the costs associated with the Lancaster PPA and associated contracts subject to the following requirements and limitations.<sup>303</sup>

229 The Company is authorized to defer, in an account separate and apart from the ERM deferral, the net costs of contracts for power supply, transmission, fuel gas transportation, and fuel gas related to the Lancaster generating facility. Any recovery

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<sup>302</sup> In essence, this parallels what Public Counsel argues with regard to its proposed adjustment to PF-1. *See* Larkin, Exh. HL-1T at 10:3-6 and Woodruff, Exh. KDW-1T at 38 (Table 7). We note that Kalich, Exh. CGK-5-X describes on page 1 that this modeling may have already been done in response to Public Counsel Data Request 470.

<sup>303</sup> Of course, this assumes that the Avista will enter into the PPA. Should the Company choose otherwise, the potential Lancaster PPA may prove useful as a benchmark for evaluating the benefit of other resources the Company may acquire.

of these deferred costs in customer rates will be considered and determined in a future rate proceeding.<sup>304</sup>

230 The deferred accounting we authorize here is for a period not to exceed twenty-four (24) months from the beginning of the Lancaster contract; provided that if during such period the Company files in a general rate case for the recovery of Lancaster contract costs, the deferral ends on the effective date of the final decision by the Commission in that proceeding.<sup>305</sup> Avista must file an accounting petition specifying accounting methods and details it will use to meet the following requirements. The Company's deferral accounting must separately identify costs for the following:

- use of the Lancaster facility;
- transmission related to power supply from the Lancaster facility;
- gas transport related to the Lancaster facility; and
- fuel supply for the Lancaster facility.

The Company is authorized to accrue a carrying charge on deferral balances at the same rate applied to its ERM deferral balances (i.e., cost of debt).

231 The Company must file the Lancaster power supply and related transmission and fuel gas transport contracts once such contracts are finally executed. In conjunction with the contract filing, or in a separate filing, the Company must file evidence to demonstrate that, as an affiliated interest transaction, the contract(s) comply with the statutory requirements set out in RCW 80.16.020.

232 Finally, the Company must make a comprehensive and orderly filing of evidence necessary for us to determine whether the standard required by RCW 80.80 applies to the Lancaster contract and, if so, whether the actual performance of the Lancaster

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<sup>304</sup> We reject Public Counsel's original recommendation (*see* Woodruff, Exh. KDW-1T at 33:22 – 34:3 and 34:17 – 35:3) to permanently disallow Lancaster-associated power costs for the 2010 rate year *and* find the Lancaster contracts imprudent over their full term.

<sup>305</sup> Although our language authorizing this deferral is similar to that contained in RCW 80.80.060(6), we do not grant this authority under that statute because our record does not contain sufficient detail to allow us to rule on the plant's status under RCW 80.80.

plant complies with the standard. We expect our staff to undertake a thorough analysis of this data.

233 We look forward to an opportunity to properly evaluate the Lancaster contracts for both short-term and long-term impact on Avista's ratepayers and on the Company itself. Such an evaluation should be facilitated with the affiliated interest filing now pending before us.

234 After considering all proposed adjustments, we find Avista's NOI should be increased by \$5.7 million on the electric side while reducing its electric rate base by almost \$63 million. We also find Avista's NOI on the natural gas side should be increased by just over \$1.6 million while reducing the corresponding rate base by just over \$9.1 million. We provide the following summary tables for the convenience of the parties. See Table 4 (electric) and Table 5 (natural gas), on the following pages.

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**TABLE 4**  
**Restating and Pro Forma Adjustments – Electric (\$000)**

	NOI	Rate Base
<b>Per Books</b>	<b>68,538</b>	<b>1,053,828</b>
<b>UNCONTESTED ADJUSTMENTS (from Table 2A)</b>		
<i>Total Uncontested Adjustments</i>	5,322	(101,633)
<b>CONTESTED ADJUSTMENTS – COMMISSION DECISION</b>		
Property Taxes	(127)	-
Injuries and Damages	(56)	
Customer Deposits	(7)	(2,473)
Board Meeting Costs	15	
Power Supply(1)	799	
Prod. Property(2)	2,464	(11,360)
Labor Non-executive	(1,130)	
Labor Executive	(98)	
Capital Add. 2008	-	-
Capital Add. 2009	(599)	21,252
Capital Add. 2010	(434)	14,592
Asset Management	-	-
Information Serv.	-	-
CDA Settlement	(539)	16,819
Incentives	-	-
Insurance	(97)	-
Director's Fees	177	-
<i>Total Contested Adjustments</i>	<b>368</b>	<b>38,830</b>
<b>Grand Total Adjustments</b>	<b>5,690</b>	<b>(62,803)</b>
<b>GRAND TOTAL</b>	<b>74,228</b>	<b>991,025</b>

(1) Public Counsel's recommended adjustment, subject to revision based on re-run of the power supply model that we require in paragraph 226.

(2) Staff's recommended adjustment, subject to revision based on the re-run of the power supply model that we require in paragraph 104.

**TABLE 5**  
**Restating and Pro Forma Adjustments – Gas**  
**(\$000)**

	NOI	Rate Base
<b>Per Books</b>	<b>12,004</b>	<b>178,717</b>
<b>UNCONTESTED ADJUSTMENTS (see Table 2B)</b>		
<i>Total Uncontested Adjustments</i>	1,413	(7,782)
<b>CONTESTED ADJUSTMENTS – COMMISSION DECISION</b>		
Property Taxes	486	
Injuries and Damages	42	
Customer Deposits	(4)	(1,353)
Board Meeting Costs	4	
Labor Non-executive	(297)	
Labor Executive	(27)	
Capital Add. 2008	-	-
Capital Add. 2009	-	-
Asset Management	-	-
Incentives	-	-
Information Services	-	-
Insurance	(26)	-
Director's Fees	49	-
<i>Total Contested Adjustments</i>	<b>227</b>	<b>(1,353)</b>
<b>Grand Total Adjustments</b>	<b>1,640</b>	<b>(9,135)</b>
<b>GRAND TOTAL</b>	<b>13,644</b>	<b>169,582</b>

235 The consequent new revenue requirements for electric and natural gas are shown in Tables 6 and 7.

**TABLE 6**  
**Electric Revenue Requirement**  
**Docket UE-090134**

Rate Base	\$991,025,000
Rate of Return	8.25 percent
NOI Revenue Requirement	\$81,760,000
Adjusted NOI	\$74,228,000
Difference	\$7,531,000
Conversion Factor	.621953
Gross Revenue Requirement Increase (Decrease)	\$12,109,000

**TABLE 7**  
**Gas Revenue Requirement**  
**Docket UG-090135**

Rate Base	\$169,582,000
Rate of Return	8.25 percent
NOI Revenue Requirement	\$13,991,000
Adjusted NOI	\$13,644,000
Difference	\$347,000
Conversion Factor	.62209
Gross Revenue Requirement Increase (Decrease)	\$557,000

## E. Decoupling

### 1. Introduction

236 As stated earlier, on April 30, 2009, Avista filed a petition to consolidate Docket UG-060518, involving its pilot natural gas decoupling mechanism, with this rate case proceeding, asking the Commission to extend the pilot program beyond its scheduled termination date of June 30, 2009. On May 15, 2009, the Commission consolidated the decoupling issue into the general rate cases (*Order 06*), and, on June 30, 2009, we granted an interim extension of Avista's existing pilot decoupling mechanism (*Order 07*). We now consider whether the program should be extended further and, if so, what form it would take and what purpose it would fulfill. We first establish the context for our decision with a general discussion of the importance placed upon conservation by Washington's policy makers, and then provide the rationale for decoupling and the Commission's consideration of that rationale in several prior proceedings.

### 2. Conservation Policy in Washington

237 The policy of this state promotes the advancement of conservation resources<sup>306</sup> and encourages the Commission to consider incentives for investment in such resources.<sup>307</sup> Consistent with this legislative directive, we have observed before that "promoting energy conservation is a goal that [the Commission] strongly supports."<sup>308</sup>

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<sup>306</sup> Conservation is defined in WAC 480-90-238(2)(c) as "any reduction in natural gas consumption that results from increases in the efficiency of energy use or distribution."

<sup>307</sup> RCW 80.28.024 states in part:

The legislature finds and declares that the potential for meeting future energy needs through conservation measures . . . may not be realized without incentives to public and private energy utilities. The legislature therefore finds and declares that actions and incentives by state government to promote conservation . . . would be of great benefit to the citizens of this state by encouraging efficient energy use.

<sup>308</sup> *In Re Petition of Avista Corporation d/b/a Avista Utilities For an Order Authorizing Implementation of a Natural Gas Decoupling Mechanism and to Record Accounting Entries*

238 Mindful of our responsibility to encourage conservation,<sup>309</sup> this Commission has promulgated rules governing integrated resource planning (IRP) that require natural gas companies to “meet system load with the least cost mix of natural gas supply and conservation.”<sup>310</sup> In support of this goal, we require companies to assess all “commercially available conservation” and to “assess new policies and programs needed to obtain the conservation improvements.”<sup>311</sup> Furthermore, we require a comparative analysis of natural gas supply options and available conservation opportunities in order to evaluate the least cost alternative.<sup>312</sup>

239 It is difficult to overstate the importance of conservation measures, as reflected in these statutes and rules, and in our policies. Though it remains in draft form at this time and relates to the electric sector, the Sixth Power Plan being developed by the Northwest Power and Conservation Council offers these observations concerning the importance of conservation in our region:

In each of its power plans, the Council has found substantial amounts of conservation to be cheaper and more sustainable than many forms of additional electric-generating capability. In this Sixth Power Plan, because of higher costs of alternative generation sources, rapidly developing technology, and heightened concerns about global climate change, conservation holds an even larger potential for the region.

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*Associated With the Mechanism*, Docket UG-060518, Order 04, Final Order Approving Decoupling Pilot Program, ¶ 10 (Feb. 1, 2007) [hereinafter *2007 Avista Pilot Decoupling Plan Order*].

<sup>309</sup> See RCW 80.28.025(1), which provides in relevant part:

In establishing rates for each gas and electric company regulated by this chapter, the commission shall adopt policies to encourage meeting or reducing energy demand through . . . measures which improve the efficiency of energy end use.

<sup>310</sup> See WAC 480-90-238(1). IRPs generally set forth a mix of supply-side options and demand-side management (DSM) options. Demand-side management is another term for conservation.

<sup>311</sup> See WAC 480-90-238(3)(b).

<sup>312</sup> See WAC 480-90-238(3)(f). See also WAC 480-100-238(3)(e) for this policy’s application to electric utilities.

The Plan finds enough conservation to be available and cost-effective to meet the load growth of the region for the next 20 years.<sup>313</sup>

Although the final report may deviate slightly from the draft, these words clearly express the fundamental point that achieving significant conservation will remain a critically important goal for utilities in this region, including Washington, into the indefinite future.

### 3. The Commission's Approach to Decoupling

240 Much debate surrounds the question of how best to achieve the potential that conservation offers. In this proceeding, we must place ourselves at the center of this debate with respect to the rate mechanism known as “decoupling,” which Avista implemented on a pilot basis in 2007 and as to which it now seeks authority to continue.<sup>314</sup> Some conservation advocates argue that such programs are essential to encourage conservation, while many ratepayer advocates argue that such programs create windfall revenues to companies and discourage consumer investment in energy efficiency.<sup>315</sup> We recognize there is sharp disagreement about the merits of this and other decoupling proposals and rely on our knowledge, experience and judgment to determine the appropriate role for a decoupling mechanism in regulating Avista Utilities.

241 The Commission has discussed decoupling and the principal elements of the decoupling debate in several prior proceedings. In 2005, the Commission conducted a rulemaking inquiry into the subject. After taking stakeholder comments and conducting a workshop, the Commission determined that “the wide variety of alternative approaches to decoupling make it more efficient to address these issues in

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<sup>313</sup> See Northwest Power and Conservation Council, Draft Sixth Power Plan, Sixth Power Plan Overview (Sept. 3, 2009), at 1 (Summary Section) (available at [www.northwestcouncil.org](http://www.northwestcouncil.org)). We take official notice of this document in accordance with WAC 480-07-495(2).

<sup>314</sup> See 2007 Avista Pilot Decoupling Plan Order.

<sup>315</sup> See *Decoupling For Electric & Gas Utilities: Frequently Asked Questions (FAQ)*, National Association of Regulatory Utility Commissioners' Grants & Research Dept. (Sept. 2007); see also *Decoupling and Public Utility Regulation*, Graniere and Cooley, National Regulatory Research Institute No. 94-14 (August 1994).

the context of specific utility proposals included in general rate case filings rather than through a generic rulemaking.”<sup>316</sup>

242 The following year, the Commission considered, and ultimately rejected as inadequate in scope and detail, a decoupling framework advocated by PacifiCorp.<sup>317</sup> Discussing the subject generally, the Commission stated:

The central goal of conservation is to encourage customers to reduce energy use. As a result, a utility engaging in conservation will likely see its sales and revenues fall, exposing it to the risk of being unable to recover its fixed costs. Because shareholders bear the burden of any shortfall in revenues, they may be reluctant to aggressively pursue energy efficiency measures. Decoupling is a way to break the link between a utility’s revenues and retail sales levels, and to reduce the utility’s risk associated with recovering its fixed costs when retail sales decrease due to customer conservation.<sup>318</sup>

243 Later, the Commission undertook a more extensive discussion of decoupling in Docket UG-060267 where Puget Sound Energy (PSE) proposed decoupling for its natural gas utility.<sup>319</sup> There, after reiterating the purpose of decoupling, the Commission said:

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<sup>316</sup> Rulemaking to Review Natural Gas Decoupling, Docket UG-050369, Notice of Withdrawal of Rulemaking (October 17, 2005).

<sup>317</sup> See *UTC v. PacifiCorp*, Docket UE-050684, Order 04, ¶¶ 108-110 (April 17, 2006), setting out the Commission’s basis for rejecting PacifiCorp’s decoupling proposal.

<sup>318</sup> *Id.*, ¶ 102.

<sup>319</sup> *UTC v. Puget Sound Energy, Inc.*, Dockets UE-060266 & UG-060267, Order 08, ¶¶ 53-69 (January 5, 2007) [hereinafter *2007 PSE Decoupling Order*]. The Commission ultimately rejected PSE’s natural gas decoupling proposal but did approve a three-year pilot electric energy efficiency incentive program for the Company (see ¶¶ 145- 158). The following week, however, the Commission conditionally approved a multi-party settlement in another company’s rate case that included a three-year natural gas pilot decoupling project. See *UTC v. Cascade Natural Gas Corp.*, Docket UG-060256, Order 05, ¶¶ 67-85 (January 12, 2007) [hereinafter *2007 Cascade Decoupling Order*]; see also Order 06 in that same docket (August 16, 2007) which approved the Conservation Plan required in the conditional approval of the decoupling pilot and Order 07 (October 1, 2007) which accepted an addendum to the Conservation Plan.

From a utility perspective, it is a means to ensure recovery of a significant part, or even all of its fixed costs regardless of reduced consumption. . . .

