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UTILITIES COMMISSION

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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-09-01
CASE NO. AVU-G-09-01

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 briefly describe your educational
9 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 Utilities,
19 an operating division of Avista Corporation, in August 2000.
20 In February 2003, I was appointed Senior Vice-President of
21 Avista Corporation, and in May 2006, I was appointed as
22 President and Chief Operating Officer. Effective January 1,
23 2008, I assumed the position of Chairman of the Board,
24 President, and Chief Executive Officer.

25 I am a member of the Western Energy Institute board of
26 directors, a member of the Gonzaga University board of

1 trustees, a member of Edison Electric Institute board of
2 directors, a member of the American Gas Association board of
3 directors, a member of ReliOn board of directors, and board
4 director of the Washington Roundtable. I also serve on the
5 board of trustees of the Greater Spokane Incorporated, which
6 was formerly two separate organizations, the Spokane Area
7 Economic Development Council and the Spokane Regional
8 Chamber of Commerce.

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

11 A. I will provide an overview of Avista Corporation
12 and Avista Utilities. I summarize the Company's rate
13 requests in this filing, and the primary factors driving the
14 Company's need for general rate relief. I will provide an
15 overview of some of the initiatives that we have undertaken
16 in recent years to achieve operating efficiencies in an
17 effort to mitigate a portion of the increase in costs that
18 Avista, as well as other utilities in the industry are
19 experiencing. I will also briefly explain the Company's
20 customer support programs that are in place to assist our
21 customers. Finally, I will introduce each of the other
22 witnesses providing testimony on the Company's behalf.

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

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12
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14
15 **Q. Are you sponsoring any exhibits in this**
16 **proceeding?**

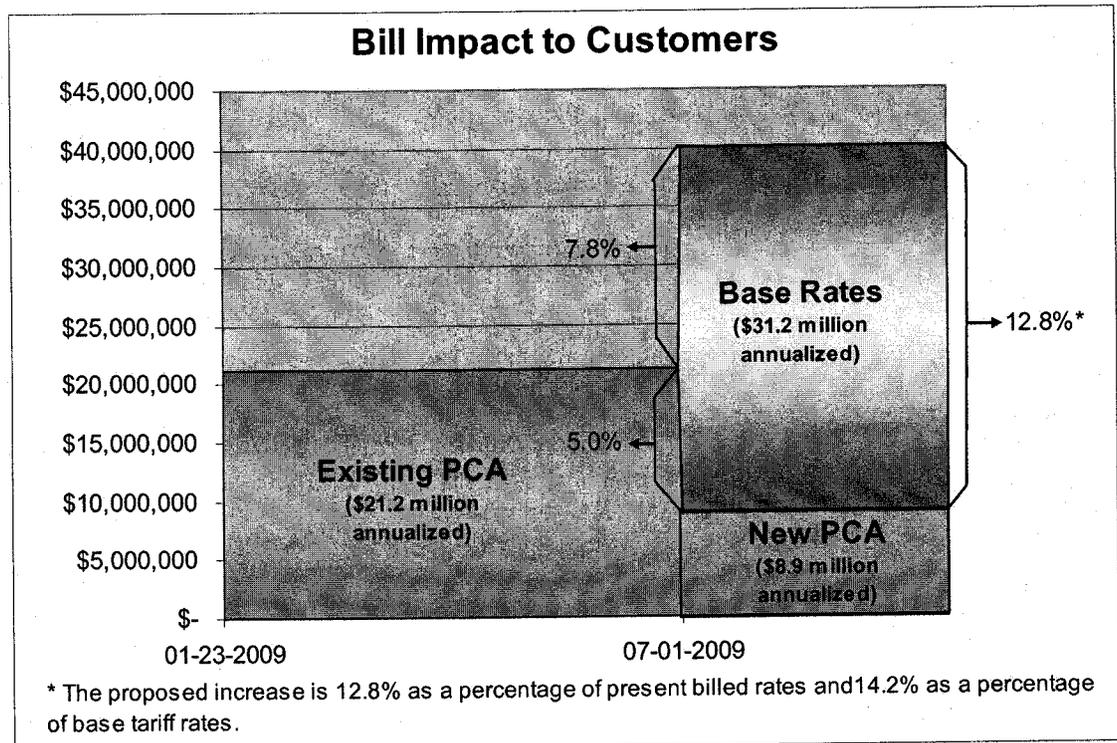
17 A. Yes. I am sponsoring Exhibit No. 1 Schedule 1,
18 pages 1 through 2. Page 1 is a diagram of Avista's
19 corporate structure; and page 2 includes a map showing
20 Avista's electric and natural gas service areas. These
21 exhibits were prepared under my direction.

22 **Q. Please summarize the proposed changes in retail**
23 **rates in this filing.**

24 A. In this filing Avista is proposing a net increase
25 in electric retail rates of 7.8%. The proposal consists of
26 an increase in electric base retail rates of \$31.2 million
27 or 12.8%, and a reduction in the current Power Cost
28 Adjustment (PCA) surcharge of 5.0%. We are proposing that
29 the reduction in the PCA surcharge become effective
30 coincident with the effective date of new retail rates from
31 this general rate case filing.

1 Company witness Mr. Hirschhorn's testimony discusses this
 2 change in the PCA surcharge. Therefore, the proposed
 3 electric bill increase to customers from this filing is a
 4 net increase of 7.8%. The proposed natural gas increase in
 5 the filing is \$ 2.74 million, or 3.0%. The following
 6 illustrates how the estimated electric net increase was
 7 derived.

