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IDAHO PUBLIC
UTILITIES COMMISSION

AVISTA Corp.

August 21, 2008

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

Re: Case Nos. AVU-E-08-01 and AVU-G-08-01
Avista's Motion for Approval of Stipulation

Dear Ms. Jewell:

Enclosed for filing with the Commission in the above-referenced docket are the original and nine (9) copies (one (1) copy designated as reporter's copy) plus a computer disk as required by Rule 231.05. of Kelly Norwood's Direct Testimony in Support of the Stipulation.

Sincerely,

Linda Gervais

Linda Gervais
Manager, Regulatory Policy

Enclosures

c: Service List

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this 21st day of August, 2008, served Kelly Norwood's testimony if support of the Stipulation 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:

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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-08-01 CASE NO. AVU-G-08-01 DIRECT TESTIMONY OF KELLY O. NORWOOD IN SUPPORT OF THE STIPULATION

FOR AVISTA CORPORATION

(ELECTRIC AND NATURAL GAS)

I. INTRODUCTION

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

A. My name is Kelly O. Norwood and I am employed as the Vice-President of State and Federal Regulation for Avista Utilities ("Company" or "Avista"), at 1411 East Mission Avenue, Spokane, Washington.

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

A. Yes. I am a graduate of Eastern Washington University with a Bachelor of Arts Degree in Business Administration, majoring in Accounting. I joined the Company in June of 1981. Over the past 27 years, I have spent approximately 16 years in the Rates Department with involvement in cost of service, rate design, revenue requirements and other aspects of ratemaking. I spent approximately 11 years in the Energy Resources Department (power supply and natural gas supply) in a variety of roles, with involvement in resource planning, system operations, resource analysis, negotiation of power contracts, and risk management. I was appointed Vice-President of State & Federal Regulation in March 2002.

Q. What is the scope of your pre-filed testimony in this proceeding?

A. The purpose of my testimony is to describe and support the Stipulation, filed on August 7, 2008 between the Staff of the Idaho Public Utilities Commission ("Staff"), Potlatch Corporation ("Potlatch"), Community Action Partnership Association of Idaho ("CAPAI"), and the Company, which, if approved by the Commission, would resolve all issues in the Company's filing. These entities are collectively referred to as the "Parties," and represent all parties in the above-referenced cases.

The Stipulation is the product of settlement discussions held in the Commission offices on July 31, 2008, which was attended by representatives of all Parties. The Stipulation between the Parties resolved all issues associated with the calculation of the Company's requested cost of capital, including capital structure and cost components, and resolved all revenue requirement, rate spread and rate design issues.

The Stipulation represents a compromise among differing points of view. Concessions were made by all Parties to reach a balancing of interests. As will be explained in the following testimony, the Stipulation represents a fair, just and reasonable compromise of the issues and is in the public interest.

Q. Please explain how the Parties arrived at the Stipulation in this proceeding.

A. The Stipulation is the end result of extensive audit work conducted through the discovery process and hard bargaining by all Parties in this proceeding. I would like to express my appreciation to all Parties involved in this proceeding for their efforts in arriving at this Stipulation and to this Commission for your willingness to hear this matter promptly, in light of the proposed October 1 effective date.

Q. Would you briefly summarize the Stipulation?

A. Yes. As part of the Stipulation, Avista will be allowed to implement revised tariff schedules designed to recover $23,163,000 in additional annual electric revenue and $3,878,000 in additional annual natural gas revenue, which represent an 11.98% and 4.7% increase in electric and natural gas annual base tariff revenues, respectively. In determining these revenue increases, the Parties have agreed to various adjustments to the Company's filing, which are summarized in the Stipulation.

The Stipulation calls for an overall rate of return of 8.45%, determined using a capital structure consisting of 47.94% common stock equity and 52.06% long-term debt, an authorized return on equity of 10.20% and the cost of debt of 6.84%.

The Stipulation also addresses accounting treatment of certain costs, including the Spokane River Relicensing costs, Confidential Litigation costs, Montana Riverbed Litigation costs and revenues associated with the sale of Carbon Financial Instruments. The accounting treatment of these items will be discussed in more detail later in my testimony.

As part of the Stipulation, the funding level of the existing low-income Demand Side Management programs would be increased, and funding would be provided to assist in low-income outreach and education concerning conservation.