Conservation advocates and others recognize decoupling as a potentially important tool to promote conservation. . . . We acknowledge that improved energy savings from cost-effective conservation, which we strongly support, is a highly appealing rationale for decoupling on its face. We emphasize, however, that decoupling is merely one regulatory tool in a larger toolbox of devices we might use to promote greater conservation.<sup>320</sup>

In that same order, we acknowledged the affect a decoupling mechanism may have upon a company's interest in pursuing conservation by noting:

As the parties argue, decoupling is principally useful in circumstances where there is a need to promote a more positive company attitude toward conservation by removing what may be a disincentive, or barrier to aggressive pursuit of conservation . . . .<sup>321</sup>

244 Most recently, in the Commission's order approving the Avista decoupling pilot that is under direct review here, we reiterated the concerns that give rise to decoupling proposals:

Under traditional ratemaking structures, utilities recover a large portion of their fixed costs through charges based on the volume of energy that consumers use. Consequently, a reduction in energy consumption may lower the probability that the utility can fully recover its fixed costs. Energy consumption may be lower for a variety of reasons. Consumers may lower their thermostats or take shorter showers. More energy efficient building codes and appliances, better and more efficient insulation, and warmer than normal weather can also reduce energy use. Conversely, an increase in energy consumption may lead to a utility over-recovering its fixed costs. The traditional financial incentives rewarding higher sales, some argue, create an environment

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<sup>320</sup> In that proceeding, the Commission mandated a direct incentive program for PSE's electric utility, wherein the company was rewarded or penalized for its conservation performance.

<sup>321</sup> 2007 PSE Decoupling Order, ¶ 55.

in which utilities do not support conservation because it is inconsistent with their economic interests.<sup>322</sup>

245 Our prior discussions of decoupling provide important context as we turn our attention specifically to Avista’s proposal to retain its decoupling mechanism in this proceeding. We start with a discussion of the history and structural characteristics of the pilot mechanism. Following that, we describe the specific proposal pending here, discuss the parties’ arguments for and against the program or various of its elements, and make our determinations concerning what will be authorized.

#### 4. Avista’s Pilot Decoupling Mechanism

246 In the context of a multi-party settlement, we approved Avista’s Pilot Decoupling Mechanism on February 1, 2007.<sup>323</sup> The settling parties urged the Commission to adopt their settlement, contending that it would “provide for an increased focus on energy efficiency and conservation” within Avista Utilities, and “align the Company’s interest with that of its customers with an increased focus on effective DSM [demand side management] programs.”<sup>324</sup> In our order, we noted that the pilot program allowed us to “test the hypothetical benefits of decoupling generally” while providing sufficient “safeguards to protect [the customer].”<sup>325</sup> We also recognized the relationship between the Company’s lost margin and the rate impacts of its decoupling mechanism. To this end, we stated:

The proportion of margin lost to company sponsored DSM relative to the amount subject to recovery is of great interest to us, and we will closely scrutinize this factor in reviewing the results of this pilot decoupling program.<sup>326</sup>

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<sup>322</sup> 2007 Avista Pilot Decoupling Plan Order, ¶¶ 8-9.

<sup>323</sup> *Id.*, ¶ 7. Public Counsel and The Energy Project opposed the Settlement.

<sup>324</sup> *Id.*, ¶ 16.

<sup>325</sup> *Id.*, ¶ 31.

<sup>326</sup> *Id.*, ¶ 26.

247 We do not fully describe the decoupling program's details here, but instead point out that details as to its composition and operation are contained in the Commission's order approving the multiparty settlement and in the settlement document that is appended to that order.<sup>327</sup> We do however believe it necessary to refer to the basic construct of the program.

248 The pilot program allowed the Company to track therms sold to its Schedule 101 (residential and small business) customers.<sup>328</sup> Any deficiency in therms sold was recorded as "lost margin".<sup>329</sup> The pilot program's design went on to require that the Company's annual lost margin be adjusted by three important factors.

249 First, the effects of adding new customers are deducted from the Company's total or gross lost margin. This adjustment increased the lost margin available for recovery, which we will refer to here as the net lost margin. Second, the net lost margin was adjusted by factoring out the affects of weather through a process referred to as "weather normalizing." As weather has perhaps the greatest effect upon a gas utility's sales, this adjustment also significantly impacted the lost margin deferred. Finally, the utility was only allowed to recover 90 percent of the "weather normalized" lost margin. In other words, the adjusted net lost margin was reduced by an additional 10 percent. According to Staff, this 10 percent reduction was intended as an approximate substitute for discounting the utility's rate of return to reflect its reduced risk of revenue loss.<sup>330</sup>

250 In addition the Settlement imposed two other limitations on the Company. First, there was an earnings test, so that Avista could not earn more than its then-authorized 9.11

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<sup>327</sup> *Id.* The Settlement Agreement is found in Appendix A to Order 04.

<sup>328</sup> In order to "match" program results with customer sales over a given period, new customers' usage was not added to Schedule 101's total of therms sold.

<sup>329</sup> By program design, annual therm sales could exceed the annual sales attributed to this class for ratemaking purposes, which would result in rebates to customers. However, the program's short history indicated that after being weather-normalized, therm sales were invariably lower than the sales target.

<sup>330</sup> *See* Steward, Docket UG-060518, TR. 96:20 – 97:13 (Dec. 21, 2006) (testimony at settlement hearing regarding Staff's position on various constraints placed into decoupling mechanism).

percent rate of return. Second, there was a DSM (demand side management) test, which made recovery of Avista's "lost margin" subject to the Company achieving specific conservation targets.<sup>331</sup>

- 251 Thus, the program's design did not capture all lost margin, but was more refined, which allowed us to better understand the relationship between conservation and the Company's total therm sales and made an effort, albeit inexact, to account for the reduction in the Company's risk resulting from the pilot's implementation. We recognized then (and now) that the pilot program was (and should be) designed to best measure the Company's conservation efforts as a reflection of its "new" attitude toward conservation. In counterbalance, we also measure the program's impact on ratepayers to ensure that the program's costs are in reasonable balance with its benefits.
- 252 The approved settlement also called for a third-party evaluation of the pilot program. That evaluation, termed the "Titus Evaluation Report" (Titus Report) was filed with the Commission on March 31, 2009. To ensure a thorough review of the program and its impacts, the Commission determined that the pilot program must be evaluated in a general rate case, and that its permanent adoption must come only after "a convincing demonstration that the mechanism has enhanced Avista's conservation efforts in a cost-effective manner."<sup>332</sup> Consistent with our direction, Avista filed a petition to

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<sup>331</sup> According to the Settlement Agreement, the Company's rate of return (ROR) of 9.11 percent was approved by the Commission in its 2005 Avista Rate Case Order in Docket UG-050483. Further, the Settlement Agreement refers to the Company's 2006 IRP as establishing a natural gas target savings level of 1,062,000 therms (Washington & Idaho combined) for each of calendar years 2006 and 2007. Subsequent target savings levels were to be documented in a later IRP. See *2007 Avista Pilot Decoupling Plan Order*, Appendix A at 5-6.

<sup>332</sup> See *2007 Avista Pilot Decoupling Plan Order*, ¶ 33. See also *UTC v. Avista Corporation*, Dockets UE-090134, UG-090135 & UG-060518 (consolidated), Order 07, Supplemental Order Temporarily Extending Decoupling Mechanism, ¶ 15, n.15 (June 30, 2009), in which we state: "We have not undertaken a thorough review of the evaluation report submitted on March 31, 2009. However, it appears that, without further elaboration and analysis, it may not be sufficient to enable the Commission to evaluate the program pursuant to the standard we set for such review in Order 04. We look forward to a more robust and focused presentation as part of Avista's attempt to provide a 'convincing demonstration' that its decoupling mechanism is cost-effective and valuable not only for the Company, but also for its ratepayers."

make its pilot program permanent, and to consolidate its consideration with this general rate case.<sup>333</sup>

## 5. Issues Raised by the Parties

- 253 *Avista*. The Company requests continuation of its decoupling mechanism with some minor modifications. According to the Company, the pilot mechanism achieved its intended purpose: to substantially increase Avista's DSM efforts and results and allow the Company to recover a substantial portion of its fixed costs.<sup>334</sup> The Company points to a 61 percent increase in total therm savings across all Washington rate classes and a 205 percent increase in therm savings in Washington's Schedule 101 class over the period of the pilot.<sup>335</sup>
- 254 The Company states there is a need to improve measurement and verification of DSM savings, stating that it is in the process of developing a revised measurement and verification approach for review by Avista's External Energy Efficiency (Triple E) Board in September 2009 and for incorporation into the 2010 DSM Business Plan.<sup>336</sup>
- 255 Perhaps the most significant question raised in the proceeding was whether 90 percent represented the appropriate amount of lost margin to recover.<sup>337</sup> The Company states the decoupling mechanism is appropriately designed because it provides recovery of fixed costs related to the decline in customer usage, whether from programmatic DSM measures, education, price signals, or other factors.<sup>338</sup> The Company also stated

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<sup>333</sup> See Dockets UG-090135 & UG-060518, Petition of Avista Corporation *and* Avista Corporation's Motion to Consolidate (April 30, 2009).

<sup>334</sup> Hirschorn, Exh. BJH-1T-A at 4:7-12.

<sup>335</sup> *Id.* at 10:3-9.

<sup>336</sup> Powell, Exh. JP-3T at 1:15-16 and 8:1-2.

<sup>337</sup> In other words, whether the deferred "lost margin" in balance with the amount of actual lost margin related to Company-sponsored conservation efforts. At hearing, this was referred to as the "proportionality" issue.

<sup>338</sup> Hirschorn, Exh. BJH-1T-A at 11:11-18. According to the Company, "programmatic measures" consist of a series of prescriptive rebates for residential measures, an enhanced incentive program for limited income customers, and a non-residential program applicable to any

that DSM expenditures for limited-income customers increased by 43 percent during the decoupling period.<sup>339</sup>

256 However, in its rebuttal case, the Company recommends reducing the recovery level to 70 percent due to “the variables outside the normal ebb and flow of customer usage over time.” At hearing, Avista acknowledged that the decoupling mechanism allows for recovery of lost margin due to all factors but weather, and agreed that the reduction in the percentage of recovery it proposed was a “rough approximation” aimed at taking into account lost margin from causes other than Company DSM efforts.<sup>340</sup>

257 The Company also proposes to modify the mechanism in a minor way. According to the Company, some customers left Schedule 101 for Schedule 111 causing phantom margin losses of about five percent of the total lost margin deferred under the pilot.<sup>341</sup> The Company suggests that the permanent program remove the effect of those customers from the deferral amount.<sup>342</sup>

258 *Commission Staff.* In responsive testimony, Staff opposes the continuation of Avista’s decoupling program for three primary reasons: administrative burden, complexity, and the proportion of DSM lost margin to the deferral amount.<sup>343</sup> As an alternative, Staff proposes phasing out the decoupling mechanism beginning January 1, 2010, and terminating it on January 1, 2011. At that time, Staff recommends

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measure that saves electric or natural gas energy. “Non-programmatic” activities are educational and outreach campaigns focused upon efficiency measures that are not included in Avista’s programmatic measures, such as “Every Little Bit”. See Powell, Exh. JP-1T at 4:2-9.

<sup>339</sup> *Id.* at 22:2-4.

<sup>340</sup> Norwood, TR. 1029:8-25 and 1030:1-9.

<sup>341</sup> *Id.* at 12:19-13:1. According to the Titus Report, “Schedule 101 (General Service – Firm – Washington) is available for residential and low usage commercial customers that use less than 200 therms per month. Schedule 111 (Large General Service – Firm – Washington) is generally a commercial rate schedule that consists of a higher minimum charge and is based on usage greater than 200 therms per month. See Exh. BJH-2-A (revised Aug. 10, 2009), at 65.

<sup>342</sup> Hirschhorn, Exh. BJH-1T-A at 12:5-12.

<sup>343</sup> Reynolds, Exh. DJR-1T at 19:5 and 25:22 – 26:2.

increasing the Schedule 101 basic charge to \$10 per month,<sup>344</sup> and asserts this would stabilize Company revenue expectations without creating complicated accounting requirements and rates for Schedule 101 customers.<sup>345</sup>

259 As an alternative, should the Commission continue the decoupling mechanism, Staff recommends two modifications: the removal of the new customer adjustment and the addition of the Schedule 111 migration adjustments as described by the Company.<sup>346</sup>

260 Regardless of the Commission's decision on the continuation of decoupling mechanism, Staff recommends the Commission direct the Company to convene meetings with Staff and interested parties to design conservation reporting and stakeholder involvement protocols, including expansion of the Company's evaluation standards.<sup>347</sup> Staff suggests the results of these meetings be filed with the Commission within 12 months of the final order.<sup>348</sup>

261 Staff concludes that the decoupling evaluation was partially incomplete because the Company's third-party evaluator (Titus) was not allowed to draw conclusions, make recommendations, or otherwise determine whether conservation increased as a result of implementing decoupling.<sup>349</sup> Staff conditionally concludes that spending on conservation and therm savings increased during the term of the mechanism, but notes that during the last four years therm savings fluctuated wildly, decreasing at times almost as much as they increased. Staff indicates this is a concern because it is unclear how much, if at all, the mechanism contributed to the therm savings.<sup>350</sup>

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<sup>344</sup> *Id.* at 2:10-16.

<sup>345</sup> *Id.* at 26:15-17.

<sup>346</sup> *Id.* at 2:17-21.

<sup>347</sup> *Id.* at 3:3-7 and 8:10-14.

<sup>348</sup> *Id.* at 2:5-7.

<sup>349</sup> *Id.* at 7:1-13 (according to Staff, "other parties on the Stakeholder Advisory Group resisted" Staff's urging of the Company that Titus be allowed "to draw conclusions and make recommendations about the design of the mechanism").

<sup>350</sup> *Id.* at 8:1-5 and 9:21.

According to Staff, this reflects a problem with the Company's evaluation program. In the end, Staff still concludes that Avista's conservation efforts have been enhanced.<sup>351</sup>

262 In considering the proportionality of deferrals to DSM lost margin, Staff notes that, even accounting for multi-year losses, the deferral was three times the lost margin attributable to the Company's programmatic conservation efforts.<sup>352</sup> It concludes however, that the purpose of the decoupling mechanism is to remove the Company's disincentive to invest in conservation by stabilizing the amount of revenue the Company could count on collecting.<sup>353</sup> Therefore, the deferral under the decoupling mechanism should not be tied to programmatic DSM lost margins only.

263 *Public Counsel.* Public Counsel testified in opposition to Avista's decoupling mechanism and recommends that it be discontinued. In support, it asserts multiple areas of concern: the DSM savings trend does not correspond to adoption of decoupling; the deferrals are not proportional to the lost margin; the customer outreach programs are not as effective as claimed; the new customer adjustment is unreasonable and violates the matching principle; the mechanism is complex and presents administrative burden; the risk of loss is shifted to the ratepayers; and Avista's calculation of DSM' savings is flawed.<sup>354</sup> We turn now to the details of Public Counsel's arguments.

264 Public Counsel argues that Avista's DSM savings did not correspond to the adoption of decoupling in Washington, noting that the greatest increase in therm savings occurred in Idaho where there is no decoupling mechanism.<sup>355</sup>

265 Public Counsel characterizes the decoupling mechanism as overly broad in scope; it collects lost margins from a number of causes unrelated to Avista's conservation

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<sup>351</sup> *Id.* at 9:21-22.

<sup>352</sup> *Id.* at 19:8-9; *see also* Staff Brief, ¶ 83 (on brief, however, Staff asserts the deferral was *four* times the lost margin attributable to the Company's programmatic conservation efforts).

<sup>353</sup> *Id.* at 19:18-20.

