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October 24, 2006

Oregon Public Utility Commission  
Attn: Filing Center  
550 Capitol St. NE, Suite 215  
Salem, OR 97301-2551

**RE: Docket UM1250**

Enclosed for filing with the Commission are the original and 5 copies of Avista Corporation's direct testimony and exhibits in Docket UM-1250, regarding the Company's request for an Order Approving a Corporate Reorganization To Create a Holding Company.

An electronic copy of these documents has also been filed pursuant to OAR 860-011-0012.

If you have any questions regarding this filing, please contact myself at 509-495-4316 or Liz Andrews at 509-495-8601.

Sincerely,

A handwritten signature in black ink, appearing to read "David J. Meyer", with a horizontal line extending to the right.

David J. Meyer  
Vice President and Chief Counsel for  
Regulatory and Governmental Affairs.

Enclosures

c: See attached service list

**CERTIFICATE OF SERVICE**

**I HEREBY CERTIFY** that I have served Avista Corporation's Direct Testimony and Exhibits in Docket UM 1250, by mailing a copy thereof or by electronic mail where paper service has been waived, to the following:

Edward A. Finklea  
Chad M. Stokes  
Cable Huston Benedict  
Haagensen & Lloyd LLP  
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Citizens' Utilities Board  
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Industrial Customers of  
Northwest Utilities  
Davison Van Cleve, P.C.  
333 S. W. Taylor, Suite 400  
Portland, OR 97204

Dated at Spokane, Washington this 22nd day of October 2006.

  
\_\_\_\_\_  
Patty Olsness  
Rates Coordinator

BEFORE THE  
PUBLIC UTILITY COMMISSION OF OREGON

DOCKET NO. UM-1250

DIRECT TESTIMONY OF KELLY O. NORWOOD  
REPRESENTING THE AVISTA CORPORATION

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Policy and Overview

1 **I. INTRODUCTION**

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

3 A. My name is Kelly O. Norwood. I am employed as the Vice-President of State and  
4 Federal Regulation for Avista Utilities at 1411 East Mission Avenue, Spokane, Washington.

5 **Q. Please briefly describe your educational background and professional  
6 experience.**

7 A. I am a graduate of Eastern Washington University with a Bachelor of Arts Degree  
8 in Business Administration, majoring in Accounting. I joined the Company in June of 1981.  
9 Over the past 25 years, I have spent approximately 14 years in the Rates Department with  
10 involvement in cost of service, rate design, revenue requirements and other aspects of  
11 ratemaking. I spent approximately 11 years in the Energy Resources Department (power supply  
12 and natural gas supply) in a variety of roles, with involvement in resource planning, system  
13 operations, resource analysis, negotiation of power contracts, and risk management. I was  
14 appointed Vice-President of State & Federal Regulation in March 2002.

15 **Q. What is the purpose of your testimony?**

16 A. My testimony provides an overview of Avista's request for authority to form a  
17 holding company in the manner and under the terms and conditions set forth within the  
18 Company's testimony. I will summarize the milestones reached thusfar in the proposed  
19 corporate reorganization, and the remaining steps necessary to complete the reorganization. I  
20 will also introduce the other witnesses providing testimony on behalf of Avista.

21 **Q. Are you sponsoring any exhibits to be introduced in this proceeding?**



1 corporation (the “Parent Company” or “AVA”) of the existing regulated company, Avista  
2 Corporation (to be renamed Avista Utilities, Inc.). The Parent Company would also be the  
3 Parent Company of Avista Capital, Inc., which would continue to hold the non-regulated  
4 affiliates.<sup>2</sup>

5 Currently the Utility is the corporate parent (Avista Corporation) and does business as  
6 (dba) Avista Utilities. Company witness Mr. Malquist describes Avista’s current business  
7 operations and Avista’s current Company organization charts for both Avista Corporation and  
8 Avista Capital are included as Exhibit No. 201.

9 In the proposed structure, Avista Utilities would become a separate company under the  
10 new holding company. Avista Corporation would no longer exist as an operating entity. Avista  
11 Capital, Inc. would remain a business entity and would be owned by the new AVA holding  
12 company. A comparison of the current and proposed structures are included as Exhibit No. 101.

13 The purpose of and process for forming the proposed holding company structure is  
14 described below, as well as anticipated benefits and commitments by Avista to its customers.

15

16

### **III. REORGANIZATION PURPOSE**

17

**Q. Please describe the purpose of the Reorganization.**

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19

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21

A. The holding company structure is a well-established form of organization for  
companies engaging in multiple lines of business, and is prevalent in the utility industry. Many  
utilities are organized under a public holding company structure and Avista is one of the few  
investor-owned utilities in the Pacific Northwest that is not currently organized under a holding

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<sup>2</sup> The only exceptions would relate to Avista Receivables, Inc. and Spokane Energy, LLC, which would continue to

1 company structure. Avista's request is similar to other utilities in the Pacific Northwest that have  
2 received approvals for similar holding company structure reorganizations in recent years, most  
3 notably Idaho Power Company in Docket No. UM 877, and Puget Sound Energy in Docket No.  
4 UE-991779. Avista has also recently received approvals to form a holding company from the  
5 Idaho Public Utilities Commission (IPUC) on June 30, 2006 by Order No. 30091, Case Nos.  
6 AVU-E-06-1 and AVU-G-06-1, and the Federal Energy Regulatory Commission (FERC), on  
7 April 18, 2006, by Docket No. EC06-85-000.

8 With the changes to the Public Utility Holding Company Act of 1935 or "PUHCA",  
9 Avista considers it to be in the best interest of the Company, its customers and its shareholders,  
10 to change the corporate structure of Avista into a holding company structure. As further  
11 discussed by Mr. Malquist, this Reorganization would provide additional protection for  
12 ratepayers by "ring fencing" or further separating utility operations from the Company's other  
13 non-regulated businesses. Such separation would further insulate Avista Utilities and its  
14 customers from the risks associated with operating other businesses, while at the same time,  
15 permitting greater financing flexibility afforded by a holding company structure.

16 **Q. Why has Avista chosen to pursue the formation of a holding company**  
17 **structure at this time?**

18 A. Avista did not pursue the formation of a holding company structure prior to this  
19 time due primarily to the requirements of PUHCA 1935. PUHCA would have required Avista to  
20 become a registered holding company, and would have imposed significant reporting and  
21 accounting burdens on the Company. The Company's multi-state operations would have made it

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remain affiliates of Avista Utilities.

1 very difficult, if not impossible, to receive an exemption under PUHCA 1935. However, with  
2 the recent repeal of PUHCA 1935 and the enactment of PUHCA 2005, effective February 8,  
3 2006, the distinction between registered holding companies and exempt holding companies that  
4 existed under PUCHA 1935 is eliminated, and the accounting and reporting requirements are  
5 reduced.

6 **Q. Are there other Utilities in the region that have sought similar Commission**  
7 **approvals?**

8 A. Yes. Many other utilities throughout the country have formed holding companies,  
9 including Idaho Power and Puget Sound Energy, as mentioned previously. In fact, Avista is one  
10 of the few remaining investor-owned utilities in the Pacific Northwest that is not organized under  
11 a Holding Company structure.

12 An example of state Commission rulings authorizing approval of similar holding  
13 company structure reorganizations in recent years include, in 1998, the Idaho Power Company  
14 received approval, with conditions, from the OPUC (Order No. 98-056 in Docket No. UM 877),  
15 authorizing the creation of a holding company structure. Avista's application, including the  
16 conditions set forth therein, is substantially identical to what was approved for Idaho Power  
17 Company in Docket No. UM 877.

