

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-11_____

DOCKET NO. UG-11_____

DIRECT TESTIMONY OF

SCOTT L. MORRIS

REPRESENTING AVISTA CORPORATION

1 **I. INTRODUCTION**

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

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

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

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

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

18 I am a member of the Western Energy Institute board of directors, a member of the
19 Gonzaga University board of trustees, a member of Edison Electric Institute board of directors, a
20 member of the American Gas Association board of directors, a member of ReliOn board of
21 directors, and board director of the Washington Roundtable. On January 1, 2011, I was
22 appointed to the Federal Reserve Bank of San Francisco, Seattle Branch board of directors. I also
23 serve on the board of trustees of Greater Spokane Incorporated.

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

2 A. In my testimony, I will first explain why Avista is requesting another rate increase
3 in this case. I will explain that much of our need for rate relief is driven primarily by the
4 increased costs associated with the need to expand and replace our aging utility infrastructure,
5 and our obligation to reliably serve customers. As a regulated company, we operate under state
6 and federal mandates that obligate us to serve every customer that requests service, and to serve
7 them reliably. Although we continue to make changes to our business to operate more
8 efficiently, it is simply not possible to cut costs enough to offset the increased costs to expand
9 and replace our aging infrastructure to comply with our obligation to serve.

10 My testimony will provide an overview of Avista Corporation. I will also summarize the
11 Company's specific electric and natural gas rate requests in this filing, and the primary factors
12 driving the Company's need for general rate relief. I will also discuss some of the measures we
13 have taken to cut costs, as well as initiatives to increase operating efficiencies in an effort to
14 mitigate future cost increases. I will briefly explain the Company's customer support programs
15 in place to assist our customers, as well as our communications initiatives to help customers
16 better understand the changes in costs that are causing our rates to increase.

17 Finally, I will introduce each of the other witnesses providing testimony on the
18 Company's behalf.

19
20
21
22
23

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

2	<u>Description</u>	<u>Page</u>
3	I. Introduction	1
4	II. Why Is Avista Requesting Another Rate Increase	3
5	III. Overview of Avista	10
6	IV. Summary of Rate Requests	13
7	V. Cost Management and Efficiencies	18
8	VI. Communications with Customers	20
9	VII. Customer Satisfaction	22
10	VIII. Customer Support Programs	23
11	IX. Other Company Witnesses	25

12

13

14

Q. Are you sponsoring any exhibits in this proceeding?

15

16

17

A. Yes. I am sponsoring Exhibit No.__(SLM-2), pages 1 and 2. Page 1 is a diagram of Avista’s corporate structure; and page 2 includes a map showing Avista’s electric and natural gas service areas. This exhibit was prepared under my direction.

18

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

19

20

A. Avista is requesting an overall electric billed rate increase of 8.7%, and a natural gas billed rate increase of 4.0%.

21

22

II. WHY IS AVISTA REQUESTING ANOTHER RATE INCREASE

23

24

Q. Why is Avista requesting another rate increase following the recent increases that were approved effective December 1, 2010?

25

26

A. As a regulated monopoly there are two major requirements that are having a significant effect on the need to change retail rates: 1) Avista has an obligation to safely and

1 reliably serve every customer that requests service, and 2) the costs associated with replacing our
2 aging infrastructure are substantial.

3 **Q. How does the “obligation to serve” create a need to increase rates?**

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

10 We occasionally receive comments from some of our customers to the effect that Avista
11 should cut its costs, and “tighten its belt” like other businesses are having to do in these difficult
12 economic circumstances, and keep retail rates the same. We hear those comments and take them
13 to heart, and have taken steps to do so. But at the same time we are not like other businesses.
14 Without the obligation to serve, we could consider refusing to hook up some new customers,
15 because it could avoid an increase in costs to our existing customers. Without an obligation to
16 serve, we could consider no longer serving some of the more remote, more costly areas to
17 provide service, which would allow us to avoid further investment, and reduce labor and other
18 operating costs. Unregulated businesses have the opportunity to shut down aging facilities or
19 under-producing retail outlets, eliminate product lines, and cut back on investment and
20 maintenance. We do not.

21 Please don’t misunderstand my point -- we do have opportunities to cut back on
22 investment and operating costs, and we have where prudent to do so. I will address that later in
23 my testimony. But those opportunities are limited by our obligation to safely and reliably serve

1 all customers, and our obligation to comply with numerous mandatory state and federal
2 requirements. We simply don't have the choice to say no to new customers, no to maintaining a
3 safe, reliable system, and no to mandatory requirements. Although we have taken measures to
4 ensure that the costs that we incur represent the most cost-effective and reliable way to continue
5 to serve our customers, we continue to experience significant increases in costs.

6 **Q. How does Avista's need to replace its aging infrastructure create a need to**
7 **change retail rates?**

