Review of Executive Officer Compensation

Attachment B

2011 Executive Officer Short Term Incentive Plan
for 2011

February 28, 2012

AVISTA CORPORATION & AVISTA UTILITIES

EXECUTIVE OFFICER INCENTIVE PLAN FOR 2011

PLAN PROVISIONS
Approved by Board February 2011

Purpose: The Executive Officer Incentive Plan (Plan) is designed to align the interests of senior management with both shareholder and customer interests to achieve overall positive financial performance for the Company.

Plan Year: January 1, 2011 – December 31, 2011

Eligibility:

- All executive officers hired prior to October 1st and employed on December 31st of the plan year, are eligible to participate
- Subsidiary officers are not eligible to participate
- Other details available in section *Exceptions to Eligibility and Circumstances for Proration*

Performance Measurements: The Executive Officer Incentive Plan incorporates Earnings per Share (EPS) and Operating & Maintenance Cost per Customer (O&M CPC) as financial performance measurements plus four non-financial measurements: Customer Satisfaction Rating (Customer Satisfaction), Reliability Index (Reliability), Dispatched Gas Emergency Response Time (Response Time) and Performance Excellence. These performance measures help to increase shareholder value, gain financial strength and maintain safe and reliable cost-effective service levels essential for the long-term success of the Company, and, with the exception of the earnings per share goals, are identical to performance goals used in the Company's annual incentive plan for non-executive employees. The Compensation Committee believes that having similar metrics for both the executive plan and the non-executive plan encourages employees at all levels of the Company to focus on common objectives.

Utility and Non-Utility Diluted EPS - These measures reflect the financial strength and alignment of interests between officers and shareholders. Non-Utility EPS includes Advantage IQ and other non-utility businesses within the corporation.

O&M CPC - The O&M CPC is a measure that focuses on controlling costs and driving efficiencies in order to keep our costs reasonable for our customers. The measure is based on our projected number of customers, targeted O&M expense and a savings mechanism between employees and the Company. These components are combined to create the O&M CPC metric.

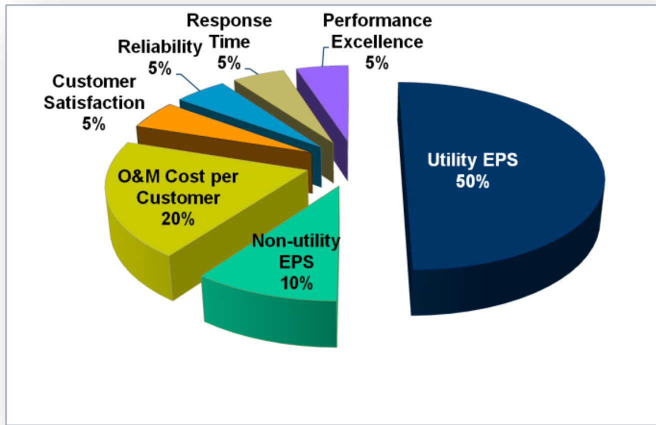
Customer Satisfaction - This measure is derived from a Voice of the Customer survey, which is conducted each quarter by an independent agency. The rating measures the customer's overall satisfaction with the service they received during a recent contact with the service and/or call center. The *Overall Satisfaction* question from surveys such as this is widely used in the industry for external reporting purposes. For this measure, the Company combines the “satisfied” and “very satisfied” ratings from the survey, rather than use the standard “satisfied” rating, which is typically used in the industry. By combining these two ratings it actually makes the target more difficult to achieve.

Reliability - Providing safe and reliable energy to our customers is the backbone of our business, therefore, it makes good sense to focus on service levels for our customers. This measure tracks how quickly the Company restores outages, how frequently customers are affected by outages and what percent of customers are experiencing more than three sustained outages per year. The Company combined three common industry indices in order to balance our focus. The industry names for the indices used are *Customer Average Interruption Duration Index (CAIDI), System Average Interruption Frequency Index (SAIFI) and Customer Experiencing Multiple Interruptions (CEMI^3)*. CEMI^3 is a fairly new metric to the utility industry and measures the percentage of customers that experience more than three sustained outages in the year. The Company chose this level of outages over others because industry data received from JD Power’s customer service surveys indicate that customers are more apt to be dissatisfied after three outages. By focusing on these measurements it enables the Company to direct our resources appropriately and efficiently in order to contain costs and plan for future infrastructure upgrades that will benefit the customer.

