

RECEIVED

DAVID J. MEYER
VICE PRESIDENT AND CHIEF COUNSEL FOR
REGULATORY & GOVERNMENTAL AFFAIRS
AVISTA CORPORATION
P.O. BOX 3727
1411 EAST MISSION AVENUE
SPOKANE, WASHINGTON 99220-3727
TELEPHONE: (509) 495-4316
FACSIMILE: (509) 495-8851
DAVID.MEYER@AVISTACORP.COM

2011 JUL -5 AM 11:44

IDAHO PUBLIC
UTILITIES COMMISSION

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION)
OF AVISTA CORPORATION FOR THE)
AUTHORITY TO INCREASE ITS RATES)
AND CHARGES FOR ELECTRIC AND)
NATURAL GAS SERVICE TO ELECTRIC)
AND NATURAL GAS CUSTOMERS IN THE)
STATE OF IDAHO)

CASE NO. AVU-E-11-01
CASE NO. AVU-G-11-01

DIRECT TESTIMONY
OF
SCOTT L. MORRIS

FOR AVISTA CORPORATION

(ELECTRIC AND NATURAL GAS)

1 I. INTRODUCTION

2 Q. Please state your name, employer and business
3 address.

4 A. My name is Scott L. Morris and I am employed as
5 the Chairman of the Board, President and Chief Executive
6 Officer of Avista Corporation (Company or Avista), at 1411
7 East Mission Avenue, Spokane, Washington.

8 Q. Would you please briefly describe your
9 educational background and professional experience?

10 A. Yes. I am a graduate of Gonzaga University with a
11 Bachelors degree and a Masters degree in organizational
12 leadership. I have also attended the Kidder Peabody School
13 of Financial Management.

14 I joined the Company in 1981 and have served in a
15 number of roles including customer service manager. In
16 1991, I was appointed general manager for Avista Utilities'
17 Oregon and California natural gas utility business. I was
18 appointed President and General Manager of Avista
19 Utilities, an operating division of Avista Corporation, in
20 August 2000. In February 2003, I was appointed Senior
21 Vice-President of Avista Corporation, and in May 2006, I
22 was appointed as President and Chief Operating Officer.
23 Effective January 1, 2008, I assumed the position of
24 Chairman of the Board, President, and Chief Executive
25 Officer.

1 I am a member of the Western Energy Institute board of
2 directors, a member of the Gonzaga University board of
3 trustees, a member of Edison Electric Institute board of
4 directors, a member of the American Gas Association board
5 of directors, a member of ReliOn board of directors, and
6 board director of the Washington Roundtable. On January 1,
7 2011, I was appointed to the Federal Reserve Bank of San
8 Francisco, Seattle Branch board of directors. I also serve
9 on the board of trustees of Greater Spokane Incorporated.

10 **Q. What is the scope of your testimony in this**
11 **proceeding?**

12 A. In my testimony, I will first explain why Avista
13 is requesting another rate increase in this case. I will
14 explain that much of our need for rate relief is driven
15 primarily by the increased costs associated with the need
16 to expand and replace our aging utility infrastructure, and
17 our obligation to reliably serve customers. As a regulated
18 company, we operate under state and federal mandates that
19 obligate us to serve every customer that requests service,
20 and to serve them reliably. Although we continue to make
21 changes to our business to operate more efficiently, it is
22 simply not possible to cut costs enough to offset the
23 increased costs to expand and replace our aging
24 infrastructure to comply with our obligation to serve.

25 My testimony will provide an overview of Avista
26 Corporation. I will also summarize the Company's specific

1 electric and natural gas rate requests in this filing, and
2 the primary factors driving the Company's need for general
3 rate relief. I will also discuss some of the measures we
4 have taken to cut costs, as well as initiatives to increase
5 operating efficiencies in an effort to mitigate future cost
6 increases. I will briefly explain the Company's customer
7 support programs in place to assist our customers, as well
8 as our communications initiatives to help customers better
9 understand the changes in costs that are causing our rates
10 to increase.