18 Another example includes the Order received by Idaho Power Company in 1998, from the  
19 IPUC (Order No. 27348 in Case No. IPC-E-97-11), and the Order of the Washington Utility and  
20 Transportation Commission (WUTC) (Docket No. UE-991779) authorizing the creation of a  
21 holding company structure for Puget Sound Energy Inc..





1 just and reasonable and in this context would continue to be able to, among other things, review  
2 transactions between AVA and any affiliated or subsidiary company.

3 **Q. If approved, what changes, if any, to the Utility or its assets are expected**  
4 **from this reorganization?**

5 A. The proposed Reorganization would not entail the transfer of Utility assets, nor  
6 would it adversely affect the financial, technical, and managerial abilities of Avista Utilities.  
7 Avista customers would see no change in the Utility or its operations, because the Utility would  
8 continue to provide the same high-quality service as before the Reorganization. After the  
9 Reorganization, Avista Utilities would continue to be subject to the same regulatory jurisdiction  
10 of the Commission as to rates, service, accounting and other general matters related to utility  
11 operations.

12 **Q. Would there be a change for Avista employees?**

13 A. Avista employees currently reporting to Avista Corporation (dba Avista Utilities)  
14 would not change after the Reorganization, with the exception of the five senior Officers who  
15 would also report to the new AVA holding company. As described further by Company witness  
16 Ms. Andrews, the allocation of these Officers' salaries and expenses as appropriate between  
17 Avista's regulated and non-regulated businesses would follow the same procedures as under the  
18 Company's current structure.

19

20

21

1 **V. STATUS OF REORGANIZATION PROPOSAL**

2 **Q. Please summarize the steps that have been taken thusfar toward**  
3 **implementation of the Reorganization proposal, and the remaining steps necessary to**  
4 **complete the Reorganization.**

5 A. For 2006, the activities and timeline for the Reorganization that have been  
6 completed to date are as follows:

- 7 • Avista received authorization from Avista Corporation's Board of Directors on  
8 February 10<sup>th</sup> to proceed with the Reorganization.
- 9 • Avista filed applications during the week of February 13<sup>th</sup> requesting approval of the  
10 Reorganization with the Public Utility Commission of Oregon, the Idaho Public  
11 Utilities Commission, the Washington Utilities and Transportation Commission, and  
12 the Montana Public Service Commission. On June 30, 2006 Avista received approval  
13 from the Idaho Public Utilities Commission, Order No. 30091, Case Nos. AVU-E-06-  
14 1 and AVU-G-06-1.
- 15 • Avista filed an application during the week of February 13<sup>th</sup> requesting approval of  
16 the Reorganization with the Federal Energy Regulatory Commission (FERC). Avista  
17 received this approval from FERC on April 18, 2006, Docket No. EC06-85-000.
- 18 • Avista filed a registration statement (S-4, File No. 333-131872) and proxy materials  
19 (File No. 1-3701) during the week of February 13<sup>th</sup> with the Securities and Exchange  
20 Commission (SEC). Avista received approval from the SEC in April 2006.
- 21 • Avista received shareholder approval of the Reorganization at the May 11<sup>th</sup> annual  
22 meeting of shareholders.
- 23 • Avista continues to assess requirements related to its currently outstanding debt and  
24 contract obligations and has received consents from appropriate parties, including  
25 consents under Avista Corp.'s credit line, Avista Corp.'s accounts receivable sale  
26 program and Avista Energy's credit line.<sup>3</sup>

27  
28 In addition, the remaining activities to be completed are as follows:

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<sup>3</sup> Avista currently has been unsuccessful in receiving consents from the 9.75% Senior Note holders to dividend Avista Capital to the new holding company. Note that Avista does not need the Senior Note holders' consent to form the holding company, only consent to dividend Avista Capital to the holding company. As a result, the actual accounting separation of Avista Capital from Avista Utilities would not occur until the Senior Notes mature on June 1, 2008, if consents are not received.



1           The meaning of “serve the public utility’s customers in the public interest” was the  
2 subject of a Commission investigation in Docket No. UM 1011. The Commission resolved the  
3 Docket by issuing Order No. 01-778, which adopted a two-pronged legal standard under ORS  
4 757.511(3): “...in addition to finding a net benefit to the utility’s customers, we must also find  
5 that the proposed transaction will not impose a detriment on Oregon citizens as a whole.” *See*  
6 Order No. 01-778 at 11. Stated differently, “if the benefits outweigh the harms, then the net  
7 benefit standard has been met and the application must be granted.” Order No. 05-114 (Dkt. UM  
8 1121) at p.33.

9           In enunciating the “net benefits” test in UM 1011, however, the Commission was careful  
10 to point out that the test is not reduced simply to “economic considerations”; rather the “total set  
11 of concerns” presented by the application must be considered:

12           We do not believe that this standard is either rigid or arbitrary, as the opposing  
13 parties assert. We do not intend to reduce the net benefit standard to economic  
14 considerations as a matter of policy. We will consider the total set of concerns  
15 presented by each merger application in determining how to assess a net benefit.  
16 This allows us to retain flexibility in our decision making, a desideratum in  
17 today’s uncertain climate.

18  
19 See Order No. 01-778, at 11.

20           **Q. Does this transaction provide “net benefits” to Avista’s customers?**

21           A. Yes, it does. There are benefits to ratepayers from the formation of a holding  
22 company. These are discussed in my testimony and that of Mr. Malquist, and may be  
23 summarized as follows:

- 24           • Avista’s utility operations would be better separated from the non-utility  
25 businesses, making cross subsidization easier to avoid and further ensuring  
26 that non-utility business risk would not affect utility operations.  
27

- 1 • The new structure would provide better legal protection for Avista Utilities  
2 from liabilities arising from other segments of Avista’s business.  
3
- 4 • The new structure would permit investors, analysts, and rating agencies to  
5 more easily analyze and value the individual lines of business.  
6
- 7 • Capital structures and financing techniques may be used that are better  
8 suited to the particular requirements, characteristics, and risks of the utility  
9 and non-utility businesses. Such structures and techniques should increase  
10 financial flexibility without adversely affecting the capital structure or  
11 creditworthiness of the utility and non-utility businesses.  
12

13 Moreover, this transaction, as proposed, will avoid harm to customers in the State of  
14 Oregon. A number of commitments are being made by Avista to protect the interests of  
15 ratepayers and assure continued regulatory oversight and access to books and records. These  
16 protections are summarized as follows:

- 17 • The cost of the formation of the Holding Company would not be included in  
18 future Avista Utility ratemaking proposals.
- 19 • Avista would continue to provide the Commission with access to information for  
20 the Holding Company and all affiliates for audit purposes.
- 21 • Avista would continue to maintain prudent utility operating standards.
- 22 • Avista would continue to maintain internal controls that preclude “cross-  
23 subsidization” between the utility and other affiliates.
- 24 • Avista would continue to assure segregation of operations among the utility and  
25 other affiliated entities, prevent co-mingling of assets, and would continue to  
26 comply with all applicable statutes, rules, and Commission practices regarding  
27 property transfers, affiliated or subsidiary transactions, and securities transactions.
- 28 • Avista would fairly allocate Holding Company costs (or corporate support costs)  
29 among the utility and other affiliates.  
30

31 These protections are expanded upon in the set of commitments set forth in Exhibit No.  
32 102, as already agreed upon in the State of Idaho and which the Company would offer in this  
33 jurisdiction as well.

1           Accordingly, Avista Utilities' customers would see no change due to this transaction.  
2           Avista Utilities would continue to own, operate, and manage all of its facilities used in the  
3           generation, transmission and sale of electricity and the distribution of natural gas. Customers  
4           would see no change in rates resulting from the cost of forming the holding company. The  
5           Reorganization would not affect the ability of the Commission to regulate Avista Utilities.