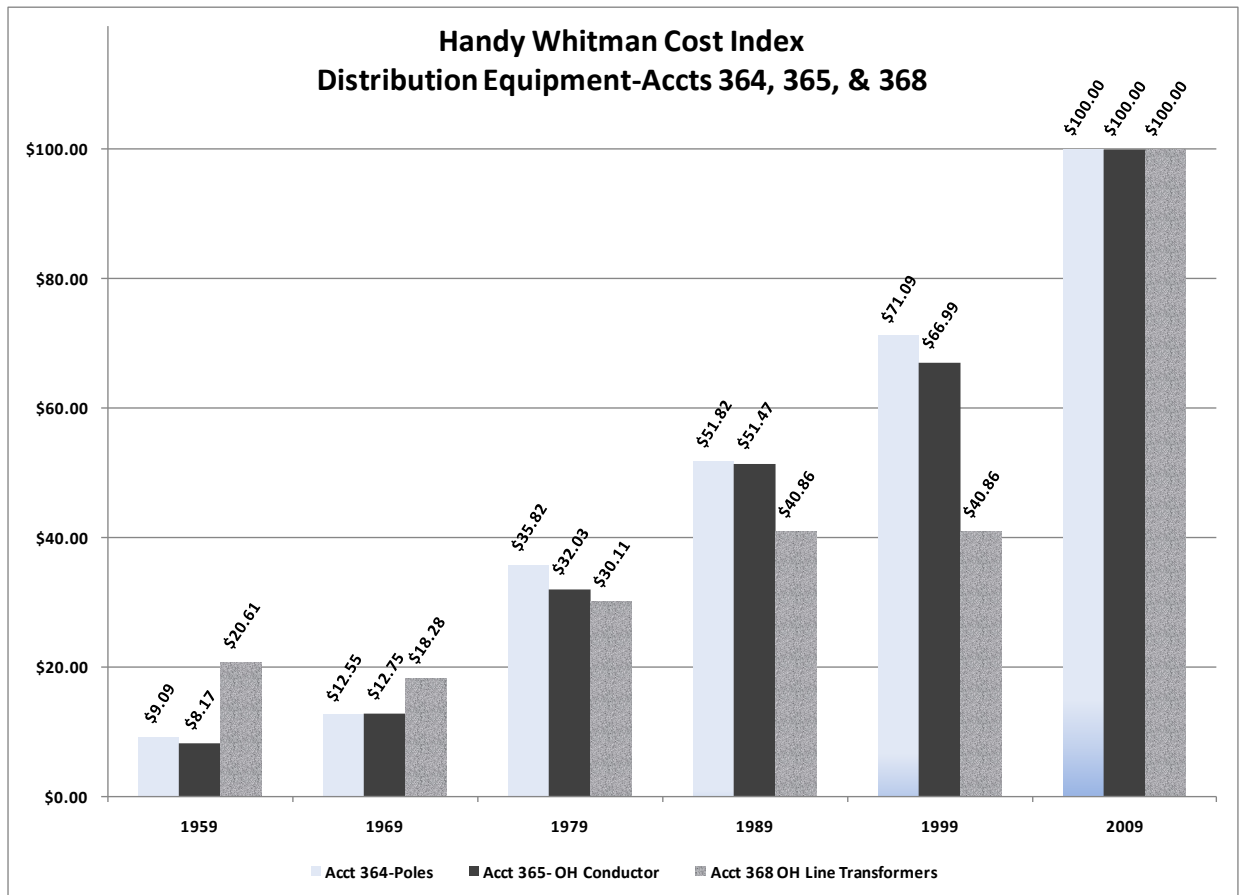
8 A. Avista's retail rates are cost-based, which means the prices customers are paying
9 now for transformers, distribution poles, substations, and transmission lines, among other
10 facilities, are based on the cost to install those facilities, in some cases, 40, 50, and even 60 years
11 ago. The cost of the same equipment and facilities today are many times more expensive than
12 those facilities installed years ago. In order for us to continue to meet our obligation to provide
13 reliable service, we must replace this aging infrastructure over time. When we replace the old
14 equipment with new, it results in increased costs, which leads to the need to increase rates to
15 cover those costs.

16 Using the Handy-Whitman Index Manual¹, the Company analyzed several major
17 categories of plant. The following chart shows what distribution equipment costs have been
18 historically on a relative scale. For example, distribution poles fifty years ago would cost 9% of
19 the current replacement cost. The chart shows that the cost of the same equipment and facilities

¹ "The Handy-Whitman Index of Public Utility Construction Costs", published by Whitman, Requardt and Associates, Baltimore, Maryland. The Handy-Whitman Indexes of Public Utility Construction Costs show the level of costs for different types of utility construction. Separate indices are maintained for general items of construction, such as reinforced concrete, and specific items of material or equipment, such as pipe or turbo-generators. Handy-Whitman Index numbers are used to trend earlier valuations and original cost at prices prevailing at a certain date.

1 that are being added today are many times more expensive than those facilities installed in the
 2 past.

3
 4 **Illustration No. 1:**



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

19 **Q. Can you give a sense for the scope of the investment necessary to replace the**
 20 **utility infrastructure over time?**

21 A. Yes. For illustrative purposes, we have over 240,000 distribution poles and
 22 34,500 transmission wood and steel poles in our electric system. If, as an example, we were to

1 replace our distribution poles on a fifty-year cycle, it would require us to replace approximately
2 4,800 poles every year. The distribution pole and transformer shown below are pre-1950, and
3 the pole has deteriorated to the point where it needs to be replaced.

4 **Illustration No. 2:**



13
14 We have many of these on our system and they must be replaced. The replacement of
15 distribution poles represents a fraction of the infrastructure that needs to be replaced each year.
16 In the next five years, our relatively small Company will need to spend approximately \$1.2
17 billion of capital on utility facilities and other requirements. This \$1.2 billion represents
18 approximately 57% of the current rate base of approximately \$2.1 billion dedicated to serving
19 customers today. Utility equipment and facilities are big and expensive, and the required
20 investment in new facilities is one of the major reasons that we need an increase in retail rates.

21 **Q. Doesn't the level of depreciation each year cover the cost to replace these**
22 **facilities?**

1 A. No. Some of our customers suggest that we set aside dollars every year to replace
2 these facilities over time – and we do. That is what depreciation is for. The level of annual
3 depreciation dollars built into retail rates is available to the Company to replace aging facilities
4 over time. However, as I explained above, because the annual depreciation is based on the actual
5 historical costs of our electric system and the cost of those facilities decades ago were orders of
6 magnitude less than what it costs to build facilities today, the annual depreciation falls
7 dramatically short of providing the funds necessary to replace facilities today. Therefore, retail
8 rate increases are necessary to cover the higher costs to replace facilities. As Ms. Andrews
9 explains in her testimony, over half of our rate increase request is based on new capital
10 investment and the return on investment. Gross plant in service included in this case increased
11 by approximately \$130.8 million (Washington share) compared to that currently included in
12 rates.

13 **Q. Is the Company experiencing increases in other cost categories such as O&M**
14 **and A&G costs?**

15 A. Yes. A number of expense items have increased since the Company's last general
16 rate case. In particular, the Company pro formed in the increased costs associated with electric
17 distribution vegetation management costs of \$2.1 million, as discussed by Company witness Mr.
18 Kinney. These additive costs are necessary to keep the trees out of our power lines. We are also
19 experiencing increased labor and medical expenses.