11 Finally, I will introduce each of the other witnesses
12 providing testimony on the Company's behalf.

13 A table of contents for my testimony is as follows:

14	<u>Description</u>	<u>Page</u>
15	I. Introduction	1
16	II. Why Is Avista Requesting Another Rate Increase	4
17	III. Overview of Avista	12
18	IV. Summary of Rate Requests	15
19	V. Cost Management and Efficiencies	20
20	VI. Communications with Customers	23
21	VII. Customer Satisfaction	26
22	VIII. Customer Support Programs	27
23	IX. Other Company Witnesses	30

24 **Q. Are you sponsoring any exhibits in this**
25 **proceeding?**

26 A. Yes. I am sponsoring Exhibit 1, pages 1 and 2.
27 Page 1 is a diagram of Avista's corporate structure; and
28 page 2 includes a map showing Avista's electric and natural

1 gas service areas. This exhibit was prepared under my
2 direction.

3 **Q. What are the rate increases requested by Avista**
4 **in this filing?**

5 A. Avista is requesting an overall electric billed
6 rate increase of 3.5%, and a natural gas billed rate
7 increase of 2.8%.

8 **II. WHY IS AVISTA REQUESTING ANOTHER RATE INCREASE**

9 **Q. Why is Avista requesting another rate increase**
10 **following the recent increases that were approved effective**
11 **October 1, 2010?**

12 A. As a regulated monopoly there are two major
13 requirements that are having a significant effect on the
14 need to change retail rates: 1) Avista has an obligation
15 to safely and reliably serve every customer that requests
16 service, and 2) the costs associated with replacing our
17 aging infrastructure are substantial.

18 **Q. How does the "obligation to serve" create a need**
19 **to increase rates?**

20 A. Avista has a legal obligation to provide safe and
21 reliable service to every customer that requests electric
22 or natural gas service from the Company. When a new
23 customer wants service, we must hook them up, even if the
24 cost to serve that customer results in increased costs to
25 all other customers. Likewise, if the facilities serving

1 an existing customer are deteriorating and need repair, we
2 must repair or replace them so that the customer continues
3 to receive safe, reliable service.

4 We occasionally receive comments from some of our
5 customers to the effect that Avista should cut its costs,
6 and "tighten its belt" like other businesses are having to
7 do in these difficult economic circumstances, and keep
8 retail rates the same. We hear those comments and take
9 them to heart, and have taken steps to do so. But at the
10 same time we are not like other businesses. Without the
11 obligation to serve, we could consider refusing to hook up
12 some new customers, because it could avoid an increase in
13 costs to our existing customers. Without an obligation to
14 serve, we could consider no longer serving some of the more
15 remote, more costly areas to provide service, which would
16 allow us to avoid further investment, and reduce labor and
17 other operating costs. Unregulated businesses have the
18 opportunity to shut down aging facilities or under-
19 producing retail outlets, eliminate product lines, and cut
20 back on investment and maintenance. We do not.

21 Please don't misunderstand my point -- we do have
22 opportunities to cut back on investment and operating
23 costs, and we have where prudent to do so. I will address
24 that later in my testimony. But those opportunities are
25 limited by our obligation to safely and reliably serve all