Response Time - The Response Time metric measures the percentage of time the Company responds within targeted time goals for dispatched natural gas emergency calls. The Company tracks the time between the receipt of the call to the time our crew or serviceman arrives on-site, assesses the situation and *reports back* to dispatch. The Company tracks two types of emergency calls: priority 1 (blowing gas, explosions and/or fires, etc.) and priority 2 (inside or outside odors, runaway furnaces, etc.). The primary objective is customer and public safety while consistently treating customers the same throughout our service territory.

Performance Excellence - Over the past year, our employees have learned a lot about their work as individuals and as a company through our Performance Excellence efforts. This metric combines two separate measurements into one. By the end of the year, the objective is to implement or complete 92 project milestones and through process improvements achieve $6.2 million in value to redeploy where needed. The metric demonstrates the Company’s commitment to continuously look for opportunities for efficiencies in order to keep costs reasonable for our customers in the long term.

Award Opportunity: The Plan has seven independent metrics, each having their own goal to achieve. The Plan is sliced into pieces – like a pie. The EPS component (Utility 50% and Non-Utility 10%) is the largest piece of the pie at 60 percent. O&M CPC makes up 20 percent of the pie while customer satisfaction, reliability, response time and Performance Excellence each weigh in at 5 percent.



Non-financial pieces: The non-financial pieces of the pie (customer satisfaction, reliability, response time and Performance Excellence) are all-or-nothing goals. If the Company meets the individual target for one of these metrics, employees receive the incentive award for that piece. If the Company fails to meet a goal, employees do not receive any of that incentive. For example, if the Company achieves Customer Satisfaction with a 90% or better rating, employees would receive 5% of their total incentive award opportunity. If the Company achieves 88% which is below the target, employees would receive no award under this piece. This works the same way for each non-financial measurement.

Financial pieces: The Utility and Non-Utility EPS and O&M CPC metrics work a little differently due to the various performance levels that can be met. Depending on the Company's level of performance, the piece of pie employees could earn could be smaller or larger than the target goal amount. In order to receive 100% of the financial piece, the Company must achieve the performance level set at target which is $1.57 for Utility EPS, $0.16 for Non-Utility EPS, or $346.85 for O&M CPC. If the Company meets the lowest performance level at threshold, employees could receive a minimum of 50% for either Utility or Non-Utility EPS or a minimum of 10% for O&M CPC. If the Company performs above target on one of the financial metrics, employees could receive more than 100% or as high as 150% of their incentive award for the specific metric. If the Company fails to meet at least the threshold or minimum on either metric, employees do not receive any of the award under the metric. For example, if the Company achieves an O&M CPC amount of $356.46, employees would receive approximately 16% of this portion (16% of 20%) of their overall award opportunity or if the Company achieves $338.00, employees would receive the maximum of 150% of this portion (150% of 20%) of their award. If the Company achieves an amount such as $359.46 which is below threshold, employees would receive no award under the O&M CPC portion of their award.

Incentive Targets for 2011:

	EPS Utility	EPS Non-Utility	O&M Cost per Customer	Customer Satisfaction	Reliability	Response Time	Performance Excellence
% of Total Award	**50%**	**10%**	**20%**	**5%**	**5%**	**5%**	**5%**
	Payout amount varies depending on level achieved			*Payout depends on achieving target goal*			
Maximum 150%	$1.65	$0.18	$341.70				
Goal Target 100%	**$1.57**	**$0.16**	**$346.85**	**90%**	**100%**	**93%**	**100%**
Minimum 50%	$1.52	$0.13					
Minimum 10%[1]			$357.52				

[1]Threshold payout level starts at 10% for O&M CPC portion of award opportunity.

