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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-12-08 CASE NO. AVU-G-12-07 DIRECT TESTIMONY OF SCOTT L. MORRIS

FOR AVISTA CORPORATION

(ELECTRIC AND NATURAL GAS)

I. INTRODUCTION

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

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

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

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

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

I am a member of the Western Energy Institute board of directors, a member of the Gonzaga University board of trustees, a member of Edison Electric Institute board of directors, a member of the American Gas Association, a member of ReliOn board of directors, and board director of the Washington Roundtable. On January 1, 2011, I was appointed to the Federal Reserve Bank of San Francisco, Seattle Branch board of directors and in January 2012 I was appointed as Chairman of the Board to Innovate Washington by Governor Christine Gregoire. I also serve on the board of trustees of Greater Spokane Incorporated.

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

A. I will first explain why Avista is requesting a rate increase through this filing, and summarize the Company's electric and natural gas rate requests. A large part of our need for a rate increase is driven by the costs associated with continuing to expand and replace the facilities we use every day to serve our customers. When we remove the old equipment and replace it with new, it results in higher overall costs to serve customers. This was the primary reason for the proposed increase in our last rate increase request, and it is expected to continue to cause a need for increased rates in the future.

I will also discuss some of the measures we have taken to cut costs, as well as initiatives to increase operating efficiencies in an effort to mitigate future cost increases to customers. I will briefly explain the Company's customer-support programs in place to assist our customers, as well as our communications initiatives to help customers better understand the changes in costs that are causing our rates to increase. Finally, I will introduce each of the other witnesses providing testimony on the Company’s behalf.

A table of contents for my testimony is as follows:

Q. Are you sponsoring any exhibits in this proceeding?

A. Yes. I am sponsoring Exhibit No. 1, Schedule Nos. 1 and 2. Schedule No. 1 includes an overview of Avista and its utility and subsidiary operations, as well as a diagram of Avista's corporate structure. Schedule No. 2 includes a map showing Avista's electric and natural gas service areas.

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

A. Avista is requesting an overall electric billed rate increase of 4.6% or $11.4 million, and a natural gas billed rate increase of 7.3% or $4.6 million.

II. WHY IS AVISTA REQUESTING A RATE INCREASE

Q. Why is Avista requesting a rate increase?

A. Before I address our rate request, I would like to specifically address the issue of the economy. The people of the State of Idaho and our Country are continuing to face the challenges of a difficult economy. In our 2011 general rate case proceeding, the Commission received a number of comments from customers related to our proposed rate increase. The comments addressed, among other things, the state of the economy, the need for Avista to "tighten its belt," concerns about executive compensation, and an inability to pay energy bills by seniors and those on limited incomes. We have read every one of the written comments, and I can assure you that the decisions we make at Avista are not made without taking into consideration the current state of the economy, as well as the other issues raised by our customers.

With regard to low income customers and seniors, we understand that when energy costs go up, especially in times like these, it affects everyone. Our prices remain among the lowest in the nation and in the Northwest. While that's an important comparison, we know it doesn't change the fact that rates are rising during tough times. But we make it a priority to do the best we can to assist customers who need more help. I will describe in more detail the Company's support programs later in my testimony.

With regard to cost-control, we contracted with a consultant in 2010 to come in to Avista to take an independent, objective look at opportunities to do our work more efficiently and more cost-effectively. Although some areas were identified where efficiencies could be gained, we also found that many of our operations were already efficient and cost-effective.

In the past several years we have also made substantial cuts in our capital budget in order to mitigate rate impacts to customers. Because we have chosen to not spend millions of dollars on facilities that need to be replaced, this has also contributed to higher unemployment in North Idaho and Eastern Washington.

At the same time, while we continue to maintain tight controls on capital and O&M budgets, our customer service surveys indicate that customer satisfaction remains high. Our overall customer satisfaction from our voice-of-the-customer surveys in the second quarter of 2012 was 93% in our Idaho, Washington, and Oregon operating divisions. This rating reflects a positive experience for customers who have contacted Avista related to the customer or field service they received.

I believe that many of our customers, however, do not understand that there are limitations on how far we, as a utility, can go with cost-cutting before we begin to jeopardize reliability of service and customer satisfaction. As a regulated company Avista has an obligation to safely and reliably serve every customer that requests service.

Q. How does that obligation to serve limit the ability of Avista to cut spending?

A. Avista has a legal obligation to provide safe and reliable service to every customer that requests electric service from the Company. When a new customer requests service, we must hook them up, even if the cost to serve that customer results in increased costs to all other customers. Likewise, if the facilities serving an existing customer are deteriorating and need repair, we must repair or replace them so that the customer continues to receive safe, reliable service.

We have highlighted some of these points in prior filings, but they bear repeating because they get to the heart of why we are requesting a rate increase in the midst of a continuing difficult economy.

We have heard the comments from some of our customers to the effect that Avista should cut its costs, and "tighten its belt" like other businesses are having to do in these difficult economic circumstances. And we have taken steps to do so. But at the same time <u>we are not like other businesses</u>. Without the obligation to serve, we could consider refusing to hook up new customers, because it could avoid an increase in costs to our existing customers. Without an obligation to serve, we could consider no longer serving some of the more remote, more costly areas to provide service, which would allow us to avoid further investment, and reduce labor and other operating costs. Unregulated businesses have the opportunity to shut down aging facilities or under-producing retail outlets, eliminate product lines, and cut back on investment and maintenance. We do not.

We do have opportunities to cut back on investment and operating costs, and we have where prudent to do so. But those opportunities are limited by our obligation to safely and reliably serve all customers, and our obligation to comply with numerous mandatory state and federal requirements. We simply don't have the choice to say no to new customers, no to maintaining a safe, reliable system, and no to mandatory requirements. Although we have taken measures to ensure that the costs that we incur represent the most cost-effective and reliable way to continue to serve our customers, we continue to experience significant increases in costs.