8
 9 **Illustration No. 1:**



1 **II. COST DRIVERS FOR AVISTA**

2 **Q. Why is Avista proposing another electric revenue**
3 **increase following the recent general rate request?**

4 A. This case is about more than just year-over-year
5 changes in utility operating costs, such as power costs,
6 fuel, materials and supplies, and labor. We are also
7 investing large amounts of capital to preserve and upgrade
8 our existing utility infrastructure to meet growing
9 customer demand. We are also continuing to experience major
10 cost impacts related to meeting new reliability standards,
11 environmental compliance, and litigation related to the
12 preservation of what have historically been our low-cost
13 resources we have used for decades to serve our customers.
14 Several examples of significant cost increases are as
15 follows:

- 16
- 17 1. **Compensation to the Coeur d' Alene Tribe (Tribe):**
18 The recently announced Settlement Agreement among the
19 Tribe, Avista, and the U.S. Department of Interior,
20 provides compensation to the Tribe related to their
21 ownership of the Southern one-third of Lake Coeur d'
22 Alene (CDA). Although these costs were reviewed in
23 the prior general rate case, they were deferred for
24 future recovery in a subsequent rate case and are
25 included in the current filing. The annual cost to
26 Idaho customers from this Agreement is \$1.5 million,
27 or a 0.7% increase in base retail rates.
- 28
- 29 2. **Spokane River Relicensing:** The resolution of issues
30 with the CDA Tribe helps clear the way for the Federal
31 Energy Regulatory Commission (FERC) to issue a new
32 license for the Post Falls Hydroelectric Project in
33 the State of Idaho. There is, however, one remaining
34 issue for the Projects in the State of Washington
35 related to water quality. We expect this issue to be

1 resolved in the first half of 2009 and a new license
2 to be issued. The majority of the relicensing costs
3 were reviewed in the prior general rate case filing,
4 but were deferred for later recovery in this filing.
5 The annual cost to Idaho customers from relicensing
6 the Spokane River Projects is \$3.8 million, or a 1.7%
7 increase in base retail rates.
8
9

10 3. **Mitigation of Mercury and Thermal O&M Cost Increases:**

11 During 2009, the Colstrip owners, including Avista,
12 will begin to incur significant costs to comply with
13 new Mercury emissions laws in the State of Montana.
14 Avista is also experiencing a significant increase in
15 O&M at its thermal plants, due in part to the rapid
16 increase in the cost of materials and the age of the
17 plants. The increase in annual costs is \$1.6 million,
18 or a 0.7% increase in base retail rates.
19

20 4. **Increase in Power Supply Costs:** In our last rate case
21 we included a "rate mitigation adjustment" such that
22 the full increase in power supply costs was not
23 included in retail rates resulting from that case.
24 This case reflects the total power supply costs to
25 serve customers' loads. The increase in costs is also
26 driven by, among other things, the expiration of low-
27 cost Mid-Columbia contracts, and an increase in retail
28 loads. Although the economy has slowed, the growth of
29 energy demands by customers continues to climb, we
30 believe due in part to a continuing increase in
31 televisions, computers, cell phone chargers, and other
32 consumer electronics in customers' homes. The
33 increase in annual power supply costs is \$8.6 million,
34 or a 3.9% increase in base retail rates.
35

36 5. **Investment in Facilities to Serve Customers:** As other
37 witnesses will explain in more detail, we are
38 continuing to invest significant dollars in utility
39 infrastructure. The investment is necessary to serve
40 new customers, upgrade aging facilities - some of
41 which are over 70 years old - and meet recently-
42 enacted reliability requirements for our energy
43 delivery facilities. Although in recent months the
44 rapid increase in the cost of materials (concrete,
45 copper, steel, etc.) has abated, such costs are still
46 orders of magnitude higher than what they were even a
47 few years ago. New investment reflected in this
48 filing results in an increase in annual costs to
49 customers of \$3.1 million, or a 1.4% increase in base
50 retail rates.
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These items alone total \$18.6 million, representing an increased revenue requirement of 8.4% for the Idaho jurisdiction, prior to even addressing other utility ownership and operating costs.

In a November 2008 report prepared by the Brattle Group for The Edison Foundation, "Transforming America's Power Industry: The Investment Challenge 2010-2030." It states, at page v:

The U.S. electric utility industry is facing the greatest challenge in its history. The demand for electric service is increasing, reserve margins are shrinking and input costs to build infrastructure for all types of electricity production are soaring. Global climate change and other environmental issues are directing the industry toward greater development and use of energy efficiency products and services and low-emissions supply sources, all of which come with costs.

We are a low-cost utility in the midst of a high-cost environment: high cost of materials for utility infrastructure, high fuel and purchased power costs, high cost of compliance with environmental and reliability requirements, and, recently, high costs to settle long-standing litigation (CDA Tribe/Relicensing and Montana Riverbed litigation). This is all in the face of increased demands for service by our customers - and we need to meet those needs by providing safe, reliable and efficient service.

1 **III. COST MANAGEMENT AND EFFICIENCIES**

2 **Q. What is Avista doing to mitigate the impact of**
3 **increased costs on its customers?**

4 A. We recognized that these increases in costs will
5 result in electric bills that will be more difficult for
6 some of our customers to pay. I can assure you that we are
7 not just sitting on the sidelines as our costs go up.

8 I will explain a number of cost-cutting and efficiency
9 measures that we have undertaken recently in an effort to
10 mitigate the overall cost impacts to our customers. In
11 addition, we have a history of making it a priority within
12 our Company to maintain meaningful programs to assist our
13 customers that are least able to pay their energy bills,
14 including working cooperatively with our local community
15 action agencies.

16 We will continue to aggressively manage costs to
17 achieve the appropriate balance in providing safe and
18 reliable service at cost-effective rates, and a high level
19 of customer satisfaction, while preserving the financial
20 health of the utility.

