

Avista Corp.
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IDAHO PUBLIC
UTILITIES COMMISSION

April 2, 2008

Jean D. Jewell
Commission Secretary
Idaho Public Utilities Commission
472 W. Washington Street
Boise, ID 83702

AVU-E-08-01/
AVU-G-08-01

Tariff I.P.U.C. No. 28 (Electric) and Tariff IPUC No. 27 (Natural Gas)

Enclosed for filing with the Commission is an original and nine copies of an Application by Avista Corporation dba Avista Utilities (Avista) dated April 2, 2008 for approval of revised electric and natural gas rates. This filing reflects a general rate increase for both electric and natural gas service in the State of Idaho, to be effective May 5, 2008.

Avista has also included for filing nine copies of its prepared direct testimony, and exhibits in support of its revised rates, as well as three copies of workpapers showing how test year data were adjusted. Computer readable copies of the testimony, exhibits, and workpapers, required under Rule 231.05, are included on the attached compact disc.

Additionally, Avista has included a signed copy of the Protective Agreement between Avista and the Commission Staff, and the Attorney's Certificate and Claim of Confidentiality Relating to Portions of Avista's Direct Testimony and Exhibits.

Sincerely,

A handwritten signature in cursive script that reads "Kelly O. Norwood".

Kelly O. Norwood
Vice President

Enclosures

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IDAHO PUBLIC
UTILITIES COMMISSION

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this 2nd day of April, 2008, served the foregoing application, and Avista's Direct Testimony and Exhibits in Docket No. AVU-E-08-01 and AVU-G-08-01 upon the following parties, by mailing a copy thereof, property addressed with postage prepaid to:

Jean D Jewell, Secretary
Idaho Public Utilities Commission
Statehouse
Boise, ID 83720-5983

Howard Ray
Mill Technical Services Manager
Potlatch Corporation
803 Mill Road
P.O. Box 1126
Lewiston, ID 83501-1126

Scott Woodbury
Deputy Attorney
Idaho Public Utilities Commission
472 W. Washington
Boise, ID 83702-0659



Patty Olsness
Rates Coordinator

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IDAHO PUBLIC UTILITIES COMMISSION

DAVID J. MEYER
VICE PRESIDENT, GENERAL COUNSEL, 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

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)
OF IDAHO)
_____)

CASE NO. AVU-E-08-01
CASE NO. AVU-G-08-01

ATTORNEY'S CERTIFICATE
CLAIM OF
CONFIDENTIALITY
RELATING TO PORTIONS
OF AVISTA'S DIRECT
TESTIMONY AND EXHIBITS

FOR AVISTA CORPORATION

1 I, David J. Meyer, represent Avista Corporation. I am
2 Vice President and General Counsel, Regulatory and
3 Governmental Affairs for Avista Corporation ("Avista" or
4 "Company") and I am appearing on its behalf in this
5 proceeding.

6 I make this certification and claim of confidentiality
7 pursuant to IDAPA 31.01.01 because Avista, through its Direct
8 Testimony, Exhibits and supporting workpapers, is disclosing
9 certain information that is CONFIDENTIAL and constitutes
10 TRADE SECRETS as defined by Idaho Code Section 9-340 and
11 48-801 and protected under IDAPA 31.01.01.067 and
12 31.01.01.233.

13 The printed information Avista provides will, as
14 required under IDAPA Rule 67, be marked as "CONFIDENTIAL,"
15 will be reproduced "on any colored paper other than white,"
16 and will be provided under separate cover. The electronic
17 information Avista provides will be reproduced separately on
18 a compact disk (CD) and will also be marked as CONFIDENTIAL.

19 The confidential information that Avista is disclosing
20 can be classified into three basic categories: 1) information
21 pertaining to contract prices, terms and conditions, 2)
22 certain results providing detailed information on the
23 Company's load and resource positions by month, and 3) Risk

1 Management Policies which contain general policies,
2 guidelines, and position limits.

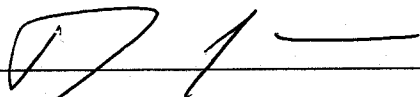
3 Avista herein asserts that the aforementioned
4 information is confidential in that: 1) the contract
5 information is prohibited, by the contract terms, from public
6 disclosure, 2) making the load and resource information
7 public will give entities access to competitive information
8 on future operating plans and market purchase requirements
9 and Avista believes the information could be used to
10 disadvantage its customers, 3) the Risk Management Policies,
11 if shared with competitors, could also be used to disadvantage
12 Avista's customers, and 4) sensitive information concerning
13 pending or threatened litigation would be disclosed.