20 **Q. Why has it been necessary for Avista to request a rate increase each year for**
21 **a number of years?**

22 A. The current ratemaking process does not allow costs beyond the next year to be
23 included in rates. In addition, processing a rate request in Washington can take up to eleven

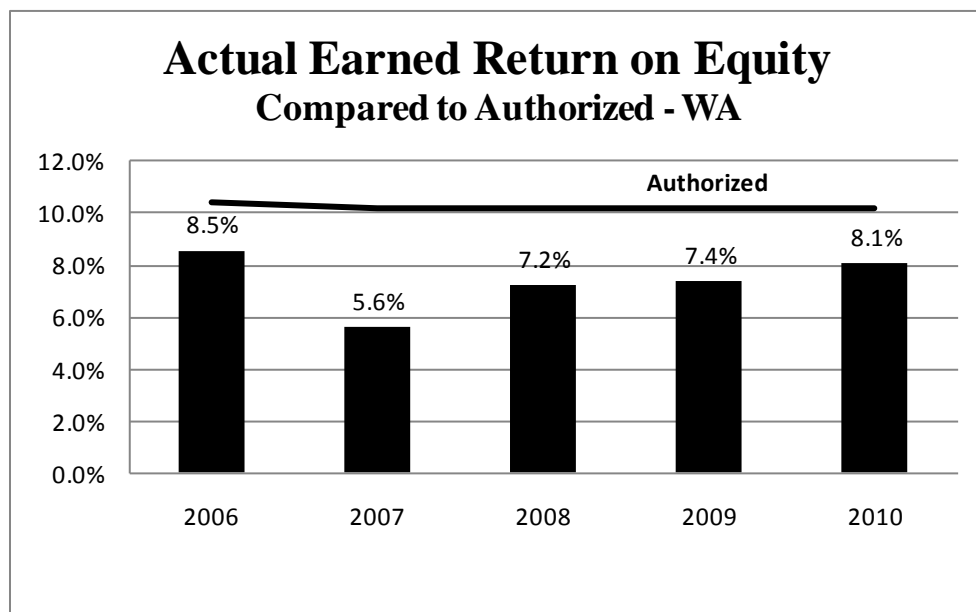
1 months, which means the only way to recover increasing costs to serve customers is to file a new
2 rate request every year.

3 Since it is simply not possible to cuts costs enough to fully offset other cost increases and
4 the costs associated with new plant investment, we have no choice but to request rate increases
5 on a regular basis. Avista is not alone in that regard; other electric utilities, whether publicly-
6 owned or investor-owned like Avista, are also increasing their rates on a more regular basis, and
7 this will likely continue into the near future.

8 The table below identifies recent rate increases for utilities in the Pacific Northwest that
9 have either already occurred, or proposals that are currently pending.

Recent Rate Increase Activity				
Idaho	Fuel	Case Status	Effective Date	Rate Increase
Rocky Mountain Power	Electric	New Rates Approved	06-28-2010	6.8%
Oregon				
Idaho Power	Electric	New Rates Approved	03-01-2010	15.4%
Pacificorp	Electric	New Rates Approved	02-01-2010	4.4%
Pacificorp	Electric	New Rates Approved	01-01-2011	8.4%
Washington				
Benton County PUD	Electric	Pending	n/a	8.0%
Clallum County PUD	Electric	New Rates Approved	01-01-2011	8.0%
Clark County PUD	Electric	New Rates Approved	09-01-2010	4.3%
Cowlitz County PUD	Electric	New Rates Approved	01-01-2011	9.0%
Grant County PUD	Electric	New Rates Approved	04-01-2010	4.5%
Okanogan County PUD	Electric	Pending	n/a	6.5%
Pacific Power	Electric	New Rates Approved	01-01-2010	5.3%
Pacific Power	Electric	Pending	04-03-2011	10.7%*
Puget Sound Energy	Electric	New Rates Approved	04-07-2010	2.8%
* Approved Increase was 10.7% (March 2011), subject to reconsideration				
<i>Source: E Source, January 2011</i>				

1 Mr. Thies, in his testimony, explains that even though we have filed rate cases each year
 2 for a number of years, our actual earned return on equity in Washington has been well below the
 3 return the Commission has determined to be reasonable. What that means is we have been
 4 unable to include in retail rates the costs to serve customers in Washington for that one upcoming
 5 year. The bar chart below shows the actual earned return on equity for Avista's Washington
 6 electric and natural gas utility operations, as compared to the return on equity authorized by the
 7 UTC.



17 Delays in filing or processing a rate case can cause our actual earned return to drop, erode
 18 our financial strength, and compromises our ability to raise capital on reasonable terms.

19 **III. OVERVIEW OF AVISTA**

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

22 A. Our strategy continues to focus on our energy and utility-related businesses, with
 23 our primary emphasis on the electric and natural gas utility business. There are four distinct

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

8 **Q. Please briefly describe Avista's subsidiary businesses.**

9 A. Avista Corp.'s primary subsidiary is the information and technology business,
10 Advantage IQ, described below, which is headquartered in Spokane, Washington. A diagram of
11 Avista's corporate structure is provided on page 1 of Exhibit No. ___(SLM-2).

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

13 A. Advantage IQ provides utility expense management and energy management
14 solutions to multi-site companies across North America. Avista currently holds a 75.75% share
15 in Advantage IQ, which is held under Avista Capital.

16 Advantage IQ's invoice processing, auditing and payment services, coupled with energy
17 procurement, comprehensive reporting and advanced analysis, provide the critical data clients
18 need to balance the financial, social and environmental aspects of doing business. Customers
19 include, CSK Auto, Jack in the Box, Staples, and Big Lots, to name a few.

20 As part of the expense management services, Advantage IQ analyzes and audits invoices,
21 then presents consolidated bills on-line, and processes payments. Information gathered from

1 invoices, service providers and other customer-specific data allows Advantage IQ to provide its
2 clients with in-depth analytical support, real-time reporting and consulting services.

3 Advantage IQ also provides comprehensive energy efficiency program management
4 services to utilities across North America. As part of these management services, Advantage IQ
5 helps utilities develop and execute energy efficiency programs with a complete turn-key solution.