II. HISTORY OF FILING

Q. Please describe the Company's general rate case request, as filed.

A. On April 3, 2008, Avista filed an Application with the Commission for authority to increase revenue from electric and natural gas service in Idaho by 16.7% and 5.8%, respectively. If approved, the Company's revenues for electric base retail rates would have increased by $32.3 million annually; Company revenues for natural gas service would have increased by $4.7 million annually.

The Company proposed to spread the electric revenue increase based on an equal percentage to each service (rate) schedule and proposed to raise the monthly electric residential basic charge to $4.60 from the current $4.00 charge. The Company proposed to move natural gas customer class rates of return approximately one-half way to unity and proposed to raise the natural gas residential basic charge to $4.00 from the current $3.28. The Company also proposed to discontinue Schedules 121 and 122, High Annual Load Factor Large General Service.

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

A. The Company's last general rate case in Idaho was based on 2002 test year data. The current filing is based on a 2007 test year. The Company's electric request is driven by changes in various operating cost components, but primarily power supply costs, plant investment or rate base growth associated with generation, transmission and distribution plant and by various hydro relicensing efforts impacting the Utility.

The level of Idaho's share of power supply expense has increased by approximately $33.4 million ($94.3 million on a system basis) from the level currently in base rates. This significant increase in power supply expense over the expense currently reflected in base rates is based on numerous factors, including higher retail loads, reduced hydro generation, increased fuel costs, increased Mid-Columbia purchases, and increased transmission expense.

Gross plant additions of approximately $236.5 million (Idaho allocation) are driven primarily by increases in investments in distribution plant which was $107.2 million from 2002 to 2007, mainly due to customer growth and the inclusion of the AMR project investment. Intangible and production plant increased by $27.6 million in that same time period, related to the hydro relicensing and compliance efforts by the Company. In addition to the hydro relicensing and compliance efforts, increases of $82.6 million for additional production and transmission investment and $19.1 million for general plant have increased overall gross plant.

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

A. The Company's natural gas request is driven by changes in various operating cost components, but primarily the addition of the Jackson Prairie expansion and the completion of the Advanced Meter Reading projects, both planned for completion in the fourth quarter of 2008. This causes an increase in the fixed costs of providing natural gas service to customers.

III. ELEMENTS OF THE STIPULATION

Q. Please explain the derivation of the Electric and Natural Gas Revenue Requirements outlined in the Stipulation.

A. The Parties agreed that Avista will reduce its electric revenue increase request to reflect the adjustments shown on the Table on Page 4 to the Stipulation. While

Avista's filing requested an electric revenue requirement increase of $32.3 million, the adjustments, including the agreed-upon rate of return, reduce this amount by approximately $9.2 million, resulting in a recommended electric revenue requirement increase of $23.1 million. Similarly, as shown on the table on Page 5 to the Stipulation, while the Company requested a natural gas revenue requirement increase of $4.7 million, the agreed-upon adjustments serve to reduce this amount by $0.8 million, resulting in a recommended gas revenue requirement increase of $3.9 million.

As can be seen by a quick review of the individual line descriptions, the adjustments accepted for settlement purposes cover a broad range of revenue and cost categories, including the authorized rate of return. The individual adjustments should not be viewed in isolation; rather, they should be viewed in total as part of the entire Stipulation, and are the result of hard bargaining and compromise.

Q. Please explain the Parties' agreement in regards to an Authorized Rate of Return, including the Return on Equity.

A. The Parties have agreed to a revenue requirement which produces an overall rate of return of 8.45%, based on a return on equity of 10.2% and an equity component at 47.94%. By comparison, the Company's original filing requested an overall rate of return of 8.74%, a return on equity of 10.8% and an equity component of 47.94%. The cost of debt of 6.84% and long-term debt component of 52.06% included in the original filing was agreed to in the Stipulation.

Q. What is the proposed effective date of the Stipulation?

A. The Parties have requested implementation of the Stipulation on October 1, 2008. This proposed effective date is an integral part of the Stipulation that was part of the negotiated resolution of all of the issues.