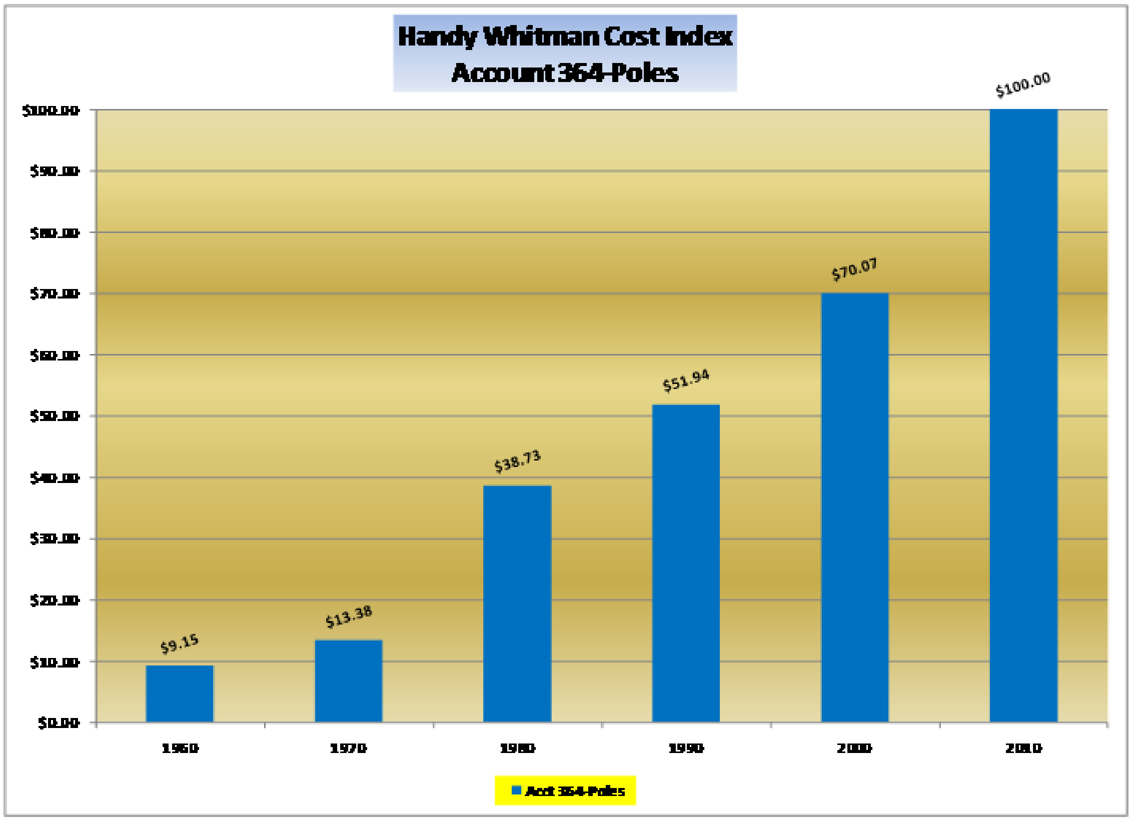
Q. You mentioned earlier that as Avista removes old worn-out equipment and replaces it with new, it results in higher overall costs. Why does this cause Avista's costs

to go up when the Company has a depreciation component included in retail rates to help cover the cost to replace facilities?

A. Avista's retail rates are cost-based, which means the prices customers are paying today for transformers, distribution poles, substations, and transmission lines, among other facilities, are based on the cost to install those facilities, in some cases, 40-, 50-, and even 60-years ago. The cost of the same equipment and facilities today are many times more expensive. The depreciation component built into retail rates today is based on the much lower cost to install those facilities many years ago. Therefore, the depreciation component in retail rates covers only a small fraction of the annual costs associated with the replacement of facilities.

Let me give you an example. The chart below provides a comparison of the relative cost of a distribution power pole in 2010, and for points in time 10-, 20-, 30-, 40- and 50-years ago. The chart shows that distribution poles are over ten times more expensive today than they were fifty years ago.

Illustration No. 1:



So when we replace a 50-year old distribution pole with a new one, that provides the same amount of service as the old one did, it results in a significant increase in costs.

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

The distribution pole located in Hayden Idaho, shown in Illustration No. 2 below, has deteriorated to the point where it needs to be replaced. We have over 240,000 distribution poles in our electric system. Based on a 40-year depreciable life, we would need to replace approximately 6,000 poles every year.

Illustration No. 2:

The replacement of distribution poles represents a fraction of the infrastructure that needs to be replaced each year. In the next five years, our relatively small Company will need to spend approximately $1.2 billion of capital on utility generation, transmission and distribution facilities and other requirements. This $1.2

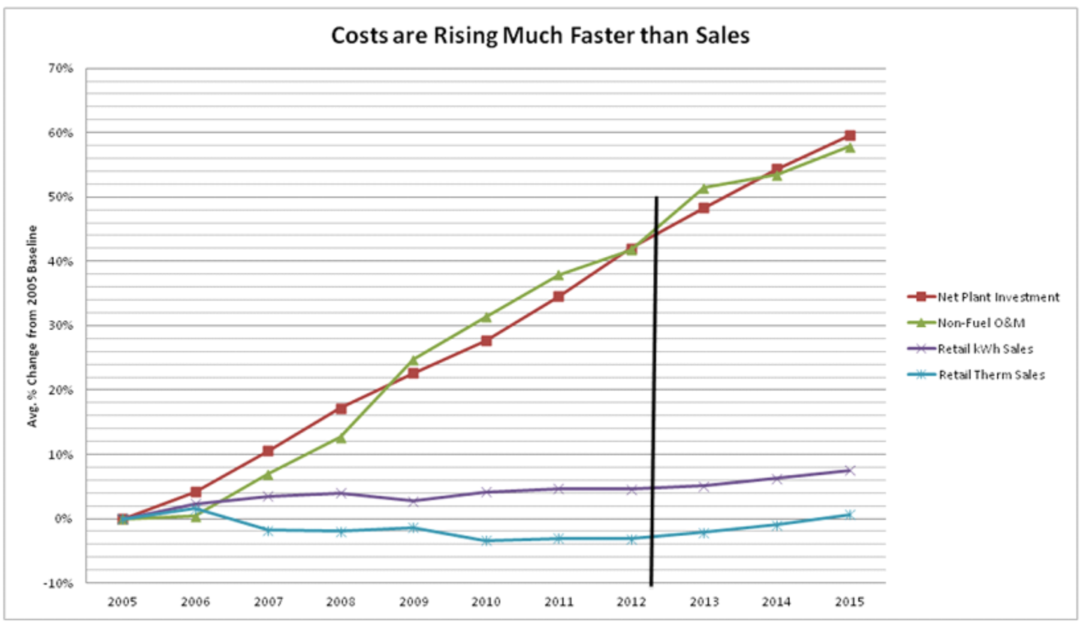
billion represents over 54% of the current rate base of approximately $2.2 billion dedicated to serving customers today. Utility equipment and facilities are big and expensive, and the required investment in new facilities is one of the major reasons that we need an increase in retail rates.