21 **Q. What measures has the Company taken?**

22 A. The measures below are among some of the actions
23 we have taken to mitigate the impact of increased costs on
24 our customers:

- 25 1. **Delayed the Reardan Wind Project.** We have recently
26 delayed the construction of the \$125+ million Reardan

- 1 Wind Project to 2013, due, in part, to the current high
2 cost of wind turbines and other materials.
3
- 4 2. **Cancelled Ross Court Office Space.** Avista's main
5 office building was constructed in 1958, and expanded
6 in 1978. Even though Avista's ratio of the number of
7 customers served per employee continues to increase, we
8 have needed additional office space for some time. In
9 2008, in order to reduce costs, we cancelled plans to
10 build additional office space adjacent to the main
11 office, and instead chose to remodel existing space
12 formerly used by Horizon Credit Union nine miles from
13 the main office.
14
- 15 3. **Outsourced Billing and Disaster Recovery.** Avista
16 recently outsourced its bill printing and mailing
17 services, and at the same time complying with
18 requirements related to disaster-recovery for billing
19 data. The objectives were to move bill printing,
20 inserting and mailing offsite and leverage core
21 competencies of the provider, to obtain disaster
22 recovery and avoid the cost of duplicate data storage,
23 ensure daily print volume flexibility, and reduce costs
24 for bill printing, inserting and mailing.
25
- 26 4. **Additional On-line Service Offerings.** In January 2008
27 the Company completed the redesign of
28 www.avistautilities.com. The primary objectives of
29 this project were to lower costs and enhance customer
30 satisfaction through the deployment of additional self-
31 service options, such as open/close/move, reporting and
32 making payment arrangements, enrolling in Comfort Level
33 Billing, and/or Automatic Payment Service (APS).
34 Customers also have access to tools to help analyze
35 their bills and are provided with meaningful
36 information to make informed energy management choices.
37 The cost-saving objective is to achieve a 10% reduction
38 in the Company's Contact Center total call volume,
39 which results in lower staffing and lower costs to
40 customers.
41
42

43 **Q. Are these the only measures the Company has taken**
44 **recently to mitigate increased costs?**

45 A. No. Avista is constantly looking for
46 improvements in the way it provides services to its
47 customers, as well as ways to reduce the costs of those

1 services. Ideas are generated through periodic evaluation
2 of its operating practices, and communications with other
3 utilities, and other industry participants, across the
4 country on best practices. While a later witness, Don
5 Kopczynski, will explore cost-saving initiatives in more
6 detail, I would like to highlight a few:

- 7
8 1. **Mobile Dispatch.** The Mobile Dispatch Project achieved
9 a number of financial and customer service benefits,
10 including increased productivity, enhanced customer
11 service, reduced costs, and improved field safety.
12 This project uses wireless communications between the
13 home office and laptop computer in service trucks to
14 dispatch field crews. These capabilities allow for
15 efficient order dispatch, enhanced customer service
16 with efficient order booking, improved safety, and
17 reduced costs to perform the work.
18
19 2. **Outage Management.** The Outage Management tool is
20 linked to the Company's Geographic Information System
21 (GIS mapping system). It allows the Company's
22 distribution facilities to be linked to individual
23 customer service points in a computer based model.
24 The connectivity provides tools to determine outage
25 areas and affected protective devices. Accurate outage
26 data can be collected for all incidents providing
27 feedback to improve reliability and outage statistics
28 which can be monitored in real time to indicate the
29 severity of major events and assist in resource
30 planning. These capabilities allow for quicker
31 restoration of electrical service for our customers,
32 thereby reducing labor expenses and enhancing customer
33 service.
34
35 3. **Regional Infrastructure Efficiency.** Prior to the
36 construction season each year, Avista, in partnership
37 with the City of Spokane, hosts Spokane's Joint
38 Utilities Coordination Council to bring together
39 regional municipalities, utility companies,
40 telecommunications providers, sewer, water and the
41 railroad to coordinate construction activities.
42 Municipalities and utilities share their project plans
43 and schedules so as to increase the coordination and
44 mitigate the risk of unknown projects. The efforts of
45 the Joint Utilities Coordination Council have resulted

1 in greater coordination and efficiencies across the
2 Spokane region.
3
4

5 **Q. Has Avista considered additional measures to**
6 **mitigate increased costs?**

7 A. Yes. In fact we are currently in the process of
8 revisiting our capital budget for 2009 for potential cuts.
9 With regard to operating expenses, in recent years Avista
10 has run its operations with attention to minimizing
11 expenses while providing reliable service and a high level
12 of customer satisfaction. Following the energy crisis of
13 2000/2001, we cut our operating expenses as we worked
14 toward regaining an investment grade credit rating. Since
15 that time we have continued to pay particular attention to
16 limiting the growth in these costs, while meeting
17 important reliability and environmental compliance
18 requirements, and preserving a high level of customer
19 satisfaction.
20

21 **IV. CUSTOMER SUPPORT PROGRAMS**

22 **Q. What is Avista doing to assist customers with**
23 **their energy bills?**

24 A. As I mentioned earlier, we have a history of
25 making it a priority within our Company to maintain
26 meaningful programs to assist our customers that are least
27 able to pay their energy bills. We also have programs to
28 assist our entire customer base, i.e., not just our low-

1 income customers. Some of the key programs that we offer
2 or support are as follows:

- 3
4 1. **Increased DSM Programs and Funding.** In March 2008
5 Avista proposed, and the IPUC approved, modifications
6 to the Company's energy efficiency program offerings.
7 The modifications further broadened the technical and
8 financial support Avista provides to its customers, and
9 provides customers with increased opportunity to manage
10 their energy bills. In 2008 Avista also launched the
11 award-winning "Every Little Bit" energy efficiency
12 promotional campaign which integrates all of the
13 Company's energy efficiency programs into one location.
14
- 15 2. **Project Share.** Project Share is a voluntary program
16 allowing customers to donate funds that are
17 distributed through community action agencies to
18 customers in need. In addition to the customer and
19 employee contributions of \$67,468 (through November,
20 2008) in Idaho, Avista shareholders contributed
21 \$74,781, Idaho's share, to the program in 2008.
22
- 23 3. **Comfort Level Billing.** The Company offers the option
24 for all customers to pay the same bill amount each
25 month of the year by averaging their annual usage.
26 Under this program, customers can avoid unpredictable
27 winter heating bills.
28
- 29 4. **Payment Arrangements.** The Company's Contact Center
30 Representatives work with customers to set up payment
31 arrangements to pay energy bills.
32
- 33 5. **CARES Program.** Customer Assistance Referral and
34 Evaluation Services provides assistance to special-
35 needs customers through access to specially trained
36 (CARES) representatives who provide referrals to area
37 agencies and churches for help with housing,
38 utilities, medical assistance, etc.
39
- 40 6. **Customer Service Automation.** Customers are able to
41 access Avista's Interactive Voice Response system
42 (IVR) for automated transactions to enter their own
43 payment arrangements, listen to outage messages and
44 conduct other business such as obtaining account
45 balances and requesting a duplicate bill.
46
- 47 7. **Power to Conserve.** In partnership with KREM
48 television, a half-hour television program is annually
49 developed that covers low-cost and no-cost ways to