Q. Please explain the accounting treatment related to the Spokane River Relicensing costs.

A. The Company included the processing costs associated with its Spokane River relicensing efforts, which expenditures included actual life-to-date costs from April 2001 through December 31, 2007, and 2008 pro forma expenditures through December 31, 2008. (See Company witness Andrews' Direct Testimony at page 32.) Although the Company anticipates receiving a final license from the Federal Energy Regulatory Commission ("FERC") in the near future, that has yet to occur. The relicensing costs will remain in CWIP (Construction Work in Progress) and the Company will continue to accrue AFUDC until issuance of the license, at which time the relicensing costs will be transferred to plant in service and depreciation will begin to be recorded. The Parties have agreed to defer as a regulatory expense item (in Account 186 - Miscellaneous Deferred Debits) on the Company's balance sheet depreciation associated with Idaho's share of the aforementioned relicensing costs and related protection, mitigation, or enhancement expenditures, until the earlier of twelve (12) months from the date of the issuance of the license or the conclusion of Avista's next general rate case ("GRC"), together with a carrying charge on the deferral, as well as a carrying charge on the amount of relicensing costs not yet included in rate base. The carrying charge for deferrals and rate base not yet included in establishing rates would be the customer deposit rate at that time (presently 5%).

Q. Please explain the accounting treatment related to the Confidential Litigation costs.

A. Company witness Andrews describes the confidential litigation at pages 32 and 33 of her pre-filed direct testimony (unredacted). Inasmuch as that matter is still pending and has yet to be finally resolved, but is expected to reach resolution in the near future, the Parties have agreed to defer as a regulatory expense item (in Account 186 - Miscellaneous Deferred Debits) on the Company's balance sheet depreciation associated with Idaho's share of the aforementioned costs with a carrying charge on the deferral as well as a carrying charge on the amount of costs not yet included in rate base for subsequent recovery in rates. The carrying charge will be the customer deposit rate (presently 5%). This deferral, together with a carrying charge, will continue until the earlier of twelve (12) months from the date of resolution of the litigation or until the conclusion of Avista's next general rate case (GRC).

Q. Please explain the treatment of the Montana Riverbed Litigation costs.

A. On November 1, 2007, Avista filed an Application with the Commission (Case No. AVU-E-07-10) requesting an accounting order authorizing deferral of settlement lease payments and interest accruals relating to the recent settlement of a lawsuit in the State of Montana over the use of the riverbed related to the Company's ownership of the Noxon Rapids and Cabinet Gorge hydroelectric projects located on the Clark Fork River. The Commission, in its Order No. 30492, authorized the deferral of settlement lease payments and delayed a decision on interest, until the matter was addressed in this general rate filing. The Parties have agreed to the Company's requested amortization of costs, together with recovery of accrued interest on the Idaho share of deferrals at the customer deposit rate (presently 5%).

Q. Please explain the accounting treatment related to the revenues associated with the sale of Carbon Financial Instruments (CFIs).

A. On May 22, 2008 Avista filed a request with the Commission (Case No. AVU-E-08-2) to defer the revenues associated with the sale of Carbon Financial Instruments (CFIs) on the Chicago Climate Exchange. The Company's Application was approved on August 5, 2008 in Order No. 30610. Idaho's share of the revenues, net of expenses, from the CFI sales is $850,571. These dollars will be amortized over a two-year period beginning in the calendar month of the effective date of new retail rates resulting from this Stipulation, with a carrying charge on the unamortized balance at the customer deposit rate. The revenue requirement included in this Stipulation has been reduced for the CFI revenues, in order to flow these benefits through to customers.

Q. Please describe the low-income portion of the Stipulation.

A. There are three areas the Company addressed in the Stipulation, as follows:

(a.) <u>Low-Income DSM Funding</u> - At present, $350,000 per year is provided to Idaho service (CAP) agencies for proposed funding of low-income Demand-Side Management (DSM). The Parties agree to increase the annual level of funding to

$465,000 for such programs (which includes administrative overhead). The continuation and level of such funding will be revisited in the Company's next general rate filing.

(b.) Funding for Outreach for Low-Income Conservation – The Parties agree that annual funding in the amount of $25,000 will be provided to Idaho (CAP) agencies for the purpose of underwriting the dedication of agency personnel to assist in low-income outreach and education concerning conservation. The dollars will be funded through the DSM Tariff Rider (Schedules 91 and 191), and will be in addition to the $465,000 of Low-Income DSM Funding. The continuation and level of such funding will be revisited in the Company's next general rate filing.