Q. Does growth in Avista's electric and natural gas retail sales revenue help cover the growth in net plant investment over time?

A. Only very little. Our investment in facilities used to serve customers is growing at a much faster pace than retail sales. The red line on the graph below shows the actual change in Avista's actual net plant investment from 2005 to 2011, and the forecasted change for 2012 to 2015. The purple and blue lines on the graph show the changes in retail kilowatt-hour (kWh) sales and retail therm sales, respectively, for the same time period. The chart clearly shows that net plant investment is growing at a much faster pace than sales. In fact, total therm sales in 2011 are about the same as in 2005, despite the addition of approximately 35,000 new customers being added during that timeframe. Total electric sales from 2005 to 2011 grew 5.76%, which is equal to only 0.96% per year.

The graph also shows this mismatch in new investment and new sales is forecasted to continue to the future. Therefore, retail rates must be increased to cover this increase in net plant investment, since sales growth is slow. The green line on the graph also shows that non-fuel operations and maintenance (O&M) expenses are growing at a faster pace than sales.

Illustration No. 3:



Q. What is driving the increase in non-fuel O&M costs?

A. Total utility non-fuel O&M increased approximately $72 million over the six-year period from 2005 to 2011. Although increasing labor and employee benefit costs, such as medical costs and retirement plan costs, are part of this increase, there have also been significant increases in other costs. In recent years there has been a significant increase in costly, mandatory requirements on utilities related to, among others things, reliability, environmental compliance, safety, and security. These mandates, together with litigation and other claims related to the ownership and operation of hydroelectric resources, have added, and continue to add, significant costs to run the utility. The penalties associated with non-compliance with some of these requirements can be as much as $1 million per day per violation. A few examples of the costs associated with these requirements are provided below:

1. **Hydro-electric Plant Relicensing** -- Under federal law we must have a license to operate our hydro-electric projects to serve customers. In recent years we negotiated new licenses for the projects on both the Clark Fork and Spokane rivers. The cost to gain new licenses was over $40 million up front and approximately $600 million over the life of the new licenses (45 to 50 years). These costs reflect aggressive bargaining on the part of the Company to keep the costs as low as possible. The requirements in the new long-term licenses address environmental and cultural protection while preserving our low-cost hydroelectric resources for the benefit of our customers, but they also represent significant increases in costs associated with owning and

operating our hydro-electric system. The increase in annual expenses from 2005 to 2011 is approximately $5 million.

2. **Compliance with Mercury Emissions** -- There are new mercury emission limitation requirements in Montana effective in 2010 related to our ownership interest in the Colstrip Generating Projects that required capital investment up front and annual costs of $1.5 million per year (Avista share).

3. **Federal Reliability Requirements** -- The Energy Policy Act of 2005 changed the national reliability standards for utilities, enforced by the North American Electric Reliability Corporation (NERC), from voluntary to mandatory beginning June 2007. Non-compliance with any of the requirements may result in monetary penalties up to $1 million per day per violation. The planning standards require utilities to perform planning studies at least 10 years in the future to ensure sufficient facilities are in place to avoid real time loss of customers or impact to neighboring utilities for the loss of transmission facilities. If a potential violation is observed in the future analysis, then Avista must develop a project plan to ensure that the violation is fixed prior to it becoming a reality. Avista budgets for future projects and ensures that the design and construction of the required projects are completed prior to the time they are needed. A Compliance Manager and Analyst was hired to coordinate the Company's compliance program. The Company also added an additional System Operator to allow adequate time for operator training, a Training Coordinator to train, track and manage all the extensive training needs and continuing education hours required for System Operators to maintain certification, and two additional engineers to support the new Critical Infrastructure Protection standards. Avista was required to construct a redundant Backup Control Center at a cost of approximately $6 million to meet one of the emergency operating standards. Avista also has approximately 25 subject matter experts that spend anywhere from 10-30% of their time working on compliance initiatives and documentation.

There are other significant cost increases from 2005 to 2011 in areas such as compliance with Sarbanes/Oxley and information technology related to cyber security and increased automation. Although we have taken extensive measures to ensure that the costs that we incur represent the most cost-effective and reliable way to continue to serve our customers, we continue to experience significant increases in annual operating expenses.

Q. Why is Avista experiencing low sales growth?

A. The slow growth in our sales is due in part to the continuing slow economy in our region. But the Company has also had aggressive energy efficiency programs in place for many years, which are designed to assist our customers in using less energy. While the partnership with our customers to conserve energy reduces the need to build new, expensive generating resources, it also limits the growth in revenue to cover increases in other investment and costs.

Q. Are other utilities experiencing the same kinds of issues related to the need to invest in utility infrastructure to maintain a reliable system, as well as increasing O&M costs?

A. Yes. Other electric utilities, whether consumer-owned or investor-owned, are also increasing their rates on a more regular basis, and this will likely continue into the near future. It is simply not possible to cuts costs enough to fully offset other cost increases and the costs associated with new plant investment.

Illustration No. 4 below identifies some of the recent rate increases for utilities in the Pacific Northwest that have either already occurred, or proposals that are currently pending.

Illustration No. 4:

Recent Rate Increase Activity				
Idaho	**Fuel**	**Case Status**	**Effective Date**	**Rate Increase**
Rocky Mountain Power	Electric	New Rates Approved	01-01-2012	7.8% (1)
Rocky Mountain Power	Electric	New Rates Approved	01-01-2013	7.2% (1)
Idaho Power	Electric	New Rates Approved	01-01-2012	4.1%
Oregon				
Eugene Water & Electric*	Electric	New Rates Approved	11-01-2012	5.0%
Eugene Water & Electric*	Electric	New Rates Approved	05-01-2012	5.5%
Idaho Power	Electric	New Rates Approved	03-01-2010	15.4%
Idaho Power	Electric	New Rates Approved	03-01-2012	4.5%
Oregon Trail Electric Coop*	Electric	New Rates Approved	10-01-2011	7.1%
Pacificorp	Electric	New Rates Approved	01-01-2011	8.5%
Pacificorp	Electric	Pending	01-01-2013	4.3%
NW Natural	Gas	Pending	11-01-2012	6.2%
Washington				
Benton County PUD	Electric	New Rates Approved	01-01-2012	6.0%
Benton County PUD	Electric	New Rates Approved	01-01-2011	8.0%
Clallum County PUD	Electric	New Rates Approved	01-01-2011	8.0%
Clallum County PUD	Electric	New Rates Approved	01-01-2012	3.0%
Clark County PUD	Electric	New Rates Approved	11-01-2011	3.9%
Cowlitz County PUD	Electric	New Rates Approved	01-01-2011	9.0%
Cowlitz County PUD	Electric	New Rates Approved	11-01-2011	17.5%
Grant County PUD	Electric	New Rates Approved	01-01-2012	6.8%
Inland Power & Light*	Electric	New Rates Approved	04-01-2012	6.0%
Pacific Power	Electric	New Rates Approved	01-01-2010	5.3%
Pacific Power	Electric	New Rates Approved	04-03-2011	10.7% (2)
Pacific Power	Electric	New Rates Approved	06-01-2012	1.5%
Puget Sound Energy	Electric	New Rates Approved	04-07-2010	2.8%
Puget Sound Energy	Electric	New Rates Approved	05-14-2012	3.2%
Snohomish County PUD*	Electric	New Rates Approved	04-01-2012	2.9%
Tacoma Power*	Electric	New Rates Approved	04-11-2012	5.8%
(1) Approved Increase was two-year rate plan, subject to compliance filing on November 1, 2012				
(2) Approved Increase was 10.7% (March 2011), subject to reconsideration				
*Source: E Source, February 2012, except where denoted by **				

III. SUMMARY OF RATE REQUESTS

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

A. Avista is proposing an increase in electric billed retail rates of $11.4 million or 4.6%. The Company's request is based on a proposed rate of return of 10.9% with a common equity ratio of 50.0% and a 8.46% return on equity.

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

Illustration No. 5:

Service Schedule	Proposed Increase in Billed Revenues
Residential Service Schedule 1	5.3%
General Service Schedules 11 & 12	4.1%
Large General Service Schedules 21 & 22	4.8%
Extra Large General Service Schedule 25	3.9%
Extra Large General Service Schedule 25P	3.3%
Pumping Service Schedules 31 & 32	5.7%
Street & Area Lighting Schedules 41-48	4.5%
Overall Increase	**4.6%**

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

A. With regard to natural gas, the Company is requesting an increase of $4.6 million or 7.3% of billed rates. As with the electric increase, the Company's request is based on a proposed rate of return of 10.9% with a common equity ratio of 50.0% and a 8.46% return on equity. The proposed rate increase for each natural gas customer class is shown in the illustration below:

Illustration No. 6:

Service Schedule	Proposed Increase in Billed Revenues
General Service Schedule 101	7.8%
Large General Service Schedule 111	5.7%
Interruptible Sales Service Schedule 131	5.9%
Transportation Service Schedule 146 (excluding natural gas costs)	12.8%
Overall Increase	**7.3%**

Q. What are the primary factors causing the Company's request for electric and natural gas rate increases in this filing?

A. Approximately 70% of the Company’s electric revenue requirement, and 48% for natural gas, is due to an increase in Net Plant Investment (including return on investment, depreciation and taxes, and offset by the tax benefit of interest).[1]

The remaining revenue requirement request is due to increases in distribution, operation and maintenance (O&M), and administrative and general (A&G) expenses for both electric and natural gas operations. However, the increased costs for electric operations are partially offset by a reduction in net power supply and transmission expenditures.

Also impacting the Company’s electric request, is the Energy Efficiency Load Adjustment (EELA), which increases the Company’s revenue requirement by approximately $1.6 million. This adjustment is explained by Mr. Ehrbar and Ms. Andrews.

Q. Is the Company proposing any changes to the cost of natural gas for its retail natural gas customers in this case?

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[1] These figures represent an approximate breakdown of amounts between the Company’s request in this case compared to that approved in the Company’s prior general rate case proceeding (Case Nos. AVU-E-11-01 and AVU-G-11-01). Due to the black-box nature of the Company’s prior settlement approved by the IPUC in Case Nos. AVU-E-11-01 and AVU-G-11-01, the Company made certain assumptions as to the amounts approved for various rate base and expense items in order to create the estimate of the breakdown of the rate increase request.

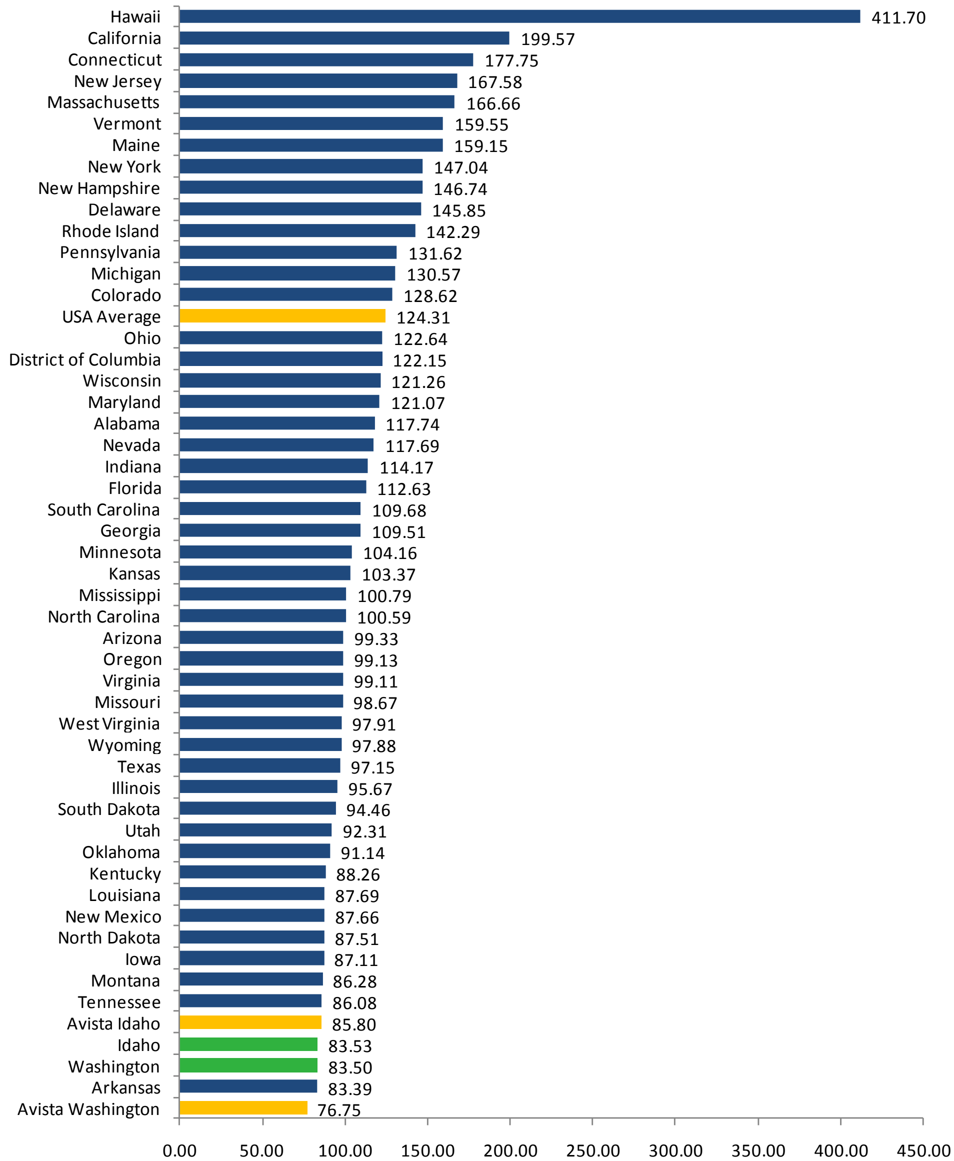
A. No. Avista is not proposing changes in this filing related to the cost of natural gas included in current rates for natural gas customers. Changes in natural gas costs are addressed in the annual Purchase Gas Adjustment (PGA) filings.

