BEFORE THE WASHINGTON UTILITIES AND
TRANSPORTATION COMMISSION

DOCKET NO. UE-01_______

DIRECT TESTIMONY OF GARY G. ELY

REPRESENTING AVISTA CORPORATION

Exhibit T-___(GGE-T)

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

A. My name is Gary G. Ely. I am the Chairman of the Board, President and CEO of Avista Corporation at East 1411 Mission Avenue, Spokane, Washington.

Q. Please provide an overview of your professional experience at Avista.

A. I joined the Company in 1967. During my thirty-four years with Avista I have held positions in the engineering, operations, marketing and natural gas departments. In 1986, I was named Vice President of Marketing and then received the added responsibility of Gas Supply in 1989. In 1991, I was named Vice President of Natural Gas and was responsible for the Company's overall natural gas systems in Washington, Idaho, Oregon and California. Beginning in 1995, my responsibilities included the overall management of Avista's hydro production and construction, transmission and generation engineering, rate and regulatory matters at the state and federal levels, as well as government relations. I served as Executive Vice President of Avista Corporation from January 1999 to October 2000.

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

A. I am testifying as the policy witness for the Company, and, in addition to providing an overview of the filing, will introduce each of the other witnesses proffering testimony on the Company's behalf.

Q. Would you please provide an overview of Avista's current situation and the Company's request in this filing?

A. Yes. Avista is continuing to take the steps necessary to improve the financial health of the Company following the impacts of the adverse hydroelectric and market price conditions experienced in 2000 and 2001. The Company's credit ratings recently dropped in October 2001 below investment grade, causing increased borrowing costs to the Company and, ultimately, to its customers. Over time, the added interest costs resulting from being below investment grade will continue to build as existing debt matures and must be refinanced, in addition to the increased costs associated with incremental borrowings. As other Company witnesses will explain, these additional costs are substantial and, therefore, it is important for Avista to regain an investment grade credit rating as soon as possible to begin to reduce these borrowing costs.

In order to improve its financial condition, the Company has scaled back and sold subsidiary businesses, sold one-half of the Coyote Springs II generating project currently under construction, and made significant cuts to its capital and operations and maintenance (O&M) costs. These measures, however, even with the recent 25% rate surcharge, do not provide financial indicators that support an investment grade credit rating for Avista Corp.

Through this filing, the Company is requesting that the Commission grant the additional relief necessary to improve Avista's financial condition such that it can obtain an investment grade credit rating as soon as possible.

The relief requested by the Company, which is briefly explained in the following pages, is as follows:

Immediate Relief Requested

- Prompt prudence ruling on the balance of deferred power costs through September 30, 2001 (subject of Docket No. UE-011514).
- Interim rate relief of 12.4% over base rates, effective March 15, 2002.
- Temporary deferred accounting, effective for the period January 1, 2002 to the end of this general rate case.

Relief Effective At The Conclusion Of The General Rate Case

- Reset base retail rates to reflect a 22.5% increase, effective at the end of this general rate case (primarily due to plant additions and increased cost of capital).
- Reset the surcharge rate to reflect a 14.9% rate increase to recover deferred power costs over a 5-year period, effective at the end of this general rate case.
- Adoption of a power cost adjustment mechanism, effective at the end of this general rate case.

Prudence of Deferred Costs By February 18, 2002

On November 13, 2001, the Company filed its prudence review filing (Docket No. UE-011514) in which it requested a prompt prudence ruling from the Commission to remove uncertainties related to the ultimate recovery of the large balance of deferred power costs through September 30, 2001. The present uncertainty, if not addressed by the Commission, will continue to adversely impact Avista's ability to complete required financings in early to mid-2002 due to continuing concerns by rating agencies and lenders. The Company has requested that the Commission establish an expedited procedural schedule that will allow an order on or before February 18, 2002.

Interim Rate Relief Effective March 15, 2002

Avista continues to incur costs to serve its customers that are in excess of the costs being collected from customers through retail rates. This continuing under-recovery of costs compounds the Company's current financial condition, and if not addressed, places further pressure on the Company's credit rating. The Company, as discussed by Witness Peterson, requests that the Commission grant an interim rate increase of 12.4%[1] over base rates effective March 15, 2002. The Company is proposing the interim rate relief on a subject to refund basis.

