BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-07-___

DIRECT TESTIMONY OF

RICHARD L. STORRO

REPRESENTING AVISTA CORPORATION

I. INTRODUCTION

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

A. My name is Richard L. Storro. My business address is 1411 East Mission Avenue, Spokane, Washington, and I am employed by the Company as the Director of Power Supply.

Q. What is your educational background?

A. I participated in a program with the College of Idaho and the University of Idaho, where upon completion I received a Bachelor of Science degree in physics from the College of Idaho and a Bachelor of Science degree in electrical engineering from the University of Idaho, both in 1973.

Q. How long have you been employed by the Company?

A. I started working for Avista in 1973 as a distribution engineer. I have worked in various engineering positions, and have held management positions in line and gas operations, system operations, hydro production and construction, and transmission. I joined the Energy Resources Department as a Power Marketer in 1997 and became Director of Power Supply in 2001. My primary responsibilities involve the oversight of both the short-term and long-term planning and acquisition of power supply resources for the Company.

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

A. My testimony will provide an overview of the history of the ERM and provide a summary of the factors contributing to the net change in power costs during the 2006 calendar year review period. I provide an overview of the documentation the Company has provided in workpapers, which the Company had agreed to provide in the ERM Settlement Stipulation approved and adopted in Docket No. UE-030751.

Q. Are other witnesses sponsoring testimony on behalf of Avista?

A. Yes. Mr. William Johnson will provide testimony regarding the calculation of the monthly power cost deferrals. Mr. Ron Mckenzie will provide testimony concerning the monthly deferral entries and deferral balance.

II. OVERVIEW

Q. Would you please explain the history of the ERM and the annual filing requirement?

A. Yes. The ERM was approved by the Commission's Fifth Supplemental Order in Docket No. UE-011595, dated June 18, 2002, and was implemented on July 1, 2002. That Order approved and adopted a Settlement Stipulation (UE-011595 Stipulation) that explained the mechanism and reporting requirements. Pursuant to the UE-011595 Stipulation, the Company is to make an annual filing on or before April 1st of each year. This filing provides an opportunity for the Commission Staff, and interested parties, to review the prudence of the ERM deferral entries for the prior calendar year. Interested parties are to be provided a 90-day review period, ending June 30th of each year, to review the deferral information. The 90-day review period may be extended by agreement of the parties participating in the review, or by Commission order.

Avista's first Annual ERM Filing covered the six-month period of July 1, 2002 through December 31, 2002. In its Order No. 5, issued February 3, 2004 in Docket No. UE-030751, the Commission approved and adopted a Settlement Stipulation (UE-030751 Stipulation) that resolved the issues related to the first review period.

Avista's most recent Annual ERM Filing to review deferrals for calendar year 2005 was addressed by the Commission's Order No. 1, dated June 28, 2006 in Docket No. UE-0060493. In that order the Commission found the filing met the requirements of Docket No. UE-011595 and UE-030751, and that the power costs deferrals for 2005 were prudent.

Q. What period is covered by this ERM filing?

A. This ERM filing covers the period January 1, 2006 through December 31, 2006.

Q. What were the changes in power costs, the amounts deferred, and the amounts absorbed by the Company during 2006?

A. During 2006 actual net power costs were less than the authorized net power costs for the Washington jurisdiction by $2,601,664. Because this amount was less than the deadband, no power supply expense was deferred ($68,246 of interest was deferred in the rebate direction). Under the ERM, the first $4.0 million of net power supply costs above or below the authorized level is absorbed by the Company. Fifty percent of the next $6 million and ninety percent of power costs above or below $10.0 million are deferred for the opportunity for later rebate or recovery. The $4.0 million deadband, the remaining fifty percent from $4 million to $10 million and the ten percent of costs beyond $10 million is absorbed by the Company.

III. SUMMARY OF DEFERRED POWER SUPPLY COSTS

Q. Would you please summarize why power supply expenses were lower than the authorized level during the review period?

A. Yes. Power supply expenses were lower than authorized due primarily to high hydro generation that more than offset the increased expense due to higher loads and higher electricity and natural prices. Hydro generation was 57 aMW above the authorized level hydro, which decreased expense. At the same time, however, retail loads were 54 aMW above the authorized level (authorized is 2004 loads), which offset most of the benefit of the good hydro conditions.