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

7 A. Avista Utilities provides electric and natural gas service within a 26,000 square
8 mile area of eastern Washington and northern Idaho². Of the Company's 358,982 electric and
9 319,141 natural gas customers (as of December 31, 2010), 235,820 and 148,247, respectively,
10 were Washington customers. The Company, headquartered in Spokane, also provides natural gas
11 distribution service in southwestern and northeastern Oregon. A map showing Avista's electric
12 and natural gas service areas is provided on page 2 of Exhibit No. ___(SLM-2).

13 As of December 31, 2010, Avista Utilities had total assets (electric and natural gas) of
14 approximately \$3.9 billion (on a system basis), with electric retail revenues of \$683 million
15 (system) and natural gas retail revenues of \$314 million (system). As of December 2010, the
16 Utility had 1,554 full-time employees.

17 Avista has a long history of innovation and environmental stewardship. At the turn of the
18 20th century, the Company built its first renewable hydro-electric generation plant on the banks
19 of the Spokane River. In the 1980's, Avista developed an award-winning biomass plant (Kettle
20 Falls) that generates energy from wood-waste.

21
22

² Avista also serves approximately 20 retail electric customers in western Montana.

IV. 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 \$38.3 million or 8.7%. The Company's request is based on a proposed rate of return of 8.23% with a common equity ratio of 48.04% and a 10.9% return on equity.

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

Illustration No. 3:

<u>Service Schedule</u>	<u>Proposed Increase</u>
Residential Service Schedule 1	9.1%
General Service Schedules 11 & 12	8.4%
Large General Service Schedules 21 & 22	8.7%
Extra Large General Service Schedule 25	7.5%
Pumping Service Schedules 31 & 32	9.1%
Street & Area Lighting Schedules 41-48	<u>8.6%</u>
Overall Increase	8.7%

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 \$6.2 million or 4.0% of billed rates. As with the electric increase, the Company's request is based on a proposed rate of return of 8.23% with a common equity ratio of 48.04% and a 10.9% return on equity. The proposed rate spread for each natural gas customer class is shown in the illustration below:

Illustration No. 4:

<u>Service Schedule</u>	<u>Proposed Increase</u>
General Service Schedule 101	5.1%
Large General Service Schedule 111	1.1%
Extra Large General Service Schedule 121	1.5%
Interruptible Sales Service Schedule 131	1.9%
Transportation Service Schedule 146	
(excluding natural gas costs)	<u>4.4%</u>
Overall Increase	4.0%

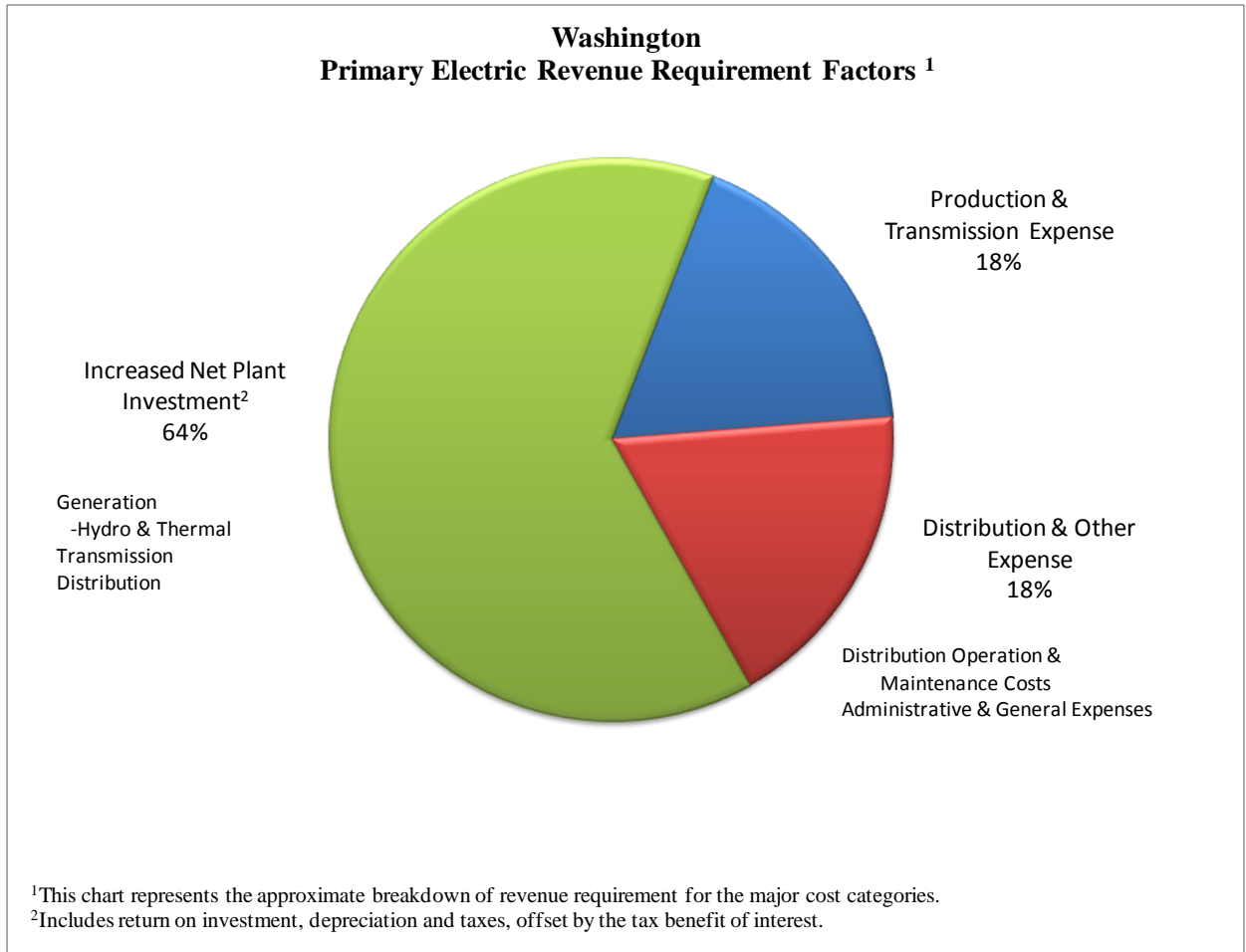
Q. What are the primary factors causing the Company's request for an electric rate increase in this filing?