Temporary Deferred Accounting Effective January 1, 2002

The Company, as explained further by Witness Norwood, is requesting the implementation of temporary deferred accounting beginning January 1, 2002 and terminating at the end of this general rate case. Coincident with the filing of this docket, the Company has filed an accounting petition seeking authorization of this temporary deferred accounting. This separate filing is intended to allow the Commission to approve this request prior to January 1, 2002. Alternatively, the Commission may wish to rule on the deferred accounting, at the same time that it responds to the Company's request for interim rate relief, early in 2002, but with an effective date of January 1, 2002. The temporary deferred accounting would preserve the opportunity to address recovery of the additional costs during this period (i.e., during the pendency of the general rate case).

Reset Base Retail Rates Effective At The End Of The General Rate Case

At the conclusion of the general rate case, as explained by Witness Falkner, the Company requests that the Commission reset base retail rates, and adjust the surcharge rate to the level necessary to recover deferred power costs. A total

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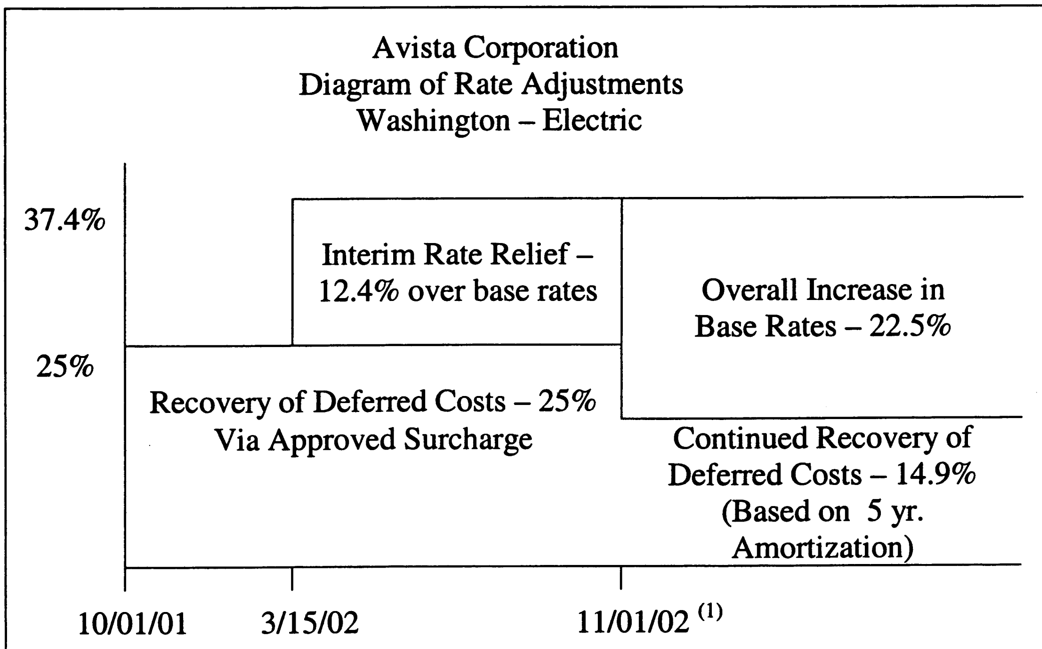
[1] The interim rate increase of 12.4% over base rates is equivalent to a 10% increase over present rates including the surcharge, as explained by Witness Hirschkorn.

increase above current base rates of 22.5% is necessary to provide recovery of ongoing costs of operating the utility that are over and above the existing base rates. In addition to the 22.5% base rate increase, the Company requests a 14.9% surcharge over a 5-year period to recover deferred power costs. The total of the 22.5% base rate increase, and the 14.9% surcharge equal a total increase of 37.4%.

This 37.4% is also equal to the total of the existing 25% surcharge, plus the requested interim relief of 12.4%. Therefore, if the interim relief is granted there would be no further change in retail rates at the conclusion of the general case. This is illustrated on the chart below, which is also provided as Exhibit__ (GGE-1).



(1) For discussion purposes, the conclusion of the general rate case is assumed to be November 1, 2002.

As shown in the chart, effective October 1, 2001, the Company increased rates, through the emergency surcharge order, by 25% to begin recovering the mounting deferred power costs. In this filing, the Company is requesting interim rate relief of 12.4% to be effective March 15, 2002, in order to improve cash flows as soon as possible and to help the Company address its current weak financial condition and related financing challenges. If approved, this means that the Company's adjusted rates, due to the emergency and interim rate relief increases, would total 37.4% as of March 15, 2002.