<sup>354</sup> Brosch, Exh. MLB-1T at 6:6-7:3.

<sup>355</sup> *Id.* at 12:4-9.

efforts.<sup>356</sup> Citing the Titus Report, Public Counsel states that the ratio of deferred lost margin to the lost margin due to Company-sponsored conservation is 10:1 in 2007 and 8:1 in 2008.<sup>357</sup> Public Counsel dismisses the Company's claim that non-programmatic DSM from Company educational programs such as "Every Little Bit" is a significant part of the deferral, although it fails to quantify a precise number.<sup>358</sup>

266 As to the mechanism's new customer adjustment, Public Counsel argues that it violates the matching principle by excluding new loads when calculating the deferral. It notes that if the adjustment were eliminated, the deferral would actually be negative, resulting in a refund to customers.<sup>359</sup> If the Commission chooses to continue the decoupling mechanism, Public Counsel recommends removing the new customer adjustment.<sup>360</sup>

267 In its brief, and at the hearing, Public Counsel spent considerable effort discussing the administrative complexity of the program. Public Counsel argues that the mechanism can lead to formal reviews under compressed schedules. It also claims that other elements of the mechanism add complexity, such as the weather adjustment, DSM test, the customer migration adjustment, and the earnings test; nevertheless, Public Counsel does not suggest eliminating any of these elements if the Commission approves continuation of the mechanism.

268 Finally, Public Counsel attacks Avista's calculation of DSM savings. It argues that the Company relies only on "engineering estimates" of DSM savings and does not measure and verify such savings on a facilities basis.<sup>361</sup> The result, Public Counsel

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<sup>356</sup> *Id.* at 13:6-10.

<sup>357</sup> *Id.* at 16:8-10.

<sup>358</sup> *Id.* at 19:7 – 20:5. Staff points out that "Every Little Bit" has a very small budget, only raises customer consciousness on conservation and directs customers to programmatic measures that are counted in the therm savings.

<sup>359</sup> *Id.* at 15:18-26.

<sup>360</sup> *Id.* at 25:15-19.

<sup>361</sup> Kimball, Exh. MMK-1T at 2:10-18.

argues, is that the Commission and stakeholders are left with insufficient evidence or information to accurately evaluate Avista's stated DSM savings.<sup>362</sup>

269 If the Commission should conclude that there is a need for financial incentives to encourage Avista's investment in energy efficiency, Public Counsel recommends an incentive mechanism with payments that are proportional to the margins lost due to Company sponsored DSM performance.<sup>363</sup> As part of an incentive mechanism, Public Counsel recommends clearly defined DSM performance targets, with meaningful measurement, verification and reporting of results achieved by the utility relative to such targets.<sup>364</sup>

270 Finally, Public Counsel argues that if the Commission approves a decoupling program, it should reduce the return on equity figure agreed to in the Settlement by 25 basis points to account for reduced investor risk. Public Counsel compares the Company's return on equity to a return that reflects the greater probability of cost recovery provided by the Decoupling Mechanism.<sup>365</sup>

271 *The Energy Project.* The Energy Project recommends that the Commission terminate the mechanism. It contends that limited income customers and many more payment-troubled customers pay higher prices for essential natural gas service but do not receive any of the potential direct benefits from the more expensive DSM programs that Avista has implemented.<sup>366</sup>

272 Citing the Titus Report, the Energy Project testifies that Avista's DSM expenditures on Washington residential customers increased 25 percent in 2007 and another 50 percent in 2008. On the other hand, such expenditures for limited income customers increased 17 percent in 2007 and only 12 percent in 2008.<sup>367</sup> The ratio of DSM

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<sup>362</sup> *Id.*

<sup>363</sup> Brosch, Exh. MLB, at 41:21-22.

<sup>364</sup> *Id.* at 41:1-18.

<sup>365</sup> Gorman, Exh. MPG-1T at 5:15-17 and 7:20-22.

<sup>366</sup> Anderson, Exh. BRA-1T at 4:6-10.

<sup>367</sup> *Id.* at 12:8-11.

dollars spent on limited income customers dropped from 1-in-6 in 2007 and 1-in-8 in 2008.<sup>368</sup>

- 273 *The NW Energy Coalition.* In responsive testimony, the NW Energy Coalition (Coalition) recommends the Commission continue Avista's decoupling mechanism. It argues that the program is necessary because there is a well established asymmetrical trend of declining use per customer and that breaking the link between sales and revenue is the best way to focus the utility on making the lowest reasonable cost investments to deliver reliable energy services to customers.<sup>369</sup> However, the Coalition suggests three modifications.
- 274 First, the Coalition suggests that Avista's maximum deferral should be reduced from 90 percent to a maximum of 70 percent of the "fixed cost margin difference" for both refunds and collections.<sup>370</sup> The Coalition supports lowering the percentage maximum deferral to 70 percent, stating that it is important in the current economic climate for a more equitable sharing of financial risk between Avista and its customers.<sup>371</sup>
- 275 Second, the Coalition proposes an incentive within the decoupling mechanism to encourage and reward performance in excess of Commission-approved targets.<sup>372</sup> Under its incentive feature, the Company would have to achieve savings greater than 120 percent of its DSM target to earn the 70 percent deferral. If the Company met its DSM target, then it would only recover 50 percent of its deferral.<sup>373</sup>

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<sup>368</sup> Titus Report at 29.

<sup>369</sup> Glaser, Exh. NLG-1T at 12:20-31 and 8:10-26.

<sup>370</sup> *Id.* at 5:7-8.

<sup>371</sup> *Id.* at 10:20-21.

<sup>372</sup> *Id.* at 6:19-31.

<sup>373</sup> *Id.* at 12:13-18.

- 276 Third, the Coalition recommends that the Company be required to meet two DSM targets: an overall DSM target, as is currently the case, and a specific DSM sub-target for Washington limited income customers.<sup>374</sup>
- 277 *Responses of Staff, The Energy Project, Public Counsel, and Coalition.* Staff's cross-answering testimony opposes The Energy Project's characterization of the decoupling mechanism's purpose as recovering lost revenues due to the implementation of efficiency programs.<sup>375</sup> Staff stresses that the design of the mechanism was to recover all lost margins associated with reductions in usage other than weather.<sup>376</sup>
- 278 Staff generally supports the Coalition's incentive proposal but argues it will encourage the Company to establish low DSM targets.<sup>377</sup> Staff agrees with The Energy Project that the Titus Report was "unable to actually confirm that the claimed energy savings have occurred."<sup>378</sup> However, Staff disagrees with Public Counsel's claim that the DSM verification adjustments are insufficient to allow for proper adjustment of the Company's total savings claims.<sup>379</sup>
- 279 In its cross-answering testimony, The Energy Project does not agree that the modifications to the decoupling mechanism and the limited income DSM spending target suggested by the Coalition can be relied on to support the program's continuation.<sup>380</sup>
- 280 The Energy Project criticizes Staff's rate design proposal because it does not address the Company's disincentive to promote conservation. Furthermore, the feature to

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<sup>374</sup> *Id.* at 12:5-21.

<sup>375</sup> Reynolds, Exh. DJR-3T at 2:21 –3:2.

<sup>376</sup> *Id.*

<sup>377</sup> *Id.* at 4:1-23.

<sup>378</sup> *Id.* at 5:9-10 (quoting Alexander, Exh. BRA-1T at 5:1-2).

<sup>379</sup> *Id.* at 5:18-23.

<sup>380</sup> Alexander, Exh. BRA-2T at 4:9-11.

reduce low-income customers' basic charge is not well developed.<sup>381</sup> It provides its own Bill Analysis Model results and claims Staff's rate design proposal would have a discriminatory impact on limited income customers.<sup>382</sup>

281 Public Counsel and The Energy Project object to Staff's proposed increase in the customer fixed charge, which would be a step toward what is termed "straight-fixed variable" (SFV) rate design.<sup>383</sup> They cite data that show local distribution companies with volumetric charges are able to achieve reasonable rates of return.<sup>384</sup> These parties jointly disagree with Staff's characterization of the effect of price elasticity, asserting that it may be hard to measure but, as several studies show, it does have a real effect on consumption.<sup>385</sup> The joint rebuttal parties conclude by reiterating their support of a \$6.00 customer basic charge (twenty-five cent increase over the existing customer charge) whether decoupling is continued or not.<sup>386</sup>

282 In cross-answering, the Coalition reasserts its support for the decoupling mechanism, arguing its recommended modifications and other recommendations address concerns raised about the mechanism. The Coalition asserts that its modification to reduce the maximum recovery amount to 70 percent addresses the concerns raised by Public Counsel about the proportionality of the mechanism.<sup>387</sup> The Coalition disagrees with Public Counsel that the mechanism should be limited just to cost recovery for programmatic DSM savings.<sup>388</sup> The Coalition asserts that such a limitation will discourage the Company's efforts to promote non-programmatic DSM and discourage

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<sup>381</sup> *Id.* at 6:5-8.

<sup>382</sup> *Id.* at 9:9-17.

<sup>383</sup> Straight-fixed variable (SFV) refers to a rate design that collects all or a substantial portion of fixed costs through a fixed monthly charge on each customer, rather than through a volumetric rate.

<sup>384</sup> Watkins, Exh. GAW-3T at 3:8-10.

<sup>385</sup> *Id.* at 11:21-12:9.

<sup>386</sup> *Id.* at 12:12-18.

<sup>387</sup> Glaser, Exh. NLG-3T at 5:18-22.

<sup>388</sup> *Id.* at 6:4-5.

support for public policies such as building codes and efficiency standards that cause a decline in therm use.<sup>389</sup>

283 The Coalition also disagrees with Staff's recommendation to replace the decoupling mechanism with higher fixed charges and asserts that higher fixed charges discourage customer investment in conservation. It also contends that Staff did not establish a relationship between its proposed \$10 customer charge and Avista's cost to serve a customer.<sup>390</sup>

284 The Coalition agrees with Public Counsel and Staff that Avista's future DSM performance should be more effectively evaluated.<sup>391</sup> Persuaded by Public Counsel and The Energy Project's evidence provided in responsive testimony, the Coalition specifically supports the recommendation to require independent bill verification analysis that examines changes in customer usage as a result of DSM programs.<sup>392</sup> The Coalition considers this particularly important as energy conservation becomes a larger resource within the utility's resource portfolio.

285 *The Company's Revised Proposal.* On rebuttal and at the hearing, the Company offers three modifications to its initial proposal, assuming that the new customer adjustment is retained.<sup>393</sup> First, the Company supports lowering the deferral recovery from 90 to 70 percent of its lost margin, so long as 100 percent of its projected DSM savings are achieved. However, the Company offered a different rationale for the 70 percent figure than the Coalition.<sup>394</sup> Avista's witness, Mr. Norwood agreed that

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<sup>389</sup> *Id.* at 6:5-8.

<sup>390</sup> *Id.* at 7:6-8.

<sup>391</sup> *Id.* at 1:10-15.

<sup>392</sup> *Id.* at 1:13-15.

<sup>393</sup> Norwood, Exh. KON-1T at 31:19-32:3 and 50:10-21.

<sup>394</sup> The allowed recovery would not be the lower of the two DSM tests (the IRP DSM savings targets and the DSM savings of limited income customers), but a product of the percentage allowed by each test. For example, if one test allowed 70 percent and the other 90 percent then the allowed percentage would be 0.7 times 0.9, or 63 percent. *See* Norwood, Exh. KON-1T at 49:10-19.

the 70 percent figure was intended as a “rough approximation” of lost margin attributable to Avista’s programmatic and non-programmatic conservation efforts.<sup>395</sup> Second, it suggested a limited income test, whereby five percent of programmatic DSM savings must come from the limited income sector.<sup>396</sup> Third, the Company would work with the parties to address the Company’s measurement and verification of DSM savings, with the results filed with the Commission by September 30, 2010.<sup>397</sup>

286 The Company recommends rejecting Staff’s and Public Counsel’s proposals to eliminate the new customer adjustment (if the decoupling mechanism is continued) and states that it would not even consider continuation of the mechanism if the new customer adjustment were to be removed.<sup>398</sup>

287 The Company also recommends rejection of Staff’s rate design alternative, stating it would prefer to collect all fixed charges through a fixed charge but claims the basic charge would need to be \$22.45 per month.<sup>399</sup> It testifies that Staff’s proposal to subsidize the fixed charge for LIHEAP and LIRAP customers is administratively burdensome.<sup>400</sup>

288 In response to the Energy Project, Avista asserts that limited income customers do obtain a proportionate benefit from its low-cost and no-cost energy education

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<sup>395</sup> Norwood, TR. 1030:4-9.

<sup>396</sup> Norwood, Exh. KON-1T at 49:12-19.

<sup>397</sup> Norwood, Exh. KON-1T at 32:1-3.

<sup>398</sup> Hirschhorn, Exh. BJH-8T at 5:21-23; *see also* Hirschhorn, TR. 1130:15-19.

<sup>399</sup> Norwood, Exh. KON-1T at 45:13-17. However, in response to questions from the bench, Mr. Norwood recognized that such a rate structure could provide less of an incentive to customers to conserve. TR. 1032:20 – 1033:7.

<sup>400</sup> *Id.* at 46:12-21.

messages delivered through Avista’s outreach programs.<sup>401</sup> Avista admits, however, that it does not collect income information from its customers.<sup>402</sup>

## 6. Commission Decision

289 Conservation is one of our cornerstone missions. Consequently, we encourage and support efficiency programs as one of the key objectives in our ratemaking. We have long recognized that conservation is, under almost all circumstances, the least cost energy resource available to a utility and its ratepayers.<sup>403</sup> To further its development, we enable company spending on conservation resources by allowing our utilities to collect all costs associated with their respective conservation programs from ratepayers, subject to an annual reconciliation or “true-up.” In addition, we have provided financial incentives for meeting and exceeding conservation targets<sup>404</sup> and have approved pilot programs for the purpose of determining whether mechanisms, such as the one we have before us, would support a “conservation” culture within our regulated utilities.<sup>405</sup> With this in mind, we judge Avista’s decoupling mechanism and whether it has effectively increased the utility’s efforts to support cost-effective conservation programs for its customers.

290 After careful evaluation, we conclude that Avista’s decoupling mechanism has enhanced the Company’s conservation efforts and that, with some further modifications, it can continue to do so in a manner that balances the interests of ratepayers and the Company. As further explained below, we grant Avista’s petition to continue the decoupling mechanism with several modifications and require the parties to study certain elements of the mechanism for future review. We believe that the modifications we require refine the mechanism to better align the Company’s

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<sup>401</sup> Powell, Exh. JP-3T at 10:16 – 11:7.

<sup>402</sup> *Id.* at 10:4-5 and 11:1-2.

<sup>403</sup> Cost-effective conservation potentials have been clearly identified for decades. The difficulty is achieving them. Hence, the Commission’s consideration of decoupling in this docket.

<sup>404</sup> *2007 PSE Decoupling Order*, ¶¶ 145-158.

<sup>405</sup> *2007 Cascade Rate Case Order*, ¶¶ 67-85; *2007 Avista Pilot Decoupling Plan Order*.

recovery of its lost margins with the impacts of its own programmatic and non-programmatic conservation efforts.