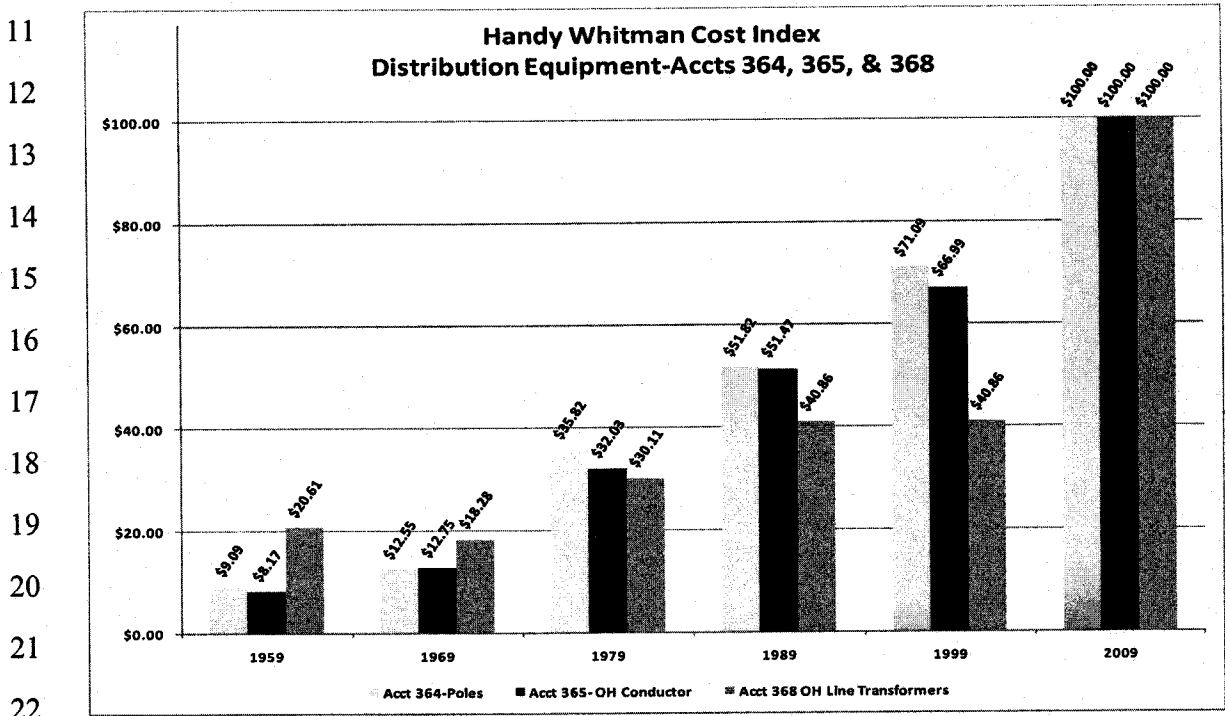
1 customers, and our obligation to comply with numerous
2 mandatory state and federal requirements. We simply don't
3 have the choice to say no to new customers, no to
4 maintaining a safe, reliable system, and no to mandatory
5 requirements. Although we have taken measures to ensure
6 that the costs that we incur represent the most cost-
7 effective and reliable way to continue to serve our
8 customers, we continue to experience significant increases
9 in costs.

10 **Q. How does Avista's need to replace its aging**
11 **infrastructure create a need to change retail rates?**

12 A. Avista's retail rates are cost-based, which means
13 the prices customers are paying now for transformers,
14 distribution poles, substations, and transmission lines,
15 among other facilities, are based on the cost to install
16 those facilities, in some cases, 40, 50, and even 60 years
17 ago. The cost of the same equipment and facilities today
18 are many times more expensive than those facilities
19 installed years ago. In order for us to continue to meet
20 our obligation to provide reliable service, we must replace
21 this aging infrastructure over time. When we replace the
22 old equipment with new, it results in increased costs,
23 which leads to the need to increase rates to cover those
24 costs.

1 Using the Handy-Whitman Index Manual¹, the Company
 2 analyzed several major categories of plant. The following
 3 chart shows what distribution equipment costs have been
 4 historically on a relative scale. For example,
 5 distribution poles fifty years ago would cost 9% of the
 6 current replacement cost. The chart shows that the cost of
 7 the same equipment and facilities that are being added
 8 today are many times more expensive than those facilities
 9 installed in the past.

10 **Illustration No. 1:**



¹ "The Handy-Whitman Index of Public Utility Construction Costs", published by Whitman, Requardt and Associates, Baltimore, Maryland. The Handy-Whitman Indexes of Public Utility Construction Costs show the level of costs for different types of utility construction. Separate indices are maintained for general items of construction, such as reinforced concrete, and specific items of material or equipment, such as pipe or turbo-generators. Handy-Whitman Index numbers are used to trend earlier valuations and original cost at prices prevailing at a certain date.

1 Company witness Mr. DeFelice provides additional
2 details related to the significant increase in the cost of
3 utility materials and equipment in recent years.

4 Q. Can you give a sense for the scope of the
5 investment necessary to replace the utility infrastructure
6 over time?

7 A. Yes. For illustrative purposes, we have over
8 240,000 distribution poles and 34,500 transmission wood and
9 steel poles in our electric system. If, as an example, we
10 were to replace our distribution poles on a fifty-year
11 cycle, it would require us to replace approximately 4,800
12 poles every year. The distribution pole shown below
13 located in Lewiston, Idaho is pre-1940, and the pole has
14 deteriorated to the point where it needs to be replaced.

15 Illustration No. 2:



1 We have many of these on our system and they must be
2 replaced. The replacement of distribution poles represents
3 a fraction of the infrastructure that needs to be replaced
4 each year. In the next five years, our relatively small
5 Company will need to spend approximately \$1.2 billion of
6 capital on utility facilities and other requirements. This
7 \$1.2 billion represents approximately 57% of the current
8 rate base of approximately \$2.1 billion dedicated to
9 serving customers today. Utility equipment and facilities
10 are big and expensive, and the required investment in new
11 facilities is one of the major reasons that we need an
12 increase in retail rates.