Q. How do Avista's electric retail rates compare to other utilities in the Northwest and across the country?

A. Edison Electric Institute prepares an annual comparison of residential electric bills for investor-owned utilities across the country. Illustration No. 7 provides a comparison of an Avista customer's monthly bill[2] in Idaho and Washington, with utility bills in other states. The chart shows that Avista's residential customers' rates are the lowest, or are among the lowest, in the Country.

[2] Based on a residential customer's average usage of 930 kWh per month.

Illustration No. 7:



Our relatively low retail rates are due in large part to a history of our Company aggressively pursuing the acquisition and preservation of a diversified portfolio of low cost resources for the benefit of our customers. This portfolio includes hydroelectric, wood-waste fired, natural gas-fired baseload, natural gas-fired peakers, and coal-fired generation, together with long-term purchases of power and an aggressive energy efficiency program.

Our low rates are also a result of Avista's aggressive efforts to control its costs, in order to keep retail rates as low as reasonably possible.

IV. COST MANAGEMENT AND EFFICIENCIES

Q. Is Avista continuing to pay particular attention to controlling its costs in order to mitigate the level of price increases to its customers?

A. Yes. In the last couple of years we have renewed our efforts to control our costs and improve efficiency, while continuing to meet our reliability and environmental compliance requirements, and preserving a high level of customer satisfaction. We are focused on long-term sustainable savings to continuously improve our service to customers and manage costs into the future.

Some of the measures from the last couple of years that we are continuing are briefly explained below, as well as a number of more recent initiatives.

Hiring Restriction

The Company continues to operate under a hiring restriction which requires approval by the Chairman/President/CEO, President of the Utility, the CFO, and the Sr. VP for Human Resources for all replacement or new hire positions.

Limitations on Capital Spending

Avista approved a lower capital budget than was requested by the Company's Engineering and Operations personnel. The original capital projects request for approval in 2012 consisted of projects totaling over $269 million. The Capital Prioritization Committee reduced the list of recommended projects by $19 million to the $250 million capital budget approved by the Board. In addition, the Company prioritized O & M facility maintenance and improvement projects and removed projects that could be delayed without safety or operational concerns.

Reduced Pension Benefit for New Hires

As part of the new contract negotiated with Avista's bargaining unit employees, the Defined Benefit Pension Plan's benefit formula was reduced by approximately 28% for all bargaining unit new hires, effective January 1, 2011. This change was earlier made for non-bargaining unit employees effective January 1, 2006.

Performance Excellence Initiative

In May 2010, the Company enlisted the help of Booz & Company to work with us on what we have referred to as Performance Excellence. They brought with them industry knowledge, expertise and a phased-approach. Phase 1 involved assessing and identifying Avista's top opportunities to better align our resources so we can run our business more efficiently, and be better prepared to meet customers' future needs for energy and energy information. In Phase 2 we designed changes to our processes to capture these opportunities. These changes encompassed six areas: T&D Work Estimating/scheduling, Supply Chain

Sourcing, Integrated Planning (Capital & O&M), Asset Management, Enterprise Technology, and Integrated Measurement(Metrics). In phase 3, teams completed work plans to implement the new designs. This work began in November 2010 and will be completed by year end. The changes have resulted in either improved efficiency, avoided costs, and/or enhanced customer service.

We recognize that our proposed rate increases will result in energy bills that will be more difficult for some of our customers to pay. I can assure you that we are not just sitting on the sidelines as our costs go up, as evidenced by the measures described above and others explained in more detail by Company witness Mr. Kopczynski.

V. COMMUNICATIONS WITH CUSTOMERS

Q. How is Avista communicating with its customers to explain what is driving increased costs for the Company?

A. The Company proactively communicates with its customers in a number of ways: electronic communications on issues of importance to them, customer forums, one-on-one customer interactions through field personnel and account representatives, bill inserts, social media, media contacts, group presentations, and through our employees' involvement in community, business and civic organizations, to name a few. We believe our communications are helping our customers and the communities we serve better understand the issues faced by the Company, such as increased environmental mitigation, infrastructure investment and generation constraints, all of which have led to higher costs for our customers.

We have listened to our customers and learned that they want information and conversations with Avista employees to better understand the choices they have to manage how they use energy and the forces that are impacting their energy prices.

That's why we are continuing to build on our communications, so that customers receive information directly from us on issues important to them. We are also continuing to engage employees in the Company in our efforts to more directly communicate with customers.

Q. How has the Company stepped-up communications with its customers?

A. One of the important principles in our intensified outreach is to meet customers where they gather. Our customer conversation uses traditional and non-traditional communication channels, including one-on-

one and group presentations, print, radio, website, newsletters, videos, social media and direct emails.