**a. Recovery of Lost Margin**

291 *The “Lost Margin” Issue.* The Company argues that its decoupling mechanism is necessary to allow the recovery of fixed costs approved in the most recent general rate case.<sup>406</sup> We disagree that decoupling’s purpose is so broad. The regulatory construct for decoupling in Washington has centered on the utility’s performance relative to conservation. Our approval of decoupling in our two pilot programs<sup>407</sup> was founded on the premise that lost margins affected the utility’s appetite for offering additional conservation programs. Thus, both pilots required the companies to account for lost margin due to conservation, and to discriminate between the various causes of lost margin. In that more limited context, we conclude that the recovery of lost margin attributable to Avista’s programmatic and non-programmatic conservation endeavors is sufficient to encourage Avista’s DSM efforts.<sup>408</sup> We seek to avoid guaranteed recovery of lost margin that would occur should lost margin from other causes be included in the mechanism.

292 For this same reason, as well as for other reasons, we decline to adopt staff’s proposed alternative of a higher fixed charge that is designed to provide for similar recovery as would have occurred under the decoupling pilot’s design.<sup>409</sup> We also note that with such rate designs, the variable charge for gas purchased would be smaller, thereby decreasing the incentive for each customer to conserve on his or her usage. However, we do approve increasing the customer charge slightly by twenty-five cents per month to \$6.00 per month. This was proposed by the Company and supported by Public Counsel and the Energy Project.

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<sup>406</sup> Norwood, Exh. KON-1T at 44:14-15 and 45:3-4. The Company states that the purpose of the mechanism is, “to provide recovery of fixed costs previously approved by this Commission,...” [emphasis in original].

<sup>407</sup> 2007 Cascade Rate Case Order, ¶¶ 67-85; 2007 Avista Pilot Decoupling Plan Order.

<sup>408</sup> Norwood, Exh. KON-1T at 36:18-21.

<sup>409</sup> Reynolds, Exh. DJR-1T at 26:15-17.

293 *Amount of Deferral Allowed for Later Recovery.* In its initial filing, Avista requested that the pilot program's 90 percent deferral feature be extended on a permanent basis.<sup>410</sup> However, in its rebuttal case, the Company recommends reducing the recovery level to 70 percent due to "the variables outside the normal ebb and flow of customer usage over time." At hearing, Avista acknowledged that the decoupling mechanism allows for recovery of lost margin due to all factors but weather, and agreed that the reduction in the percentage of recovery it proposed was a "rough approximation" aimed at taking into account lost margin from causes other than Company DSM efforts.<sup>411</sup>

294 We do not agree with what appears to be the Company's arbitrary 70 percent figure for recoverable lost margin.<sup>412</sup> We find no real record support for the Company's linking that percentage to the lost margin attributable to its programmatic and non-programmatic conservation programs. In our approval of the pilot program, we assigned to Avista the burden of justifying the continuation of the program. In our view, basing a 70 percent deferral on a "rough approximation" is not adequate to meet that burden. In effect, that is a "top-down" approach: determine the total lost margin and then subtract some estimated percentage that may be attributable to other causes of lost margin.

295 We recognize that determining how much of the Company's lost margins are attributable to its conservation efforts is a difficult task. However, it is not impossible. We have a record before us that shows the parties' estimates of recoverable lost margin to range from 10 percent to the Company's 70 percent.<sup>413</sup> It appears that Staff and Public Counsel have determined their estimates of the

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<sup>410</sup> Staff, asserts that the programs purpose was to include lost margin due to all reasons, not just conservation programs. Reynolds, Exh. DJR-3T at 2:19 – 3:3. The pilot decoupling program approved was a *partial* decoupling mechanism that excluded weather before it calculated all other effects.

<sup>411</sup> *Id.*

<sup>412</sup> Reynolds, Exh. DJR-1T at 19:11-13.

<sup>413</sup> In the future, we expect the Company (and indeed the parties, too) to do better at making such an empirical assessment.

Company's percentage of lost margin by using a "bottom up" approach, which we believe best to arrive at a fair and equitable result. Using this approach, we start with evidence as to Avista's programmatic conservation efforts, add the ascertainable impacts of its non-programmatic (including educational) efforts, and fix this amount for deferral and later recovery. We turn now to the record before us.

296 As noted above, nearly every party submitted evidence from which we can gauge the lost margin attributable to the Company's programmatic conservation efforts:

- *Avista.* Avista concludes that the *total* deferral and recovery should be 70 percent. It does not effectively distinguish between its programmatic and non-programmatic efforts and all other causes.<sup>414</sup>
- *Public Counsel.* Citing the Titus Report to support its conclusion, Public Counsel states that the ratio of the lost margin due to Company's programmatic conservation to the deferred lost margin was 10 percent in 2007 and 12.5 percent in 2008.<sup>415</sup> It notes, however, that these ratios do not take into account the effect of interceding rate cases.<sup>416</sup>
- *Staff.* Commission Staff portrays a more favorable view of the proportionality of the Company's deferrals to its programmatic lost margin and concludes that, even accounting for multi-year losses, Avista's deferred lost margin was three times the lost margin caused by its DSM program, or 33 percent of the total deferral.<sup>417</sup> We note that Staff's ratio includes the effect of the interceding rate case. (However, in its brief, Staff estimates the percentage as 25 percent.)<sup>418</sup>

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<sup>414</sup> In fact, Avista's own third-party evaluator did not attribute 70 percent of the Company's lost margin to its conservation program. See Exh. BJH-2-A (Titus Report) at 9.

<sup>415</sup> Brosch, Exh. MLB-1T at 16:8-10.

<sup>416</sup> We recognize that the amount of money deferred over a twelve month period grows with the amount of time between rate cases, resulting in different percentages depending on how long the gap between rate cases. We expect an increase in the incremental DSM achieved over time and, therefore, incremental increases in the lost margin from Company sponsored programmatic and non-programmatic efforts. Though the Company, in recent years, has filed rate cases annually, this fact should encourage, at least somewhat, the Company to refrain from filing general rates so frequently.

<sup>417</sup> Reynolds, Exh. DJR-1T at 19:8-9.

<sup>418</sup> Staff Brief, ¶ 83.

- *Coalition.* The NW Energy Coalition proposes that if the Company should meet its DSM target, then it should be allowed to recover 50 percent of its deferral.<sup>419</sup> However, the Coalition also recommends the Company be provided an incentive for achieving DSM levels above its current target. It also supports allowing the Company to recover lost margins due to other causes in addition to those related to programmatic and non-programmatic conservation.

297 We now turn to the impacts of the Company's non-programmatic DSM efforts which are even more difficult to determine. The Company asserts its educational DSM efforts, such as its "Every Little Bit" program, produce DSM savings that contribute to lost margins.<sup>420</sup> These claims rest on descriptions of the Company's various non-programmatic efforts<sup>421</sup> and the testimony of Mr. Kelly Norwood, who opined that the Every Little Bit program works as intended. However, the Company does not make an effort to quantify the *actual* impact of its efforts.<sup>422</sup> In rebuttal, Public Counsel offers its own assessment and in brief argues the Company presented no *quantifiable* evidence of DSM savings from its non-programmatic efforts.<sup>423</sup> Basing its conclusions on the education program's budget, Public Counsel states that the non-programmatic savings are not significant.<sup>424</sup> Commission Staff testifies that the non-programmatic efforts have made a significant contribution to conservation, but does not quantify the effect.<sup>425</sup> The Coalition states it believes that conservation from the non-programmatic efforts are significant, but also does not quantify it.<sup>426</sup>

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<sup>419</sup> Glaser, Exh. NLG-1T at 12:13-18.

<sup>420</sup> Powell, Exh. JP-1T at 4:1-17.

<sup>421</sup> *Id.* The "Every Little Bit" education and outreach program is part of the Company's non-programmatic DSM efforts. See Exh. JP-2.

<sup>422</sup> Exh. KON-2-X.

<sup>423</sup> Brosch, MLB-1T at 19:19 – 20:5; Public Counsel Brief, ¶46.

<sup>424</sup> Brosch, MLB-1T at 19:19 – 20:5.

<sup>425</sup> Reynolds, DJR-1T at 9:21 – 10:3.

<sup>426</sup> Glaser, NLG-1T at 12:27-29.

298 We recognize that the Company's non-programmatic efforts are an important part of its overall conservation efforts and encourage the Company to continue to educate its ratepayers as to the benefits of energy efficiency. Unlike the testimony offered in response to the Company's programmatic efforts, the record here presents only opinions of the amount of savings attributable to the Company's non-programmatic efforts or, in the case of Public Counsel, an indirect method of assessing the program's effect. Given this record, we conclude that the Company's non-programmatic efforts produce real savings. However, it appears that such savings do not compare with savings due to the Company's programmatic expenditures.

299 Combining our judgment on the level of the Company's non-programmatic and programmatic efforts, and based on the record before us, we conclude that 45 percent of Schedule 101's lost margins are attributable to these efforts and set the maximum recovery at that amount. This level provides for the recovery of all lost margins from Company sponsored conservation, allocates a generous percentage to its non-programmatic efforts, and balances the Company's recovery under the program with ratepayers' interests. In choosing a percentage level for the target to achieve this goal we recognize the complexity and uncertainty of the task revealed in the record and that this maximum deferral percentage may change in future cases as the parties develop further evidence. We leave the percentage point reductions in the percentages of lost margin recoverable for falling below the DSM target unchanged.

**Current Mechanism**

<b>Actual vs. Target DSM Savings</b>	<b>Amount Deferred</b>
<70%	60%
>80% and <90%	70%
>90% and <100%	80%
100%	90%

**Commission Decision**

<b>Actual vs. Target DSM Savings</b>	<b>Amount Deferred</b>
<70%	15%
>80% and <90%	25%
>90% and <100%	35%
100%	45%

300 *Other Modifications.* There are two other modifications to the program that we find necessary and appropriate. First, we agree that DSM savings attributable to Idaho should be excluded from the target. At its initiation, the pilot program's target included DSM savings for Idaho. Since that time, the Company has been able to allocate program impacts between the jurisdictions. Consequently, both the Titus Report and Company testimony present DSM savings on a Washington jurisdictional basis. Therefore, to better match benefits to those paying the cost, we modify the decoupling mechanism to set the program's targets and measure its achievement using only Washington DSM savings. This new requirement will be effective with the target set as a result of the Company's 2009 natural gas Integrated Resource Plan.

301 Second, we require that the lost margin calculation be adjusted to remove the effect of customer migration between Schedule 101 and Schedule 111. The Company has testified that customer migration may account for five percent of the total lost margin deferred.<sup>427</sup> We accept the method the Company proposes for removing the effect of customer migration.

302 *New Customer Adjustment.* We reject Staff and Public Counsel's proposal to eliminate the new customer adjustment. In approving the pilot mechanism, we agreed to include this adjustment in order to better understand the actual impacts of Avista's conservation program. In this order, we reiterate our support for basing recovery under the program upon the conservation efforts of the Company. Were we to remove this adjustment, recovery of lost margins due to conservation would decrease due to the addition of therms sold to new customers, undercutting the central reason we allow this program to go forward.

303 *Future Inclusion of All Customer Classes.* By reducing the Company's natural gas load, including its peak requirements, Avista's conservation program benefits all customers. In fact, the decoupling program includes conservation from all rate schedules in setting its targets and determining its success. Even so, as now put in place, the program's lost margin is only collected from Schedule 101 customers. Following the principle of costs following benefits discussed above, we expect the

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<sup>427</sup> Hirschhorn, Exh. BJH-1T-A at 12:7 – 13:12.

parties to address whether the program should recover DSM-related lost margin from all rate schedules in Avista's next general rate case.

**b. Measurement of DSM Achievement**

304 It is obvious from the record that the parties have struggled to determine the actual impact of the Company's conservation program.<sup>428</sup> Testimony relates this problem in part to the lack of evaluation, measurement and verification (EM&V) techniques for conservation programs. Public Counsel's analysis, while a sampling, indicates significant shortcomings in the Company's EM&V methods.<sup>429</sup> Staff recommends the Company work with interested parties in a collaborative process to design a consistent and accurate measurement method. The Coalition supports this idea.<sup>430</sup> On rebuttal, the Company agrees there is a need to improve measurement and verification of DSM savings, stating that it is in the process of developing a revised measurement and verification approach for review by its Triple-E board. After review the Company will incorporate the revised approach into its 2010 DSM Business Plan.<sup>431</sup>

305 We recognize that the cost-effectiveness and therefore prudence of programmatic DSM expenses and lost margin recovery under any decoupling or incentive mechanism rests on the evaluation, measurement and verification of energy savings achieved. Furthermore, we agree with the parties that Company's EM&V efforts need to be improved. We require the parties to join in the collaborative planned for this subject, and expect them to participate in the development of consistent and accurate methods to judge the effectiveness of all energy efficiency programs and measures. We also require the Company to file an EM&V plan for its DSM programs

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<sup>428</sup> Various intervenors question the accuracy of the therm savings claimed by the Company during the decoupling pilot program. *See* Reynolds, Exh. DJR-1T at 8:7-14; Kimball, Exh. MMK-1T at 2:9 – 3:11; Glaser, Exh. NLG-5T at 1:9-15.

<sup>429</sup> Kimball, Exh. MMK-1T at 2:9-3:11.

<sup>430</sup> Glaser, Exh. NLG-5T at 1:9-13.

<sup>431</sup> Powell, Exh. JP-1T at 8:1-2.

by September 1, 2010. The plan should include a bill verification analysis that examines changes in customer usage as a result of DSM programs.

**c. Low-Income Conservation Achievement**

306 The Company's low-income conservation achievement during the decoupling pilot is particularly disappointing. As the program's impact on low-income customers remains a key issue, we direct the Company, working in collaboration with the parties, to explore new approaches to promote low-income conservation, to identify barriers to its development, and to address the issues raised by The Energy Project. The Company shall report its conclusions to the Commission at the same time it submits the EM&V report.

**d. Deferrals Made from July 1, 2009, to the Effective Date of This Order**

307 In our order granting the Company an interim extension of its pilot program, we deferred consideration of the issue of how the decoupling program would operate from the end of the pilot until the effective date of this Order.<sup>432</sup> The Company agreed in its extension request to adjust deferral accounts to reflect modifications to the mechanism that the Commission required. Therefore, we now order the application of the conditions of this order to deferrals calculated on or after July 1, 2009.

**e. Risk Reduction and Modified Return on Equity (ROE)**

308 We decline here to adopt a modification to the Company's return on equity. We acknowledge that reducing a Company's risk can result in a reduction of its return on equity. However, the testimony supporting such a reduction does not address the modifications we have made to the mechanism. The only evidence presented was an adjustment sponsored by Public Counsel and ICNU based on the Company's recovery of 90 percent of the deferred margin.<sup>433</sup> As reflected herein, we have reduced the recovery amount to 45 percent. We believe this reduction to be a substantive change

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<sup>432</sup> Dockets UE-090134, UG-090135 & UG-060518, Order 07, ¶¶ 13, 16, 17.

<sup>433</sup> Gorman, MPG-1T at 5:15-17 and 7:20-22.

not addressed by the Public Counsel and ICNU joint testimony. For this reason, we withhold judgment on this issue, but remain open to the parties developing this concept further in future proceedings.