1 save energy at home. The goal of the program is to
2 help limited income seniors and other vulnerable
3 populations with their energy bills by providing home
4 energy conservation education. The program provides
5 helpful energy conservation tips, information on
6 community resources and ways for customers to manage
7 their energy bills. A DVD of the program has also
8 been produced which is included as part of energy
9 conservation kits provided in senior conservation
10 workshops.

11
12 8. **Senior Energy Workshops.** Energy efficiency workshops
13 that focus on comfort and safety as well as the wise
14 use of energy have been specially designed for the
15 senior population. Kits are provided that contain
16 energy-saving items such as compact fluorescent light
17 bulbs, draft stoppers, rope caulking, etc. The Power
18 to Conserve program DVD along with energy efficiency
19 tip sheets are also included in the kit. Workshops
20 are held at senior meal sites, senior centers and
21 other senior support locations.

22
23 9. **KHQ.com - Caregivers Resource.** Avista sponsors the
24 Caregivers Resource page on KHQ's Senior Life website
25 in order to reach seniors and caregivers with a wide
26 variety of resource information including energy
27 efficiency, energy assistance information, Avista
28 CARES, bill paying assistance, etc. Several video
29 clips offer low-cost, no-cost energy saving ideas.

30
31 10. **Senior Publications.** Avista created a one page
32 advertisement that is placed in several senior
33 directories and publications as part of an effort to
34 reach seniors with information about energy
35 efficiency, Comfort Level Billing, Avista CARES, and
36 energy assistance information.

37
38 Again, Mr. Kopczyński provides additional detail in
39 his testimony concerning these and other programs designed
40 to assist customers.

41 As discussed in Mr. Folsom's testimony, the Company
42 proposes to increase its low-income weatherization funding
43 for electric and natural gas service by a percentage
44 amount equal to the percentage rate increase granted in

1 this case for residential customers (net of the PCA
2 surcharge reduction for electric service). The additional
3 funding would be provided through the DSM tariff rider,
4 Schedules 91 and 191.

5 In addition, Avista actively participated in the
6 energy affordability workshops in Case No. GNR-U-08-01. In
7 that Case, workshop participants are exploring ways to
8 address energy affordability and the difficulty some
9 customers experience in paying their energy bill. Avista
10 supports Staff's recommendation in that Case in favor of
11 legislation to allow the Commission to adopt a Low Income
12 Rate Assistance Program (LIRAP) for its Idaho customers,
13 at the request of the utility.

14 The LIRAP program would allow Avista, with IPUC
15 approval, to collect through a small monthly charge to all
16 customers, additional dollars that would be directed to
17 customers least able to pay their energy bills. The local
18 community actions agencies that are already in place would
19 administer these dollars.

20 **Q. Are there other programs in the State of Idaho**
21 **that are available to provide assistance to customers that**
22 **need help with their energy bill?**

23 A. Yes. On September 30, 2008, President Bush
24 signed legislation that provides \$5.1 billion for the Low
25 Income Home Energy Assistance Program (LIHEAP) for the
26 2008/2009 heating season. This increased funding will

1 serve an additional two million households and raise the
2 average grant from \$355 to \$550, and also allows states to
3 carryover any funds remaining to next year's heating
4 season. Idaho's share of the LIHEAP funding was increased
5 from \$12,376,000 to \$26,969,000. This bill also provides
6 increased funding for weatherization assistance programs.

7 **Q. Is Avista communicating with its customers to**
8 **explain what is driving the increase in costs?**

9 A. Yes. The Company proactively communicates with
10 its customers in a number of ways: electronic customer
11 communications, one-on-one customer interactions through
12 field personnel and account representatives, proactive and
13 reactive media contacts, and through our employees'
14 involvement in community, business and civic
15 organizations, to name a few. We believe our
16 communications are helping our customers, and the
17 communities that we serve, better understand the issues
18 faced by the Company, such as increased environmental
19 mitigation, infrastructure investment, and generation
20 constraints, all of which have lead to higher costs for
21 our customers.

22 We have made extensive efforts to communicate with
23 our customers concerning the cost challenges that we are
24 facing, and we believe these communications are helping
25 customers better understand the factors that are causing

1 increased costs for Avista, and the utility industry in
2 general.

3 **Q. Would you please comment on the employees'**
4 **dedication to achieve customer satisfaction?**

5 A. Yes, I am pleased with the dedication of Avista
6 Utilities' employees and their commitment to provide
7 quality service to our customers. While we continue to
8 maintain tight controls on capital and O&M budgets, our
9 customer service surveys indicate that customer
10 satisfaction remains high. Our recent fourth quarter 2008
11 customer survey results show an overall customer
12 satisfaction rating of 93% in our Idaho, Washington and
13 Oregon operating divisions. This rating reflects a
14 positive experience for the majority of customers who have
15 contacted Avista related to the customer service they
16 received. These results can be achieved only with very
17 committed and competent employees.