The Company then requests that this total increase of 37.4% remain in place at the conclusion of the general rate case, but with some adjustments to the components of the 37.4% total.

As of the end of the general rate case, a total increase in base rates of 22.5%, is necessary to provide recovery of ongoing costs of operating the utility that are over and above the existing base rates, including the regulatory treatment of the Company's Coyote Springs II and other normalized costs.

In addition, a surcharge rate of 14.9% is necessary to recover the deferred power costs over a 5-year period, as explained by Mr. Falkner. The combination of the base rate increase of 22.5% and the surcharge of 14.9% equals a total increase of 37.4% from current base rates.

Power Cost Adjustment Mechanism

Through this filing the Company is requesting that the Commission authorize a power cost adjustment (PCA) mechanism, at the conclusion of the general rate case. The variation of power costs experienced by the Company from year to year would be "smoothed-out" through the PCA, which would add stability to the financial results of the Company.

Implementation of such a mechanism, as proposed by the Company, would clearly provide benefits to both the Company's customers and its shareholders. The PCA would add stability to the various financial indices viewed by rating agencies and other members of the financial community to assess the financial health of the Company, and the risk associated with the Company. The ability of the Company to more consistently meet interest coverage ratios and other financial benchmarks would reduce the perceived risk by lenders and investors. This added financial stability would not only improve access to capital, but also allow the Company to obtain financing at more reasonable terms. The result would be lower financing costs and lower retail rates for customers, than would otherwise occur. Several of the Company's witnesses further explain Avista's PCA proposal.

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

A. Yes. In addition to myself, the following witnesses are presenting direct testimony on behalf of Avista.

Mr. Scott Morris, President of Avista Utilities, will provide an overview of Avista's utility operations. He also summarizes the major factors driving the Company's need for general rate relief and explains the cost controls implemented by Avista in response to the difficult financial situation that the Company continues to face. Finally, he will discuss our customer support programs that are in place to assist our customers.

Mr. Jon Eliassen, Senior Vice President and Chief Financial Officer will address the problems that need to be resolved to improve the Company's financial condition, and how the Company's present financial situation affects our customers. He will explain the actions the Company has taken to supply needed capital and mitigate the mounting financial concerns. He will also summarize what the Company is asking of the Commission in this proceeding, and the probable consequences with and without the requested relief.

Mr. Ron Peterson, Vice President and Treasurer of Avista Corp., will address the need for interim rate relief and whether the Commission's criteria for interim relief have been satisfied. He will also explain covenants under the Company's financing arrangements and how they impact the Company. In addition, he will discuss the financial benefits of a power cost adjustment mechanism to Avista's customers and other stakeholders.

Mr. Kelly Norwood, Vice President and General Manager of Energy Resources, will explain Avista's request for deferred accounting on a temporary basis for the period January 1, 2002 through the conclusion of the general rate case, to allow the Company the opportunity for recovery of the additional power supply related costs during this period. He will also explain Avista's request for a power cost adjustment mechanism to be implemented at the conclusion of this general rate case. Finally, he will discuss the basis for using 60 years of water data for power supply modelling purposes.

Mr. William E. Avera, as a principal in Financial Concepts and Applications (FINCAP), Inc., has been retained to present testimony with respect to the Company's cost of capital and capital structure and will testify in support of a

12.75% return on equity which includes a return on equity adjustment related to implementation of a PCA.

Mr. Bob Lafferty, Manager of Wholesale Power, will explain the prudence of several resource acquisitions made by the Company in 2000 and 2001. His testimony will provide an overview of Avista's resource planning and power operations including the resource planning that led to the solicitation of resource proposals through the Request For Proposals (RFP) in the year 2000.

Mr. William Johnson, Senior Power Supply Analyst, will describe the adjustments to the 2000 test period power supply revenues and expenses. He will also describe the methodology of the power cost adjustment mechanism the Company is proposing.

Mr. Clint Kalich, Manager of Power Supply Analysis, will describe the Company's Hourly Prosym model, used to dispatch the Company's resources over the pro forma period, including a discussion of key inputs, assumptions, and results.

Mr. Tom Dukich, will discuss his study of the historical water years of record and his conclusions regarding the appropriateness of using 60 years of water record in this case.

Mr. Ron McKenzie, Senior Rate Accountant, addresses the procedures and related accounting associated with the proposed temporary deferred accounting and the proposed Power Cost Adjustment (PCA) mechanism. The Company is requesting that the temporary deferred accounting begin January 1, 2002 and remain in effect until the end of the general rate case, and that the PCA mechanism be effective at the end of the general rate case.