**f. Summary**

309 Despite some shortcomings, the Company's pilot decoupling mechanism achieved the goal of incrementally increasing Avista's company-sponsored conservation efforts. However, its initial design should be modified to better align the Company's interests with that of its customers. We believe this is accomplished by allowing the Company the opportunity to recover lost margins related to its programmatic and non-programmatic conservation efforts. While lower than the amount requested by Avista, we believe this amount is sufficient to encourage and support its ongoing and developing conservation program. We note that decoupling is but one method of supporting conservation, and we encourage the Company and parties to consider alternatives that avoid the mechanism's inherent complications, while accomplishing the objectives we set forth herein.<sup>434</sup>

**FINDINGS OF FACT**

310 Having discussed above in detail the evidence received in this proceeding concerning all material matters, and having stated findings and conclusions upon issues in dispute among the parties and the reasons therefore, the Commission now makes and enters the following summary of those facts, incorporating by reference pertinent portions of the preceding detailed findings:

- 311 (1) The Washington Utilities and Transportation Commission is an agency of the State of Washington, vested by statute with authority to regulate the rates, rules, regulations, practices, and accounts of public service companies, including electrical and gas companies.
- 312 (2) Avista is a "public service company," an "electrical company," and a "gas company" as those terms are defined in RCW 80.04.010 and used in Title 80

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<sup>434</sup> See, e.g., 2007 PSE Decoupling Order.

RCW. Avista is engaged in Washington in the business of supplying utility services and commodities to the public for compensation.

- 313 (3) Avista filed on January 23, 2009, certain revisions to its currently effective tariffs, including rate increases for customers of its electric service and gas services in Washington. The revised tariff sheets bore an effective date of February 23, 2009.
- 314 (4) The Commission suspended the operation of the proposed tariff revisions on February 3, 2009, pending an investigation and hearing in Docket UE-090134 and UG-090135.
- 315 (5) On September 4, 2009, the parties filed a Settlement Stipulation that, if approved, would resolve some, but not all, issues concerning cost of capital, power costs, rate spread and rate design, and other matters.
- 316 (6) Considering the proposed Settlement Stipulation and the full evidentiary record following hearing, the Commission determined that Avista's existing rates for electric service and natural gas service provided in Washington are insufficient to yield reasonable compensation for the services rendered. Avista accordingly requires prospective relief with respect to the rates it charges for electric and natural gas services provided in Washington.
- 317 (7) Avista requires additional revenue as reflected in the Settlement Stipulation as conditioned by this Order, the uncontested adjustments summarized in Table 2A for electric service and Table 2B for natural gas service, and the Commission's resolution of contested adjustments as detailed in the body of this Order and summarized in Table 4 for electric service and Table 5 for natural gas service.
- 318 (8) It is in the public interest to increase the Low Income Rate Assistance Program portion of Schedules 91 and 191 as specified in the Settlement Stipulation.
- 319 (9) Avista failed to file the necessary documentation in this proceeding to allow the Commission to adequately review the Lancaster contracts as an affiliated transaction or for compliance with greenhouse gas emissions standards.

- 320 (10) On April 30, 2009, Avista filed a petition to consolidate Docket UG-060518, concerning its pilot natural gas decoupling mechanism, with the rate case proceedings in Dockets UE-090134 and UG-090135. The Company asked the Commission, among other things, to extend the pilot program beyond its scheduled termination date of June 30, 2009. The Commission consolidated the decoupling issues into the general rate case proceedings and granted an interim extension of the pilot decoupling mechanism pending the outcome of these proceedings.
- 321 (11) Avista's decoupling mechanism has enhanced the Company's conservation efforts and, with modifications discussed in the body of this Order that better align the Company's recovery of its lost margins with the impacts of its own programmatic and non-programmatic conservation efforts, it can continue to do so in a manner that balances the interests of ratepayers and the Company.
- 322 (12) Forty-five percent (45%) of Schedule 101's lost margins are attributable to Avista's programmatic and non-programmatic conservation efforts.
- 323 (13) The rates, terms, and conditions of service that result from adoption of the Settlement Stipulation attached to and incorporated into the body of this Order as if set forth in full, coupled with the Commission's determinations of contested issues as discussed in the body of this order, result in rates for Avista's electric service and natural gas service that are fair, just, reasonable, and sufficient.
- 324 (14) The rates, terms, and conditions of service that result from the Commission's determinations in this Order are neither unduly preferential nor discriminatory.

#### **CONCLUSIONS OF LAW**

325 Having discussed above all matters material to this decision, and having stated detailed findings, conclusions, and the reasons therefore, the Commission now makes the following summary conclusions of law, incorporating by reference pertinent portions of the preceding detailed conclusions:

- 326 (1) The Washington Utilities and Transportation Commission has jurisdiction over the subject matter of, and parties to, these proceedings.
- 327 (2) The rates proposed by tariff revisions filed by Avista on January 23, 2009, and suspended by prior Commission order, were not shown to be fair, just or reasonable and should be rejected.
- 328 (3) The existing rates for electric service and gas service that Avista provides in Washington are insufficient to yield reasonable compensation for the services rendered.
- 329 (4) Avista requires relief with respect to the rates it charges for electric service and gas service provided in Washington.
- 330 (5) The Settlement Stipulation filed by the Parties to this proceeding on September 4, 2009, if approved subject to the conditions stated in this Order requiring adjustment to power costs to reflect the Commission's disallowance of recovery of costs associated with the Lancaster Power Purchase Agreement (PPA), would result in rates for Avista that are fair, just, reasonable and sufficient, and are neither unduly preferential nor discriminatory. The Settlement Stipulation is attached to this Order as Appendix A, and incorporated by reference as if set forth in full in the body of this Order.
- 331 (6) The Partial Settlement Stipulation should be approved by the Commission, subject to the conditions stated in this Order requiring adjustment to power costs to reflect the Commission's disallowance of recovery of costs associated with the Lancaster PPA, as a reasonable resolution of the issues presented. Approval and adoption of the Partial Settlement Stipulation, as conditioned, is in the public interest.
- 332 (7) The Low Income Rate Assistance Program portion of Schedules 91 and 191 should be increased in the Company's electric and gas tariffs to levels specified in the Settlement Stipulation: 9.0 percent for electricity and 1.75 percent for gas.

- 333 (8) Avista should be allowed to recover in rates additional revenue as reflected in the Settlement Stipulation, the uncontested adjustments summarized in Table 2A for electric service and Table 2B for natural gas service, and the Commission's resolution of contested adjustments as detailed in the body of this Order and summarized in Table 4 for electric service and Table 5 for natural gas service.
- 334 (9) Avista's maximum recovery of lost margin via the decoupling mechanism should be limited to forty-five percent (45%) of Schedule 101's lost margins, which the Commission finds are attributable to Avista's programmatic and non-programmatic conservation efforts.
- 335 (10) To better match benefits to those paying the costs, the Commission should modify the decoupling mechanism effective with the target set as a result of the Company's 2009 natural gas Integrated Resource Plan, by setting and measuring achievement under the DSM target with DSM savings for Idaho removed so that only DSM savings for Washington are considered.
- 336 (11) The lost margin calculation under Avista's decoupling mechanism should be adjusted to remove the effect of customer migration between Schedule 101 and Schedule 111 because there is no recovery of DSM lost margin from Schedule 111 customers.
- 337 (12) Avista should be required to make such compliance and subsequent filings as are necessary to effectuate the terms of this Order.
- 338 (13) The Commission should retain jurisdiction to effectuate the terms of this Order.

**ORDER**

THE COMMISSION ORDERS:

- 339 (1) The tariff revisions Avista Corporation, d/b/a Avista Utilities, filed on January 23, 2009, and suspended by prior Commission order, are rejected.
- 340 (2) The Settlement Stipulation filed by the parties on September 4, 2009, is approved and adopted as being in the public interest, subject to the Commission's determination that the costs associated with the Lancaster PPA must be removed, necessitating a rerun of the AURORA power cost model during the compliance phase of this proceeding and an adjustment to the power cost set forth in the Settlement Stipulation for recovery in rates.
- 341 (3) Avista Utilities is authorized and required to file tariff sheets that are necessary and sufficient to effectuate the terms of this Order. The required tariff sheets must be filed no later than 5:00 p.m. on Monday, December 28, 2009, to give the Commission an opportunity to review the Company's compliance filing, and shall bear an effective date of January 1, 2010.
- 342 (4) Avista Utilities is authorized to defer the costs associated with the Lancaster PPA for a period not to exceed twenty-four (24) months from the beginning of the Lancaster contract. If the Company files a general rate case seeking to recover Lancaster contract costs during the twenty-four (24) month period, the deferral ends on the effective date of the Commission's Final Order in such proceeding. This authorization for deferral is conditioned on the Company filing a petition for accounting treatment consistent with the terms and requirements of this Order.
- 343 (5) Increases to levels specified in the Settlement Stipulation are approved for the Low Income Rate Assistance Program portion of Schedules 91 and 191.

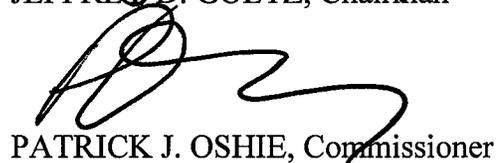
- 344 (6) Avista Utilities is authorized to continue its decoupling mechanism, as modified by the terms of this Order. Deferrals recorded since June 30, 2009, are required to be adjusted as if deferred under the modified mechanism and are subject to recovery on that basis.
- 345 (7) Avista Utilities must convene a collaborative to discuss evaluation, measurement and verification (EM&V) methodology for its DSM programs and file a plan in accordance with this Order by September 1, 2010.
- 346 (8) Avista Utilities must also file by September 1, 2010, a separate report investigating the impact of its decoupling mechanism on low-income customers.
- 347 (9) The Commission Secretary is authorized to accept by letter, with copies to all parties to this proceeding, such filings as Avista Utilities makes to comply with the terms of this Order.
- 348 (10) The Commission retains jurisdiction to effectuate the terms of this Order.

Dated at Olympia, Washington, and effective December 22, 2009.

WASHINGTON STATE UTILITIES AND TRANSPORTATION COMMISSION



JEFFREY D. GOLTZ, Chairman



PATRICK J. OSHIE, Commissioner



PHILIP B. JONES, Commissioner

**KC REPLY APPENDIX 229**

**RCW 34.05.546****Petition for review—Contents.**

A petition for review must set forth:

- (1) The name and mailing address of the petitioner;
- (2) The name and mailing address of the petitioner's attorney, if any;
- (3) The name and mailing address of the agency whose action is at issue;
- (4) Identification of the agency action at issue, together with a duplicate copy, summary, or brief description of the agency action;
- (5) Identification of persons who were parties in any adjudicative proceedings that led to the agency action;
- (6) Facts to demonstrate that the petitioner is entitled to obtain judicial review;
- (7) The petitioner's reasons for believing that relief should be granted; and
- (8) A request for relief, specifying the type and extent of relief requested.

[ 1988 c 288 § 510.]

**RCW 34.05.570****Judicial review.**

(1) Generally. Except to the extent that this chapter or another statute provides otherwise:

(a) The burden of demonstrating the invalidity of agency action is on the party asserting invalidity;  
 (b) The validity of agency action shall be determined in accordance with the standards of review provided in this section, as applied to the agency action at the time it was taken;

(c) The court shall make a separate and distinct ruling on each material issue on which the court's decision is based; and

(d) The court shall grant relief only if it determines that a person seeking judicial relief has been substantially prejudiced by the action complained of.

(2) Review of rules. (a) A rule may be reviewed by petition for declaratory judgment filed pursuant to this subsection or in the context of any other review proceeding under this section. In an action challenging the validity of a rule, the agency shall be made a party to the proceeding.

(b)(i) The validity of any rule may be determined upon petition for a declaratory judgment addressed to the superior court of Thurston county, when it appears that the rule, or its threatened application, interferes with or impairs or immediately threatens to interfere with or impair the legal rights or privileges of the petitioner. The declaratory judgment order may be entered whether or not the petitioner has first requested the agency to pass upon the validity of the rule in question.

(ii) From June 10, 2004, until July 1, 2008:

(A) If the petitioner's residence or principal place of business is within the geographical boundaries of the third division of the court of appeals as defined by RCW **2.06.020**(3), the petition may be filed in the superior court of Spokane, Yakima, or Thurston county; and

(B) If the petitioner's residence or principal place of business is within the geographical boundaries of district three of the first division of the court of appeals as defined by RCW **2.06.020**(1), the petition may be filed in the superior court of Whatcom or Thurston county.

(c) In a proceeding involving review of a rule, the court shall declare the rule invalid only if it finds that: The rule violates constitutional provisions; the rule exceeds the statutory authority of the agency; the rule was adopted without compliance with statutory rule-making procedures; or the rule is arbitrary and capricious.

(3) Review of agency orders in adjudicative proceedings. The court shall grant relief from an agency order in an adjudicative proceeding only if it determines that:

(a) The order, or the statute or rule on which the order is based, is in violation of constitutional provisions on its face or as applied;

(b) The order is outside the statutory authority or jurisdiction of the agency conferred by any provision of law;

(c) The agency has engaged in unlawful procedure or decision-making process, or has failed to follow a prescribed procedure;

(d) The agency has erroneously interpreted or applied the law;

(e) The order is not supported by evidence that is substantial when viewed in light of the whole record before the court, which includes the agency record for judicial review, supplemented by any additional evidence received by the court under this chapter;

(f) The agency has not decided all issues requiring resolution by the agency;

(g) A motion for disqualification under RCW **34.05.425** or **34.12.050** was made and was improperly denied or, if no motion was made, facts are shown to support the grant of such a motion that were not known and were not reasonably discoverable by the challenging party at the appropriate time for making such a motion;

(h) The order is inconsistent with a rule of the agency unless the agency explains the inconsistency by stating facts and reasons to demonstrate a rational basis for inconsistency; or

(i) The order is arbitrary or capricious.

(4) Review of other agency action.

(a) All agency action not reviewable under subsection (2) or (3) of this section shall be reviewed under this subsection.

(b) A person whose rights are violated by an agency's failure to perform a duty that is required by law to be performed may file a petition for review pursuant to RCW **34.05.514**, seeking an order pursuant to this subsection requiring performance. Within twenty days after service of the petition for review, the agency shall file and serve an answer to the petition, made in the same manner as an answer to a complaint in a civil action. The court may hear evidence, pursuant to RCW **34.05.562**, on material issues of fact raised by the petition and answer.

(c) Relief for persons aggrieved by the performance of an agency action, including the exercise of discretion, or an action under (b) of this subsection can be granted only if the court determines that the action is:

- (i) Unconstitutional;
- (ii) Outside the statutory authority of the agency or the authority conferred by a provision of law;
- (iii) Arbitrary or capricious; or
- (iv) Taken by persons who were not properly constituted as agency officials lawfully entitled to take such action.

[ **2004 c 30 § 1**; **1995 c 403 § 802**; **1989 c 175 § 27**; **1988 c 288 § 516**; **1977 ex.s. c 52 § 1**; **1967 c 237 § 6**; **1959 c 234 § 13**. Formerly RCW **34.04.130**.]

#### **NOTES:**

**Findings—Short title—Intent—1995 c 403:** See note following RCW **34.05.328**.

**Effective date—1989 c 175:** See note following RCW **34.05.010**.

## **RCW 80.04.130**

### **Suspension of tariff change—Mandatory measured telecommunications service—Washington telephone assistance program service—Effect of abandonment of electrical generation facility on which tax exemption for pollution control equipment is claimed—Waiver of provisions during state of emergency.**

(1) Except as provided in subsection (2) of this section, whenever any public service company shall file with the commission any schedule, classification, rule, or regulation, the effect of which is to change any rate, charge, rental, or toll theretofore charged, the commission shall have power, either upon its own motion or upon complaint, upon notice, to enter upon a hearing concerning such proposed change and the reasonableness and justness thereof. Pending such hearing and the decision thereon, the commission may suspend the operation of such rate, charge, rental, or toll for a period not exceeding ten months from the time the same would otherwise go into effect. After a full hearing, the commission may make such order in reference thereto as would be provided in a hearing initiated after the same had become effective.