One important customer segment that we target are those customers who gather online. We are continuing to focus on our social media program with the Avista blog as our foundation. We also communicate on Twitter©, in online discussion forums when appropriate and this year have added the Avista Utilities Facebook© page. For customers who want a more private online conversation, we offer customers a conversation email account to make sure they're comfortable communicating with us.

One important customer communication channel is our website at www.avistautilities.com. A section focusing on rates provides customers a video on how rates are set, including the regulatory process; other videos focus on the components of general rate requests, and provided additional information on general rate requests.

Our employees provide excellent customer service, and this focus on communicating with our customers includes providing them messaging and new tools and training to make it easier to have conversations about Avista with friends, family and customers. We are finding that once a customer talks with one of our employees and has the opportunity to voice their concerns and receive answers to their questions, their satisfaction level increases.

We are continuing our focus on informing customers of the many programs we offer to provide assistance in managing their energy bills, and ensuring that our employees are equipped to engage in these conversations.

Q. What are some of the topic areas you are focusing on as you communicate with your customers?

A. Among other areas, we are increasing our efforts to directly address some of the issues raised by our customers in their comments to the Commission. For example, our proxy statement issued each year prior to our annual shareholder meeting includes compensation information for each of our top five executive officers. This information is usually published in our local newspaper, which triggers comments from our customers to the Commission, letters to the editor, and a flurry of activity on social media.

Many of the comments suggest that our customers believe all, or the majority, of the compensation reflected in the proxy is being included in the retail rates approved by the Commission. Although the stakeholders involved in the ratemaking process know this is not true, many of our customers do not. So we are providing more information to our customers. None of the long-term incentive compensation is included in customers' rates, and even a portion of the base salary of officers is allocated to our subsidiary operations and is not paid by our customers. Approximately 42% of the total executive officer salaries and short term incentives are included in retail rates for customers in Idaho, Washington, and Oregon. The remainder is born by shareholders. Ms. Andrews provides additional details related to Avista's compensation for all employees, including officers.

Q. Is Avista providing additional information to customers related to Company profits?

A. Yes. Following each quarter we issue an earnings release that details the profits for Avista Corp., including the utility and our subsidiary operations. Some of the comments from our customers, in response to the earnings release, suggest that they believe the profits are excessive, or represent dollars that are over and above what is needed to own and operate the utility. So we are making more information available to explain that the utility profit is not excess profit, but represents a rate of return for our common equity shareholders for the use of their money to finance the utility infrastructure used to provide service to customers, and therefore, it is an essential cost of owning and operating the utility.

Q. Are there any other topics the Company is emphasizing in its communications?

A. Yes. There are other related areas that I have already addressed in my testimony, and I will not belabor them here. Some of our customers believe that our annual depreciation expense should cover the cost to replace our old facilities, and others have wondered why we are still talking about replacing our aging infrastructure when we did that last year and the year before.

Therefore, we are providing more information to our customers to explain, as I illustrated earlier, that the cost of new facilities is multiple times more expensive than the old facilities, and the annual depreciation expense we are currently collecting in retail rates is well below what is needed to cover the cost of new facilities. And with each passing year, our facilities are getting older and we need to replace some of them every year to maintain a safe, reliable system.

We believe our communication efforts; including both the content as well as the avenues in which we are communicating, are helping more customers better understand why we need to increase retail rates on a regular basis.

VI. CUSTOMER SATISFACTION

Q. What kind of feedback are you receiving from customers related to customer satisfaction?

A. I am pleased with the dedication of Avista Utilities' employees and their commitment to provide quality service to our customers. As I indicated earlier, while we continue to maintain tight controls on capital and O&M budgets, our customer service surveys indicate that customer satisfaction remains high. Our overall customer satisfaction from our voice-of-the-customer surveys in the second quarter of 2012 was 93% in our Idaho, Washington, and Oregon operating divisions. This rating reflects a positive experience for customers who have contacted Avista related to the customer or field service they received. These results can be achieved only with very committed and competent employees.

VII. CUSTOMER SUPPORT PROGRAMS

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

A. More than 360,450 electric and 320,741 natural gas customers in three states rely on Avista for their electricity and natural gas services. One of the challenging aspects of the utility business is to receive payment from those least able to pay. In the past few years, this challenge has broadened with the serious economic impact the national recession has had on individuals and businesses.

Avista is committed to reducing the burden of energy costs for our customers most affected by rising energy prices, including low income individuals and families, seniors, disabled and vulnerable customers. To assist our customers' in their ability to pay, the Company focuses on actions and programs in four primary areas: 1) advocacy for and support of programs providing direct financial assistance; 2) low income and senior outreach programs; 3) energy efficiency and energy conservation education; and 4) support of community programs that increase customers' ability to pay basic costs of living.

In the 2011/2012 heating season, 23,695 Idaho customers received approximately $4 million in various forms of energy assistance (Federal LIHEAP program, Project Share, and local community funds). Some of the key programs that we offer or support are as follows:

1. **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 2011, Avista Utilities' customers donated $302,505 on a system-wide basis, of which $82,009 was directed to Idaho Community Action Agencies. In addition, the Company contributed $61,800 to Project Share for the benefit of Idaho customers in 2011.

2. **Comfort Level Billing.** The Company offers the option for all customers to pay the same bill amount each month of the year by averaging their annual usage. Under this program, customers can avoid unpredictable winter heating bills.

3. **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.

These programs and the partnerships we have formed with community action agencies have been helpful to customers who often have nowhere else to go. Company witness Mr. Kopczynski provides additional detail in his testimony concerning these and other programs designed to assist customers.

VIII. OTHER COMPANY WITNESSES

Q. Would you please provide a brief summary of the testimony of the other witnesses representing Avista in this proceeding?

A. Yes. The following additional witnesses are presenting direct testimony on behalf of Avista:

Mr. Mark Thies, Senior Vice President and Chief Financial Officer, will provide a financial overview of the Company and will explain the overall rate of return proposed by the Company in this filing for its electric and natural gas operations. The proposed rate of return is derived from Avista's total cost of long-term debt and common equity, weighted in proportion to the proposed capital structure.

He will address the proposed capital structure, as well as the proposed cost of total debt and equity in this filing. In brief, he will provide information that shows:

- Avista's plans call for significant capital expenditure requirements for the utility over the next two years to assure reliability in serving our customers and meeting customer growth. Capital expenditures of approximately $500 million are planned for 2012-2013 for customer growth, investment in generation upgrades and transmission and distribution facilities, as well as necessary maintenance and replacements of our natural gas utility systems. Capital expenditures of approximately $1.2 billion are planned for the five-year period ending December 31, 2016. Avista needs adequate cash flow from operations to fund these requirements, together with access to capital from external sources under reasonable terms.