18

19

V. OVERVIEW OF AVISTA

20 **Q. Please describe Avista's current business focus**
21 **for the utility and subsidiary operations.**

22 A. Our strategy continues to focus on our energy and
23 utility-related businesses, with our primary emphasis on
24 the electric and natural gas utility business. There are
25 four distinct components to our business focus for the
26 utility, which we have referred to as the four legs of a

1 stool, with each leg representing customers, employees, the
2 communities we serve, and our financial investors. For the
3 stool to be level, each of these legs must be in balance by
4 having the proper emphasis. This means we must maintain a
5 strong utility business by delivering efficient, reliable
6 and high quality service, at a reasonable price, to our
7 customers and the communities we serve, and provide the
8 opportunity for sustained employment for our employees,
9 while providing an attractive return to our investors.

10 The Company recently received upgrades its corporate
11 credit ratings to investment grade by Moody's Investors
12 Service in December 2007 and Standard & Poor's in February
13 2008. Although we are continuing to make progress in
14 improving the Company's financial condition, we are still
15 not as strong financially as we need to be. The Company
16 continues to be below investment grade with Fitch Ratings.
17 Timely rate relief through this filing is an important
18 element in continuing to gain financial strength and
19 improving our credit rating. With higher levels of
20 capital spending required over the next several years(i.e.,
21 approximately \$420 million during 2009-2010), it is more
22 important than ever that the Company remain financially
23 healthy in order to attract capital investment and
24 financing at the lowest cost possible. Company witness Mr.
25 Thies will discuss further the actions taken by the Company

1 to improve cash flow, reduce debt, and our continuing
2 efforts to improve our financial condition.

3 **Q. Please briefly describe Avista's subsidiary**
4 **businesses.**

5 A. Avista Corp.'s primary subsidiary is the
6 information and technology business, Advantage IQ,
7 described below, which is headquartered in Spokane,
8 Washington. In 2007, Avista completed the sale of the
9 operations of Avista Energy to Coral Energy Holding, L.P.,
10 and certain of its subsidiaries, a subsidiary of Shell.
11 Avista currently holds a 6.8% share in Avista Labs'
12 successor company, ReliOn, which is held under Avista
13 Capital. A diagram of Avista's corporate structure is
14 provided on page 1 of Exhibit No.1, Schedule 1.

15 **Q. Please provide an overview of Advantage IQ.**

16 A. Advantage IQ, formerly known as Avista Advantage,
17 commenced operations in 1998 and is a provider of utility
18 bill processing, payment and information services to multi-
19 site customers. Advantage IQ analyzes and presents
20 consolidated bills on-line, and pays utility and other
21 facility-related expenses for multi-site customers
22 throughout North America. Customers include, CSK Auto, Jack
23 in the Box, Staples, and Big Lots, to name a few.
24 Information gathered from invoices, providers and other
25 customer-specific data allows Advantage IQ to provide its
26 customers with in-depth analytical support, real-time

1 reporting and consulting services with regard to facility-
2 related energy, waste, repair and maintenance, and telecom
3 expenses. In 2007, Advantage IQ was awarded the ENERGY
4 STAR® Sustained Excellence Award in recognition of its
5 continued leadership in protecting our environment through
6 energy efficiency.

7 **Q. What is the status of the formation of a holding**
8 **company?**

9 A. In February 2006, Avista filed for regulatory
10 approval of the proposed formation of a holding company
11 (reorganization) with the Federal Energy Regulatory
12 Commission (FERC) and the public utility commissions in
13 Idaho, Washington, Oregon and Montana, conditioned on
14 approval by shareholders. On April 18, 2006, FERC issued
15 its "Order Authorizing Disposition of Jurisdictional
16 Facilities" in Docket No. EC06-85-000, approving the
17 Company's reorganization. Shareholder approval of the
18 reorganization was granted at Avista Corp.'s Annual
19 Shareholder meeting May 11, 2006. On June 30, 2006, the
20 Idaho Public Utilities Commission issued an order approving
21 Avista's reorganization application, based on a settlement
22 in that state. On February 28, 2007, the Washington
23 Utilities and Transportation Commission issued an order
24 approving Avista's reorganization application, based on a
25 settlement in that state. The Montana Commission has yet
26 to act on Avista's Reorganization application, and the

1 procedural schedule for consideration of the Company's
2 application in Oregon has been suspended by agreement of
3 the parties to allow additional time for discussion among
4 the parties.

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

6 A. Avista Utilities provides electric and natural
7 gas service within a 26,000 square mile area of eastern
8 Washington and northern Idaho. Of the Company's 352,423
9 electric and 309,912 natural gas customers (as of
10 September 30, 2008), 120,972 and 72,326, respectively,
11 were Idaho customers. The Company, headquartered in
12 Spokane, also provides natural gas distribution service in
13 southwestern and northeastern Oregon. A map showing
14 Avista's total electric and natural gas service areas are
15 provided in page 2 of Exhibit No. 1, Schedule 1.

16 As of September 30, 2008, Avista Utilities had total
17 assets (electric and natural gas) of approximately \$3.3
18 billion (on a system basis), with electric retail revenues
19 of \$620 million (system) and natural gas retail revenues of
20 \$447 million (system). As of September 2008, the Utility
21 had 1,491 full-time employees.

22 Avista has a long history of innovation and
23 environmental stewardship. At the turn of the 20th century,
24 the Company built its first renewable hydro generation
25 plant on the banks of the Spokane River. In the 1980's,

1 Avista developed an award-winning biomass plant (Kettle
2 Falls) that generates energy from wood-waste.

3 To the future, Avista as well as other utilities are
4 facing new state and federal mandates for renewable energy
5 and carbon control standards. For example, Washington's
6 Senate Bill 6001 and Initiative 937 require certain public
7 and private utilities to produce 15 percent of their power
8 from new renewable resources by 2020, not including legacy
9 hydro production, and to eliminate the option of coal-fired
10 generation because of carbon emission limitations.
11 Recognizing these changes, the Company dropped all new coal
12 generation in its 2007 electric IRP, instead relying on
13 natural gas, renewables, and energy efficiency. Today,
14 Avista has one of the smallest carbon footprints in the
15 U.S.