(2)(a) The commission shall not suspend a tariff that makes a decrease in a rate, charge, rental, or toll filed by a telecommunications company pending investigation of the fairness, justness, and reasonableness of the decrease when the filing does not contain any offsetting increase to another rate, charge, rental, or toll and the filing company agrees to not file for an increase to any rate, charge, rental, or toll to recover the revenue deficit that results from the decrease for a period of one year.

(i) The filing company shall file with any decrease sufficient information as the commission by rule may require to demonstrate the decreased rate, charge, rental, or toll is above the long run incremental cost of the service. A tariff decrease that results in a rate that is below long run incremental cost, or is contrary to commission rule or order, or the requirements of this chapter, shall be rejected for filing and returned to the company.

(ii) The commission may prescribe a different rate to be effective on the prospective date stated in its final order after its investigation, if it concludes based on the record that the originally filed and effective rate is unjust, unfair, or unreasonable.

(b) The commission shall not suspend a promotional tariff. For the purposes of this section, "promotional tariff" means a tariff that, for a period of up to ninety days, waives or reduces charges or conditions of service for existing or new subscribers for the purpose of retaining or increasing the number of customers who subscribe to or use a service.

(3) The commission may suspend the initial tariff filing of any water company removed from and later subject to commission jurisdiction because of the number of customers or the average annual gross revenue per customer provisions of RCW **80.04.010**. The commission may allow temporary rates during the suspension period. These rates shall not exceed the rates charged when the company was last regulated. Upon a showing of good cause by the company, the commission may establish a different level of temporary rates.

(4) At any hearing involving any change in any schedule, classification, rule, or regulation the effect of which is to increase any rate, charge, rental, or toll theretofore charged, the burden of proof to show that such increase is just and reasonable shall be upon the public service company.

(5) The implementation of mandatory local measured telecommunications service is a major policy change in available telecommunications service. The commission shall not accept for filing a price list, nor shall it accept for filing or approve, prior to June 1, 2004, a tariff filed by a telecommunications company which imposes mandatory local measured service on any customer or class of customers, except that, upon finding that it is in the public interest, the commission may accept for filing a price list or it may accept for filing and approve a tariff that imposes mandatory measured service for a telecommunications company's extended area service or foreign exchange service. This subsection does not apply to land, air, or marine mobile service, or to pay telephone service, or to any service which has been traditionally offered on a measured service basis.

(6) The implementation of Washington telephone assistance program service is a major policy change in available telecommunications service. The implementation of Washington telephone assistance program

service will aid in achieving the stated goal of universal telephone service.

(7) If a utility claims a sales or use tax exemption on the pollution control equipment for an electrical generation facility and abandons the generation facility before the pollution control equipment is fully depreciated, any tariff filing for a rate increase to recover abandonment costs for the pollution control equipment shall be considered unjust and unreasonable for the purposes of this section.

(8) During a state of emergency declared under RCW 43.06.010(12), the governor may waive or suspend the operation or enforcement of this section or any portion of this section or under any administrative rule, and issue any orders to facilitate the operation of state or local government or to promote and secure the safety and protection of the civilian population.

[ 2008 c 181 § 401; 2003 c 189 § 1; 2001 c 267 § 1; 1998 c 110 § 1; 1997 c 368 § 14; 1993 c 311 § 1; 1992 c 68 § 1; 1990 c 170 § 1; 1989 c 101 § 13. Prior: 1987 c 333 § 1; 1987 c 229 § 2; prior: 1985 c 450 § 12; 1985 c 206 § 1; 1985 c 161 § 2; 1984 c 3 § 2; 1961 c 14 § 80.04.130; prior: 1941 c 162 § 1; 1937 c 169 § 2; 1933 c 165 § 3; 1915 c 133 § 1; 1911 c 117 § 82; Rem. Supp. 1941 § 10424.]

#### NOTES:

**Part headings not law—2008 c 181:** See note following RCW 43.06.220.

**Effective date—2001 c 267:** "This act is necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and takes effect immediately [May 11, 2001]." [ 2001 c 267 § 2.]

**Findings—Intent—Rules adoption—Severability—Effective date—1997 c 368:** See notes following RCW 82.08.810.

**Effective date—1993 c 311:** "This act is necessary for the immediate preservation of the public peace, health, or safety, or support of the state government and its existing public institutions, and shall take effect immediately [May 12, 1993]." [ 1993 c 311 § 2.]

**Effective date—1987 c 333:** "This act is necessary for the immediate preservation of the public peace, health, and safety, the support of the state government and its existing public institutions, and shall take effect June 1, 1987." [ 1987 c 333 § 2.]

**Legislative review—1985 c 450:** See RCW 80.36.901.

**RCW 80.04.250****Valuation of public service property.**

(1) The commission has power upon complaint or upon its own motion to ascertain and determine the fair value for rate making purposes of the property of any public service company used and useful for service in this state and shall exercise such power whenever it deems such valuation or determination necessary or proper under any of the provisions of this title. In determining what property is used and useful for providing electric, gas, wastewater company services, or water service, the commission may include the reasonable costs of construction work in progress to the extent that the commission finds that inclusion is in the public interest.

(2) The commission has the power to make revaluations of the property of any public service company from time to time.

(3) The commission shall, before any hearing is had, notify the complainants and the public service company concerned of the time and place of such hearing by giving at least thirty days' written notice thereof, specifying that at the time and place designated a hearing will be held for the purpose of ascertaining the value of the company's property, used and useful as aforesaid, which notice must be sufficient to authorize the commission to inquire into and pass upon the matters designated in this section.

[ 2011 c 214 § 9; 1991 c 122 § 2; 1961 c 14 § 80.04.250. Prior: 1933 c 165 § 4; 1913 c 182 § 1; 1911 c 117 § 92; RRS § 10441.]

**NOTES:**

**Findings—Purpose—Limitation of chapter—Effective date—2011 c 214:** See notes following RCW 80.04.010.

**Findings—1991 c 122:** "The legislature finds that the state is facing an energy shortage as growth occurs and that inadequate supplies of energy will cause harmful impacts on the entire range of state citizens. The legislature further finds that energy efficiency improvement is the single most effective near term measure to lessen the risk of energy shortage. In the area of electricity, the legislature additionally finds that the Northwest power planning council has made several recommendations, including an update of the commercial building energy code and granting flexible ratemaking alternatives for utility commissions to encourage prudent acquisition of new electric resources." [ 1991 c 122 § 1.]

**Severability—1991 c 122:** "If any provision of this act or its application to any person or circumstance is held invalid, the remainder of the act or the application of the provision to other persons or circumstances is not affected." [ 1991 c 122 § 4.]

**RCW 80.28.010****Duties as to rates, services, and facilities—Limitations on termination of utility service for residential heating.**

(1) All charges made, demanded or received by any gas company, electrical company, wastewater company, or water company for gas, electricity or water, or for any service rendered or to be rendered in connection therewith, shall be just, fair, reasonable and sufficient. Reasonable charges necessary to cover the cost of administering the collection of voluntary donations for the purposes of supporting the development and implementation of evergreen community management plans and ordinances under RCW **80.28.300** must be deemed as prudent and necessary for the operation of a utility.

(2) Every gas company, electrical company, wastewater company, and water company shall furnish and supply such service, instrumentalities and facilities as shall be safe, adequate and efficient, and in all respects just and reasonable.

(3) All rules and regulations issued by any gas company, electrical company, wastewater company, or water company, affecting or pertaining to the sale or distribution of its product or service, must be just and reasonable.

(4) Utility service for residential space heating shall not be terminated between November 15 through March 15 if the customer:

(a) Notifies the utility of the inability to pay the bill, including a security deposit. This notice should be provided within five business days of receiving a payment overdue notice unless there are extenuating circumstances. If the customer fails to notify the utility within five business days and service is terminated, the customer can, by paying reconnection charges, if any, and fulfilling the requirements of this section, receive the protections of this chapter;

(b) Provides self-certification of household income for the prior twelve months to a grantee of the department of commerce, which administers federally funded energy assistance programs. The grantee shall determine that the household income does not exceed the maximum allowed for eligibility under the state's plan for low-income energy assistance under 42 U.S.C. 8624 and shall provide a dollar figure that is seven percent of household income. The grantee may verify information provided in the self-certification;

(c) Has applied for home heating assistance from applicable government and private sector organizations and certifies that any assistance received will be applied to the current bill and future utility bills;

(d) Has applied for low-income weatherization assistance to the utility or other appropriate agency if such assistance is available for the dwelling;

(e) Agrees to a payment plan and agrees to maintain the payment plan. The plan will be designed both to pay the past due bill by the following October 15th and to pay for continued utility service. If the past due bill is not paid by the following October 15, the customer is not eligible for protections under this chapter until the past due bill is paid. The plan may not require monthly payments in excess of seven percent of the customer's monthly income plus one-twelfth of any arrearage accrued from the date application is made and thereafter during November 15 through March 15. A customer may agree to pay a higher percentage during this period, but shall not be in default unless payment during this period is less than seven percent of monthly income plus one-twelfth of any arrearage accrued from the date application is made and thereafter. If assistance payments are received by the customer subsequent to implementation of the plan, the customer shall contact the utility to reformulate the plan; and

(f) Agrees to pay the moneys owed even if he or she moves.

(5) The utility shall:

(a) Include in any notice that an account is delinquent and that service may be subject to termination, a description of the customer's duties in this section;

(b) Assist the customer in fulfilling the requirements under this section;

(c) Be authorized to transfer an account to a new residence when a customer who has established a plan under this section moves from one residence to another within the same utility service area;

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(d) Be permitted to disconnect service if the customer fails to honor the payment program. Utilities may continue to disconnect service for those practices authorized by law other than for nonpayment as provided for in this subsection. Customers who qualify for payment plans under this section who default on their payment plans and are disconnected can be reconnected and maintain the protections afforded under this chapter by paying reconnection charges, if any, and by paying all amounts that would have been due and owing under the terms of the applicable payment plan, absent default, on the date on which service is reconnected; and

(e) Advise the customer in writing at the time it disconnects service that it will restore service if the customer contacts the utility and fulfills the other requirements of this section.

(6) A payment plan implemented under this section is consistent with RCW **80.28.080**.

(7) Every gas company and electrical company shall offer residential customers the option of a budget billing or equal payment plan. The budget billing or equal payment plan shall be offered low-income customers eligible under the state's plan for low-income energy assistance prepared in accordance with 42 U.S.C. 8624(C)(1) without limiting availability to certain months of the year, without regard to the length of time the customer has occupied the premises, and without regard to whether the customer is the tenant or owner of the premises occupied.

(8) Every gas company, electrical company, wastewater company, and water company shall construct and maintain such facilities in connection with the manufacture and distribution of its product, or provision of its services, as will be efficient and safe to its employees and the public.

(9) An agreement between the customer and the utility, whether oral or written, does not waive the protections afforded under this chapter.

(10) In establishing rates or charges for water service, water companies as defined in RCW **80.04.010** may consider the achievement of water conservation goals and the discouragement of wasteful water use practices.

[ 2011 c 214 § 11; 2008 c 299 § 35; 1995 c 399 § 211. Prior: 1991 c 347 § 22; 1991 c 165 § 4; 1990 1st ex.s. c 1 § 5; 1986 c 245 § 5; 1985 c 6 § 25; 1984 c 251 § 4; 1961 c 14 § 80.28.010; prior: 1911 c 117 § 26; RRS § 10362.]

#### NOTES:

**Findings—Purpose—Limitation of chapter—Effective date—2011 c 214:** See notes following RCW **80.04.010**.

**Short title—2008 c 299:** See note following RCW **35.105.010**.

**Purposes—1991 c 347:** See note following RCW **90.42.005**.

**Findings—1991 c 165:** See note following RCW **35.21.300**.

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## WAC 480-07-500

### General rate proceedings—Statement of policy.

(1) **Scope of this subpart.** This subpart explains the special requirements for certain rate increase filings by electric, natural gas, pipeline, telecommunications, and water companies, low-level radioactive waste sites, and solid waste collection companies.

(2) **Inconsistencies with subpart A requirements.** If there is any inconsistency between the requirements in subpart B and those in subpart A, the requirements in subpart B control.

(3) **Purpose of special rules.** The special requirements in subpart B are designed to standardize presentations, clarify issues, and speed and simplify processing.

(4) **Summary rejection for failure to comply.** The commission may summarily reject any filing for a general rate proceeding that does not conform to the requirements of subpart B. If the commission summarily rejects a filing for a general rate, it will provide a written statement of its reasons and will provide an opportunity for the case to be refiled in conformance with these rules.

(5) **Less than statutory notice.** The commission may grant requests to alter tariffs on less than statutory notice for good cause shown, in accordance with RCW **80.28.060** and **81.28.050**. A company that seeks to implement general rate proceeding tariff changes on less than statutory notice must include with its filing a complete explanation of the reasons that support such treatment.

[Statutory Authority: RCW **80.01.040** and **80.04.160**. WSR 03-24-028 (General Order R-510, Docket No. A-010648), § 480-07-500, filed 11/24/03, effective 1/1/04.]

## WAC 480-07-505

### General rate proceedings—Definition.

(1) **Rate filings that are considered general rate proceedings.** A general rate proceeding filing is a filing by any regulated company specified in WAC 480-07-500 for an increase in rates that meets any of the following criteria:

(a) The amount requested would increase gross annual revenue of the company from activities regulated by the commission by three percent or more.

(b) Tariffs would be restructured such that the gross revenue provided by any customer class would increase by three percent or more.

(c) The company requests a change in its authorized rate of return on common equity or a change in its capital structure.

(d) The company is a solid waste company regulated under chapter 81.77 RCW, except for filings specified under subsection (3)(a) of this section.

(2) **Rate filings under Title 80 RCW that are not considered general rate proceedings.** The following proceedings are not considered general rate increases even though the revenue requested may exceed three percent of the company's gross annual revenue from Washington regulated operations:

(a) Periodic rate adjustments for electric and natural gas companies that may be authorized by the commission (e.g., power cost adjustments and purchased gas cost adjustments).

(b) Emergency or other short-notice increases caused by disaster or weather-related conditions unexpectedly and substantially increasing a public service company's expense.

(c) Rate increases designed to recover government-imposed increases in costs of doing business such as changes in tax laws or ordinances.

(d) Other increases designed to recover increased expenses arising on short notice and beyond a public service company's control.

(3) **Rate filings under chapter 81.77 RCW that are not considered general rate proceedings.** The following filings are not considered general rate proceedings for solid waste companies regulated under chapter 81.77 RCW even though the request may meet one or more criteria identifying general rate proceedings:

(a) Filings by companies that provide neither traditional residential or commercial solid waste operations. This category includes specialized carriers generally hauling specific waste products for specific customers and carriers providing only on-call or nonscheduled service (i.e., "class C" companies, as defined in WAC 480-70-041).

(b) Disposal fee pass-through charges for drop-box service, provided there are no affiliated interest relationships.