Establish Targets: The Compensation and Organization Committee of the Board (Committee) in conjunction with management reviews and reestablishes the targets for each measurement on an annual basis. The computations for this Plan are described below:

Utility EPS and Non-Utility EPS: To determine the Utility and Non-Utility EPS goals for the plan, the Committee, in conjunction with the Finance Committee of the Board and management, considers and incorporates the EPS target range contained in the Company's original publicly disclosed earnings guidance and reviews this in light of the budgeted EPS numbers. The earnings guidance for the Utility EPS excludes the earnings impact associated with changes in the Energy Recovery Mechanism (ERM). The target in the Plan is Diluted Earnings per Share and is prior to executive incentive payout/accrual-pro-forma and net of taxes. The actual Utility EPS results will be affected by positive or negative changes in the ERM when computing the plan payout. Occasionally, adjustments to actual results may be deemed necessary. An example of such an adjustment was in 2008 when the positive effect of an accounting error related to Allowance for Funds Used during Construction (AFUDC) was excluded from EPS.

The 2011 guidance for EPS is $1.47 to $1.62 for the Utility and $0.13 to $0.18 for Non-Utility (Advantage IQ and Other combined). The budget is $1.54 for the Utility and $0.16 for Non-Utility. The projected ERM benefit is $0.07, which is excluded from this information for EPS guidance and budget purposes.

To compute the Utility EPS threshold or minimum level, the Company used budgeted EPS less $0.02. To compute the target level, the Company used the budgeted EPS plus $0.03 which reflects zero impact associated with the ERM. To compute the maximum level, the Company added to the top end of the guidance range to create more stretch with respect to budget and guidance. In this Plan, the target is set at $1.57, minimum at $1.52 and maximum at $1.65.

To compute the Non-Utility EPS threshold level, the Company used the low end of the guidance range. To compute the target level, the Company used the budgeted amount.

To compute the maximum level, the Company used the top end of the guidance range. In this Plan, the target is set at \$0.16, minimum at \$0.13 and maximum at \$0.18.

O&M CPC: For this measurement the Company used the total budgeted O&M cost to establish performance goals at different levels. Certain items are excluded from the total budgeted O&M cost such as A/R Sale, Pacesetter, payroll accrual, certain accounting adjustments, and the potential payout for the non-financial measures (customer satisfaction, reliability, response time and Performance Excellence) which are already included in the O&M budget. The Company excludes the amount for the non-financial measures because the Company budgets enough to cover most of the potential payout.

The Company also estimates, at each performance level, the potential payout for the O&M CPC award piece which includes payroll taxes and subtracts the result from the total budgeted O&M cost. The Company uses this methodology in order to build into the performance levels the amount that must be saved in order to pay the incentive. The estimation is based on budget labor costs, employee job levels and corresponding incentive target award opportunities.

Last year the Company used sharing bands where cost reductions were shared between the employee and the Company. In this Plan, the Company continues to use the sharing bands. The performance levels are constructed so that 25% of the first \$2 million in O&M savings is shared with the employees, the other 75% is shared with the Company. Then the next \$3 million in savings is shared 50/50 and any savings in excess of \$5 million is shared 75% with employees. These savings are then subtracted from the total budgeted O&M cost resulting in various levels of performance. The different results are divided by a customer growth target. Using this method, the Company creates varies performance levels: threshold or minimum (10%), target (100%) and exceeds or maximum (150%) for this portion of the plan. In this Plan, the target is set at \$346.85, minimum at \$357.52 and maximum at \$341.70.

Customer Satisfaction: For this measure the Company uses the ratings from question Q3 from the Voice of the Customer survey which measures the customer's *Overall Satisfaction* with the service they received in a recent contact through the call or service center. In this Plan the Company uses the average of the combined "*satisfied*" and "*very satisfied*" ratings. The target is set at 90% very satisfied/satisfied for the customer's Overall Satisfaction rating.

Reliability: This index combines SAIFI, CAIDI and CEMI[3]. To determine the target for the Reliability portion of the Plan, the Company sets a separate target for each metric, weighs them equally and combines them into one metric (see the formula below). In this Plan the target is set at 100%.

$$\text{Index} = \frac{\text{CAIDI Target / CAIDI Actual}}{3} + \frac{\text{SAIFI Target / SAIFI Actual}}{3} + \frac{\text{CEMI}^3\text{ Target / CEMI}^3\text{ Actual}}{3}$$

The formula used to set the target for each metric is described below:

- Customer Average Interruption Duration Index (CAIDI): *outage duration multiplied by the number of customers affected for all sustained outages (> 5 minutes), divided by* *the number of customers which had sustained outages*. The Company excludes larger outages that impact a significant portion of the service territory, and typically last more than 24 hours from the data per industry practice. In this Plan the Company uses a 5 year average with a standard deviation of 0.72 (76% probability) to set the target which is 2 hours and 3 minutes restoration time.