A. The Company's electric general rate case is based on a 12-months ending December 31, 2010 test period, and a January 1, 2012 through December 31, 2012 pro forma rate period. The Company's electric request is driven primarily by three components or segments shown in Illustration No. 5 below.

The first segment, representing increases in Net Plant Investment and return on investment, comprises approximately 64% of the overall request, and is due primarily to an increase of approximately \$71.7 million in net rate base for the Washington jurisdiction.

The next two segments, each representing 18% of the Company's overall request, includes the increases in Production and Transmission Expense, related to increases in net power supply and transmission expenditures, and the Distribution, O&M and A&G Expense. This latter segment includes increases to all other operating categories, such as distribution expenses, including increases in vegetation management expenses, and administrative and general expenses, such as increases in employee medical costs.

1 **Illustration No. 5:**



15 Later witnesses provide details explaining these changes in costs.

16 **Q. What are the primary factors driving the Company’s request for a natural**
 17 **gas rate increase?**

18 A. The Company’s natural gas request is driven by changes in various operating cost
 19 components, mainly distribution operation and maintenance and administrative and general
 20 expenditures. In addition, over 24% (or \$1.5 million) of the overall increase in requested
 21 revenue requirement is due to the additional Jackson Prairie storage facility inventory and O&M

1 expense received by the Utility on May 1, 2011. Company witness Mr. Christie discusses this
2 project in further detail within his testimony.

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

5 A. No. Avista is not proposing changes in this filing related to the cost of natural gas
6 included in current rates for natural gas customers (other than the adjustment for JP Storage
7 explained above). Changes in natural gas costs are addressed in the annual PGA filings.

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

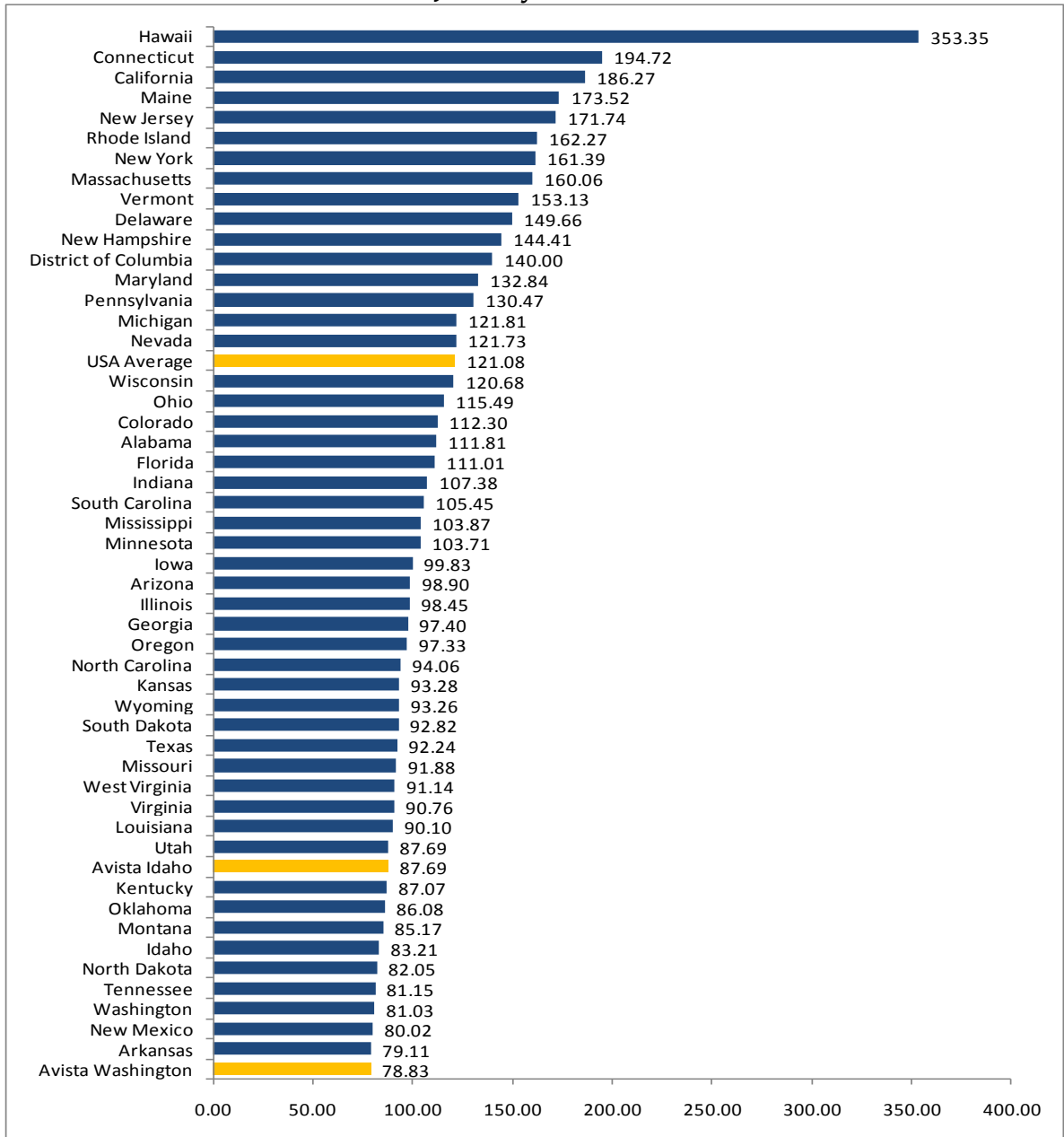
10 A. Edison Electric Institute periodically prepares a comparison of residential electric
11 bills for investor-owned utilities across the country. The chart below provides a comparison of
12 an Avista customer's monthly bill³ in Washington and Idaho, with utility bills in other states.
13 The chart shows that Avista's residential customers' rates are the lowest, or are among the
14 lowest, in the country.

15
16
17
18
19
20
21
22

³ Based on a residential customer's usage of 1,000 kWh per month.