Mr. Don Falkner, Senior Rate Analyst, will discuss the Company's overall revenue requirement proposals. In addition, his testimony and exhibits in this proceeding will generally cover accounting and financial data in support of the Company's need for the proposed increase in rates. He will also explain pro formed operating results including expense and rate base adjustments made to actual operating results and rate base.

Mr. Bruce Folsom, Regulatory Analyst, addresses the expenditures for the Company's energy efficiency programs funded under the DSM Tariff Rider, and addresses updated rates for miscellaneous fees.

Ms. Tara Knox, Rate Analyst, sponsors the cost of service studies for electric service. She will also provide the results of alternative scenarios to show the potential impact of different key allocation decisions in the cost of service process. Ms. Knox also discusses her base case study and how each schedule compares to the overall return at present rates.

Mr. Brian Hirschkorn, Senior Rate Analyst, discusses the spread of the following proposed annual revenue changes among the Company's general service schedules: 1) the proposed interim revenue increase, 2) the proposed total annual general increase (including the interim revenue), and 3) the proposed annual revenue associated with the Power Cost Surcharge. In addition, he will also address the Company's revenue normalization adjustment.

Q. Would you please briefly explain the recent events or actions taken by the investment community that have impacted the Company?

A. Yes. As will be further discussed by Witness Eliassen, rating agencies and lenders have taken actions over the last several months reflecting uncertainty surrounding the recoverability of the deferred power cost balance, and the ability of the Company to recover its ongoing costs to serve customers. In response to the WUTC surcharge order, Moody's and Standard & Poor's both lowered Avista's credit ratings. In S&P's October 10, 2001 release, included in Exhibit__(JEE-1), pages 7 through 9, they explained their negative outlook as follows:

> "The downgrade reflects Avista's substantially weakened financial profile, which is not expected to recover to levels commensurate with those of investment-grade companies over the near term, considerable uncertainty surrounding the regulatory environment in Washington despite the recently approved 25% rate surcharge, and management's ongoing challenges to ensure adequate liquidity until a final regulatory order is approved."

Although they recognized that the recent 25% surcharge will provide some relief to Avista's liquidity, they added:

> "….. Avista's ability to defer additional power costs in excess of rates will terminate on Dec. 31, 2001, creating further uncertainty as to the recovery of additional power cost deferrals. Avista plans to address the unrecovered deferred balances, the ability to defer additional power costs, and the ability to share power costs with ratepayers in the upcoming general rate case filing, which is to be submitted by Dec. 1, 2001. …… At the same time, Avista management is pursuing various alternatives to ensure adequate liquidity until the WUTC responds to the company's general rate filing. These plans include alternative financing for the Coyote Springs 2 combined-cycle plant, which is expected to come on line in early summer 2002, a planned equity offering that the company may be challenged to complete due to adverse market conditions, reductions in operating costs and planned capital expenditures, and the disposition of certain noncore assets. Although these measures may provide the necessary relief during a transition period, clearly Avista needs a strong show of regulatory support in the form of a rate order that addresses the current cost under-recovery and

> provides a supportive regulatory framework that addresses the evolving and volatile nature of the electric utility industry. Without such a show of support, Standard & Poor's is concerned that Avista's financial profile may deteriorate further, leading to even weaker credit-protection measures."

In Moody's October 8, 2001 release, included in Exhibit__(JEE-1), pages 5 and 6, they explained their negative outlook, and added:

> "...a favorable outcome of the general rate filing to be made by December 1, 2001 would help stabilize the current negative rating outlook. This would be especially so if the outcome implements a power cost adjustment mechanism to create more certainty surrounding recovery of Avista's power supply costs incurred to serve its customers in the Washington jurisdiction."

The recent downgrades in the Company's credit rating together with continuing concerns by the rating agencies and lenders make it necessary to resolve the uncertainty associated with the deferred cost balance as soon as possible, prompting Avista's November 13, 2001 prudence filing. Furthermore, the Company is requesting in this filing, temporary deferred accounting to recognize power costs incurred through the end of the general rate case, interim rate relief to provide current cash flows that contribute toward underlying expenses of electric service, and a PCA mechanism to provide the ability to collect or refund revenues to offset varying power costs on an ongoing basis.

Q. Could you now please summarize actions taken by the Company to cut costs in order to address the Company's weakened financial situation?

