BEFORE THE

IDAHO PUBLIC UTILITIES COMMSSION

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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-09-1/ AVU-G-09-1

DIRECT TESTIMONY OF RANDY LOBB IN SUPPORT OF STIPULATION

IDAHO PUBLIC UTILITIES COMMISSION

JUNE 24, 2009

Q. Please state your name and business address for the record.

A. My name is Randy Lobb and my business address is 472 West Washington Street, Boise, Idaho.

Q. By whom are you employed?

A. I am employed by the Idaho Public Utilities Commission as Utilities Division Administrator.

Q. What is your educational and professional background?

A. I received a Bachelor of Science Degree in Agricultural Engineering from the University of Idaho in 1980 and worked for the Idaho Department of Water Resources from June of 1980 to November of 1987. I received my Idaho license as a registered professional Civil Engineer in 1985 and began work at the Idaho Public Utilities Commission in December of 1987. My duties at the Commission currently include case management and oversight of all technical Staff assigned to Commission filings. I have conducted analysis of utility rate applications, rate design, tariff analysis and customer petitions. I have testified in numerous proceedings before the Commission including cases dealing with rate structure, cost of service, power supply, line extensions, regulatory policy and facility acquisitions.

Q. Are you the same Randy Lobb that previously filed direct testimony in this case?

A. Yes I am.

Q. What is the purpose of your testimony today?

A. The purpose of my testimony is to describe the Stipulation (the Proposed Settlement) filed in this case and to explain the rationale for Staff's support.

Q. Please summarize your testimony.

A. Staff believes that the comprehensive Stipulation and Settlement resolving all issues in the general rate case is in the public interest. The Settlement was agreed to by all parties. It is just and reasonable and should be approved by the Commission.

Q. Please provide an overview of the Stipulation and Settlement.

A. The Stipulation filed with the Commission on June 16, 2009 settles a variety of issues to arrive at an overall base rate revenue requirement increase of $9.43 million or 4.29% for electric service and $1.939 million or 2.11% for natural gas service. The parties also acknowledged that the revenue requirement for electric service could increase to $12.548 million or 5.7% if FERC issued a new Spokane River hydroelectric license by July 22, 2009.[1] Nevertheless, the likely increase is relatively

[1]On June 18, 2009, FERC issued a new 50-year license for Avista's five hydroelectric facilities on the Spokane River. This issue is discussed in greater detail below.

close to the Staff recommendation provided in pre-filed direct testimony of $8.62 million (3.91%) and $1.89 million (2.06%) for electric and natural gas service respectively. It also represents a significant decrease in the Company's requested increase of $31.2 million (12.8%) and $2.7 million (3.0%) for electric and natural gas service, respectively.

When proposed decreases in the Power Cost Adjustment (PCA) rate for electric service and the Purchase Gas Adjustment (PGA) rate for gas service are included, there is no overall revenue requirement increase for gas or electric service. However, overall electric revenue requirement will increase by 1.5% when the Spokane River relicensing costs are included.

Q. How does the revenue adjustments specified in the Stipulation compare to revenue adjustments previously proposed by Staff?

A. The difference in the base electric revenue requirement agreed to in the Stipulation and that proposed by Staff in pre-filed direct testimony is due to movement by Staff on four issues. They are: 1) an increase in anticipated net power supply costs using more current forward natural gas prices, 2) a slight increase in executive labor to reflect actual 2008 compensation, 3) an increase in Information Services expense to reflect the actual 2009 level of employees and 4) rate base treatment of costs associated with Montana riverbed leases. With the exception of the Spokane River Relicensing, all other revenue requirement adjustments listed in the Stipulation are as proposed by Staff in direct testimony.

Q. How do the stipulated non-revenue issues compare to the Staff position presented in pre-filed testimony?

A. All other issues described in the Stipulation such as class revenue spread, rate component adjustments, evaluation of payment plans and review of low income deposit requirements were resolved as proposed by Staff or other intervenors in direct testimony. Finally, resolution of the remaining issues represented a reasonable alternative to litigation in this case. For example, the Company agreed to withdraw its request to change the PCA sharing percentage, and agreed to request prudency of DSM program costs in a subsequent docket. Moreover, all parties agreed that the Company would further study cost of service issues and continue to address a variety of low income concerns.