6           In conclusion, when taking into account the net benefits and the "total set of concerns"  
7           being addressed by the application, the Commission can conclude that this transaction is in the  
8           public interest.

9

10           **Q.     In the IPUC's recent Order No. 30091, referred to above, did the IPUC come**  
11           **to the conclusion that the Reorganization as proposed by the Company was in the public**  
12           **interest?**

13           A.     Yes. Within their Order No. 30091, at page 4, the IPUC states:

14                     "The commission finds that the commitments in the Stipulation assure  
15                     that the public interest is protected with ring-fencing provisions and that these  
16                     barriers are not overcome by any affiliate where the credit rating of one is used  
17                     to offset the diminished rating of the other. The operations and structure of  
18                     Avista Utilities and the Parent Corporation will continue to meet the  
19                     requirements of having the bona fide intent and financial ability to operate and  
20                     maintain said property in the public service."

21

22           **Q.     As previously mentioned, FERC has also recently approved Avista's**  
23           **application to form a holding company. What conclusion did FERC reach in its Order?**





BEFORE THE  
PUBLIC UTILITY COMMISSION OF OREGON

DOCKET NO. UM-1250

AVISTA CORP

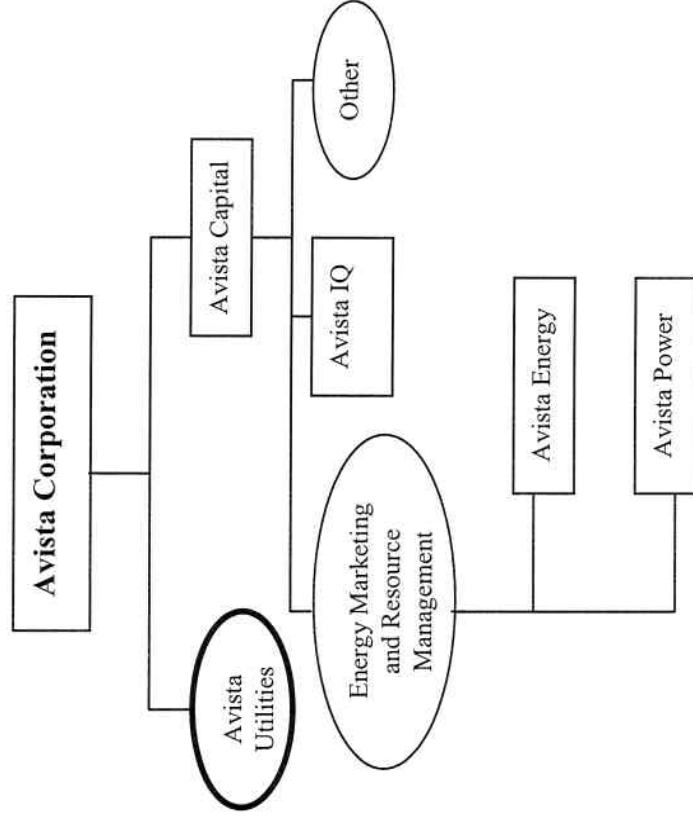
KELLY O. NORWOOD  
**Exhibit No. 101**

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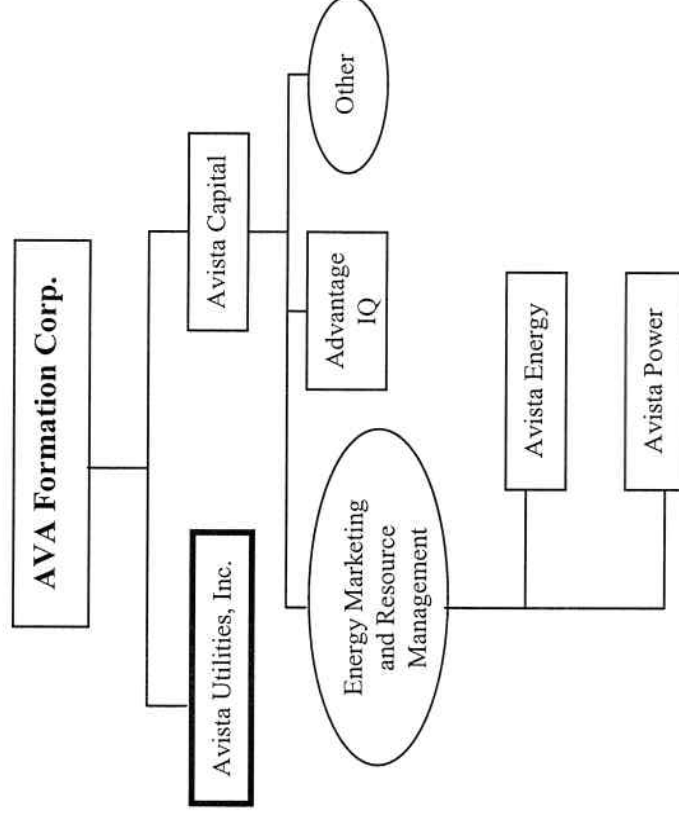
Policy and Overview

# Avista Corporation Comparison of Organization Structures

Current Organization Structure



Proposed Organization Structure



- denotes a business entity; Advantage IQ is also a business segment.  
 - denotes business segment.

BEFORE THE  
PUBLIC UTILITY COMMISSION OF OREGON

DOCKET NO. UM-1250

AVISTA CORP

KELLY O. NORWOOD  
**Exhibit No. 102**

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Policy and Overview

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION )  
OF AVISTA CORPORATION DBA AVISTA ) CASE NOS. AVU-E-06-1  
UTILITIES FOR AN ORDER APPROVING A ) AVU-G-06-1  
CORPORATE REORGANIZATION TO )  
CREATE A HOLDING COMPANY, AVA ) ORDER NO. 30091  
FORMATION CORP. )

On February 16, 2006, Avista Corporation dba Avista Utilities (“Avista” or “Company”) filed an Application with the Idaho Public Utilities Commission seeking an order for authority to conduct a corporate reorganization and form a holding company to be known as AVA Formation Corp. This Commission has the jurisdiction over such request pursuant to *Idaho Code* § 61-328.

On April 28, 2006, the Commission issued a Notice of Application, Notice of Workshop and Notice of Modified Procedure, seeking comments from any interested persons. See Order No. 30026. The Order specifically set forth that a public workshop would be held on May 16, 2006 to discuss issues arising from the Application. No person or entity petitioned to intervene in the matter.

Avista requested an order granting the Company authority to modify its current corporate structure through the establishment of a holding company. The holding company, AVA Formation Corp. (the “Parent Corporation”), would be formed as the parent company of the existing regulated company, Avista Corporation. The Parent Corporation would also be the parent company of Avista Capital, Inc., which would continue to hold non-regulated subsidiaries.

Avista Corporation, doing business as Avista Utilities, is currently the corporate parent. The proposed structure would make Avista Utilities a separate company under the Parent Corporation and Avista Corporation would no longer exist as an operating entity.

Avista states that due to the recent repeal of the Public Utilities Holding Company Act of 1935 (PUHCA), the Company considers it to be in the best interest of customers and shareholders to change the corporate structure of Avista by forming a holding company structure. The Company believes that this reorganization would provide additional protection for ratepayers by “ring-fencing” or further separating utility operations from the Company’s other non-regulated businesses.

### THE STIPULATION

Pursuant to Order No. 30026, representatives of the parties conducted a public workshop on May 16, 2006, and engaged in discussions focusing on key protections for ratepayers with a view toward resolving issues arising from the Application. No other persons attended the meeting. Based upon the discussions between the parties as a compromise of the positions in this case, and for other consideration as set forth below, the parties agreed to various commitments that the Company will undertake as part of the reorganization.