A. Yes. The Company has worked hard to continue to operate what I believe to be a very efficient utility. Over the last year and half the Company has faced a number of challenges and has instituted several aggressive measures to relieve financing pressure related to record-low hydro conditions, high wholesale market prices and power plant construction expenditures. These measures include the sale of 50% of the Coyote Springs II project, divestiture of Avista Communications, and significant temporary reductions in capital and operation and maintenance (O&M) budgets, intended to get the Company through this critical financial period by reducing expenditures and improving cash flows. Mr. Morris and Mr. Eliassen will further discuss the actions taken by the Company to improve liquidity and reduce debt.

Q. Could you please now describe Avista's current business focus and plans for the future for the utility and subsidiary operations.

A. Yes. Our strategy refocuses Avista Corp. activities on our energy and energy-related businesses. For the Utility, this means we must maintain a strong, low-cost utility business by focusing on delivering efficient, reliable and high quality service to our customers. This also means, owning or contracting for sufficient generation to meet retail loads, providing adequate reserves and developing generation to serve the growing power requirements in our service area. In order to accomplish this, we must continue to rebuild our utility business, strengthen our cash flows and work with regulators to recover the costs of providing service to our customers.

For our subsidiaries, specifically our non-regulated energy trading activities, we must manage the size and the risk associated with this business, which we have done by scaling back operations to the WSCC (Western Systems Coordinating Council) region, and to make the best use of our knowledge and experience in markets we know well.

Q. Could you please describe your more significant subsidiary businesses.

A. Yes. Avista Corp.'s subsidiaries, each headquartered in Spokane, Washington, include the energy trading and marketing businesses, Avista Energy and Avista Power, and the information and technology businesses, Avista Advantage and Avista Labs, described below.

Avista Energy is our electricity and natural gas trading and marketing business focused on marketing energy in the western United States. Avista Energy's customers primarily include electric utilities, natural gas distribution companies and other trading companies. Avista Energy also trades electricity and natural gas derivative commodity instruments, including futures, options, swaps, and other contractual arrangements on national exchanges and through unregulated exchanges and brokers from whom these commodity derivatives are available.

Avista Power is a 49 percent owner of a 270 MW natural gas combined cycle combustion turbine plant in Rathdrum, Idaho, which commenced commercial operation in September 2001. The output from this plant is contracted to Avista Energy for 25 years. Avista Power is also in the process of constructing the Coyote Springs II power plant and as announced in October 2001, 50% of its interest has been sold to Mirant Corp. Upon completion of the plant in mid-2002, Avista

Power's 50% ownership interest will transfer to Avista Utilities. Due to changing market conditions and as a part of the Company's overall business strategy, we have decided to not develop any additional non-regulated generation projects.

Avista Advantage is a leading provider of facilities management billing and information services to large commercial customers with multiple operational sites, which now includes more than 200 chains, representing over 93,000 sites throughout the U.S. and Canada. Avista Advantage processes and presents consolidated bills on-line, and pays utility and maintenance and repair bills for multi-site commercial and industrial customers with in-depth analytical support, real-time reporting and unbiased consulting in regard to energy, water, waste, repair and maintenance, open/close services, and telecommunications.

Avista Labs is a developer of proton exchange membrane (PEM) fuel cell technology and fuel cell components. This unique modular PEM fuel cell cartridge design delivers reliable, affordable and clean distributed power solutions. The modular design allows fuel cell cartridges to be easily removed and replaced without interruption of power. The Company believes this exclusive "hot swap" feature makes Avista Labs' technology more scalable, configurable, reliable and durable than other fuel cell technologies. In addition to its modular-based PEM fuel cell, Avista Labs is dedicated to commercializing a broad array of components to complement its fuel cell in order to deliver system solutions to residential, industrial and commercial markets.

Q. Would you also explain the current status of Avista Communications?

A. Yes. As mentioned earlier, Avista Corp. is in the process of divesting its ownership of Avista Communications to reduce expenditures and improve cash flows. In October 2001, Avista Communications announced that its minority shareholder, One Eighty Communications, would acquire ownership of their Montana and Cody, Wyoming markets, and dial-up internet access customers in Spokane, Washington, and Coeur d'Alene, Idaho. In November 2001, Avista Communications announced their agreement with Advanced TelCom Group, Inc. to sell assets and customer accounts in Yakima and Bellingham, Washington.