- System Average Interruption Frequency Index (SAIFI): *the number of customers which had sustained outages (> 5 minutes), divided by the number of customers served.* The Company excludes larger outages that impact a significant portion of the service territory, and typically last more than 24 hours from the data per industry practice. In this Plan the Company uses a 5 year average and a standard deviation of 0.72 (76% probability) to set the target which is 1.43 outages per customer.
- Customers Experiencing Multiple Sustained Interruptions more than 3 (CEMI[3]): *the total number of customers that experience more than 3 sustained outages per year, divided by total number of customers served.* Per industry practice large outages are not excluded from this metric. In this Plan the Company uses a 5 year average with a standard deviation of 0.72 (76% probability) to set the target at 12.8% of our customers.

Response Time: This metric represents the percent of time the Company responds within targeted goals for natural gas emergency calls. The Company sets separate response goals for each type of emergency call: 60 minutes for priority 1 calls (blowing gas, explosions and/or fires, etc.) and 120 minutes for priority 2 calls (inside or outside odors, runaway furnaces, etc.). The Company wants crews and/or serviceman to respond within the targeted response time goal for each type of call. The Company excludes anything below 85% (outliers) from the data. In this Plan the Company uses a 2 year average with a standard deviation of 0.72 (76% probability) to set the target at 93% of the time.

Performance Excellence: This metric measures the Company's performance under the Performance Excellence initiatives. The Company is focused on four key initiatives: Asset Management, Supply Chain, Enterprise Technology and Work & Resource Management. Each initiative has established milestones to complete and each has a projected dollar value represented by net present value and/or avoided costs which may occur outside three years. The Company sets a separate goal for each measurement: complete 102 milestones and achieve $6.9 million in realized value. In this Plan the Company used 90% of the total to establish the targeted goals for each measurement: 92 (90% of 102) milestones and $6.2 (90% of $6.9) million in value. Both measurements must be achieved in order to meet this portion of the incentive award, therefore, the target for this metric is 100%.

Individual Target Award Opportunities: During the February Board meeting, the Committee and the Chief Executive Officer (CEO) jointly review and approve the individual target award opportunities for the participants of the Plan. Each employee has an incentive target award opportunity expressed as a percentage of their base salary. Target opportunities range from 40% to 90% of base salary and are assigned based on position. Actual award payments are calculated based on the employee's target award opportunity in effect as of December 31st and year-end regular earnings (see regular earnings definition under *Exceptions to Eligibility and Circumstances for Proration* section).

	Individual Target Award Opportunity			
	VP	President	Senior VP	CEO
% of Base Pay by Position Type	40%	60%	60%	90%

Incentive amounts in excess of 100% (up to 150%) of an individual's target opportunity may be paid in the form of non-cash equivalents, at the discretion and approval of the CEO and the Committee.

Example Award Calculation:
The Company achieved the targets indicated below:
Utility EPS = 100.0% on the sliding scale
Non-Utility EPS = 116.7% on the sliding scale
Cost per Customer = 130.1% on the sliding scale
Customer Satisfaction = 100% = met/pass
Reliability = 100% = met/pass
Response Time = 100% = met/pass
Performance Excellence = 0% = not met/fail

Non-CEO Avg base pay = $252,242 Avg Target Opportunity = 47% = $118,554

Utility EPS	$118,554	X	50%	X	100.0%	=	$59,277
Non-Utility EPS	$118,554	X	10%	X	116.7%	=	$13,835
Cost per Customer	$118,554	X	20%	X	130.1%	=	$30,848
Customer Satisfaction	$118,554	X	5%		pass	=	$5,928
Reliability Index	$118,554	X	5%		pass	=	$5,928
Response Time	$118,554	X	5%		pass	=	$5,928
Performance Excellence	$118,554	X	5%		fail	=	$0.00
Total Payout = $121,744							

Distribution of Awards: Incentive awards, if earned, will be distributed after the February meeting of the Board of Directors of the next Plan year. In most instances actual amounts will be calculated using the participant's regular year-end earnings, individual target award opportunity and employment status in effect as of December 31st of the Plan year. See the section *Exceptions to Eligibility and Circumstances for Proration* for exceptions.