The settlement Stipulation contains 33 “commitments” or conditions that the Company commits to perform in support of the Application. The commitments address the need for ring-fencing, allow the Commission and Staff substantial access to the books and records of the utility and Parent Corporation, set forth cost allocation methodologies, and address equity building mechanisms and dividend payments. The Stipulation parties assert that the commitments satisfy the statutory standards for the Company’s reorganization as set out in *Idaho Code* § 61-328. Stipulation at § 9. In the Motion that accompanied the Stipulation, the parties urged the Commission to adopt the Stipulation, its commitments, and issue an Order approving the reorganization.

The Company will need to approach other states to seek their approval of the reorganization. The settlement Stipulation also contains a “most favored nations” provision. Stipulation at § 7. This provision allows the Commission to review and adopt any commitment or condition ordered by the other states, even after an Order in this matter is issued. Thus, any assurances, conditions or benefits adopted in the other states that would create a benefit to Idaho customers could subsequently be adopted in Idaho under the terms of the Stipulation.

The parties to the Stipulation recommended that the Commission approve and adopt the commitments in their entirety. They further agree not to appeal any portion of the Stipulation or any Order approving the same. The Stipulation parties also recognize that approval of the Stipulation and commitments shall not bind the Commission “in other proceedings with respect to the determination of prudence, just and reasonable character, rate or ratemaking treatment, or public interest of services, accounts, costs, investments, in any particular construction project expenditures or actions referred to in (the) Commitments.”

### COMMENTS

Comments to the Application were received from a member of the public and from the Commission Staff. The member of the public is a customer and shareholder of the Company. The customer expressed concern that the Parent Corporation may be unable to resolve bad loans it may procure without negatively impacting the utility company. The customer urged the Commission to deny the Company's Application.

Staff contends that the Application along with the commitments in the Stipulation meet the requirements set forth under *Idaho Code* § 61-328. Staff points out that Commitment Nos. 1, 4, 8, 9, 10, 11, 15, 17, 18, 19, 29, 30, and 31 address the need for ring-fencing, with provisions ranging from separate books and records for each entity to providing a non-consolidated opinion to the Commission demonstrating that the ring-fencing around Avista Utilities is sufficient to prevent Avista Utilities from being pulled into a Parent Corporation bankruptcy proceeding. Additionally, Commitment Nos. 2, 3, 5, 13, 23, and 24 provide Staff with access to a full range of books, records and other documents which would pertain to Avista Utilities and its affiliates, including the Parent Corporation. Comprehensive reporting requirements are also included in the commitments that would require the Parent Corporation and Avista Utilities to report to Staff and request approval from the Commission when certain events occur, such as the procurement of loans, the spin-off of any entity, the dissolution of business activities, dividend payment arrangements, and changes in the credit ratings of each entity.

In addition, Staff supports the commitments that include comprehensive arrangements for complying with cost allocation methodologies, as well as commitments involving the payment of dividends. The Company agreed, in Commitment No. 18, that Avista Utilities will not make any dividends to the Parent Corporation that would reduce Avista Utilities' common equity capital below 25% of its Total Adjusted Capital without the Commission's approval.

Staff believes that the reorganization should reduce the utility's risk and improve credit ratings. Staff does not anticipate rating downgrades based on recent credit rating reviews. However, in the event of a credit rating downgrade due to the reorganization, Staff will calculate the impact on customers and propose an adjustment be made to Avista Utilities' revenue requirement in the appropriate rate proceedings.

Staff recommended approval of the proposed reorganization given that the Company and its affiliates have agreed to implement these specific commitments, conditions and reporting mechanisms. Staff recommended that the Commission accept and approve the Stipulation and adopt the Commitments in Appendix A thereto. Staff asserts that these Commitments adequately protect Idaho ratepayers and serve the public interest.

#### COMMISSION FINDINGS

Before authorizing such a transaction, the Commission must find that: (1) the transaction is consistent with the public interest; (2) the cost of and rates for supplying service will not be increased by reason of such transaction; and (3) Avista has the bona fide intent and financial ability to operate and maintain Avista's operation in Idaho. Based on its review of the Application, the Stipulation, the comments and other documents related to this matter, the Commission finds that the above standard has been met.

In reviewing the Company's Application and the agreed-upon commitments, the Commission finds that the parties took into account customer comments that expressed concerns regarding loan arrangements and inter-company financing. Commitment No. 29 addresses these concerns by requiring Avista Utilities to demonstrate that the procurement of any loan from the Parent Corporation does not interfere with any of the ring-fencing mechanisms that secure the utility.

The Commission finds that the commitments in the Stipulation assure that the public interest is protected with ring-fencing provisions and that these barriers are not overcome by any affiliate where the credit rating of one is used to offset the diminished rating of the other. The operations and structure of Avista Utilities and the Parent Corporation will continue to meet the requirement of having the bona fide intent and financial ability to operate and maintain said property in the public service.

#### CONCLUSIONS OF LAW

The Commission has jurisdiction over this matter pursuant to *Idaho Code* § 61-328. Section 61-328 prohibits Avista from transferring any interest in Avista without the written authorization of this Commission. The Commission may attach conditions to its authorization and enter any final Order consistent with its authority under Title 61.

ORDER

IT IS HEREBY ORDERED that the Applications of Avista Corporation, Case Nos. AVU-E-06-1 and AVU-G-06-1, and the Stipulation and the commitments therein, are approved.

THIS IS A FINAL ORDER. Any person interested in this Order may petition for reconsideration within twenty-one (21) days of the service date of this Order with regard to any matter decided in this Order. Within seven (7) days after any person has petitioned for reconsideration, any other person may cross-petition for reconsideration. *See Idaho Code* § 61-626.

DONE by Order of the Idaho Public Utilities Commission at Boise, Idaho this 30<sup>th</sup> day of June 2006.

  
\_\_\_\_\_  
PAUL KJELLANDER, PRESIDENT

  
\_\_\_\_\_  
MARSHA H. SMITH, COMMISSIONER

  
\_\_\_\_\_  
DENNIS S. HANSEN, COMMISSIONER

ATTEST:

  
\_\_\_\_\_  
Jean D. Jewell  
Commission Secretary

O:AVU-E-06-01\_AVU-G-06-01\_cg2



APR 15 2006 4:2  
PUBLIC UTILITIES COMMISSION

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BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION OF	)	CASE NO. AVU-E-06-1
AVISTA CORPORATION DBA AVISTA	)	AVU-G-06-1
UTILITIES FOR AN ORDER APPROVING	)	
A CORPORATE REORGANIZATION TO	)	STIPULATION
CREATE A HOLDING COMPANY,	)	
<u>AVA FORMATION CORP.</u>	)	

This Stipulation ("Stipulation") is entered into by and between Avista Corporation, doing business as Avista Utilities ("Avista"), and the Idaho Public Utilities Commission Staff ("Staff") (collectively referred to as the "Parties").

I. INTRODUCTION

1. The terms and conditions of this Stipulation are set forth herein. The Parties agree that this Stipulation represents a fair, just and reasonable compromise of the issues raised in this proceeding and that this Stipulation is in the public interest. The Parties, therefore, recommend that the Public Utilities Commission ("Commission") approve the Stipulation and all of its terms and conditions. Reference IDAPA 31.01.01.272,274.

## II. BACKGROUND

2. On February 16, 2006, Avista filed an Application with the Commission seeking an order for authority to conduct a corporate reorganization and form a holding company to be known as AVA Formation Corp (hereinafter referred to as the "Reorganization"). This Commission has the jurisdiction over such request pursuant to *Idaho Code* § 61-328. The holding company, AVA Formation Corp. (the "Parent Corporation" or "AVA"), would be formed as the parent company of the existing regulated company, Avista Corporation. The Parent Corporation would also be the parent company of Avista Capital, Inc., which would continue to hold non-regulated subsidiaries.<sup>1</sup>

3. On April 28, 2006, the Commission issued its Order No. 30026, providing a Notice of Application, Notice of Workshop, and a Notice of Modified Procedure.