Illustration No. 6

**Average Residential Monthly Electric Bill
1,000 Kilowatt-Hours per Month
January 2011**



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

1 resources for the benefit of our customers. This portfolio includes hydroelectric, wood-waste
2 fired, gas-fired baseload, gas-fired peakers, and coal-fired generation, together with long-term
3 purchases of power and an aggressive energy efficiency program.

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

6 **V. COST MANAGEMENT AND EFFICIENCIES**

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

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

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

16 **Hiring Restriction**

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

20
21 **Limitations on Capital Spending**

22 Avista approved a lower capital budget than was requested by the Company's
23 Engineering and Operations personnel. The original capital projects request for approval
24 in 2011 consisted of projects totaling over \$292 million. The Capital Prioritization
25 Committee reduced the list of recommended projects by \$62 million to the \$230 million
26 capital budget approved by the Board (excluding Stimulus Projects⁴). In addition, the

⁴ Avista was awarded matching grants from the U.S. Department of Energy for two "Smart Grid" projects. One project will upgrade portions of the utility's electric distribution system to smart grid standards in Spokane,

1 Company prioritized O & M facility maintenance and improvement projects and removed
2 projects that could be delayed without safety or operational concerns.

3
4 **Reduced Pension Benefit for New Hires**

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

9
10 **Refinance Long Term Debt**

11 As explained by Company witness Mr. Thies, the Company has reduced its overall cost
12 of debt to 5.61% in December 2010, from approximately 6.5% in 2008, due primarily to
13 issuing the following debt, some of which represents an early redemption of higher-cost
14 debt to take advantage of historically low interest rates:

- 15
16 - September 2009:
17 \$250 million of secured debt at a coupon of 5.125% due in 2022
18 - December 2010:
19 \$52.0 million of secured debt at a coupon of 3.89% due in 2020
20 \$35.0 million of secured debt at a coupon of 5.55% due in 2040
21 \$50.0 million of secured debt at a coupon of 1.68% due in 2013
22

23 **Performance Excellence Initiative**

24 In May 2010, the Company enlisted the help of Booz & Company to work with us on
25 what we are calling Performance Excellence. They brought with them industry
26 knowledge, expertise and a phased-approach. Phase 1 involved assessing and identifying
27 Avista's top opportunities to better align our resources so we can run our business more
28 efficiently, and be better prepared to meet customers' future needs for energy and energy
29 information. In Phase 2 we are designing processes to capture these opportunities, and
30 are still early in the implementation phase.

31
32 Through the initial assessment phase we discovered that many of our processes were
33 already efficient, but the outside, third-party, best practices perspectives brought in by
34 Booz & Company has provided us the opportunity to identify areas where we can fine-
35 tune our practices and further mitigate increased costs to our customers. One example is
36 in our Supply Chain. Each year we spend over \$5 million on transformers. This year we
37 changed our transformer bidding process, which included revisiting how we buy
38 transformers, made changes to the suppliers we use, how contracts are structured, as well
39 as the volume of transformers we buy at one time. We estimate that these changes alone
40 will allow us to save approximately \$2 million in capital costs per year on transformers
41 for the next three years. This savings will enable our available capital dollars to replace
42 other utility infrastructure on a more timely basis than would otherwise occur.

Washington and the other project is a demonstration project in Pullman, Washington that involves automation of many parts of the electric distribution system using advanced metering, enhanced utility communication and other elements of smart grid technologies.

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

5 **VI. COMMUNICATIONS WITH CUSTOMERS**

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

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

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

19 That's why we are continuing to build on our communications efforts begun in 2009, so
20 that customers receive information directly from us on issues important to them. We are also
21 continuing to engage employees in the Company in our efforts to more directly communicate
22 with customers.

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

1 A. One of the important principles in our intensified outreach is to meet customers
2 where they gather. Our customer conversation uses traditional and non-traditional
3 communication channels including print, radio, website, face-to-face listening posts, newsletters,
4 videos, social media, emails, and one-on-one and group presentations.

5 One important customer segment that we target are those customers who gather online.
6 We are continuing to focus on our social media program with the Avista blog as our foundation.
7 We also communicate on Twitter and in online discussion forums when appropriate. For
8 customers who want a more private online conversation, we offer customers a conversation
9 email account to make sure they were comfortable having this new conversation with us.

10 A cornerstone of our enhanced customer communication is an enhanced rates section of
11 the Company's web site at www.avistautilities.com. There customers can view a video on how
12 rates are set, including the regulatory process, view other videos on the components of current
13 general rate requests, and access additional information on general rate requests. Our employees
14 provide excellent customer service, and this focus on communicating with our customers
15 includes providing them messaging and new tools to make is easier to have conversations about
16 Avista with friends, family and customers. We are finding that once a customer talks with one of
17 our employees and has the opportunity to voice their concerns and receive answers to their
18 questions, their satisfaction level increases significantly. We're listening to our customers'
19 point-of-view and sharing ours about energy issues that directly affect us all.

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

1 decisions today, specifically in areas such as energy efficiency, sustainability, reliability and
2 renewable energy, will affect our energy future.

3 **VII. CUSTOMER SATISFACTION**

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

6 A. I am pleased with the dedication of Avista Utilities' employees and their
7 commitment to provide quality service to our customers. While we continue to maintain tight
8 controls on capital and O&M budgets, our customer service surveys indicate that customer
9 satisfaction remains high. Our recent first quarter 2011 customer survey results show an overall
10 customer satisfaction rating of 93% in our Washington, Idaho, and Oregon operating divisions.
11 This rating reflects a positive experience for the majority of customers who have contacted
12 Avista related to the customer service they received. These results can be achieved only with
13 very committed and competent employees.

14 In September 2010, J.D. Power and Associates⁵ ranked Avista "Highest in Customer
15 Satisfaction with Residential Natural Gas Service in the Western U.S. among Mid-Sized Utilities
16 in a Tie." Avista's score of 654 placed the Company highest in the segment, tied with Boise-
17 based Intermountain Gas Company. The segment average score on this study was 629. The
18 study surveys customer satisfaction across a number of factors, including billing and payment,
19 price, corporate citizenship, communications, customer service and field service.