14 I am of the opinion that this information is
15 "CONFIDENTIAL," as defined by Idaho Code Sections 9-340D and
16 48-801, should therefore be protected from public inspection,
17 examination and copying, and should be utilized only in
18 accordance with the terms of the PROTECTIVE AGREEMENT BETWEEN
19 AVISTA CORPORATION AND IDAHO PUBLIC UTILITIES COMMISSION
20 STAFF.

21 RESPECTFULLY SUBMITTED this 2nd day of April, 2008

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David J. Meyer
Vice President, General Counsel,
Regulatory & Governmental Affairs
Avista Corporation

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DAVID J. MEYER
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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-08-01
CASE NO. AVU-G-08-01

APPLICATION OF AVISTA CORPORATION

(ELECTRIC AND NATURAL GAS)

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Kelly Norwood
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II.

Avista is a public utility primarily engaged in the generation, transmission and distribution of electric power and the distribution of natural gas in certain portions of eastern and central Washington, northern Idaho, as well as distribution of natural gas in northeast and southwest Oregon. The Company is subject to the jurisdiction of this Commission, the Washington Utilities and Transportation Commission, the Oregon Public Utility Commission, the Montana Public Service Commission and the Federal Energy Regulatory Commission.

III.

Applicant's existing base rates and charges for electric service were approved as a result of the Commission's Order No. 29602 dated October 8, 2004, in Case No. AVU-E-04-01 that were later adjusted to include the second half of Coyote Springs 2 generating plant in Case No, AVU-E-05-1. The existing rates and charges for electric service on file with the Commission

1 designated as Applicant's Tariff No. 28 are incorporated herein
2 as though fully attached hereto.

3 **IV.**

4 Applicant's existing base rates and charges for natural
5 gas service were approved as a result of the Commission's Order
6 No. 29602 dated October 8, 2004, in Case No. AVU-G-04-01. The
7 existing rates and charges for natural gas service on file with
8 the Commission designated as Applicant's Tariff No. 27 are
9 incorporated herein as though fully attached hereto.

10 **V.**

11 The electric and natural gas rates and charges which
12 Applicant desires to have the Commission approve are filed
13 herewith as Exhibit A. Also included in Exhibit A are copies
14 of the tariff schedules showing the proposed changes by
15 striking over the existing rates and underlining the proposed
16 rates. Company witness Mr. Hirschhorn fully describes in his
17 testimony and exhibits the proposed changes herein.

18 **VI.**

19 The circumstances and conditions relied upon and
20 justification for approval of the proposed increase in rates
21 for electric and natural gas service are as follows:

22 Applicant's present electric and natural gas rates will
23 not produce sufficient revenue to provide operating income
24 required to allow the Applicant the opportunity to earn the

1 8.74% rate of return being requested and supported in this
2 Application.

3 The Applicant's last electric and natural gas general rate
4 case (Case Nos. AVU-E-04-01 and AVU-G-04-01) in Idaho was
5 effective in September 2004². The proposed revenue increases
6 are driven primarily by increased power supply costs, capital
7 investments in upgrading aging infrastructure to increase
8 capacity and reliability, relicensing costs for Avista's
9 Spokane River hydropower projects, its investment in Advanced
10 Meter Reading (AMR), and expanding the natural gas storage and
11 delivery capacity at its Jackson Prairie Storage Facility.

12 Unless the increased rates as requested in this filing are
13 approved, Applicant's rates will not be fair, just and
14 reasonable and it will not have the opportunity to realize a
15 fair rate of return on its investment.

16 Applicant's evidence in support of its need for increased
17 electric and natural gas rates is based on a 2007 test year.
18 Applicant's rate base evidence is presented on an average
19 basis. Documentation showing how the test year data was
20 adjusted is provided in the testimony and exhibits of Company
21 witness Elizabeth Andrews.

22

² An additional rate adjustment related to the Coyote Springs 2 generating project was implemented April 12, 2005 (AVU-E-05-01).

1 Applicant provides utility service in states other than
2 Idaho. A jurisdictional separation of all investments,
3 revenues and expenses allocated or assigned in whole or in part
4 to the Idaho utility business regulated by this Commission are
5 described in the testimony and exhibits of Company witness
6 Elizabeth Andrews.