In order to communicate and calculate payout amounts consistently for each financial based metric, the Company will round results to the nearest 10th percent based on accounting rules. For example, if the O&M CPC result is 130.12% or 130.072%, the Company will use 130.1% to communicate results and calculate the payment of the O&M CPC portion of the award. The non-financial metrics will be communicated and calculated differently. In order to communicate the results for each non-financial based metric, the Company will round results to the nearest whole percent such as 93% for customer satisfaction or 137% for reliability. Unlike the financial metrics which use the final results in the payment calculation (130.1% of the 20% O&M CPC portion of the total award), the non-financial metrics use the percent assigned to the metric (5% customer satisfaction, 5% reliability, 5% response time and 5% Performance Excellence) to calculate the payout amount. For example, if the Company achieves 137% under the Reliability piece, employees will receive 5% of their total award, not 137% of the 5% piece. See detail calculation above.

All incentive awards earned by a participant under this Plan are subject to the Recoupment Policy adopted by the Company's Board of Directors as amended from time to time ("Recoupment Policy"). If a participant becomes subject to the Recoupment Policy any award may be forfeited in whole or in part and all or part of any distribution payable to a participant or his or her beneficiary under this Plan may be recovered by the Company pursuant to the Recoupment Policy.

Administration of Plan: The Committee is responsible for administering the Plan and may delegate specific administrative tasks to corporate staff, as appropriate.

The Committee has the authority to:

- Terminate, amend or modify this Plan in whole or in part for any reason at any time without prior notice to participants
- Modify or adjust financial targets due to extraordinary occurrences and/or significant reorganizations
- Grant discretionary awards up to 15% of the individual target award opportunity

Participation in this Plan should in no way be construed as a contract or promise of employment and/or compensation.

Exceptions to Eligibility and Circumstances for Proration

Proration: Proration is determined by the change of status (COS) date as well as the number of pay periods during the eligibility period. There are 26 pay periods during a Plan year. No matter if the COS date occurs on the first day or the last day of the pay period, the employee would receive credit for the full pay period. For example, an employee who is hired on the third day of the 12th pay period of the year and remains employed throughout the Plan year would be eligible for 15 pay periods of their award.

Regular Earnings: Regular earnings (pensionable earnings) will be used in calculating the awards for employees. The earnings to be used in the calculation are as follows: earnings designated regular, alternative/dual, One Leave (used, sick, & FMLA), short-term disability (100% and 60%), workers compensation, holiday, jury duty, and military pay.

New Hires: Employees hired on or after October 1st will not be eligible for an award under this Plan.

Leave of Absence: Eligible employees on approved unpaid leave of absence during the Plan year may receive an award on a prorated basis. *Short-term disability leave is excluded from this provision and may be eligible to receive awards.*

Resignation/Termination: Any employee who resigns or is terminated for reasons other than retirement, disability or death prior to December 31st will not be eligible to receive an award under this Plan. Employees who are eligible for an award and employed as of December 31st but resign or terminate after the Plan year may receive an award at the time of distribution.

Death, Long-term Disability & Retirement: In the case of death, total disability (as defined under the Company's Long-term Disability Plan) or retirement (as defined under the Retirement Plan for Employees), an eligible employee or estate must have at least 3 full months of service within the Plan year to be eligible to receive an award on a prorated basis.

Discipline or Poor Performance: Employees who receive a **fails to meet** performance rating for the Plan year or a **Last Chance Agreement** under the Company's formal discipline program as of December 31st are not eligible to receive an award under this Plan.

Transfers from Subsidiaries to Corp/Utilities: Eligible employees who transfer from a subsidiary will be treated as a new hire to the Company and all Plan criteria apply as is. Prorated awards are at the discretion of the Committee and CEO.

Other Company Short-term Incentive Plans: Employees can only participate under one formal incentive plan a year. If the employee becomes eligible for a different plan during the year, the Committee and CEO has full discretion to determine which plan the employee may receive an award under. Status and/or time in position may be factors considered in determining whether the employee will receive a prorated award from both plans or an award based on the employee's position and/or status as of December 31st.