20 I believe we achieved this award because the Company has been listening closely and
21 doing the right things to serve our customers well, as affirmed by the J.D. Power and Associates

⁵ <http://www.jdpower.com/news/pressRelease.aspx?ID=2010168>

1 2010 study. Achieving the highest ranking was a wonderful recognition of our dedicated
2 employees who are making the difference.

3 **VIII. CUSTOMER SUPPORT PROGRAMS**

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

5 A. More than 600,000 customers in three states rely on Avista for their electricity
6 and natural gas. One of the challenging aspects of the utility business is to collect on bills from
7 those least able to pay. In the past two years, this challenge has broadened with the serious
8 economic impact the national recession has had on individuals and businesses. Federal energy
9 assistance for those in need is supplemented with Avista's Low Income Rate Assistance Program
10 (LIRAP) and Project Share, an emergency energy assistance program funded through Avista, its
11 employees and customer donations. A 2009 study conducted by the Institute for Public Policy
12 and Economic Analysis at Eastern Washington University⁶ revealed that an estimated 30 percent
13 of Avista's eligible low income households received energy assistance grants, significantly
14 higher than the national average of 16 percent.

15 But one-time, annual grants alone are not enough to meet the long-term challenges faced
16 by those living on limited incomes. In 2010 Avista initiated and hosted two Energy Fairs— one in
17 Spokane, Washington, and one in Coeur d'Alene, Idaho. The fairs provided information and
18 demonstrations on energy assistance, energy efficiency and home weatherization to limited
19 income families and senior citizens. But the fairs went beyond the business focus of helping
20 customers pay their utility bill. They provided an opportunity for attendees to learn about
21 employment opportunities, earned income tax credits, child care options, community college

⁶ "Assessing Heating Assistance Programs in Spokane County", Institute for Public Policy & Economic Analysis (Grant Forsyth, PhD, D. Patrick Jones, PhD, and Mark Wagner). January 2010.

1 offerings and other community resources. Nearly 700 people attended the two fairs. The Energy
2 Fairs provided a convenient environment for customers to learn about billing options and energy
3 assistance, while offering them tips and tools to use to help manage their limited financial
4 resources.

5 In the 2009/2010 heating season 26,751 Washington customers received approximately
6 \$11.1 million in various forms of energy assistance (Federal LIHEAP program, LIRAP, Project
7 Share, and local community funds). Some of the key programs that we offer or support are as
8 follows:

- 9
- 10 1. **Low-Income Rate Assistance Program (LIRAP).** Avista's Low Income Rate
11 Assistance Program in Washington collects approximately \$4.5 million per year
12 through electric and natural gas tariff surcharges. The Company, with the assistance
13 of community action agencies, directs these funds to customers least able to pay for
14 electric and natural gas service. The purpose of the LIRAP program is to reduce the
15 energy cost burden among those customers least able to pay energy bills. In the
16 2009/2010 heating period for example, the LIRAP funds supplied close to 10,529
17 grants to our customers.
18
 - 19 2. **Increased Demand-Side Management (DSM) Programs and Funding.** In January
20 2009 Avista proposed, and the UTC approved, modifications to the Company's
21 energy efficiency program offerings. The modifications further broadened the DSM
22 technical and financial support Avista provides to its customers, and provides
23 customers with increased opportunity to manage their energy bills. In 2008 Avista
24 also launched the award-winning "Every Little Bit" energy efficiency promotional
25 campaign which integrates all of the Company's energy efficiency programs into one
26 location.
27
 - 28 3. **Project Share.** Project Share is a voluntary program allowing customers to donate
29 funds that are distributed through community action agencies to customers in need. In
30 addition to the customer and employee contributions in 2010 of \$316,600 in
31 Washington, the Company also contributed \$282,274 (Washington's share) to the
32 program.
33
 - 34 4. **Comfort Level Billing.** The Company offers the option for all customers to pay the
35 same bill amount each month of the year by averaging their annual usage. Under this
36 program, customers can avoid unpredictable winter heating bills.
37

1 these requirements, together with access to capital from external sources under
2 reasonable terms.

- 3
- 4 • Avista's corporate credit rating from Standard & Poor's (S&P) is currently BBB and
5 Baa2 from Moody's Investors Service (Moody's). Avista must operate at a level that will
6 support a solid investment grade corporate credit rating, meaning "BBB" or "BBB+", in
7 order to access capital markets at reasonable rates, which will decrease long-term
8 borrowing costs to customers. In March 2011, S&P upgraded Avista's Corporate Credit
9 Rating to BBB from BBB- and Moody's upgraded Avista's Corporate Credit Rating to
10 Baa2 from Baa3. A supportive regulatory environment is an important consideration by
11 the rating agencies when reviewing Avista. Maintaining solid credit metrics and credit
12 ratings will also help support a stock price necessary to issue equity under reasonable
13 terms to fund capital requirements.
 - 14
 - 15 • The Company is proposing an overall rate of return of 8.23%, including a 48.04% equity
16 ratio and a 10.90% return on equity. Our proforma cost of debt is 5.76%.
 - 17

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

- 21 • In order to reflect the risks and prospects associated with Avista's jurisdictional utility
22 operations, his analyses focused on a proxy group of twenty-eight other utilities with
23 comparable investment risks. Consistent with the fact that utilities must compete for
24 capital with firms outside their own industry, he also references a proxy group of
25 comparable risk companies in the non-utility sector of the economy;
- 26 • Because investors' required return on equity is unobservable and no single method
27 should be viewed in isolation, he applied both the DCF and CAPM methods, as well
28 as the expected earnings approach, to estimate a fair ROE for Avista;
- 29 • Based on the results of these analyses, and giving less weight to extremes at the high
30 and low ends of the range, he concluded that the cost of equity for the proxy groups
31 of utilities and non-utility companies is in the 10.3 percent to 11.3 percent range, or
32 10.45 percent to 11.45 percent after incorporating an adjustment to account for the
33 impact of common equity flotation costs; and,
- 34 • As reflected in the testimony of Mr. Thies, Avista is requesting a fair ROE of 10.9
35 percent, which is essentially equal to the midpoint of Dr. Avera's recommended
36 range. Considering capital market expectations, the exposures faced by Avista, and
37 the economic requirements necessary to maintain financial integrity and support
38 additional capital investment even under adverse circumstances, it is his opinion that
39 10.9 percent represents a fair and reasonable ROE for Avista.