Q. Does Staff believe the proposed Stipulation and Settlement is reasonable?

A. Yes. As previously stated, the overall base revenue requirement increase for electric and gas service of $9.43 million (4.29%) and $1.939 million (2.11%)

respectively, is quite close to the $8.62 million (3.91%) and $1.89 million (2.01%) originally proposed by Staff in direct testimony. Even with Spokane River relicensing costs included, the increase of $12.548 (5.7%) million for electric service is about 60% less than the Company's original $31.2 million (12.8%) request. The Company originally requested an increase of $2.7 million (3.0%) for gas service.

Other issues such as use of the PCA and PGA rate reductions to offset the base rate increases, rate spread, rate design, treatment of Lancaster costs, changes to PCA sharing percentages, prudency review of DSM costs and customer service considerations were consistent with Staff's direct testimony. Staff believes that the additional issues addressed in the Stipulation including further cost of service analysis, agreement on low income issues and rate implementation date were fairly straight forward, reasonable accommodations to achieve comprehensive settlement.

A. How did Staff approach settlement in this case?

Q. After filing direct testimony on May 29, 2009, Staff met with the Company and other parties on June 5, 2009, in an effort to resolve any undisputed issues. Staff was only willing to consider movement on its revenue requirement adjustments for those issues where updated information was available or errors were identified.

Q. In what areas did Staff agree to modify its revenue requirement recommendations?

A. Staff agreed to modify its revenue requirement recommendations in the following four areas: 1) increase net power supply costs recovered in base rates (line b, Electric Table, p. 5); 2) slightly increase executive compensation (line f, p. 5); 3) increase information service expense (line g, p. 5); and 4) allow rate base treatment of costs associated with Montana riverbed leases (note 3, p. 5). Staff also agreed to include Spokane River relicensing costs in this case if FERC issued a new hydroelectric operating license by July 22, 2009.

While the Production Property Adjustment (line c, p. 5) and the Restatement of Debt Interest (line p, p. 5) changed from that proposed by Staff in its direct testimony, these adjustments are the direct results of changes in other Staff adjustments as specified in the Stipulation and flow through automatically.

Net Power Supply Costs

Q. Please explain the difference in the Idaho jurisdictional net power supply cost adjustment of $14,455,000 as recommended by Staff in its pre-filed direct testimony and the $13,869,000 adjustment agreed to in the Stipulated Settlement on line b, page 5.

A. The difference is primarily due to a difference in gas prices used in the AURORA analysis performed to develop net power supply cost. In its initial Application in this case, Avista used a three-month average of natural gas prices from September 1, 2008 to November 30, 2008, of monthly forward prices for the pro forma period. Staff, in its analysis, used a one-month average of forward gas prices from March 27, 2009 to April 27, 2009. Staff chose to use a one-month average of prices because they were the most recently available at the time it performed the AURORA analysis. Staff believed that the most recent gas forward prices were a better indication of prices likely to occur in the pro forma period.

In the Settlement Stipulation, Avista adopts Staff's position to use a one-month average of gas prices, but proposes to use a more current average of prices from May 1, 2009 to May 31, 2009 for the un-hedged portion of the generation. Staff agrees that a one-month average of gas prices using a more current period to derive the net power supply costs is appropriate.

Q. Were any other changes made in Staff's analysis to derive the net power supply cost included in the Settlement Stipulation?

A. Yes, a minor error in Staff's analysis was corrected. The error involves necessary after-the-fact additions of start-up fuel costs to the AURORA results, and adjustment of fuel costs at Coyote Springs 2 that cannot be accommodated in AURORA.

Q. Does Staff agree with the results of the analysis done to develop the net power supply cost recommendation included in the Settlement Stipulation?