16 VI. RATE REQUESTS

17 **Q. Please provide an overview of Avista's electric**
18 **rate request in this filing.**

19 A. As previously discussed, in this filing Avista is
20 proposing a net increase in electric retail rates of 7.8%.
21 The proposal consists of an increase in electric base retail
22 rates of \$31.2 million or 12.8%, and a reduction in the
23 current Power Cost Adjustment (PCA) surcharge of 5.0%. The
24 Company's request is based on a proposed rate of return of

1 8.80% with a common equity ratio of 50.00% and an 11.0%
2 return on equity.

3 Mr. Hirschhorn will provide details related to rate
4 spread and rate design. The proposed rate spread for the
5 net increase to each electric customer class is shown in the
6 illustration below.

7

8 **Illustration No. 2:**
9

10 Proposed

11 <u>Service Schedule</u>	12 <u>Increase</u>
13 Residential Service Schedule 1	8.7%
14 General Service Schedules 11 & 12	7.8%
15 Large General Service Schedules 21 & 22	7.8%
16 Extra Large General Service Schedule 25	7.8%
17 Potlatch Service Schedule 25P	5.7%
18 Pumping Service Schedules 31 & 32	7.8%
19 Street & Area Lighting Schedules 41-49	<u>8.9%</u>
20 Overall Increase	7.8%

21 **Q. What is Avista's natural gas rate request in this**
22 **filing?**

23 A. With regard to natural gas, the Company is
24 requesting an increase of \$2,740,000 or 3.0%. As with the
25 electric increase, the Company's request is based on a
26 proposed rate of return of 8.80% with a common equity ratio
27 of 50.00% and an 11.0% return on equity. The proposed rate
28 spread for each natural gas customer class is shown in the
29 illustration below.

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Illustration No. 3:

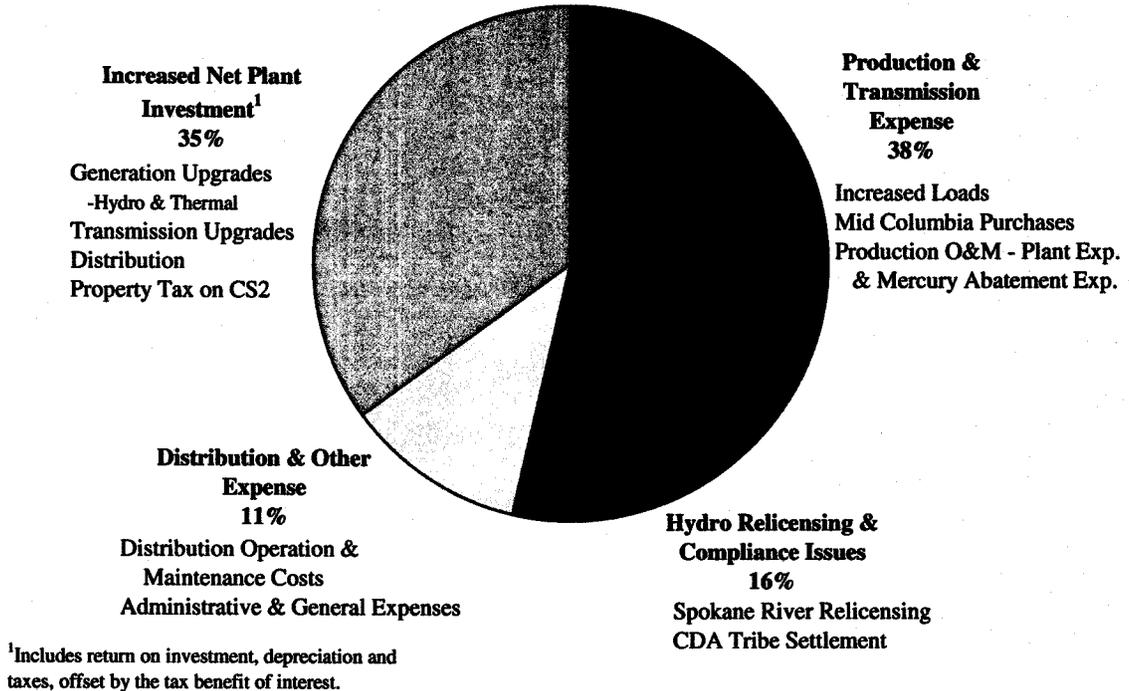
<u>Proposed Service Schedule</u>	<u>Increase</u>
General Service Schedule 101	3.1%
Large General Service Schedule 111/112	2.5%
Interruptible Sales Service Schedule 131/132	1.7%
Transportation Service Schedule 146 (excluding natural gas costs)	<u>10.9%</u>
Overall Increase	3.0%

Q. What are the primary factors causing the Company's request for an electric rate increase in this filing?

A. The Company's electric general rate case test period is based on 12 months ending September 30, 2008, and a July 1, 2009 through June 30, 2010 proforma period. As shown in Illustration No. 4, the Company's electric request is driven primarily by hydro relicensing and compliance costs, increased capital investment to preserve and upgrade our utility infrastructure to meet growing customer demand, and higher power supply costs.

1 Illustration No. 4:

2
3 **Primary Components of Electric Revenue Requirement**



16 Later witnesses provide details explaining these
17 changes in costs.

18 Q. What are the primary factors driving the Company's
19 request for a natural gas rate increase?

20 A. The Company's natural gas request is primarily
21 driven by changes in various operating cost components,
22 mainly distribution operation and maintenance and
23 administrative and general expenditures. This causes an
24 increase in the fixed costs of providing gas service to
25 customers.

1 growth, investment in generation,
2 transmission and distribution facilities for
3 the electric utility business as well as
4 necessary maintenance and replacements of
5 our natural gas utility systems. Avista
6 needs adequate cash flow from operations to
7 fund these requirements, together with
8 access to capital from external sources
9 under reasonable terms.