(c) Filings for collection of per-customer pass-through surcharges and taxes imposed by the jurisdictional local government based on the current year customer count either as a specified dollar amount or percentage fee amount.

(d) Filings by existing solid waste companies for the implementation of new solid waste collection programs.

(4) **Commission discretion.** The commission may require that any filing or proposal by a regulated company to increase rates for any customer class, or to restructure rates, is subject to the procedures and protections of subpart B of these rules.

[Statutory Authority: RCW 80.01.040 and 80.04.160. WSR 03-24-028 (General Order R-510, Docket No. A-010648), § 480-07-505, filed 11/24/03, effective 1/1/04.]

## WAC 480-07-510

### General rate proceedings—Electric, natural gas, pipeline, and telecommunications companies.

General rate proceeding filings for electric, natural gas, pipeline, and telecommunications companies must include the information described in this section. The commission may reject a filing that fails to meet these minimum requirements, without prejudice to the company's right to refile its request in conformance with this section. For purposes of this rule, "file with the commission," means filed with the commission's executive secretary under WAC 480-07-140 at the time the company files its general rate case; whereas "serve" or "provide" to commission staff or another party, means delivery to such persons, not filed with the commission.

(1) **Testimony and exhibits.** The company must file with the commission nineteen paper copies of all testimony and exhibits that the company intends to present as its direct case if the filing is suspended and a hearing held, unless the commission preapproves the filing of fewer copies. In addition, the company must provide one electronic copy of all filed material in the format identified in WAC 480-07-140(6). Material that the company has not produced under its direction and control and that is not reasonably available to it in electronic format, such as generally available copyrighted published material, need not be provided in electronic format. The company must serve a copy of the materials filed under this section on public counsel at the time of filing with the commission in any proceeding in which public counsel will appear. The utility must provide an exhibit that includes a results-of-operations statement showing test year actual results and the restating and pro forma adjustments in columnar format supporting its general rate request. The utility must also show each restating and pro forma adjustment and its effect on the results of operations. The testimony must include a written description of each proposed restating and pro forma adjustment describing the reason, theory, and calculation of the adjustment.

(2) **Tariff sheets.** The company must file with the commission and provide to public counsel a copy of the proposed new or revised tariff sheets in legislative format, with strike-through to indicate any material to be deleted or replaced and underlining to indicate any material to be inserted, in paper and electronic format, unless already provided as an exhibit under subsection (1) of this section. The company must also file with the commission copies of any tariff sheets that are referenced by new or amended tariff sheets.

(3) **Work papers and accounting adjustments.**

(a) At the time the company makes its general rate case filing, the company must provide one copy of all supporting work papers of each witness to public counsel and three copies to staff in a format as described in this subsection. Staff and each other party must provide work papers to all other parties within five days after the filing of each subsequent round of testimony filed (e.g., response, rebuttal). If the testimony, exhibits, or work papers refer to a document, including, but not limited to, a report, study, analysis, survey, article or decision, that document must be included as a work paper unless it is a reported court or agency decision, in which case the reporter citation must be provided in the testimony. If a referenced document is voluminous, it need not be provided, but the company must identify clearly the materials that are omitted and their content. Omitted materials must be provided or made available if requested. The following information is required for work papers:

(b) *Organization.* Work papers must be plainly identified and well organized, and must include an index and tabs. All work papers must be cross referenced and include a description of the cross referencing methodology.

(c) *Electronic documents.* Parties must provide all electronic files supporting their witnesses' work papers. The electronic files must be fully functional and include all formulas and linked spreadsheet files. Electronic files that support the exhibits and work papers must be provided using logical file paths, as necessary, by witness, and using identifying file names. A party may file a document with locked, hidden or password protected cells only if necessary to protect the confidentiality of the information within the cells or proprietary information in the document. The party shall designate that portion of the document as

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confidential under RCW **80.04.095**, WAC **480-07-160**, and/or a protective order, and the party shall provide it to any person requesting the password who has signed an appropriate confidentiality agreement.

(d) A detailed portrayal of the development of any capital structure and rate of return proposal and all supporting work papers in the format described in this subsection.

(e) *Restating and pro forma adjustments.* Parties must provide work papers that contain a detailed portrayal of restating actual and pro forma adjustments that the company uses to support its filing or that another party uses to support its litigation position, specifying all relevant assumptions, and including specific references to charts of accounts, financial reports, studies, and all similar records relied on by the company in preparing its filing, and by all parties in preparing their testimony and exhibits. All work papers must include support for, and calculations showing, the derivation of each input number used in the detailed portrayal and for each subsequent level of detail. The derivation of all interstate and multiservice allocation factors must be provided in the work papers.

(i) *Change in methodologies for adjustments.* If a party proposes to calculate an adjustment in a manner different from the method that the commission most recently accepted or authorized for the company, it must also present a work paper demonstrating how the adjustment would be calculated under the methodology previously accepted by the commission, and a brief narrative describing the change. Commission approval of a settlement does not constitute commission acceptance of any underlying methodology unless so specified in the order approving the settlement.

(ii) "Restating actual adjustments" adjust the booked operating results for any defects or infirmities in actual recorded results that can distort test period earnings. Restating actual adjustments are also used to adjust from an as-recorded basis to a basis that is acceptable for rate making. Examples of restating actual adjustments are adjustments to remove prior period amounts, to eliminate below-the-line items that were recorded as operating expenses in error, to adjust from book estimates to actual amounts, and to eliminate or to normalize extraordinary items recorded during the test period.

(iii) "Pro forma adjustments" give effect for the test period to all known and measurable changes that are not offset by other factors. The work papers must identify dollar values and underlying reasons for each proposed pro forma adjustment.

(f) A detailed portrayal of revenue sources during the test year and a parallel portrayal, by source, of changes in revenue produced by the filing, including an explanation of how the changes were derived.

(g) If the public service company has not achieved its authorized rate of return, an explanation of why it has not and what the company is doing to improve its earnings in addition to its request for increased rates.

(h) A representation of the actual rate base and results of operation of the company during the test period, calculated in the manner used by the commission to calculate the company's revenue requirement in the commission's most recent order granting the company a general rate increase.

(i) Supplementation of the annual affiliate and subsidiary transaction reports as provided in rules governing reporting requirements for each industry, as necessary, to include all transactions during the test period. The company is required to identify all transactions that materially affect the proposed rates.

(4) **Summary document.** The company must file with the commission a summary document that briefly states the following information on an annualized basis, if applicable. In presenting the following information, the company must itemize revenues from any temporary, interim, periodic, or other noncontinuing tariffs. The company must include in its rate change percentage and revenue change calculations any revenues from proposed general rate change tariffs that would supersede revenue from noncontinuing tariffs. The summary document must also include:

(a) The date and amount of the latest prior general rate increase authorized by the commission, and the revenue realized from that authorized increase in the test period, based on the company's test period units of revenue.

(b) Total revenues at present rates and at requested rates.

(c) Requested revenue change in percentage, in total, and by major customer class.

(d) Requested revenue change in dollars, in total, and by major customer class.

(e) Requested rate change in dollars, per average customer, by customer class, or other representation, if necessary to depict representative effect of the request. The summary document must

also state the effect of the proposed rate increase in dollars per month on typical residential customers by usage categories.

(f) Most current customer count, by major customer class.

(g) Current authorized overall rate of return and authorized rate of return on common equity.

(h) Requested overall rate of return and requested rate of return on common equity, and the method or methods used to calculate rate of return on common equity.

(i) Requested capital structure.

(j) Requested net operating income.

(k) Requested rate base and method of calculation, or equivalent.

(l) Requested revenue effect of attrition allowance, if any is requested.

(5) **Required service of summary document.** The company must serve the summary document on public counsel and mail the summary document described in subsection (4) of this section to the persons designated below on the same date it files the summary document with the commission:

(a) All intervenors on the commission's master service list for the company's most recent general rate proceeding;

(b) All intervenors on the master service list for any other rate proceeding involving the company during the five years prior to the filing, if the rates established or considered in that proceeding may be affected in the company's proposed general rate filing;

(c) All persons who have informed the company in writing that they wish to be provided with the summary document required under this section. The company must enclose a cover letter stating that the prefiled testimony and exhibits and the accompanying work papers, diskettes, and publications specified in this rule are available from the company on request or stating that they have been provided. This provision does not create a right to notice in persons named to receive the summary.

(6) **Cost studies.** The company must file with the commission any cost studies it performed or relied on to prepare its filing, identify all cost studies conducted in the last five years for any of the company's services, and describe the methodology used in such studies.

(7) **Other.** The company must file with the commission its most recent annual report to shareholders, if any, and any subsequent quarterly reports to shareholders; the most recent FERC Form 1 and FERC Form 2, if applicable; and the company's Form 10K's, Form 10Q's, any prospectuses for any issuances of securities, and quarterly reports to stockholders, if any, for the most recent two years prior to the filing date.

[Statutory Authority: RCW **80.01.040** and **80.04.160**. WSR 08-18-012 (Docket A-072162, General Order R-550), § 480-07-510, filed 8/22/08, effective 9/22/08; WSR 06-16-053 (Docket A-050802, General Order R-536), § 480-07-510, filed 7/27/06, effective 8/27/06; WSR 03-24-028 (General Order R-510, Docket No. A-010648), § 480-07-510, filed 11/24/03, effective 1/1/04.]

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## WAC 480-100-123

### Refusal of service.

(1) An electric utility may refuse requests to provide service to a master meter in a building with permanent occupants when all of the following conditions exist:

- (a) The building or property has more than one dwelling unit;
- (b) The occupants control a significant part of the electricity used in the individual units; and
- (c) It is cost-effective for the occupants to have the utility purchase and install individual meters considering the long-run benefits of measuring and billing each occupant's electric use separately.

(2) The utility may refuse to provide new or additional service if:

- (a) Providing service does not comply with government regulations or the electric industry accepted standards concerning the provision of service;
- (b) In the utility's reasonable judgment, the applicant's or customer's installation of wiring or electrical equipment is considered hazardous or of such a nature that safe and satisfactory service cannot be provided;
- (c) The applicant or customer does not comply with the utility's request that the applicant or customer provide and install protective devices, when the utility, in its reasonable judgment deems such protective devices are necessary to protect the utility's or other customers' properties from theft or damage;
- (d) After reasonable efforts by the responsible party, all necessary rights of way, easements, approvals, and permits have not been secured; or
- (e) The customer is known by the utility to have tampered with or stolen the utility's property, used service through an illegal connection, or fraudulently obtained service and the utility has complied with WAC 480-100-128(2), disconnection of service.

(3) An electric utility may not refuse to provide new or additional service to a residential applicant or residential customer who has a prior obligation. A prior obligation is the dollar amount, excluding deposit amounts owed, the utility has billed to the customer and for which the utility has not received payment at the time the service has been disconnected for nonpayment. The utility must provide service once the customer or applicant has paid all appropriate deposit and reconnection fees. This subsection does not apply to customers that have been disconnected for failure to honor the terms of a winter low-income payment program.

(4) The utility may not refuse to provide service to an applicant or customer because there are outstanding amounts due from a prior customer at the same premises, unless the utility can determine, based on objective evidence, that a fraudulent act is being committed, such that the applicant or customer is acting in cooperation with the prior customer with the intent to avoid payment.

(5) The utility may refuse to provide new or additional service for reasons not expressed in subsections (1) and (2) of this section, upon prior approval of the commission. The commission may grant the request upon determining that the utility has no obligation to provide the requested service under RCW 80.28.110. Prior to seeking commission approval, the utility must work with the applicant or customer requesting service to seek resolution of the issues involved.

(6) Any applicant or customer who has been refused new or additional service may file with the commission an informal complaint under WAC 480-07-910, Informal complaints; or a formal complaint under WAC 480-07-370, Pleadings—General.

[Statutory Authority: RCW 80.01.040 and 80.04.160. WSR 03-24-028 (General Order R-510, Docket No. A-010648), § 480-100-123, filed 11/24/03, effective 1/1/04; WSR 01-24-076 (General Order No. R-495, Docket No. UE-990473), § 480-100-123, filed 12/3/01, effective 1/3/02.]

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## WAC 480-100-128

### Disconnection of service.

(1) **Customer-directed.** The utility may require customers to give at least three days' notice prior to the date service is to be discontinued. The customer is not responsible for usage after the requested date for discontinuance of service, provided the customer gave proper notice. If the customer moves from the service address and fails to request that service be discontinued, the customer will be responsible to pay for service taken at that service address until the utility can confirm either that the customer has vacated the premises and can access the meter or that a new responsible party is taking service.

(2) **Utility-directed without notice or without further notice.** The utility may discontinue service without notice or without further notice when:

(a) After conducting a thorough investigation, the utility determines that the customer has tampered with or stolen the utility's property, has used service through an illegal connection, or has fraudulently obtained service. The utility has the burden of proving that fraud occurred. For the purpose of this section, a nonsufficient funds check or dishonored electronic payment alone will not be considered fraud.

(i) First offense. The utility may disconnect service without notice when it discovers theft, tampering, or fraud, unless the customer immediately pays all of the following:

(A) The tariffed rate for service that the utility estimates was used as a result of the theft, tampering, or fraud;

(B) All utility costs resulting from such theft, tampering, or fraud; and

(C) Any required deposit.

(ii) Second offense. The utility may disconnect service without notice when it discovers further theft, tampering, or fraud. The utility may refuse to reconnect service to a customer who has been twice disconnected for theft, tampering, or fraud, subject to appeal to the commission.

(b) After conducting a thorough investigation, the utility determines that the customer has vacated the premises;

(c) The utility identifies a hazardous condition in the customer's facilities or in the utility's facilities serving the customer;

(d) A customer pays a delinquent account with a check or electronic payment the bank or other financial institution has dishonored after the utility has issued appropriate notice as described in subsection (6) of this section;

(e) The customer has not kept any agreed-upon payment arrangement for payment of a delinquent balance after the utility has issued appropriate notice as described in subsection (6) of this section; or

(f) The utility has determined a customer has used service prior to applying for service. The utility must charge the customer for service used in accordance with the utility's filed tariff.

This section should not be interpreted as relieving the customer or other person of civil or criminal responsibility.

(3) **Utility-directed with notice.** After properly notifying the customer, as explained in subsection (6) of this section, the utility may discontinue service for any one of the following conditions:

(a) For delinquent charges associated with regulated electric service (or for regulated electric and gas service if the utility provides both services), including any required deposit. However, the utility cannot disconnect service when the customer has met the requirements of subsection (5) of this section for medical emergencies, or has agreed to or maintains agreed-upon payment arrangements with the utility, as described in WAC 480-100-143, Winter low-income payment program;

(b) For use of electric service for purposes or properties other than those specified in the customer's service application;

(c) Under flat-rate service for nonmetered load, for increased electric use without the utility's approval;

(d) For refusing to allow the utility's representatives access to the customer's premises as required in WAC 480-100-168, Access to premises; identification;

(e) For violating rules, service agreements, or filed tariff(s); or

(f) For use of equipment that detrimentally affects the utility's service to its other customers.

(4) Electric service may not be disconnected for amounts that may be owed the utility for nonregulated service.

(5) **Medical emergencies.** When the utility has cause to disconnect or has disconnected a residential service, it must postpone disconnection of service or must reinstate service for a grace period of five business days after receiving either verbal or written notification of the existence of a medical emergency. The utility must reinstate service during the same day if the customer contacts the utility prior to the close of the business day and requests a same-day reconnection. Otherwise, the utility must restore service by 12:00 p.m. the next business day. When service is reinstated the utility will not require payment of a reconnection charge and/or deposit prior to reinstating service but must bill all such charges on the customer's next regular bill or on a separate invoice.