13 **Q. Doesn't the level of depreciation each year cover**
14 **the cost to replace these facilities?**

15 A. No. Some of our customers suggest that we set
16 aside dollars every year to replace these facilities over
17 time and we do. That is what depreciation is for. The
18 level of annual depreciation dollars built into retail
19 rates is available to the Company to replace aging
20 facilities over time. However, as I explained above,
21 because the annual depreciation is based on the actual
22 historical costs of our electric system and the cost of
23 those facilities decades ago were orders of magnitude less
24 than what it costs to build facilities today, the annual
25 depreciation falls dramatically short of providing the
26 funds necessary to replace facilities today. Therefore,

1 retail rate increases are necessary to cover the higher
2 costs to replace facilities. As Ms. Andrews explains in
3 her testimony, approximately 90% of our rate increase
4 request is based on new capital investment and the return
5 on investment. Gross plant in service included in this
6 case increased by approximately \$66.2 million (Idaho share)
7 compared to that currently included in rates.

8 **Q. Is the Company experiencing increases in other**
9 **cost categories such as O&M and A&G costs?**

10 A. Yes. A number of expense items have increased
11 since the Company's last general rate case. In particular,
12 the Company pro formed in the increased costs associated
13 with electric distribution vegetation management costs of
14 approximately \$1.3 million, as discussed by Company witness
15 Mr. Kinney. These additive costs are necessary to keep the
16 trees out of our power lines. We are also experiencing
17 increased labor and medical expenses.

18 **Q. Why has it been necessary for Avista to request a**
19 **rate increase each year for a number of years?**

20 A. The current ratemaking process has not allowed
21 costs beyond the next year to be included in rates. In
22 addition, processing a rate request in Idaho can take seven
23 to nine months, which means the only way to recover
24 increasing costs to serve customers is to file a new rate
25 request every year.

1 Since it is simply not possible to cut costs enough
 2 to fully offset other cost increases and the costs
 3 associated with new plant investment, we have no choice but
 4 to request rate increases on a regular basis. Avista is
 5 not alone in that regard; other electric utilities, whether
 6 publicly-owned or investor-owned like Avista, are also
 7 increasing their rates on a more regular basis, and this
 8 will likely continue into the near future.

9 The table below identifies recent rate increases for
 10 utilities in the Pacific Northwest that have either already
 11 occurred, or proposals that are currently pending.

12 **Table No. 1.**

Recent Rate Increase Activity				
Idaho	Fuel	Case Status	Effective Date	Rate Increase
Idaho Power	Electric	Pending	n/a	9.9%
Rocky Mountain Power	Electric	New Rates Approved	06-28-2010	6.8%
Rocky Mountain Power	Electric	Pending	n/a	15.0%
Oregon				
Idaho Power	Electric	New Rates Approved	03-01-2010	15.4%
Pacificorp	Electric	New Rates Approved	02-01-2010	4.4%
Pacificorp	Electric	New Rates Approved	01-01-2011	8.4%
Portland General	Electric	New Rates Approved	01-01-2011	5.9%
Washington				
Benton County PUD	Electric	Pending	n/a	8.0%
Challum County PUD	Electric	New Rates Approved	01-01-2011	8.0%
Clark County PUD	Electric	New Rates Approved	09-01-2010	4.3%
Cowlitz County PUD	Electric	New Rates Approved	01-01-2011	9.0%
Grant County PUD	Electric	New Rates Approved	04-01-2010	4.5%
Okanogan County PUD	Electric	Pending	n/a	6.5%
Pacific Power	Electric	New Rates Approved	01-01-2010	5.3%
Pacific Power	Electric	Pending	04-03-2011	10.7%
Puget Sound Energy	Electric	New Rates Approved	04-07-2010	2.8%
Puget Sound Energy	Electric	Pending	n/a	8.1%*
Puget Sound Energy	Natural Gas	Pending	n/a	3%*
* Filed June 13, 2011 after E Source report				
Source: E Source, June 2011				

1 III. OVERVIEW OF AVISTA

2 Q. Please describe Avista's current business focus
3 for the utility and subsidiary operations.

4 A. Our strategy continues to focus on our energy and
5 utility-related businesses, with our primary emphasis on
6 the electric and natural gas utility business. There are
7 four distinct components to our business focus for the
8 utility, which we have referred to as the four legs of a
9 stool, with each leg representing customers, employees, the
10 communities we serve, and our financial investors. For the
11 stool to be level, each of these legs must be in balance by
12 having the proper emphasis. This means we must maintain a
13 strong utility business by delivering efficient, reliable
14 and high quality service at a reasonable price to our
15 customers and the communities we serve, and provide the
16 opportunity for sustained employment for our employees,
17 while providing a reasonable return to our investors.