- 10
- 11 • Avista's corporate rating from Standard &
12 Poor's is currently BBB-. Avista Utilities
13 needs to operate at a level that will
14 support a strong investment grade corporate
15 credit rating, meaning "BBB" or "BBB+", in
16 order to access debt capital markets at
17 reasonable rates, which will decrease long-
18 term costs to customers. Maintaining solid
19 credit metrics and credit ratings will also
20 help support a stock price necessary to
21 issue equity to fund capital requirements.
22
 - 23 • The Company has proposed an overall rate of
24 return of 8.80%, including a 50.00% equity
25 ratio and an 11.0% return on equity. We
26 believe the 11.0% provides a reasonable
27 balance of the competing objectives of
28 continuing to improve our financial health,
29 and the impacts that increased rates have on
30 our customers.
31
32

33

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

- 38 • Application of quantitative methods to alternative
39 groups of proxy companies imply a cost of equity
40 range of 11.3 percent to 13.3 percent.
- 41 • Because Avista's requested ROE of 11.0% percent
42 falls below the lower end of the recommended
43 range, it represents a conservative estimate of
44 investors' required rate of return.

- 1 • Considering investors' expectations for capital
2 markets and the need to support financial
3 integrity and fund crucial capital investment even
4 under adverse circumstances, 11.0% percent is a
5 reasonable, albeit conservative, ROE for Avista.
6 • Because of Avista's reliance on hydroelectric
7 generation, the Company is exposed to relatively
8 greater risks of power cost volatility.
9 • Investors view the Power Cost Adjustment ("PCA")
10 as supportive of the Company's financial
11 integrity, but they understand that the PCA does
12 not insulate Avista from the need to finance
13 accrued power production and supply costs or
14 shield the Company from potential regulatory
15 disallowances.
16 • Avista's requested capitalization is consistent
17 with the Company's need to strengthen its credit
18 standing and financial flexibility as it seeks to
19 raise additional capital to fund significant
20 system investments and meet the requirements of
21 its service territory.
22 • The reasonableness of a minimum 11.0% percent ROE
23 for Avista is also supported by the greater risks
24 associated with the Company's relatively small
25 size and the need to consider flotation costs.

26
27 Mr. Richard Storro, Vice President of Energy Resources,
28 will provide an overview of Avista's resource planning and
29 power operations. He will discuss the Company's resources,
30 current and future load and resource position, and future
31 resource plans. He will also discuss Company hydroelectric
32 upgrades, current hydro relicensing issues, and mercury
33 abatement at Colstrip. Mr. Storro explains:

- 34 • Avista's electric generation portfolio, including
35 power supply operations;
36 • The Company is in an annual balanced-to-surplus
37 energy position through 2017 with the addition of
38 the Lancaster Power Purchase Agreement (PPA);
39 • The Company's involvement with the Chicago Climate
40 Exchange; and
41 • Avista's risk management policy for energy
42 resources, including the electric hedging plan.

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

- The key assumptions driving the Dispatch Model's market forecast of electricity prices. This discussion includes the variables of natural gas, Western Interconnect loads and resources, and hydroelectric conditions.
- The model dispatches Avista's resources and contracts in a manner that maximizes benefits to customers.
- The use of quantitative rate-period loads for July 2009 through June 2010, for modeling pro forma net power supply expenses.
- The output results from the model, including thermal generation and short-term wholesale sales and purchases, were provided to Mr. Johnson to incorporate into the power supply pro forma adjustments.

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

- The adjustment of revenues and expenses based on normal streamflow and weather conditions, and expected wholesale market power prices.

- 1 • Adjustments made to reflect known and measurable
2 changes in power contracts, thermal generation
3 fuel expense, and transmission expense, between
4 the test period, and the pro forma period.
5 • The net effect of the adjustments to the test
6 period power supply expense is an increase of
7 \$27,645,000 on a system basis, \$9,789,095 Idaho
8 allocation.
9 • This increase in pro forma power supply expense
10 over the expense currently in base rates is based
11 on numerous factors, primarily reduced hydro
12 generation due to the elimination of the rate
13 mitigation adjustment included in last year's
14 general rate case and higher retail loads.
15 • Certain proposed revisions to the PCA, including a
16 95%/5% sharing mechanism.
17

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

- 23 • Avista's customer service programs such as energy
24 efficiency, Project Share, CARES program, Senior
25 Outreach Program, and payment plans. Some of
26 these programs will serve to mitigate the impact
27 on customers of the proposed rate increase.
28 • The Company's multi-faceted effort to increase
29 customer service automation, including replacement
30 and upgrade of the new Interactive Voice Response
31 (IVR) system, Mobile Dispatch, Outage Management
32 System, transmission and distribution system
33 efficiencies, and Web Redesign.
34 • The decision by the Company to outsource our bill
35 printing and mailing services. This decision was
36 based on Company needs for disaster recovery
37 compliance, added scalability and flexibility, and
38 cost savings.
39

40 Mr. Scott Kinney, Director, Transmission Operations,
41 will discuss the electric transmission and distribution

1 investments included in this case, and presents the
2 Company's pro forma period transmission revenues and
3 expenses. In addition, he describes the Company's Asset
4 Management Program. Mr. Kinney explains:

- 5 • Avista is expecting to invest over \$15.1 million
6 (system) in electric transmission projects with
7 completion dates in 2009.
- 8 • Several revisions have been made to transmission
9 expenses for the 2009/2010 pro forma period.
- 10 • Changes in replacement and maintenance costs
11 associated with the Company's asset management.
12

13 Mr. Dave DeFelice, Senior Business Analyst, will
14 describe the pro forma adjustment for non-revenue capital
15 expenditures. Mr. DeFelice explains:

- 16 • The rising cost of essential materials specific to
17 the utility industry is causing significant
18 increases in capital project funding requirements.
- 19 • These costs must be pro formed into historical
20 test-year computations in order to allow necessary
21 recovery of our costs to serve customers.
22

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

- 28 • Electric and natural gas revenue requirement
29 calculations.
- 30 • Electric and natural gas results of operations.
- 31 • Pro forma operating results including expense and
32 rate base adjustments.
- 33 • System and jurisdictional allocations.
34