4. No petitions to intervene in this proceeding were filed in this matter.

5. Pursuant to the Commission's Order No. 30026, representatives of the Parties conducted a workshop on May 16, 2006, and engaged in informal settlement discussions with a view toward resolving the Application in this case.

Based upon the settlement discussions among the Parties as a compromise of the positions in this case, and for other consideration as set forth below, the Parties agree to the following terms:

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<sup>1</sup>Avista Corporation, doing business as Avista Utilities, is currently the corporate parent. The proposed structure would make Avista Utilities a separate company under the Parent Corporation and Avista Corporation would no longer exist as an operating entity.

### III. TERMS OF THE STIPULATION

6. Appendix A contains the complete list of commitments that Avista agrees to make related to the formation and future conduct of the holding company corporate structure (hereinafter referred to as "Commitments"). By virtue of executing this Stipulation, Avista agrees to perform all of the Commitments set forth in Appendix A according to the provisions of each Commitment as set forth therein.

7. In the process of obtaining approvals of the Reorganization in other states, the Commitments may be expanded or modified as a result of regulatory decisions or settlements. Avista agrees that the Commission shall have an opportunity and the authority to consider and adopt in Idaho any commitments or conditions to which Avista agrees or with which Avista is required to comply in other jurisdictions, even if such commitments and conditions are agreed to after the Commission enters its order in this docket. To facilitate the Commission's consideration and adoption of the commitments and conditions from other jurisdictions, the Parties urge the Commission to issue an order accepting this Stipulation as soon as practical, but to reserve in such order the explicit right to re-open Appendix A to add (without modification of the language thereof except such non-substantive changes as are necessary to make the commitment or condition applicable to Idaho) commitments and conditions accepted or ordered in another state jurisdiction. The Parties recommend the following process related to potential additional commitments and conditions originating from proceedings in other states:

- Within five calendar days after a stipulation with new or amended commitments is filed by Avista with a commission in another state

jurisdiction, Applicants will send a copy of the stipulation and commitments to the Idaho Commission Staff.

- Within five calendar days after a commission in another state jurisdiction issues an order that accepts a stipulation to which Avista is a party or otherwise imposes new or modified commitments or conditions, that order, together with all commitments and conditions of any type agreed to by Avista or ordered by the commission in such other state, will be filed with the Commission and served on all Parties to this docket by the most expeditious means practical. Within fifteen business days after receiving the last such filing from the other states (“Final Filing”), any Party to the docket wishing to do so shall file with the Commission its response, including its position as to whether any of the covenants, commitments and conditions from the other jurisdictions (without modification of the language thereof except such non-substantive changes as are necessary to make the commitment or condition applicable to Idaho) should be adopted in Idaho.
- Within five calendar days after any such response filing, any Party to the docket may file a reply with the Commission. The Parties agree to support in their filings the issuance by the Commission of an order regarding the adoption of such commitments and conditions as soon as practical thereafter, recognizing that the Reorganization cannot close until final state orders have been issued.

8. Not later than the Final Filing, Avista will disclose to the Parties any written commitments, conditions or covenants made in another state jurisdiction (between the date of the filing of the Stipulation and the receipt of the last state order in the Reorganization docket) intended to encourage approval of the Reorganization or avoidance of an objection thereto.

9. The Staff, by signing this Stipulation, acknowledges that Avista has satisfied the standard under *Idaho Code* § 61-328 for approval of the Reorganization and requests that the Commission issue its order approving the Application and this Stipulation. The Parties encourage the Commission to enter a final Idaho approval order by July 31, 2006.

10. The Parties submit this Stipulation to the Commission and recommend approval in its entirety pursuant to IDAPA 31.01.01.274. Parties shall support this Stipulation before the Commission, and no Party shall appeal any portion of this Stipulation or Order approving the same. If this Stipulation is challenged by any person not a party to the Stipulation, the Parties to this Stipulation reserve the right to cross-examine witnesses and put on such case as they deem appropriate to respond fully to the issues presented, including the right to raise issues that are incorporated in the settlements embodied in this Stipulation. Notwithstanding this reservation of rights, the Parties to this Stipulation agree that they will continue to support the Commission's adoption of the terms of this Stipulation.

11. The Parties agree that this Stipulation represents a compromise of the positions of the Parties in this case. Other than the above-referenced positions and any testimony or comments filed in support of the approval of this Stipulation, and except to the extent necessary for a Party to explain before the Commission its own statements and positions with respect to the Stipulation, all

negotiations relating to this Stipulation shall not be admissible in evidence in this or any other proceeding regarding this subject matter.

12. Avista acknowledges that the Commission's approval of the Stipulation, the Commitments or the Application shall not bind the Commission in other proceedings with respect to the determination of prudence, just and reasonable character, rate or ratemaking treatment, or public interest of services, accounts, costs, investments, expenditures or actions referenced in these Commitments.

13. In the event the Commission rejects any part or all of this Stipulation, or imposes any additional material conditions on approval of this Stipulation, each Party reserves the right, upon written notice to the Commission and other Parties to this proceeding, within 14 days of the date of such action by the Commission, to withdraw from this Stipulation. In such case, no Party shall be bound or prejudiced by the terms of this Stipulation, and each Party shall be entitled to seek reconsideration of the Commission's order, file testimony as it chooses, cross-examine witnesses, and do all other things necessary to put on such case as it deems appropriate. In such case, the Parties immediately will request the prompt convening of a prehearing conference for purposes of establishing a procedural schedule for the completion of the case. The Parties agree to cooperate in development of a schedule that concludes the proceeding on the earliest possible date, taking into account the needs of the Parties in participating in hearings and preparing briefs.

14. No Party shall be bound, benefited or prejudiced by any position asserted in the negotiation of this Stipulation, except to the extent expressly stated herein, nor shall this Stipulation be construed as a waiver of the rights of any Party unless such rights are expressly waived herein. Execution of this Stipulation shall not be deemed to constitute an acknowledgment by any Party of

the validity or invalidity of any particular method, theory or principle of regulation or cost recovery. No Party shall be deemed to have agreed that any method, theory or principle of regulation or cost recovery employed in arriving at this Stipulation is appropriate for resolving any issues in any other proceeding in the future. No findings of fact or conclusions of law other than those stated herein shall be deemed to be implicit in this Stipulation.


15. Subject to Paragraph 16 of this Stipulation, the effective date of this Stipulation shall be the date of the completion of the Reorganization.

16. The obligations of Avista under this Stipulation are subject to the Commission's approval of the Application in this docket on terms and conditions acceptable to Avista, in its sole discretion, and the completion of the Reorganization.

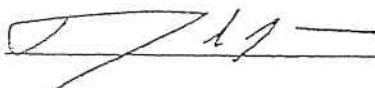
17. To the extent any of the above referenced filing dates fall on a weekend or a holiday, the filing shall be due on the next business day.

Respectfully submitted this 15<sup>th</sup> day of June, 2006.