(a) The utility may require that the customer, within five business days, submit written certification from a qualified medical professional stating that the disconnection of electric service would aggravate an existing medical condition of a resident of the household. "Qualified medical professional" means a licensed physician, nurse practitioner, or physician's assistant authorized to diagnose and treat the medical condition without supervision of a physician. Nothing in this section precludes a utility from accepting other forms of certification, but the maximum the utility can require is written certification. If the utility requires written certification, it may not require more than the following information:

(i) Residence location;

(ii) An explanation of how the current medical condition will be aggravated by disconnection of service;

(iii) A statement of how long the condition is expected to last; and

(iv) The title, signature, and telephone number of the person certifying the condition;

(b) The medical certification is valid only for the length of time the health endangerment is certified to exist but no longer than sixty days, unless renewed;

(c) A medical emergency does not excuse a customer from having to pay delinquent and ongoing charges. The utility may require the customer to do the following within a five-business-day grace period:

(i) Pay a minimum of ten percent of the delinquent balance;

(ii) Enter into an agreement to pay the remaining delinquent balance within one hundred twenty days; and

(iii) Agree to pay subsequent bills when due.

Nothing in this section precludes the utility from agreeing to an alternate payment plan, but the utility may not require the customer to pay more than this subsection prescribes. The utility must send a notice to the customer confirming the payment arrangements within two business days of having reached the agreement;

(d) If the customer fails to provide an acceptable medical certificate or ten percent of the delinquent balance within the five-business-day grace period, or if the customer fails to abide by the terms of the payment agreement, the utility may not disconnect service without first mailing a written notice providing a disconnection date not earlier than 5:00 p.m. of the third business day after the date of mailing, if mailed from within the states of Washington, Oregon, or Idaho, or the sixth business day, if mailed from outside the states of Washington, Oregon, and Idaho, or by personally delivering a notice providing a disconnection date of not earlier than 5:00 p.m. of the second business day following the date of delivery;

(e) A customer may claim medical emergency and be entitled to the benefits described in this subsection only twice within any one hundred twenty-day period.

(6) **Disconnection notification requirements.** The utility must notify customers before disconnecting their service, except as described in subsection (2) of this section. Notification consists of the following requirements:

(a) The utility must serve a written disconnection notice to the customer either by mail or by personal delivery to the customer's address with notice attached to the primary door. If the disconnection notice is for nonpayment during the winter months, the utility must advise the customer of the payment plan described in WAC 480-100-138, Payment arrangements, and WAC 480-100-143, Winter low-income payment program. Each disconnection notice must include:

(i) A disconnection date that is not less than eight business days after the date of personal delivery or mailing, if mailed from inside the states of Washington, Oregon, or Idaho, or a disconnection date that is not less than eleven business days, if mailed from outside the states of Washington, Oregon, and Idaho.

(ii) All relevant information about the disconnection action including the cause for disconnection; the amount owed for regulated electric service and, if applicable, regulated natural gas service; and how to avoid disconnection;

(iii) All relevant information about any charges that may be assessed; and

(iv) The utility's name, address, and toll-free telephone number by which a customer may contact the utility to discuss the pending disconnection of service;

(b) If the utility discovers the notice information in (a) of this subsection is inaccurate, the utility must issue another notice to the customer as described in subsection (6)(a) of this section;

(c) If the utility has not disconnected service within ten business days of the disconnection date stated in (a)(i) of this subsection, the disconnection notice will be considered void unless the customer and the utility have agreed to a payment arrangement. Upon a void notice, the utility must provide a new disconnection notice to the customer as described in (a) of this subsection;

(d) In addition to the notice required by (a) of this subsection, a second notice must be provided by one of the three options listed below:

(i) Delivered notice. The utility must deliver a second notice to the service premises and attach it to the customer's primary door. The notice must state a scheduled disconnection date that is not earlier than 5:00 p.m. of the second business day after the date of delivery;

(ii) Mailed notice. The utility must mail a second notice which must include a scheduled disconnection date that is not earlier than 5:00 p.m. of the third business day after the date of mailing, if mailed from within the states of Washington, Oregon, or Idaho; or the sixth business day, if mailed from outside the states of Washington, Oregon, and Idaho; or

(iii) Telephone notice. The utility must attempt at least two times to contact the customer during regular business hours. A log or record of the calls must be kept for a minimum of ninety calendar days showing the telephone number called, the time of the call, and details of the results of each attempted call. If the utility is unable to reach the customer by telephone, a written notice must be mailed to the customer providing a disconnection date not earlier than 5:00 p.m. of the third business day after the date of mailing, if mailed from within the states of Washington, Oregon, or Idaho, or the sixth business day, if mailed from outside the states of Washington, Oregon, and Idaho, or written notice must be personally delivered providing a disconnection date of not earlier than 5:00 p.m. of the second business day following the date of delivery.

For utilities billing for electric and gas service, each type of notice listed above must provide the information contained in (a)(iii) of this subsection;

(e) If the utility discovers the written notice information required under the options in (d) of this subsection is inaccurate, the utility must issue another notice to the customer as described in (a) of this subsection;

(f) If the utility provides a second notice within ten business days of the disconnection date required by (a)(i) of this subsection, the disconnection date is extended an additional ten working days from the disconnection date of the second notice. If the utility does not disconnect service within the extended ten-business-day period, the notice will be considered void unless the customer and the utility have agreed upon a payment arrangement. Upon a void notice, the utility must provide an additional notice as required under (d) of this subsection;

(g) If the utility provides a second notice after the ten business days of the disconnection date required by (a)(i) of this subsection, the notice will be considered void unless the customer and the utility have agreed upon a payment arrangement. Upon a void notice, the utility must provide a new disconnection notice to the customer as described in (a) of this subsection;

(h) Utilities with combined accounts for both natural gas and electric service will have the option of choosing which service will be disconnected;

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(i) When the service address is different from the billing address, the utility must determine if the customer of record and the service user are the same party. If not, the utility must notice the service user as described in (a) of this subsection prior to disconnecting service;

(j) Except in case of danger to life or property, the utility may not disconnect service on Saturdays, Sundays, legal holidays, or on any other day on which the utility cannot reestablish service on the same or following day;

(k) A utility representative dispatched to disconnect service must accept payment of a delinquent account at the service address, but will not be required to give change for cash paid in excess of the amount due and owing. The utility must credit any over-payment to the customer's account. The utility may charge a fee for the disconnection visit to the service address if provided for in the utility's tariff;

(l) When service is provided through a master meter, or when the utility has reasonable grounds to believe service is to other than the customer of record, the utility must undertake reasonable efforts to inform the occupants of the service address of the impending disconnection. Upon request of one or more service users, where service is to other than the customer of record, the utility must allow five days past the original disconnection date to permit the service users to arrange for continued service;

(m) Medical facilities. When service is known to be provided to:

(i) A hospital, medical clinic, ambulatory surgery center, renal dialysis facility, chemical dependency residential treatment facility, or other medical care facility licensed or certified by the department of health, a notice of pending disconnection must be provided to the secretary of the department of health and to the customer. The department of health secretary or designee may request to delay the disconnection for five business days past the original disconnection date to allow the department to take the necessary steps to protect the interests of the patients residing at the facility; or

(ii) A nursing home, boarding home, adult family home, group care facility, intermediate care facility for the mentally retarded (ICF/MR), intensive tenant support residential property, chemical dependency residential treatment facility, crisis residential center for children or other group home or residential care facility licensed or certified by the department of social and health services, a notice of pending disconnection must be provided to the secretary of the department of social and health services and to the customer. The department of social and health services secretary or designee may request to delay the disconnection for five business days past the original disconnection date to allow the department to take the necessary steps to protect the interests of the patients residing at the facility;

(n) Any customer may designate a third party to receive a disconnection notice or notice of other matters affecting the customer's service. The utility must offer all customers the opportunity to make such a designation. If the utility believes that a customer is not able to understand the effect of the disconnection, the utility must consider a social agency to be the third party. In either case, the utility must delay service disconnection for five business days past the original disconnection date after issuing a disconnection notice to the third party. The utility must determine which social agencies are appropriate and willing to receive the disconnection notice, the name and/or title of the person able to deal with the disconnection, and provide that information to the customer.

(7) For purposes of this section, the date of mailing a notice will not be considered the first day of the notice period.

**(8) Payments at a payment agency.** Payment of any past-due amounts to a designated payment agency of the utility constitutes payment when the customer informs the utility of the payment and the utility has verified the payment.

**(9) Remedy and appeals.** Service may not be disconnected while the customer is pursuing any remedy or appeal provided by these rules or while engaged in discussions with the utility's representatives or with the commission. Any amounts not in dispute must be paid when due and any conditions posing a danger to health, safety, or property must be corrected. The utility must inform the customer of these provisions when the customer is referred to a utility's supervisor or to the commission.

[Statutory Authority: RCW 80.01.040 and 80.04.160. WSR 01-11-004 (Docket No. UE-990473, General Order No. R-482), § 480-100-128, filed 5/3/01, effective 6/3/01.]

## KC REPLY APPENDIX 247

## **KC REPLY APPENDIX 248**



**Consumer Help Line**  
888-333-WUTC (9882)  
consumer@utc.wa.gov

**TTY**  
800-416-5289

**Education and Outreach**  
360-664-1110

**Media Line**  
360-664-1116

The UTC regulates the services of private or investor-owned utility and transportation companies. Our mission is to ensure that services are fairly priced, available, reliable and safe.

**Regulated companies:**

- Telephone
- Electricity
- Natural Gas
- Water
- Garbage
- Recycling
- Residential Movers
- Charter Buses
- Airport Shuttles
- Commercial Ferries
- Natural Gas Pipeline

**General Information**  
360-664-1160  
www.utc.wa.gov

PO Box 47250  
1300 S Evergreen Pk Dr SW  
Olympia WA 98504

## Rate-making Process

In Washington state, the Utilities and Transportation Commission (UTC) is charged with ensuring private or investor-owned energy, water, telephone and garbage companies are providing services that are fairly priced, reliable and safe. Regulated companies must receive approval from the commission to adjust the rates they charge for service. These formal requests, known as general rate cases, are adjudicated proceedings with a judge, parties, evidence and hearings.

### How do I learn about rate cases?

Companies regulated by the commission must give their customers a minimum of 30 days advance notice for any proposed rate increase. The notice must explain how the company's proposal would affect them and how to comment before the commission takes action.

### How often can a regulated company apply for a rate increase?

There are no restrictions on how often a utility can request a rate increase. However, the company must prove to the commission that it requires additional revenue to provide safe and reliable service.

### What does the commission consider when it reviews rates?

Commission staff look at five main issues:

- The cost to provide service based on 12 months of financial records.
- The company's total investment in equipment to provide service.
- The appropriate profit level the company should be allowed for its investments.
- The appropriate amount that each customer class (i.e., residential, commercial or industrial) should pay.
- The overall rate design. The two primary goals of rate design are to allow rates to match the company's required revenue to run its operations and allocate the costs to the appropriate customer group (i.e., residential, commercial, or industrial). Additional goals for rate design are to minimize complexity, stabilize costs by reducing uncertainty, encourages utilities to minimize costs, encourage conservation, improve affordability for low-income customers, and encourage economic development.

### What happens during a rate case?

- The company submits a request to change rates.
- The new rates become effective unless the commission suspends the filing at a public meeting.

# Ratemaking Process

- If the request is suspended, an administrative law judge holds a prehearing conference. This meeting identifies what groups will actively participate in the case, and sets the schedule for testimony and hearings.
- The company's request is accompanied by supporting documents and written testimony about the request. The parties and commission staff also submit written testimony with their findings.
- The company then files written testimony in response to the parties' testimony.
- All witnesses are made available for cross-examination in a series of hearings that can take from one day to two weeks before the three commissioners.
- Public hearings are held to give customers a chance to comment on the case directly to the commissioners. This information, along with comments submitted to the commission become evidence in the case.
- The final arguments or briefs are presented in writing to the commission.
- The commissioners make a decision and issue a final order.
- Any of the parties to the case may request the commission clarify or reconsider the final decision. Parties may also appeal the commission's decision to Superior Court.

## How do I comment or receive updates on a rate case?

Customers can submit comments on a rate case:

- Online at [www.utc.wa.gov/comments](http://www.utc.wa.gov/comments);
- Call 1-888-333-WUTC (9882);
- Email [comments@utc.wa.gov](mailto:comments@utc.wa.gov); or
- Mail P.O. Box 47250, Olympia, WA 98504-7250. Please include a return address and a description of the filing.

PROOF OF SERVICE

Dawnelle Patterson declares as follows:

1. I am and at all times hereinafter mentioned was a citizen of the United States, a resident of the State of Washington, over the age of 21 years, competent to be a witness in the above action, and not a party thereto.

2. On the 16th day of December, 2016, I caused a true and correct copy of the foregoing document to be delivered to the following in the manner indicated:

Court of Appeals Div. II  
950 Broadway, Suite 300  
Tacoma, WA 98402  
[Coa2filings@courts.wa.gov](mailto:Coa2filings@courts.wa.gov)

Legal messenger  
 E-Filing by Email  
 JIS Portal E-filing  
 U.S. Mail, first-class  
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Juliean Beattie  
Christopher M. Casey  
Krista Gross  
Betsy DeMarco  
Assistant Attorney General  
Utilities and Transportation Division  
Washington Attorney General's Office  
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[jbeattie@utc.wa.gov](mailto:jbeattie@utc.wa.gov)  
[ccasey@utc.wa.gov](mailto:ccasey@utc.wa.gov)  
[KGross@utc.wa.gov](mailto:KGross@utc.wa.gov)  
[BDeMarco@utc.wa.gov](mailto:BDeMarco@utc.wa.gov)

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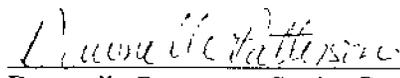
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I declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED December 16, 2016 at Seattle, Washington.

  
\_\_\_\_\_  
Dawnelle Patterson, Senior Practice  
Assistant

**KL GATES LLP**

**December 16, 2016 - 1:52 PM**

**Transmittal Letter**

Document Uploaded: 7-493471-Reply Brief.PDF

Case Name: King County v. Washington Utilities and Transportation Commission, et. al.  
Court of Appeals Case Number: 49347-1

**Is this a Personal Restraint Petition?** Yes  No

**The document being Filed is:**

Designation of Clerk's Papers Supplemental Designation of Clerk's Papers

Statement of Arrangements

Motion: \_\_\_\_\_

Answer/Reply to Motion: \_\_\_\_\_

Brief: Reply

Statement of Additional Authorities

Cost Bill

Objection to Cost Bill

Affidavit

Letter

Copy of Verbatim Report of Proceedings - No. of Volumes: \_\_\_\_\_

Hearing Date(s): \_\_\_\_\_

Personal Restraint Petition (PRP)

Response to Personal Restraint Petition

Reply to Response to Personal Restraint Petition

Petition for Review (PRV)

Other: \_\_\_\_\_

**Comments:**

No Comments were entered.

Sender Name: Kathryn L Jacobson - Email: [dawnelle.patterson@klgates.com](mailto:dawnelle.patterson@klgates.com)

A copy of this document has been emailed to the following addresses:

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