- Avista's corporate credit rating from Standard & Poor's (S&P) is currently BBB and from Moody's Investors Service (Moody's) it is Baa2. Avista must operate at a level that will support a solid investment grade corporate credit rating in order to access capital markets at reasonable rates, which will result in lower long-term borrowing costs to customers. A supportive regulatory environment is an important consideration by the rating agencies when reviewing Avista. Maintaining solid credit metrics and credit ratings will also help support a stock price necessary to issue equity under reasonable terms to fund capital requirements.

- The Company is proposing an overall rate of return of 8.46%, including a 50.0% equity ratio and a 10.90% return on equity. Our proforma cost of debt is 6.02%.

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

- In order to reflect the risks and prospects associated with Avista's jurisdictional utility operations, his analyses focused on a proxy group of twenty-six other utilities with comparable investment risks. Consistent with the fact that utilities must compete for capital with firms outside their own industry, he also references a proxy group of comparable risk companies in the non-utility sector of the economy;
- Because investors' required return on equity is unobservable and no single method should be viewed in isolation, he applied the DCF, CAPM, and risk premium methods, as well as the expected earnings approach, to estimate a fair ROE for Avista;
- Based on the results of these analyses, and giving less weight to extremes at the high and low ends of the range, Dr. Avera concluded that the cost of equity for the proxy group of utilities is in the 10.0 percent to 11.4 percent range, or 10.2 percent to 11.6 percent after incorporating an adjustment to account for the impact of common equity flotation costs; and,
- Avista is requesting a fair ROE of 10.9 percent, which is equal to the midpoint of his recommended range. Considering capital market expectations, the exposures faced by Avista, and the economic requirements necessary to maintain financial integrity and support additional capital investment even under adverse circumstances, it is Dr. Avera's opinion that 10.9 percent represents a fair and reasonable ROE for Avista.

Mr. Robert Lafferty, Director of Power Supply, will provide an overview of Avista's resource planning and power supply operations. This includes summaries of the Company's generation resources, the current and future load and resource position, and future resource plans, including the power purchase agreement with Palouse Wind, LLC. As part of an overview of the Company's risk management policy, he will provide an update on the Company's hedging practices. He will address hydroelectric and thermal project upgrades, followed by an update on recent developments regarding hydro licensing.

Mr. Clint Kalich, Manager of Resource Planning & Power Supply Analyses, will describe the Company's use of the AURORA$_{XMP}$ dispatch model, or "Dispatch Model." He will explain the key assumptions driving the Dispatch Model's market forecast of electricity prices. The discussion includes the variables of natural gas, Western Interconnect loads and resources, and hydroelectric conditions. He will also describe how the model dispatches its resources and contracts to maximize customer benefit and tracks their values for use in pro forma calculations. Finally, he will present the modeling results provided to Company witness Mr. Johnson for his power supply pro forma adjustment calculations.

Mr. William Johnson, Wholesale Marketing Manager, will 1) identify and explain the proposed normalizing and pro forma adjustments to the July 2011 through June 2012 test period power supply revenues and expenses, and 2) describe the proposed level of expense and load change adjustment rate for Power Cost Adjustment (PCA) purposes, using the pro forma costs proposed by the Company in this filing.

Mr. Steve Harper, Director of Gas Supply, will describe Avista's natural gas procurement planning process for retail distribution service, and provide an overview of the Company's 2012 Natural Gas Integrated Resource Plan development.

Mr. Don Kopczynski, Vice President of Energy Delivery, will describe Avista's electric and natural gas energy delivery facilities and operations, and recent efforts to increase efficiency and improve customer service. He will describe Avista's efforts to control costs, increase efficiency, and improve customer service. He will also discuss the replacement of the Company's legacy customer information system (CIS), as well as summarize Avista's customer support programs in Idaho. Finally, he will address the Company's plans to replace Aldyl A piping in our natural gas distribution system.

Mr. Scott Kinney, Director, Transmission Operations, describes Avista's pro forma period transmission revenues and expenses. He will also discuss the Transmission and

Distribution expenditures that are part of the capital additions, as well as projects associated with the Company's Asset Management Program.

Ms. Elizabeth Andrews, Manager of Revenue Requirements, will cover accounting and financial data in support of the Company's need for the proposed increase in rates. She will explain pro formed operating results, including expense and rate base adjustments made to actual operating results and rate base.

Mr. Dave DeFelice, Senior Business Analyst, will cover the Company's proposed pro forma adjustments for capital investments in utility plant for the 2013 rate period. In addition, his testimony and exhibits will cover the Company's proposed changes in depreciation rates pertaining to electric and natural gas plant-in-service using the recently completed depreciation study.

Ms. Tara Knox, Senior Regulatory Analyst, will cover the Company's electric and natural gas cost of service studies performed for this proceeding. Additionally, she is sponsoring the electric and natural gas revenue normalization adjustments to the test year results of operations and the proposed Load Change Adjustment Rate (LCAR) to be used in the Power Cost Adjustment (PCA).

Mr. Patrick Ehrbar, Manager of Rates and Tariffs, discusses the spread of the proposed annual revenue changes among the Company's general service schedules as well as the proposed rate design within each schedule. He explains, among other things, that:

- The proposed increase in electric base rates is 4.6%, which consists of an increase in electric base retail revenues of $11.4 million.
- The monthly bill for a residential customer using an average of 930 kWhs per month would increase from $78.69 to $82.89 per month, an increase of $4.20 or 5.3%.
- The proposed natural gas annual revenue increase in base rates is $4.6 million, or 7.2%.
- The monthly bill for a residential customer using 60 therms per month would increase from $52.55 to $56.67 per month, an increase of $4.12 or 7.8%.

In addition, he will provide further information related to the Company's proposed Energy Efficiency Load Adjustment, and provide an overview of the items required of the Company in Order No. 32371, and the related Settlement Stipulation, in Case Nos. AVU-E/G-11-01.