Idaho Public Utilities Commission Staff

By   
Cecelia A. Gassner  
Deputy Attorney General

Avista Corporation

By   
David J. Meyer  
Vice President and Chief Counsel of Regulatory and Governmental Affairs

AVISTA CORPORATE REORGANIZATION  
TO FORM A HOLDING COMPANY  
(CASE NO. AVU-E-06-1/AVU-G-06-1)

- 1.) Avista Utilities will maintain its own books and records, separate from AVA's books and records. Avista Utilities' financial books and records and state and federal utility regulatory filings and documents will continue to be available to the Commission, upon request.
- 2.) AVA and Avista Utilities will provide the Commission access to all books of account as well as all documents, data, and records of their affiliated interests, which pertain to transactions between Avista Utilities and its affiliated interests or which are otherwise relevant to the business of Avista Utilities.
- 3.) AVA, Avista Utilities and all affiliates will make their employees, officers, directors and agents available to testify before the Commission to provide information relevant to matters within the jurisdiction of the Commission.
- 4.) AVA and Avista Utilities agree that one of its independent directors on each Board of Directors will have had prior experience with respect to the operation, financial analysis or regulation of the regulated gas or electric utility industry.
- 5.) The Commission or its agents may audit the accounting records of AVA and its subsidiaries that are the bases for charges to Avista Utilities, to determine the reasonableness of allocation factors used by AVA to assign costs to Avista Utilities and amounts subject to allocation or direct charges. AVA agrees to cooperate fully with such Commission audits.
- 6.) Avista Utilities will file on an annual basis a copy of any affiliated interest report filed in other jurisdictions.
- 7.) AVA and Avista Utilities will comply with all applicable Commission statutes and regulations regarding affiliated interest transactions, including timely filing of applications and reports.
- 8.) Avista Utilities and AVA will not cross-subsidize between the regulated and non-regulated businesses or between any regulated businesses, and shall comply with the Commission's applicable orders and rules with respect to such matters.
- 9.) Any proposed cost allocation methodology for the allocation of corporate and affiliate investments, expenses, and overheads, required by law or rule to be



submitted to the Commission for approval, will comply with the following principles:

- a. For services rendered to Avista Utilities or each cost category subject to allocation to Avista Utilities by AVA or any of its affiliates, AVA must be able to demonstrate that such service or cost category is necessary to Avista Utilities for the performance of its regulated operations, is not duplicative of services already being performed within Avista Utilities, and is reasonable and prudent.
- b. Cost allocations to Avista Utilities and its subsidiaries will be based on generally accepted accounting standards; that is, in general, direct costs will be charged to specific subsidiaries whenever possible and shared or indirect costs will be allocated based upon the primary cost-driving factors.
- c. AVA and its subsidiaries will have in place accounting systems adequate to support the allocation and assignment of costs of executives and other relevant personnel to Avista Utilities.
- d. An audit trail will be maintained such that all costs subject to allocation can be specifically identified, particularly with respect to their origin. In addition, the audit trail must be adequately supported. Failure to adequately support any allocated cost may result in denial of its recovery in rates.
- e. Costs which would have been denied recovery in rates had they been incurred by Avista Utilities regulated operations will likewise be denied recovery whether they are allocated directly or indirectly through subsidiaries in the AVA group.
- f. Any corporate cost allocation methodology used for rate setting, and subsequent changes thereto, will be submitted to the Commission for approval if required by law or rule. An Intercompany Administrative Services Agreement (IASA) will be developed that will include the corporate and affiliate cost allocation methodologies. The IASA will be filed with the Commission as soon as practicable after the closing of the transaction. Approval of the IASA will be requested if required by law or rule, but approval for ratemaking purposes will not be requested in such filing. Amendments to the IASA will also be filed with the Commission.
- g. AVA and Avista Utilities commit to use asymmetrical pricing (i.e., lower of cost or market for transactions to Avista Utilities and higher of cost or market for transactions from Avista Utilities) for affiliate charges or costs not covered by the provisions of any cost sharing agreement, if a readily

identifiable market for the goods, services or assets exists, and if the transaction involves a cost of more than \$100,000.

- 10.) Avista Utilities will maintain separate debt and, if outstanding, preferred stock ratings. Avista Utilities will maintain its own corporate credit rating, as well as ratings for each long-term debt and preferred stock (if any) issuance.
- 11.) Within three months of closing of the transaction, AVA and Avista Utilities commit to obtain from one or more rating agencies written confirmation that Avista Utilities will have its own corporate credit rating, separate and apart from AVA, as well as separate ratings for each long-term debt and preferred stock (if any) issuance, and that it will not otherwise be consolidated with AVA for ratings purposes. If the ring-fencing provisions of this stipulation are insufficient for purposes of obtaining a separate rating for Avista Utilities, AVA and Avista Utilities will so notify the Commission and propose and implement, upon Commission approval, such additional ring-fencing provisions that are sufficient to secure separate corporate ratings for AVA and Avista Utilities.
- 12.) AVA and Avista Utilities will exclude all costs of the formation of the Holding Company from Avista Utilities' utility accounts.
- 13.) AVA and Avista Utilities will provide the Commission with unrestricted access to all written information provided by and to credit rating agencies that pertains to Avista Utilities or AVA. AVA will also provide the Commission with unrestricted access to all written information provided by and to credit rating agencies that pertains to AVA's subsidiaries to the extent such information may potentially impact Avista Utilities.
- 14.) The capital requirements of Avista Utilities, as determined to be necessary to meet its obligation to serve the public, will be given a high priority by the Board of Directors of AVA and Avista Utilities.
- 15.) Neither Avista Utilities nor its subsidiaries will, on a prospective basis, without prior notification to the Commission, make loans or transfer funds (other than dividends and payments for inter-company services provided as part of the normal course of business or routine cash management functions or current money pool arrangements) to AVA or its affiliates, or assume any obligation or liability as guarantor, endorser, surety or otherwise for AVA or its affiliates; provided that this condition will not prevent Avista Utilities from assuming any obligation or liability on behalf of a subsidiary of Avista Utilities. Any changes to current money pool arrangements will require Commission approval. AVA will not pledge any of the assets of the business of Avista Utilities as backing for any securities which AVA or its affiliates (but excluding Avista Utilities and its subsidiaries) may issue.

- 16.) Nothing in these restructuring commitments shall be interpreted as a waiver of Avista Utilities' or AVA's rights to request confidential treatment for information that is the subject of any commitments.
- 17.) Equity Building Mechanism: The Company agrees that it will increase the actual utility equity component to 35% by December 31, 2007 and to 38% by December 31, 2008. To the extent the Company incurs increased power supply or purchased gas costs that are not recovered in retail rates in a timely manner, it would impair the Company's ability to build equity. Accordingly, the calculations to determine whether the targets are met will be adjusted for any additional deferred power supply or purchased gas costs recorded on the Company's books after January 1, 2006, which have been approved for recovery, but over a period longer than proposed by the Company.

Failure to meet the first target will result in an automatic reduction in base utility rates (spread uniformly across all classes) of 2% effective April 1, 2008. Failure to meet the second target would result in a reduction of 2% effective April 1, 2009. If the Company fails to achieve the first target but meets the second one, the 2% reduction on April 1, 2008 would be reversed prospectively as of April 1, 2009. If it meets the first target but misses the second, the April 1, 2009 reduction would remain in effect until its next general rate case. If the Company misses both targets, the total reduction would equal 4%, which would remain in effect until the next general rate case.
- 18.) AVA and Avista Utilities commit that Avista Utilities will not make any dividends to AVA that will reduce Avista Utilities' common equity capital below 25% of its Total Adjusted Capital without Commission approval. This percentage will be adjusted, as necessary, to account for any changes to Generally Accepted Accounting Principles (GAAP) after approval of this transaction. For purposes of calculating the numerator of the percentage, common equity will not include any portion of Avista Utilities preferred stock issued and outstanding. Avista Utilities' Total Adjusted Capital is defined as common equity, preferred equity, long-term debt, short-term debt and capitalized lease obligations.
- 19.) Through December 31, 2016, Avista Utilities will provide the Commission notice when it increases the amount of any dividend payment by 10% or more over the previously-paid dividend.
- 20.) In the event of a credit rating downgrade of Avista Utilities, the Company will schedule a meeting with Staff within one month of the downgrade to discuss the reason for the downgrade and the Company's plans going forward.
- 21.) On or before April 1, 2008, and on or before every anniversary date thereafter, Avista Utilities will provide to the Commission an annual report for the preceding calendar year, in which it describes its compliance with the