1 Ms. Tara Knox, Senior Regulatory Analyst, sponsors the
2 cost of service studies for electric and natural gas
3 service, the revenue normalization adjustments to results of
4 operations, and the proposed retail revenue credit rate for
5 the PCA. Ms. Knox studies indicate:

- 6 • Electric residential service, extra large general
7 service and street and area lighting service
8 schedules are earning less than the overall rate
9 of return under present rates, while general
10 service, large general service and pumping
11 service schedules are earning more than the
12 overall rate of return under present rates.
13 However, all customer groups are currently
14 providing a rate of return lower than the rate of
15 return requested in this case.
- 16 • Natural Gas small firm service is earning less
17 than the overall rate of return at present rates,
18 while residential, interruptible and
19 transportation service schedules are earning more
20 than the overall rate of return to varying
21 degrees. All of the schedules are relatively
22 close to the overall return indicating the
23 current rate spread is fair.
24

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

- 29 • The proposed net increase in electric retail rates
30 is 7.8%, which consists of an increase in electric
31 base retail rates of \$31.2 million or 12.8%, and a
32 reduction in the current PCA Surcharge.
- 33 • The monthly bill for a residential customer using
34 an average of 982 kWhs per month would increase
35 from \$78.47 to \$85.18 per month, an increase of
36 \$6.71 or 8.6%. This includes the proposed
37 increase in the monthly basic or customer charge
38 from \$4.60 to \$5.00.
- 39 • To achieve this, the Company is requesting that
40 the reduction in the PCA Surcharge become

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effective coincident with the effective date of new retail rates.

- The proposed natural gas annual revenue increase is \$2.7 million, or 3.0%.
- The monthly bill for a residential customer using 66 therms per month would increase from \$79.38 to \$81.94 per month, an increase of \$2.56 or 3.2%. This includes the proposed increase in the monthly basic or customer charge from \$4.00 to \$4.25.

Mr. Bruce Folsom, Senior Manager of Demand Side Management, provides an overview of the Company's DSM programs and documents Avista's expenditures for electric and natural gas energy efficiency programs. Mr. Folsom explains that:

- The Company exceeded its 2008 electric efficiency targets by approximately 40% and 2008 natural gas efficiency target by approximately 34%.
- Avista's expenditures for electric and natural gas energy efficiency programs from January 1, 2008 through November 30, 2008 have been prudently incurred.

Q. Does this conclude your pre-filed direct testimony?

A. Yes.

RECEIVED

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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

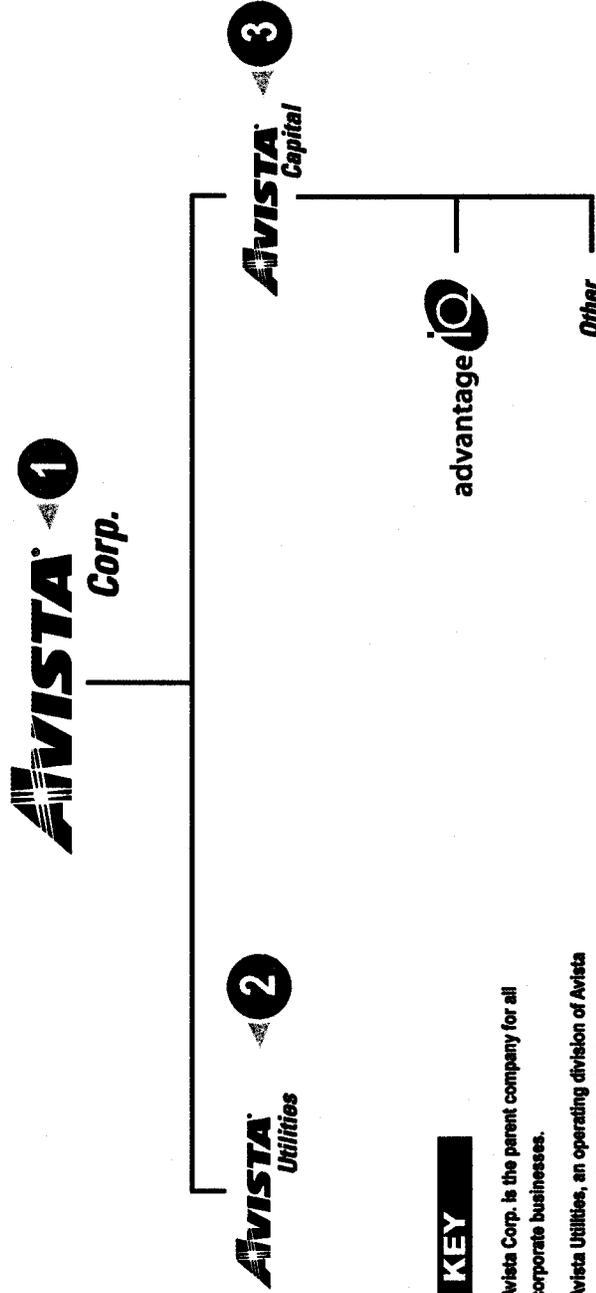
IN THE MATTER OF THE APPLICATION) CASE NO. AVU-E-09-01
OF AVISTA CORPORATION FOR THE) CASE NO. AVU-G-09-01
AUTHORITY TO INCREASE ITS RATES)
AND CHARGES FOR ELECTRIC AND)
NATURAL GAS SERVICE TO ELECTRIC) EXHIBIT NO. 1
AND NATURAL GAS CUSTOMERS IN THE)
STATE OF IDAHO) SCOTT L. MORRIS
_____)

FOR AVISTA CORPORATION

(ELECTRIC AND NATURAL GAS)

Avista Corporation Overview

Avista Corporate Business Organizational Structure



KEY

- ① Avista Corp. is the parent company for all corporate businesses.
- ② Avista Utilities, an operating division of Avista Corp., includes the regulated businesses, serving customers in Washington, Idaho and Oregon.
- ③ Avista Capital is the parent company of all non-regulated subsidiaries. Avista Capital is a wholly owned subsidiary of Avista Corp.