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

A. Yes.

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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION	)	CASE NO. AVU-E-12-08
OF AVISTA CORPORATION FOR THE	)	CASE NO. AVU-G-12-07
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)

Description of Avista Utilities

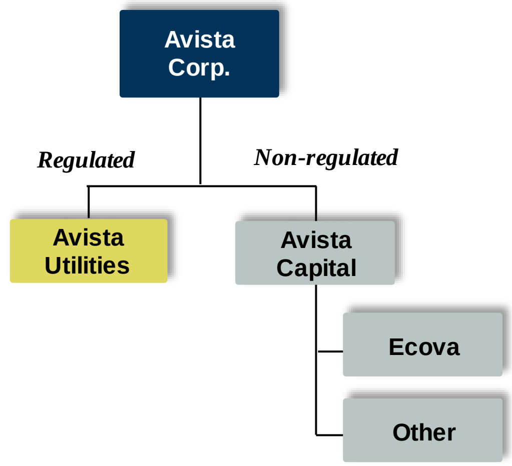
Avista Utilities provides electric and natural gas service within a 26,000 square mile area of eastern Washington and northern Idaho[1]. Of the Company's 360,450 electric and 320,741 natural gas customers (as of December 31, 2011), 236,623 and 149,161, respectively, were Washington customers. The Company, headquartered in Spokane, also provides natural gas distribution service in southwestern and northeastern Oregon. A map showing Avista's electric and natural gas service areas is provided in Exhibit 1, Schedule 2.

As of December 31, 2011, Avista Utilities had total assets (electric and natural gas) of approximately $4.1 billion (on a system basis), with electric retail revenues of $736 million (system) and natural gas retail revenues of $352 million (system). As of December 2011, the Utility had 1,594 full-time employees.

[1] Avista also serves approximately 20 retail electric customers in western Montana.

Description of Avista's subsidiary businesses

Avista Corp.'s primary subsidiary is the information and technology business, Ecova, described below, which is headquartered in Spokane, Washington. A diagram of Avista's corporate structure is provided below:



Advantage IQ, and Ecos, an Advantage IQ subsidiary delivering electric and natural gas utility demand-side management services, joined forces to become Ecova in October 2011. Ecova provides utility expense management and energy management solutions to multi-site companies across North America. This includes more than 450,000 business sites. Ecova clients include Fortune 1000 companies such as GameStop, Panda Restaurant Group, Petco, Shell, Staples and, many North American electric and natural gas utilities. Avista currently holds a 79.2% share in Ecova, which is held under Avista Capital.

Avista's Electric and Natural Gas Service Areas

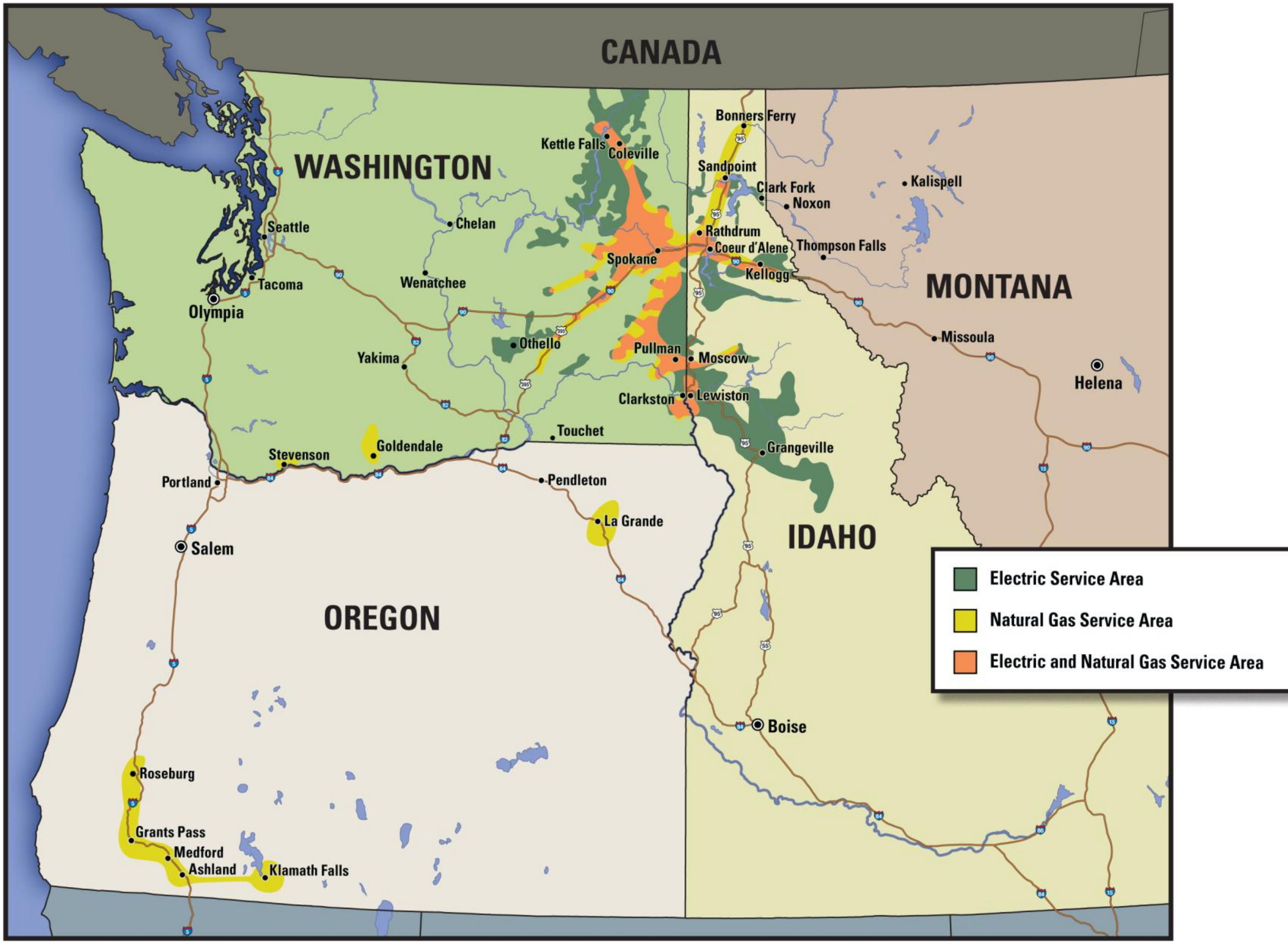


Exhibit No. 1
Case No. AVU-E-12-08/AVU-G-12-07
S. Morris, Avista
Schedule 2, p. 1 of 1