A. Yes, Staff has reviewed the analysis, including replication of the revised AURORA results and including the minor errors identified in Staff's analysis. Staff agrees with the revised AURORA results and supports using the more current gas prices in the Staff proposed one-month average. The parties agree as part of the Settlement to support Staff's recommendation to exclude short-term contracts already entered into for the pro forma period and instead to recover these costs through the PCA subject to the 90/10 percent sharing. Consequently, Staff supports the net power supply cost decrease adjustment of $13.869 million included in the Settlement Stipulation.

Executive Labor Compensation

Q. What was Staff's position regarding Executive Labor Compensation in its pre-filed testimony?

A. Staff removed all proposed increases to Executive Labor expenses for 2009 and 2010, and annualized the executive salaries at their current level of expense.

Q. Why did Staff agree to the smaller adjustment specified in the Stipulation on line f, page 5?

A. Staff's original filing did not calculate the overhead loading associated with the executive labor. The Stipulation accepts Staff's position of excluding 2009 and 2010 increases for executives, and annualizes the current level of Executive Labor expense. However, the Stipulation recognizes the associated overhead applied to the annualized Executive Labor.

Staff believes it is appropriate to account for indirect overhead expenses when computing labor expense. The settlement on this adjustment corrects an oversight in Staff's original filing.

Information Service Expense

Q. What was Staff's position regarding Information Service (IS) Expense in its pre-filed testimony?

A. Staff excluded IS labor expense for four positions that the Company intended to, but had not yet filled. Staff further reduced IS expense to recognize operating efficiencies gained by including the pro forma level of expense in rates.

Q. Why did Staff agree to the smaller adjustment specified in the Stipulation on line g, page 5?

A. The Stipulation includes Staff's recognition of operating efficiencies, however, two positions that Staff excluded were positions that were actually filled but the amounts were being capitalized rather than expensed. The Stipulation recognizes that these positions were filled, but because the Company did not include any expense associated with these two positions in its original filing, no Staff adjustment was necessary.

Montana Riverbed Leases

Q. In the last rate case, the Company was allowed to defer unamortized payments it made to the State of Montana for lease of the riverbeds for the Noxon Rapids and the Cabinet Gorge hydroelectric projects. In this rate case, the Company requested inclusion of the unamortized balance in its rate base, thus collecting a return on that balance. What was Staff's position on the inclusion of the unamortized balance of deferred payments in the Company's rate base with a return?

A. Staff initially agreed that the Company should be allowed to amortize the unamortized balance over the remaining eight (8) year life of the lease, but did not recommend allowing the Company to earn a return on the unamortized balance.

Q. How does the Stipulation treat the unamortized balance for the Montana lease?

A. The Stipulation allows the Company to include the unamortized balance of $1,582,501 in rate base to earn at the authorized rate of return. The balance remains amortized over eight (8) years.

Q. Why did Staff agree to include the unamortized balance of $1,582,501 in the Company's rate base at the overall rate of return?

A. The unamortized balance is the amount paid by the Company to the State of Montana for its use of the riverbeds at the Company's hydro-electric projects in Montana. The Montana courts have determined that the Company was liable for use of the riverbeds owned by the State of Montana at the Company's projects. Thus, the Company entered into a lease with the State of Montana for the use of the riverbeds.

In the last rate case the Company sought and obtained an Order (Order No. 30647) from this Commission to defer any payments it made pursuant to the lease and prior to this rate case. Pursuant to our settlement discussions and the Commission's prior approval to defer these lease payments, Staff believes the payments were reasonable and prudent for the production of electricity at the Company facilities. Therefore, Staff included the amortization in rates for recovery. Staff now accepts including the unamortized balance in rate base at the Company's authorized return because it was previously included in this manner to establish the stipulated revenue requirement in the last rate case, Case No. AVU-E-08-1. Language included in that prior Stipulation indicated that the return on the unamortized balance was at the customer deposit rate (Stipulation, p. 7, 9(c) AVU-E-08-1). However, this language related to the return during the deferral period, not the return once it was included in rates.