18 Q. Please briefly describe Avista's subsidiary
19 businesses.

20 A. Avista Corp.'s primary subsidiary is the
21 information and technology business, Advantage IQ,
22 described below, which is headquartered in Spokane,
23 Washington. A diagram of Avista's corporate structure is
24 provided on page 1 of Exhibit 1.

25 Q. Please provide an overview of Advantage IQ.

1 A. Advantage IQ provides utility expense management
2 and energy management solutions to multi-site companies
3 across North America. Avista currently holds a 75.75% share
4 in Advantage IQ, which is held under Avista Capital.

5 Advantage IQ's invoice processing, auditing and
6 payment services, coupled with energy procurement,
7 comprehensive reporting and advanced analysis, provide the
8 critical data clients need to balance the financial, social
9 and environmental aspects of doing business. Customers
10 include, CSK Auto, Jack in the Box, Staples, and Big Lots,
11 to name a few.

12 As part of the expense management services, Advantage
13 IQ analyzes and audits invoices, then presents consolidated
14 bills on-line, and processes payments. Information gathered
15 from invoices, service providers and other customer-
16 specific data allows Advantage IQ to provide its clients
17 with in-depth analytical support, real-time reporting and
18 consulting services.

19 Advantage IQ also provides comprehensive energy
20 efficiency program management services to utilities across
21 North America. As part of these management services,
22 Advantage IQ helps utilities develop and execute energy
23 efficiency programs with a complete turn-key solution.

24 **Q. Please briefly describe Avista Utilities.**

1 A. Avista Utilities provides electric and natural
2 gas service within a 26,000 square mile area of northern
3 Idaho and eastern Washington². Of the Company's 358,982
4 electric and 319,141 natural gas customers (as of December
5 31, 2010), 122,506 and 74,209, respectively, were Idaho
6 customers. The Company, headquartered in Spokane, also
7 provides natural gas distribution service in southwestern
8 and northeastern Oregon. A map showing Avista's electric
9 and natural gas service areas is provided on page 2 of
10 Exhibit 1.

11 As of December 31, 2010, Avista Utilities had total
12 assets (electric and natural gas) of approximately \$3.9
13 billion (on a system basis), with electric retail revenues
14 of \$683 million (system) and natural gas retail revenues of
15 \$314 million (system). As of December 2010, the Utility
16 had 1,554 full-time employees.

17 Avista has a long history of innovation and
18 environmental stewardship. At the turn of the 20th century,
19 the Company built its first renewable hydroelectric
20 generation plant on the banks of the Spokane River. In the
21 1980's, Avista developed an award-winning biomass plant
22 (Kettle Falls) that generates energy from wood-waste.

² Avista also serves 19 retail electric customers in western Montana.

1 IV. SUMMARY OF RATE REQUESTS

2 Q. Please provide an overview of Avista's electric
3 rate request in this filing.

4 A. Avista is proposing an increase in electric
5 billed retail rates of \$9.0 million or 3.5%. The Company's
6 request is based on a proposed rate of return of 8.49% with
7 a common equity ratio of 50.15% and a 10.9% return on
8 equity.

9 Mr. Ehrbar will provide details related to rate spread
10 and rate design. The proposed rate spread for the increase
11 to each electric customer class is shown in the
12 illustration below.

13 Illustration No. 3:

14 <u>Service Schedule</u>	15 <u>Proposed Increase</u>
16	17 <u>in Billed Revenues</u>
18 Residential Service Schedule 1	3.6%
19 General Service Schedules 11 & 12	3.5%
20 Large General Service Schedules 21 & 22	3.5%
21 Extra Large General Service Schedule 25	3.4%
22 Extra Large General Service Schedule 25P	3.3%
23 Pumping Service Schedules 31 & 32	3.6%
24 Street & Area Lighting Schedules 41-48	3.6%
25 Overall Increase	3.5%
26	