- provision of items 17, 18 and 19, concerning the equity building mechanism and payment of dividends.
- 22.) Avista Utilities is required to apply to the Commission for approval of security issuances pursuant to Idaho Code Title 61, Chapter 9. Avista Utilities will not seek an exemption from this requirement for twelve months following the closing of this transaction. Staff will evaluate the "all-in-cost" of issuances for inclusion in rates and the cost of any debt issuance recognized for ratemaking will not be higher than it otherwise would have been without the corporate reorganization.
  - 23.) AVA and Avista Utilities will provide the Commission access to corporate minutes including Board of Director's minutes and all committee minutes, along with any related source documents that are relevant to the business and risk analysis of Avista Utilities. Avista Utilities and the Commission Staff will establish an agreeable procedure to review these confidential documents in Spokane, WA upon request.
  - 24.) AVA and Avista Utilities will provide the Commission access to operational, internal and risk audit reports and documentation. Avista Utilities and the Commission Staff will establish an agreeable procedure to review these confidential documents upon request.
  - 25.) AVA and Avista Utilities will provide the Commission and Staff with notification of all publicly announced proposals for divestiture, spin-off, or sale of any integral Avista Utilities function. AVA and Avista Utilities will also file for Commission approval of divestiture, spin-off, or sale of any integral Avista Utilities function, which is subject to IPUC jurisdiction. This condition does not limit any jurisdiction the Commission may have.
  - 26.) Avista Utilities or AVA will notify the Commission prior to implementation of plans by Avista Utilities or AVA: (1) to form an affiliate for the purpose of transacting business with Avista Utilities' regulated operations; (2) to commence new business transactions between an existing affiliate and Avista Utilities; or (3) to dissolve an affiliate which has transacted substantial business with Avista Utilities.
  - 27.) Avista Utilities or AVA will notify the Commission subsequent to AVA's or Avista Utilities' board approval and as soon as practicable following any public announcement of: (1) any acquisition of a regulated or unregulated business representing 5 percent or more of the capitalization of AVA; or (2) the change in effective control or acquisition of any material part or all of Avista Utilities by any other firm, whether by merger, combination, transfer of stock or assets.

- 28.) Avista Utilities will provide to the Commission, upon request, on an informational basis, credit rating agency news releases and final reports regarding Avista Utilities when such reports are known to Avista Utilities and are available to the public.
- 29.) AVA and Avista Utilities commit that in the event that Avista Utilities obtains a loan from its parent company or any affiliated company, Avista Utilities will, in any subsequent rate proceeding demonstrate that the debt obligation interest, terms, and conditions are comparable to or less than what Avista Utilities could have obtained in the market at the time the debt was obtained by Avista Utilities, that the loan is on reasonable terms and without markup to the holding company's cost of funds, and that the debt procurement will not interfere with any ring-fencing mechanisms that secure the utility.
- 30.) AVA and Avista Utilities will enter into an agreement that incorporates the ring-fencing provisions set forth herein, which agreement shall be binding upon AVA and Avista Utilities, and their respective Boards of Directors. This agreement will be filed with the Commission within three months of closing of the transaction. AVA and Avista Utilities commit that no amendments, revisions or modifications will be made to this agreement or any ring-fencing provisions without prior Commission approval for the sole purpose of addressing the ring-fencing provisions.
- 31.) Within three months of closing of the transaction, AVA commits to obtain a non-consolidation opinion that demonstrates that the ring-fencing around Avista Utilities is sufficient to prevent Avista Utilities from being pulled into an AVA bankruptcy. AVA commits to promptly file such opinion with the Commission. If the ring-fencing provisions of this agreement are insufficient to obtain a non-consolidation opinion, AVA agrees to promptly undertake the following actions:
- a) Notify the Commission of this inability to obtain a non-consolidation opinion.
  - b) Propose and implement, upon Commission approval, such ring-fencing provisions that are sufficient to prevent Avista Utilities from being pulled into an AVA bankruptcy.
  - c) Obtain a non-consolidation opinion.
- 32.) Unless another process is provided by statute, Commission regulations or approved Avista Utilities' tariff, AVA and Avista Utilities encourage the Commission to use the following process for administering the commitments. The Commission should give AVA and Avista Utilities written notification of any violation by either company of the commitments made in this application. If such failure is corrected within ten (10) business days for failure to file

reports, or five (5) business days for other violations, the Commission should take no action. The Commission shall have the authority to determine if the corrective action has satisfied or corrected the violation. AVA or Avista Utilities may request, for cause, an extension of these time periods. If AVA or Avista Utilities fails to correct such violations within the specified time frames, as modified by any Commission-approved extensions, the Commission may seek to assess penalties for violation of a Commission order, against either AVA or Avista Utilities, as allowed under state laws and regulations.

- 33.) The applicants agree that the Commission shall have an opportunity and the authority to consider and adopt in Idaho any commitments or conditions to which the Applicants agree or with which the Applicants are required to comply in other jurisdictions, even if such commitments and conditions are agreed to after the Commission enters its order in this docket. To facilitate the Commission's consideration and adoption of the commitments and conditions from other jurisdictions, the Parties urge the Commission to issue an order accepting this Stipulation as soon as practical, but to reserve in such order the explicit right to re-open to add commitments and conditions accepted or ordered in another state jurisdiction.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 15<sup>TH</sup> DAY OF JUNE 2006,  
SERVED THE FOREGOING MOTION FOR APPROVAL OF STIPULATION AND  
STIPULATION, IN CASE NO. AVU-E-06-1/AVU-G-06-1, BY E-MAILING A COPY  
THEREOF AND BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE  
FOLLOWING:

DAVID J. MEYER  
SR VP AND GENERAL COUNSEL  
AVISTA CORPORATION  
PO BOX 3727  
SPOKANE WA 99220-3727  
E-mail [dmeyer@avistacorp.com](mailto:dmeyer@avistacorp.com)

KELLY NORWOOD  
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\_\_\_\_\_  
SECRETARY

BEFORE THE  
PUBLIC UTILITY COMMISSION OF OREGON

DOCKET NO. UM-1250

DIRECT TESTIMONY OF MALYN K. MALQUIST  
REPRESENTING THE AVISTA CORPORATION

---

Operations, Ratepayer Protection



1 **I. INTRODUCTION**

2 **Q. Please state your name, business address, and present position with Avista**  
3 **Corp.**

4 A. My name is Malyn K. Malquist. My business address is 1411 East Mission  
5 Avenue, Spokane, Washington. I am employed by Avista Corp. (Company or Avista) as  
6 Executive Vice President and Chief Financial Officer.

7 **Q. Would you please describe your education and business experience?**

8 A. I received a Bachelors degree and a Master of Business Administration degree  
9 from Brigham Young University. I have also attended a variety of utility finance courses and  
10 leadership programs.

11 I joined Avista Corp. in September of 2002 as Senior Vice President. In November 2002  
12 I was named to the additional position of Chief Financial Officer. In March 2004 the position of  
13 Treasurer was temporarily added until January 2006. Prior to joining Avista, I was General  
14 Manager of Truckee Meadows Water Authority in Reno, Nevada, which was separated out from  
15 Sierra Pacific Power Company in 2001. I was Chief Executive Officer of Data Engines, Inc., a  
16 high tech company located in Reno from June to October of 2000. From April 1994 to April  
17 2000, I was employed by Sierra Pacific Resources, first as the company's chief financial officer  
18 and later as its chairman of the board and chief executive officer. Following the merger of Sierra  
19 Pacific Resources with Nevada Power Company in 1999, I became the President of both Sierra  
20 Pacific Power Company and Nevada Power Company. For the sixteen-year period up to 1994, I  
21 was employed by San Diego Gas & Electric Company in various positions, including Treasurer  
22 and Vice President – Finance.