Q. Do you have any concluding remarks?

A. Yes. Although the Company has worked very hard to implement budget cuts and other cost saving measures to reduce expenses and improve cash flows, the further cuts that would be required to offset, even in part, the mounting deferral balances and ongoing costs to operate the utility could not be accomplished without crippling our utility operations and our ability to provide even minimal levels of service. For these reasons, and given the additional need to improve the financial standing of the Company in the eyes of the investment community, the Company requests that the Commission provide the following relief:

Immediate Relief Requested

- Prompt prudence ruling on the balance of deferred power costs through September 30, 2001 (subject of Docket No. UE-011514).
- Interim rate relief of 12.4% over base rates, effective March 15, 2002.
- Temporary deferred accounting, effective for the period January 1, 2002 to the end of this general rate case.

Relief Effective At The Conclusion Of The General Rate Case

- Reset base retail rates to reflect a 22.5% increase, effective at the end of this general rate case (primarily due to plant additions and increased cost of capital).
- Reset the surcharge rate to reflect a 14.9% rate increase to recover deferred power costs over a 5-year period, effective at the end of this general rate case.
- Adoption of a power cost adjustment mechanism, effective at the end of this general rate case.

Each of the items listed above is necessary to provide ongoing cash relief to the utility during these unprecedented times; conversely, to not grant the additional rate relief would clearly jeopardize the financial integrity of Avista and would cause a detriment to our customers. In addition, continued regulatory support of our efforts to work through these financial difficulties would go a long way toward reassuring the investment community, and would allow the Company to continue to access capital markets under reasonable terms, all of which is necessary to fund ongoing operations so the Company can meet its public service obligations.

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

A. Yes, it does.

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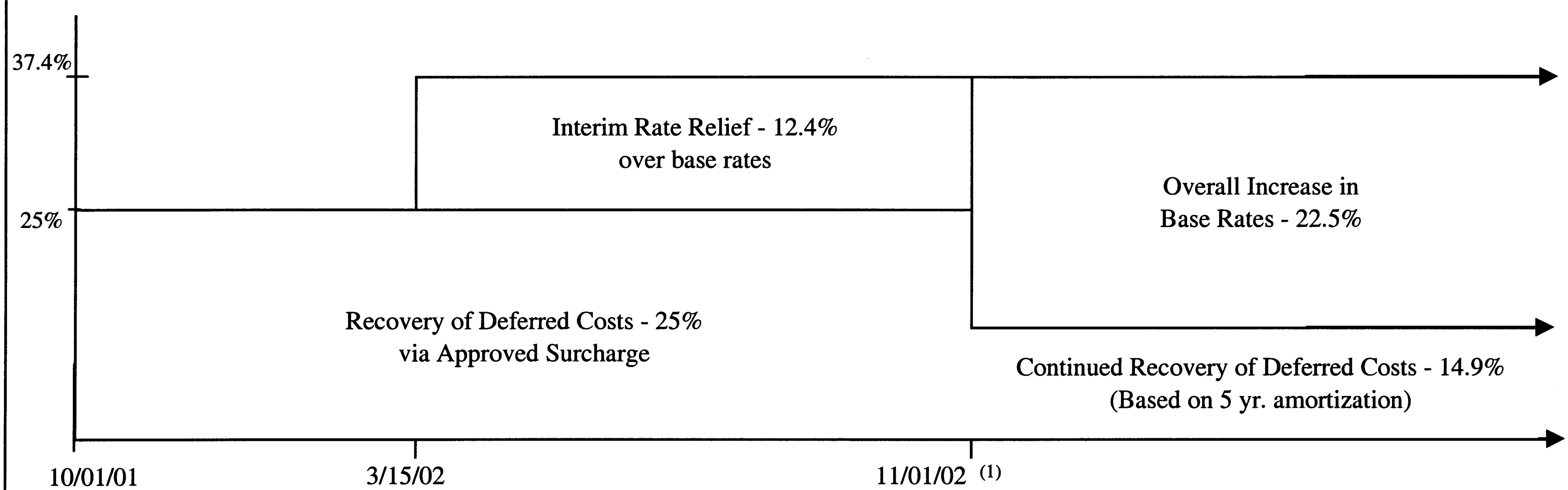
EXHIBIT NO. _____ (GGE-1)

WITNESS: GARY G. ELY, AVISTA CORP.

Avista Corporation
Diagram of Rate Adjustments
Washington Electric



(1) For discussion purposes, the conclusion of the general rate case is assumed to be November 1, 2002.

Exhibit No._____ (GGE-1)
Docket No. UE-_____.
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