1 Mr. Robert Lafferty, Director of Power Supply, will provide an overview of Avista's
2 resource planning and power supply operations. This includes summaries of the Company's
3 generation resources, the current and future load and resource position, future resource plans, and
4 an update on the Company's plans regarding the acquisition of new renewable resources. As
5 part of an overview of the Company's risk management policy, he will provide an update on the
6 Company's hedging practices. He will address hydroelectric and thermal project upgrades,
7 followed by an update on recent developments regarding hydro licensing.

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

16 Mr. William Johnson, Wholesale Marketing Manager, will identify and explain the
17 proposed normalizing and pro forma adjustments to the January 2010 through December 2010
18 test period power supply revenues and expenses, and describe the proposed level of authorized
19 expense and retail revenue credit for Energy Recovery Mechanism (ERM) purposes, using the
20 pro forma costs proposed by the Company in this filing. His testimony also shows the change in
21 power supply expense incorporating the Energy Efficiency Load Adjustment proposed by the
22 Company in this case.

1 Mr. Kevin Christie, Director of Gas Supply, will describe Avista's natural gas
2 procurement planning process, provide an overview of the Jackson Prairie natural gas storage
3 facility, and discuss how the Company uses Jackson Prairie for balancing on behalf of our Local
4 Distribution Company (LDC) customers.

5 Mr. Don Kopczynski, Vice President of Customer Solutions, will describe Avista's
6 electric and natural gas energy delivery facilities and operations, and recent efforts to increase
7 efficiency and improve customer service. Mr. Kopczynski describes:

- 8 • Avista's customer service programs such as the Low-Income Rate Assistance
9 Program (LIRAP), energy efficiency, Project Share, CARES program, Senior
10 Outreach Program, and payment plans. Some of these programs will serve to
11 mitigate the impact on customers of the proposed rate increase.
- 12 • The Company's multi-faceted effort to increase customer service automation,
13 including replacement and upgrade of the new Enterprise Voice Portal (EVP)
14 system.

15
16 Mr. Scott Kinney, Director, Transmission Operations, will discuss the electric
17 transmission and distribution capital investments included in this case, and presents the
18 Company's pro forma period transmission revenues and expenses. In addition, he describes the
19 Company's Asset Management Program (including the additional vegetation management
20 expenses included in the Company's case).

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

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

1

2 In addition, she will explain the Company's request for deferred accounting treatment of
3 major changes in generation plant O&M costs, and the Company's compliance with certain
4 requirements as Ordered by the Commission in Order No. 7, Docket Nos. UE-100467 and UG-
5 100468.

6 Mr. Dave DeFelice, Senior Business Analyst, will cover the Company's proposed
7 restating and pro forma adjustments for capital investments in utility plant for the 2010 test
8 period. Mr. DeFelice explains:

- 9
- 10 • The rising cost of essential materials specific to the utility industry is causing
significant increases in capital project funding requirements.
 - 11 • These costs must be pro formed into the test-year in order to allow necessary
12 recovery of our costs to serve customers.
- 13

14 Ms. Karen Feltes, Senior Vice-President, Human Resources and Corporate Secretary, will
15 discuss Avista Corporation's Compensation Programs and employee benefits. In addition, she
16 will describe Avista's employee incentive plan and why the costs associated with Avista's
17 employee incentive plan, as part of the total compensation for employees, are appropriate to
18 include in utility customer rates.

19 Ms. Tara Knox, Senior Regulatory Analyst, sponsors the Company's electric and natural
20 gas cost of service studies performed for this proceeding. Additionally, she is sponsoring the
21 electric and natural gas revenue normalization adjustments to the test year results of operations
22 and the proposed retail revenue credit rate to be used in the Energy Recovery Mechanism. Ms.
23 Knox's studies indicate:

- 24
- 25 • Electric residential service, extra large general service, and pumping service
26 schedules are earning less than the overall rate of return under present rates,
while general service, large general service and the street and area lighting

1 service schedules are earning more than the overall rate of return under present
2 rates.

- 3
- 4 • Natural Gas residential service schedule is earning slightly less than the overall
5 rate of return at present rates, and small firm, large firm, interruptible, and
6 transportation service schedules are earning slightly more than the overall rate of
7 return.

8
9
10 Mr. Patrick Ehrbar, Manager of Rates and Tariffs, discusses the spread of the proposed
11 annual revenue changes among the Company's general service schedules as well as the proposed
12 rate design within each schedule. He explains, among other things, that:

- 13 • The proposed increase in electric base rates is 9.1%, which consists of an increase
14 in electric base retail revenues of \$38.3 million.
- 15
- 16 • The monthly bill for a residential customer using an average of 977 kWhs per
17 month would increase from \$77.01 to \$84.14 per month, an increase of \$7.13 or
18 9.3%. This includes the proposed increase in the monthly basic or customer
19 charge from \$6.00 to \$9.00
- 20
- 21 • The proposed natural gas annual revenue increase in base rates is \$6.2 million, or
22 4.0%.
- 23
- 24 • The monthly bill for a residential customer using 67 therms per month would
25 increase from \$63.45 to \$66.71 per month, an increase of \$3.26 or 5.1%. This
26 includes the proposed increase in the monthly basic or customer charge from
27 \$6.00 to \$9.00.
- 28

29 In addition, he will provide further information related to the Company's proposed
30 Energy Efficiency Load Adjustment, and provides an overview demonstrating how the Company
31 met the requirements from the Settlement Stipulation approved in Docket Nos. UE-100467 and
32 UG-100468.

33 Mr. Bruce Folsom, Senior Manager of Demand Side Management, will report on the
34 status of requirements relative to energy efficiency, resulting from the Company's two previous
35 general rate cases. This is preceded by a brief overview of the Company's DSM programs and

1 recent results, including compliance with the conservation component of “I-937” (codified as
2 RCW Chapter 19.285 and WAC Chapter 480-109). He will also describe the process for
3 Commission review of DSM expenditures through annual tariff rider filings.

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

5 A. Yes.