7 **VII.**

8 Applicant's evidence will show that an overall rate of
9 return of 8.74% is fair, just and reasonable. The Company's
10 exhibits and testimony support an increase in retail electric
11 and natural gas revenue of \$32.3 million and \$4.7 million
12 respectively. Simultaneous with the filing of this
13 Application, Applicant has filed its prepared direct
14 testimony, and exhibits in support of its revised rates, as well
15 as workpapers showing how test year data were adjusted.

16 **VIII.**

17 A complete justification of the proposed increases in
18 electric and natural gas rates are provided in the testimony
19 and exhibits of Company witnesses. The testimony and exhibits,
20 among other studies and justification, show financial
21 information, costs of capital and appropriate cost of service
22 studies. These witnesses and a brief summary of their testimony
23 is as follows.
24

1 Mr. Scott L. Morris, Chairman, President, and Chief
2 Executive Officer of Avista Utilities, presents the Company's
3 policy testimony and describes Avista Corporation and Avista
4 Utilities' overall utility operations. He summarizes the
5 Company's request in this filing, the major factors driving the
6 Company's need for general rate relief, and some of the current
7 and future challenges being addressed by the Company. Finally
8 Mr. Morris introduces other witnesses providing testimony on
9 the Company's behalf. Mr. Morris explains that:

- 10 • The proposed revenue increases are driven primarily
11 by capital investments in upgrading aging
12 infrastructure to increase capacity and
13 reliability, relicensing costs for Avista's Spokane
14 River hydropower projects, and expanding the natural
15 gas storage and delivery capacity at its Jackson
16 Prairie Storage Facility.
17
- 18 • Among the capital investments included in the filing
19 are upgrades to the company's Noxon Rapids
20 hydroelectric project to gain additional renewable
21 generation capacity, as well transmission upgrades
22 added over 100 circuit miles of new 230 kV
23 transmission line to Avista's system, and increased
24 the capacity of an additional 50 miles of
25 transmission line.
26
- 27 • Costs incurred in the seven-year public process to
28 relicense five of Avista's six hydroelectric
29 projects on the Spokane River. The projects annually
30 generate a combined 105 average megawatts of
31 renewable energy. Avista generates about 57 percent
32 of its electricity with renewable resources,
33 including hydropower. To date, Avista has invested
34 \$21 million in the Spokane River relicensing
35 process.
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- 37 • Driving the natural gas rate request is Avista's
38 investment in the expansion of storage and delivery
39 capacity of its Jackson Prairie Natural Gas Storage
40 Facility. The ability to deliver more lower-priced

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natural gas lessens the need to purchase higher priced spot gas in winter to meet customer demand, an important component in managing customer costs.

- In addition to working diligently to gain efficiencies and control the cost of providing energy service, Avista continues to provide a number of energy assistance programs to aid customers who are most affected by rising energy costs. These include Project Share, CARES, Senior Energy Outreach and energy efficiency workshops.
- Avista's energy efficiency programs offer 34 residential and commercial programs that deliver more than 300 efficiency measures. In 2007, Avista provided \$9.4 million in incentives to customers making energy efficiency improvements to their home or business in an effort to reduce energy usage. Program information is available at www.everylittlebit.com.

Mr. Malyn Malquist, Executive Vice President and Chief Financial Officer will describe, among other things, the overall financial condition of the Company, its current credit ratings, the Company's plan for improving its financial health, its near term capital requirements, the proposed capital structure, and the overall rate of return proposed by the Company. Mr. Malquist explains that:

- Avista's plans call for significant capital expenditure requirements for the utility over the next three to five years to assure reliability in our energy systems, and to keep pace with regional growth and customer demand. Capital expenditures are planned for 2008-2009 of approximately \$390 million for customer growth, investment in generation, transmission and distribution facilities for the electric utility business as well as necessary maintenance and replacements of our natural gas utility systems. Avista needs adequate cash

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flow from operations to fund these requirements.

- Avista's corporate rating from Standard & Poor's is currently BBB-. Avista Utilities should operate at a level that will support a strong investment grade credit rating, meaning at least a strong "BBB" or weak "A". The Company's financial performance has improved; however, we have not improved financial ratios to a level that would result in a strong investment grade credit rating.
- We have made solid progress in improving our financial health by improving our cash flow, managing our costs and paying down debt and refinancing debt at lower rates. The Company plans to issue up to \$350 million of secured, fixed rate bonds during 2008 to fund existing debt maturities as well as to repay funds borrowed under our credit facility. Further, the Company plans to obtain a portion of our capital requirements through equity issuance.

The Company has proposed an overall rate of return of 8.74% including a 47.94% equity ratio and an 10.8% return on equity.