(c.) Establishment of Generic Workshops – Avista agrees to support and actively participate in any Commission-established workshops for the purpose of examining issues surrounding energy affordability and customers' ability to pay energy bills with respect to all jurisdictional utilities. As part of this process, Avista agrees to explore the feasibility of establishing a Low-Income Rate Assistance Program (LIRAP), or similar program, to assist low-income residential customers in Idaho.

Q. Does the Company have other programs in place to mitigate the impacts on customers of the proposed rate increase?

A. Yes. Avista Utilities offers a range of programs to help customers who have difficulty paying their energy bills. Some programs are in cooperation with local Idaho community action agencies, who are specialized in targeting assistance where it is most needed. We are very aware of the impacts energy costs have on our customers.

Programs designed to assist customers include:

- Energy efficiency programs. Avista Utilities offers energy efficiency services to electric and natural gas residential, commercial, and industrial customers.

- Project Share. Project Share is a voluntary program allowing customers to donate funds that are distributed through community action agencies to customers in need. In addition to the customer and employee contributions of $88,910 in Idaho, Avista shareholders contributed $50,000 to the program in 2007.

- Comfort Level Billing. The Company offers the option for customers to pay the same bill amount each month of the year by averaging their annual usage.

- Payment arrangements. The Company's Contact Center Representatives work with customers to set up payment arrangements to pay energy bills.

- CARES program. Customer Assistance Referral and Evaluation Services provides assistance to special-needs customers through access to specially trained (CARES) representatives who provide referrals to area agencies and churches for help with housing, utilities, medical assistance, etc.

- Customer service automation. Customers are able to access Avista's Interactive Voice Response system (IVR) for automated transactions to enter their own payment arrangements, listen to outage messages and conduct other business such as obtaining account balances and requesting a duplicate bill.

IV. RATE SPREAD & RATE DESIGN

Q. How did the Stipulation address rate spread?

A. Appendix 2 of the Stipulation shows the impact on each service schedule of the agreed-upon electric and natural gas increases. The proposed electric revenue increase of $23,163,000 represents an overall increase of 11.98% in base rates, and with one exception, is spread on a uniform percentage basis to all schedules. Schedule 25P (for Potlatch's Lewiston plant), however, will receive an increase of 10.36%, in order to reflect a Schedule 25P rate that is no higher than the tailblock rate of Schedule 25. With this change, the relative rate of return for Schedule 25P would move approximately one-half way toward unity, more consistent with the movement of other service schedules. All other schedules will receive a 12.33% increase.

The spread of the increased natural gas revenue requirement of $3,878,000 is set forth in Appendix 2 of the Stipulation, and represents an overall increase of 4.7% in base rates. It reflects a reduction to what the Company had proposed by way of an increase for each of the gas service schedules proportional to the reduction in the overall increase.

Q. What is the basis of the Stipulation relating to the rate design?

A. The Parties agree to changes in the electric customer and demand charges as set forth in the Company's filing, and summarized in Appendix 2 of the Stipulation. This includes an increase in the residential monthly basic charge from $4.00 to $4.60. The energy rates within each electric service schedule are increased by a uniform percentage.

With respect to natural gas rate design, the Parties agree to apply the increase in rates within each service schedule in the same manner as proposed by the Company. The monthly basic charge for the residential schedule will increase from $3.28 to $4.00, as proposed by the Company.

V. CONCLUSION

Q. What is the effect of the Stipulation?

A. The Stipulation represents a negotiated compromise on a variety of issues among the Parties. Thus, the Parties have agreed that no particular party shall be deemed to have approved the facts, principles, methods, or theories employed by any other in arriving at these stipulated provisions, and that the terms incorporated should not be viewed as precedent setting in subsequent proceedings except as expressly provided.

Q. In conclusion, why is this Stipulation in the public interest?

A. This Stipulation strikes a reasonable balance between the interests of the Company and its customers, including its low-income customers. As such, it represents a reasonable compromise among differing interests and points of view.

The Parties have agreed that the Company has demonstrated need for a revenue requirement increase for both its electric and natural gas customers. The Stipulation provides for recovery of these costs. In the final analysis, however, any settlement reflects a compromise in the give-and-take of negotiations. The Commission, therefore, has before it a Stipulation that is supported by sound analysis and supporting evidence, the approval of which is in the public interest.

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

A. Yes, it does.