Spokane River Relicensing

Q. How did Staff originally propose to treat Spokane River relicensing costs in this case?

A. Staff reviewed the costs associated with relicensing and determined that they should not be included for recovery in this case because a new FERC operating license had not yet been obtained. The expenditures were therefore, not deemed used and useful.

Q. Why did Staff agree to include the relicensing costs in this case if a new license was issued by July 22, 2009?

A. The Company maintained that a new license was imminent. In fact FERC issued the new 50-year license on June 18, 2009 - two days after the Stipulation was filed. Staff agreed that if a new license was obtained prior to the Company's filed rebuttal or during the course of the hearings, it is likely that the Commission would include the cost in this case. It would also be difficult for Staff to continue to argue that the relicensing costs were not used and useful. Therefore, Staff agreed to the July 22, 2009 cutoff date for the Company to obtain a license with the caveat that un-audited costs are subject to audit before they are reflected in rates. Additional revenue requirement subject to recovery in this case with timely receipt of the new license totals $3.11 million annually. See Note 1 to Table on page 5 of the Stipulation.

Other Issues

Q. What other revenue requirement adjustments are itemized in the Settlement Stipulation and how do they compare to Staff's original recommendation?

A. Other revenue requirement adjustments itemized in the Stipulation include return on equity (10.5%), regulatory fees, non-executive labor, asset management, Colstrip mercury emissions O&M, compensation incentives, generation O&M expense, insurance expense, miscellaneous expenses and the Coeur d'Alene Tribe Settlement. Other than allocation of system adjustments, the capital additions adjustment is the only issue specifically identified on the natural gas side. All of these adjustments are the same as those originally recommended in Staff's pre-filed direct testimony.

Q. What does the Stipulation provide in terms of revenue spread and rate design?

A. The parties agreed in paragraph 15 to spread the electric revenue increase uniformly across all customer classes and increase only the energy component of rates in each class as originally proposed by Staff. Likewise, the Agreement follows Staff's original proposal to spread the natural gas revenue increase to customer schedules based on the Company's cost of service study and increase only the commodity component of the gas rate.

The Settlement endorses Staff's proposal to reduce the PCA and PGA rates to mitigate the base rate increase. The required PCA rate reduction is 0.266 cents per kWh for electric customers and the required PGA rate reduction is 2.662 cents per therm for natural gas customers. The PCA rate reduction will not fully offset the base rate revenue requirement with the Spokane River relicensing costs included in this case. The PGA rate reduction offsets the base rate increase in Schedule 101 and reduces the overall rate in other schedules by various amounts.

Q. Are the higher PCA and PGA rate reductions specified by the Settlement of any concern to you?

A. I have no concern regarding the PGA reduction. Forecasted gas prices over the period that rates will be in effect are well below the weighted average cost of gas (WACOG) currently embedded in rates. The PCA reduction is only slightly more likely to produce higher deferral balances for surcharge than that proposed by Staff in direct testimony. The risk caused by the slightly lower PCA rate is also partially offset by stipulated higher power supply costs embedded in rates.

Q. Are there other issues identified in the Stipulation that are consistent with Staff recommendations presented in direct testimony?

A. Yes, the Stipulation in paragraph 14 on page 11 specifically addresses the Company's proposal to change the PCA sharing percentage from 90%/10% to 95%/5%. Staff did not believe the Company sufficiently justified its proposal in direct testimony and the Company withdrew the issue as part of the settlement.

The Stipulation in paragraph 12 on page 11 also specifies that the issue of prudence review of DSM expenditures for the period January 1, 2008 through November 30, 2008 will be addressed in a future docket. Staff did not believe the Company provided sufficient evidence in its direct case to justify a finding of prudency for these expenditures. Consequently, Staff believes it is reasonable to delay a prudency review to a later date when more information is available.

In addition, the Stipulation reiterates Staff's position supporting the Company's proposed cost recovery of the Lancaster power project tolling agreement. See ¶ 10.