Dr. William E. Avera, as a President of Financial Concepts and Applications (FINCAP), Inc., has been retained to present testimony with respect to the Company's cost of common equity. He concludes that:

- Applications of quantitative methods to alternative groups of proxy companies imply a cost of equity range of 10.7 percent to 12.2 percent.
- Because Avista's requested ROE of 10.8% percent falls at the lower end of the recommended range, it represents a conservative estimate of investors' required rate of return.
- Considering investors' expectations for capital markets and the need to support financial integrity and fund crucial capital investment even under

- 1 adverse circumstances, 10.8% percent is a reasonable
2 ROE for Avista.
- 3 • Because of Avista's reliance on hydroelectric
4 generation, the Company is exposed to relatively
5 greater risks of power cost volatility.
 - 6 • Investors view the Power Cost Adjustment ("PCA") as
7 supportive of the Company's financial integrity, but
8 they understand that the PCA does not insulate Avista
9 from the need to finance accrued power production and
10 supply costs or shield the Company from potential
11 regulatory disallowances.
 - 12 • Avista's requested capitalization is consistent with
13 the Company's need to strengthen its credit standing
14 and financial flexibility as it seeks to raise
15 additional capital to fund significant system
16 investments and meet the requirements of its service
17 territory.
 - 18 • The reasonableness of a minimum 10.8% percent ROE for
19 Avista is also supported by the greater risks
20 associated with the Company's relatively small size
21 and the need to consider flotation costs.

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24 Mr. Dennis Vermillion, Vice President of Energy Resources,
25 will provide an overview of Avista's resource planning and power
26 operations. He will discuss the Company's resources, current and
27 future load and resource position, and future resource plans.
28 He will also discuss Company hydroelectric upgrades, the Montana
29 riverbed lease agreement, current hydro relicensing issues,
30 mercury abatement at Colstrip, and Jackson Prairie storage. Mr.
31 Vermillion explains:

- 32 • Avista's electric generation portfolio, including
33 power supply operations.
- 34 • The Company is in an annually balanced-to-surplus
35 energy position through 2017 with the addition of
36 Lancaster, with the Company's net resource position
37 becoming deficient in 2018.
- 38 • The Company's decision to join the Chicago Climate
39 Exchange.

- 1 • Avista's risk management policy for energy resources,
2 including the electric hedging plan.
3

4 Mr. Clint Kalich, Manager of Resource Planning & Power
5 Supply Analyses, will describe the Company's AURORA_{XMP} model
6 (Dispatch Model) inputs, assumptions, and results related to the
7 economic dispatch of Avista's resources to serve load
8 requirements, and market forecast of electricity prices. He
9 explains:

- 10 • The key assumptions driving the Dispatch Model's
11 market forecast of electricity prices. This
12 discussion includes the variables of natural gas,
13 Western Interconnect loads and resources, and
14 hydroelectric conditions.
15 • The model dispatches Avista's resources and contracts
16 in a manner that maximizes benefits to customers.
17 • The use of quantitative rate-period loads for 2009,
18 for modeling pro forma net power supply expenses.
19 • The output results from the model, including thermal
20 generation and short-term wholesale sales and
21 purchases, were provided to Mr. Johnson to
22 incorporate into the power supply pro forma
23 adjustments.
24 • The inclusion of a "rate mitigation adjustment" in the
25 Company's AURORA_{XMP} model, reducing power supply
26 expenses and therefore reducing the overall rate
27 impact to customers.
28

29 Mr. William Johnson, Wholesale Marketing Manager, will
30 identify and explain the proposed normalizing and pro forma
31 adjustments to the 2007 test period power supply revenues and
32 expenses. He will also explain the new base level of power supply
33 costs for Power Cost Adjustment (PCA) calculation purposes using
34 the pro forma costs proposed by the Company in this filing. Mr.
35 Johnson describes:

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- The adjustment of revenues and expenses based on normal stream flow and weather conditions, and expected wholesale market power prices.
- Adjustments made to reflect known and measurable changes in power contracts, thermal generation fuel expense, and transmission expense, between the 2007 test period, and the pro forma period of 2009.
- The net effect of the adjustments to the 2007-test period power supply expense is an increase of \$971,000 on a system basis.
- The significant increase in power supply expense over the expense currently in base rates is based on numerous factors, including higher retail loads, reduced hydro generation, increased fuel costs, increased Mid-Columbia purchases costs, and increased transmission expense.

Mr. Bruce Howard, Director of Environmental Affairs, will provide an overview of the Spokane River relicensing, including an overview of the Spokane River projects, and the main areas of contention in the process. Finally, Mr. Howard will discuss the costs that have been included in this case.