The impact of higher loads on power supply expense cannot be understated. Because the cost of securing energy to serve that additional load, either through purchasing market electricity or natural gas for generation, is higher than the average cost of production included in base rates, the additional load leads to higher power supply expenses. In the ERM the higher expense of increased loads is partially offset by the retail revenue credit. The retail revenue credit is based on the average cost of production, which is the amount that customers paid in their rate for the energy commodity. Because Avista is still a relatively low cost producer of power, that average production cost, however, is less than the marginal cost of securing additional power supplies to serve growing loads. The difference between the marginal cost of power and the average cost of power included in base rates, coupled with load growth and the use of a historical test year in setting base rates, will cause power supply expenses to be higher than the authorized level. Only because of favorable hydro conditions during 2006 was the Company fortunate enough to keep power supply expenses below the authorized level.

Q. Please quantify the factors driving the change in power supply expenses included in the ERM during the 2006 review period.

A. The table below shows the impact on power supply expenses of the three largest factors affecting expenses in 2006 (Washington allocation shown). Favorable hydro conditions decreased expenses by over $13 million. This decreased expense, however, was mostly negated by the cost of serving higher loads and the increased cost of natural gas to fuel Coyote Spring 2.

The other factor decreasing expenses was the impact of some very lucrative contracts, primarily green power sales to California utilities. Overall, thanks to good hydro conditions, power supply expenses were approximately $2.6 million below the authorized level, resulting in no deferrals, other than a very small amount of interest.

Factors Contributing to Decreased Power Supply Expenses 2006 - Washington Allocation	
Decreased Expense Due to Higher Hydro Generation	-$13,410,242
Increased Expense Due to Higher Prices and Higher Loads	$9,076,997
Increased Expense Due to Higher Fuel Costs for Coyote Springs 2	$3,152,401
Decreased Expense Due to Contracts and Other Factors	-$1,420,820
Total Expenses Below Authorized Level	-$2,601,664

IV. NEW LONG-TERM CONTRACTS ENTERED INTO IN 2006

Q. Please provide a brief description of new long-term contracts that the Company entered into in 2006.

The Company entered into four new long-term contracts during the 2006 review period. In August 2006, the Company entered into a one-year capacity exchange agreement that allows the Company to receive power during on-peak hours and return power during off-peak hours. In September 2006 the Company entered into an agreement to purchase power for ten years from a small power qualifying facility. In November 2006, the Company renewed an exchange capacity agreement for 2007. Finally, in December 2006 the Company entered into an eight-year agreement to sell energy and associated renewable energy credits. These contracts were provided as confidential attachments to the monthly deferral reports.

Q. Are any of these new contracts subject to the limitation for inclusion in the ERM that was part of the recent ERM settlement?

A. No. The recent ERM settlement included limitations on cost recovery for new or renewed contracts that are greater than 50 MW and have more than a two year term. Although one of the new contracts included in this proforma meet that criteria, i.e., it is more than 50 MW and longer than 2 years, it is a sale. The Company chose to not limit the revenue that is credited to customers from this sale in the ERM. The Company has credited all the revenue from this contract to customers even though the ERM Settlement could be interpreted to read that only the amount up to the average cost of production be included in the revenue for ERM calculation purposes. This new long-term sale was entered into in December of 2006, after the ERM settlement.

V. SUPPORTING DOCUMENTATION

R. Please provide a brief overview of the documentation provided by the Company in this filing.

A. The Company maintains a number of documents that record relevant factors considered at the time of a transaction. The following is a list of documents that are maintained and that have been provided as part of this filing on a compact disk:

Gas/Electric Transaction Record: These documents record the key details of the price, terms and conditions of a transaction. As part of this filing the Company has provided two confidential worksheets showing each gas and electric term (one month or longer) transaction during 2006, including all key transactions details such as trade date, delivery period, price, volume and counter-party. Also provided is a Heat Rate Summary worksheet that lists the purchases and sales of natural gas and electricity related to fueling Avista's natural gas fired generation. Additional information can be provided, upon request, for any of these transactions.

Position Reports: These daily reports provide a summary of transactions and plant generation. Also included are forward electric and natural gas prices.

Long-Term Physical Electric Load & Resource Tabulation: For transactions with deliveries extending greater than the 18-month period covered by the Position Report, the Company includes this document to show the net average system position during the extended period. This document also shows variability associated with an 80% confidence interval around the combined variability of hydroelectric generation and variability of load.

Forward Market Electric and Natural Gas Price Curves: This daily data is maintained in Nucleus, the Company's electronic energy transaction database record system.

These documents are in addition to the detailed monthly reports, which are filed with the Commission and provided to interested parties, as discussed by Mr. Mckenzie.

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

A. Yes.