The Stipulation also supports Staff's original recommendation provided in direct testimony for cost recovery of the Coeur d'Alene Tribe Agreement. See ¶ 9(o) on p. 10.

Finally, the Stipulation supports Staff's original proposals that the Company evaluate its payment plans and low income deposit policies for effectiveness. See ¶ 16(d) and (e) on p. 15.

Q. What issues are included in the Stipulation that were not originally addressed by Staff in direct testimony?

A. Issues supported by Staff in the Stipulation that were not originally addressed by Staff in direct testimony include additional cost of service evaluation (see ¶ 13), continuation of low income customer service programs (see ¶ 16(b) and (c)), and new rate implementation on August 1, 2009 (¶ 15(f)). The cost of service recommendations to evaluate various methods of allocating transmission facilities and to provide twelve months of current load data in a timely manner are necessary to properly determine cost of service and are supported by Staff.

The low income recommendations for Avista to support low income rate assistance legislation, to continue funding for low income weatherization and outreach education are a continuation of existing support and programs. Staff supports these recommendations based on its belief that they reasonably improve low income affordability.

Q. Why did Staff support an August 1, 2009 implementation date for new rates rather than the statutory deadline of August 23, 2009?

A. This provision was agreed to by Staff as part of the give and take of settlement negotiations. Staff believed that the accelerated implementation date was reasonable given that comprehensive settlement would reduce the need for lengthy hearings, complicated deliberations and time consuming development of the final Commission Order. Staff also accepted the Company position that a first of the month implementation of new rates would simplify calculation of monthly power supply costs for determination of PCA deferral balances.

Q. Does this conclude your testimony in this proceeding?

A. Yes, it does.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 24TH DAY OF JUNE 2009, SERVED THE FOREGOING **DIRECT TESTIMONY IN SUPPORT OF STIPULATION OF RANDY LOBB**, IN CASE NOS. AVU-E-09-1 & AVU-G-09-1, BY ELECTRONIC MAIL TO THE FOLLOWING:

DAVID J. MEYER
VICE PRESIDENT AND CHIEF COUNSEL
AVISTA CORPORATION
PO BOX 3727
SPOKANE WA 99220
E-MAIL: david.meyer@avistacorp.com

KELLY NORWOOD
VICE PRESIDENT – STATE & FED. REG.
AVISTA UTILITIES
PO BOX 3727
SPOKANE WA 99220
E-MAIL: kelly.norwood@avistacorp.com

DEAN J MILLER
McDEVITT & MILLER LLP
PO BOX 2564
BOISE ID 83701
E-MAIL: joe@mcdevitt-miller.com

SCOTT ATKINSON
PRESIDENT
IDAHO FOREST GROUP LLC
171 HIGHWAY 95 N
GRANGEVILLE ID 83530
E-MAIL: scotta@idahoforestgroup.com

CONLEY E WARD
MICHAEL C CREAMER
GIVENS PURSLEY LLP
PO BOX 2720
BOISE ID 83701-2720
E-MAIL: cew@givenspursley.com
mcc@givenspursley.com

DENNIS E PESEAU, Ph.D.
UTILITY RESOURCES INC
SUITE 250
1500 LIBERTY STREET SE
SALEM OR 97302
E-MAIL: dpeseau@excite.com

BETSY BRIDGE
ID CONSERVATION LEAGUE
710 N SIXTH STREET
PO BOX 844
BOISE ID 83701
E-MAIL: bbridge@wildidaho.org

ROWENA PINEDA
ID COMMUNITY ACTION NETWORK
3450 HILL RD
BOISE ID 83702-4715
E-MAIL: Rowena@idahocan.org

CARRIE TRACY
1265 S MAIN ST, #305
SEATTLE WA 98144
E-MAIL: carrie@nwfco.org

BRAD M PURDY
ATTORNEY AT LAW
2019 N 17^{TH} ST
BOISE ID 83702
E-MAIL: bmpurdy@hotmail.com

Glenda D. Koch
SECRETARY