Ms. Toni Pessemier, Advisor to the Office of the President, will provide testimony regarding other hydro relicensing and compliance issues.

Mr. Don Kopczynski, Vice President of Transmission and Distribution Operations, will describe Avista's electric and natural gas energy delivery facilities and operations, and recent efforts to increase efficiency and improve customer service. Mr. Kopczynski describes:

- 1 • Avista's customer service programs such as energy
2 efficiency, Project Share, CARES program, Senior
3 Outreach Program, and payment plans. Some of these
4 programs will serve to mitigate the impact on
5 customers of the proposed rate increase.
6 • The Company's multi-faceted effort to increase
7 customer service automation, including replacement
8 and upgrade of the new Interactive Voice Response
9 (IVR) system, Mobile Dispatch, Outage Management
10 System and Web Redesign.
11 • The decision by the Company to outsource our bill
12 printing and mailing services. This decision was
13 based on Company needs for disaster recover, added
14 scalability and flexibility, and cost savings.
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16 Mr. Scott Kinney, Chief Engineer, System Operations, will
17 discuss Avista's nearly completed five-year transmission
18 upgrade project, the additional electric transmission and
19 distribution investments included in this case, and presents the
20 Company's pro forma period transmission revenues and expenses.
21 In addition, he describes the Company's Asset Management
22 Program. Mr. Kinney explains:

- 23 • Avista is expecting to invest over \$12.1 million
24 (system) in electric transmission projects with
25 completion dates in 2008.
26 • Several revisions have been made to transmission
27 expenses for the 2009 pro forma period.
28 • Changes in replacement and maintenance costs
29 associated with the Company's asset management.
30 • The near completion of the five-year transmission
31 upgrade projects at a total cost of \$136.4 million.
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33 Mr. Dave DeFelice, Senior Business Analyst, will describe
34 the pro forma adjustments for non-revenue capital expenditures.
35 Mr. DeFelice explains:

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- The rising cost of essential materials specific to the utility industry is causing significant increases in capital project funding requirements.
- These costs must be pro formed into historical test-year computations in order to allow necessary recovery of our costs to serve customers.

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Mr. Greg Paulson, Manager of Customer Service, Analytics and Technology, will discuss the implementation of Advanced Meter Reading for Avista's customers in the State of Idaho, and our request for recovery of capital expenditures related to its deployment. Mr. Paulson explains:

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- The history of the AMR project in Idaho, including an overview of the system, the technologies deployed in the Company's electric and natural gas meters, and the types of technologies used in areas with high and low meter densities.
- A discussion around AMR and AMI, Advanced Metering Infrastructure, which is a newer technology that could provide further functionality for utilities, but which is still in the very early stages of development.
- An overview of the benefits the Company has realized from the deployment of AMR, including safety of our customers and employees, elimination of the need for estimated reads, reduction in the volume of phone calls associated with estimated reads, and more accurate customer billing.
- The Company will have invested approximately \$28.8 million from 2005 through 2008 on this project in Idaho.

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Ms. Elizabeth Andrews, Manager of Revenue Requirements, will discuss the Company's overall revenue requirement proposals. In addition, her testimony generally provides accounting and financial data in support of the Company's need for the proposed increase in rates. She sponsors:

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- Electric and natural gas revenue requirement calculations.
- Electric and natural gas results of operations.
- Pro forma operating results including expense and rate base adjustments.
- System and jurisdictional allocations.

8 Ms. Tara Knox, Senior Regulatory Analyst, sponsors the cost
9 of service studies for electric and natural gas service, the
10 revenue normalization adjustments to results of operations, and
11 the proposed production property adjustment. Ms. Knox studies
12 indicate:

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- Electric residential service, extra large general service and street and area lighting service schedules are earning less than the overall rate of return under present rates, while general service, large general service and pumping service schedules are earning more than the overall rate of return under present rates. However, all customer groups are currently providing a rate of return lower than the rate of return requested in this case.
- Natural Gas high load factor large firm service and interruptible schedules are earning considerably less than the overall rate of return at present rates, the transportation service schedule is earning substantially more than the overall rate of return, while small firm schedules are also above unity but below the requested return and residential service is slightly below unity.

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Mr. Brian Hirschhorn, Manager of Pricing, discusses the
spread of the proposed annual revenue changes among the
Company's general service schedules. He explains, among other
things, that:

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- The proposed electric annual revenue increase is \$32.3 million, or 15.8%.