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

2           A.    I will discuss Avista’s current business operations, and how the proposed  
3 reorganization to a holding company structure provides protection for ratepayers by “ring  
4 fencing” utility operations from the Company’s other non-regulated businesses. This  
5 reorganization would allow Avista to continue to operate its regulated utility business efficiently,  
6 while effecting the legal separation of its non-regulated businesses from its regulated utility  
7 business. Avista Utilities would continue to have a financial and capital structure of its own, its  
8 own debt securities and preferred stock, lines of credit, sources of revenue, operations, and its  
9 own employees. Lastly, I will discuss the Plan of Share Exchange approved by the Board of  
10 Directors to create the holding company.

11           **Q.     Are you sponsoring any exhibits to be introduced in this proceeding?**

12           A.    Yes. I am sponsoring Exhibit No. 201, which illustrates Avista’s current Company  
13 organization charts for both Avista Corporation and Avista Capital, and Exhibit No. 202, which  
14 provides a copy of the Plan of Exchange .

15           **Q.     Please describe Avista’s current business operations.**

16           A.    Avista Corporation is an energy company engaged in the generation, transmission  
17 and distribution of energy and, through its affiliates, other energy-related businesses. Avista’s  
18 businesses are divided into four segments, as follows:

- 19           • Avista Utilities is an operating division of Avista Corporation that provides  
20 generation, transmission and distribution of electric energy and distribution of natural  
21 gas to retail customers, as well as wholesale purchases and sales of electric capacity  
22 and energy. Avista Utilities provides service to approximately 338,000 electric

1 customers and 205,000 natural gas customers in a 26,000-square-mile area in eastern  
2 Washington and northern Idaho. The largest community served in the area is  
3 Spokane, Washington, which is the location of the corporate headquarters. Avista  
4 Utilities also serves 92,400 natural gas customers in Oregon.

5  
6 Avista Capital, Inc., is a wholly-owned affiliate of Avista Corporation, and is the parent  
7 corporation of Avista Corporation's non-regulated affiliate investments and operations<sup>1</sup>, which  
8 includes the remaining three segments as described below.

- 9 • Energy Marketing and Resource Management is a segment which provides electricity  
10 and natural gas marketing, trading and resource management. This business segment  
11 is conducted primarily by Avista Energy, Inc., an electricity and natural gas  
12 marketing, trading and resource management business, operating primarily in the  
13 Western Electricity Coordinating Council (WECC) geographical area, which is  
14 comprised of eleven Western states and the provinces of British Columbia and  
15 Alberta, Canada.
- 16 • Advantage IQ is a segment which provides information and cost management services  
17 for multi-site customers throughout North America. Its primary product lines include  
18 consolidated billing, resource accounting, energy analysis and load profiling services.

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<sup>1</sup> The only exceptions relate to Avista Receivables, Inc., a special purpose affiliate formed in connection with the sale of accounts receivable, and Spokane Energy, LLC, which was formed for the purpose of implementing a long-term capacity contract between Avista Utilities and Portland General Electric Company. At present, these entities are directly owned by Avista Corporation.



1 Directors of Avista Corporation (Avista Utilities) and the Parent Company. (The Parent  
2 Company is referred to as “AVA Formation Corp.” in the Plan of Exchange.) AVA was  
3 incorporated in the State of Washington on February 10, 2006.

4 Under the terms of the Plan of Exchange, AVA would issue common stock in the same  
5 number of shares as there are shares of Avista Corporation common stock outstanding. Each  
6 share of Avista Corporation common stock would then be exchanged for one share of common  
7 stock in AVA, except to the extent that any holders of Avista Corporation common stock are  
8 entitled to dissent to the proposed transaction and receive payment of their shares pursuant to  
9 such dissenter’s rights. After the share exchange is completed, the Parent Company would own  
10 all the common stock of Avista Corporation and the former holders of the common stock of  
11 Avista Corporation would hold the common stock of the Parent Company. The outstanding first  
12 mortgage bonds, unsecured debt and preferred stock, and all other contracts and agreements to  
13 which Avista is a party, would remain with Avista Utilities. A copy of the Plan of Exchange is  
14 attached as Exhibit No. 202.

15 **Q. How are Avista’s affiliates affected by the Plan of Share Exchange?**

16 A. Avista Capital, Inc. is a wholly owned affiliate of Avista Corporation, which holds  
17 the stock of Avista Corporation’s non-regulated affiliate investments. In conjunction with the  
18 Reorganization, ownership of Avista Capital, Inc. would be transferred from Avista Corporation  
19 to the Parent Company.<sup>2</sup>

20

1 **III. RATEPAYER PROTECTION**

2 **Q. Please summarize some of the overall benefits of the reorganization.**

3 A. Avista believes that the holding company structure would facilitate the protection  
4 of its utility business and customers from its non-utility businesses. The benefits of a holding  
5 company structure may be generally summarized as follows:

- 6 • Avista's utility operations would be better separated from the non-utility  
7 businesses, making cross subsidization easier to avoid and further ensuring  
8 that non-utility business risk would not affect utility operations.  
9  
10 • The new structure would provide better legal protection for Avista Utilities  
11 from liabilities arising from other segments of Avista's business.  
12  
13 • The new structure would permit investors, analysts, and rating agencies to  
14 more easily analyze and value the individual lines of business.  
15  
16 • Capital structures and financing techniques may be used that are better  
17 suited to the particular requirements, characteristics, and risks of the utility  
18 and non-utility businesses. Such structures and techniques should increase  
19 financial flexibility without adversely affecting the capital structure or  
20 creditworthiness of the utility and non-utility businesses.  
21

22 **Q. Please describe how the proposed Reorganization provides protection for**  
23 **ratepayers by "ring fencing" utility operations from the Company's other non-regulated**  
24 **businesses.**

25 A. The Reorganization to a holding company structure would allow Avista (as Avista  
26 Utilities) to continue to operate its regulated utility business efficiently while effecting the legal

---

<sup>2</sup> The dividend of Avista Capital to the Parent Company will not occur until June 1, 2008 when the 9.75% Senior Notes mature, unless consent is received prior to that time.

1 separation of certain non-regulated businesses of Avista from regulated utility businesses.<sup>3</sup>  
2 Avista Utilities would continue to have a financial and capital structure of its own, and would  
3 continue to issue its own debt securities and preferred stock. It would also continue to have its  
4 own lines of credit, sources of revenue, operations, and employees.

5 **Q. How does “ring fencing” the utility operations provide legal separation**  
6 **between the regulated and non-regulated businesses?**

7 A. Avista’s current corporate structure cannot accommodate the same degree of  
8 financial and legal separation as can a holding company structure. All business activities now  
9 must be either part of Avista itself or conducted in entities owned by Avista. As a result, any  
10 volatility in earnings associated with these other businesses will continue to be reflected in  
11 Avista’s financial results. In a holding company structure, these other businesses are expected to  
12 be conducted as holding company affiliates separate from Avista. Avista Utilities’ earnings  
13 would be insulated from the potential volatility of these businesses because their activities would  
14 not be reflected in the utility’s financial statements.

15 Avista, as Avista Utilities, would continue to be a separate legal entity and would be  
16 managed as such, separate and distinct from AVA and other AVA affiliates (please see Exhibit  
17 No. 101, which illustrates Avista’s organization structure before and after the formation of a  
18 holding company). The Avista Utilities board of directors would continue to be an active board  
19 that will act in good faith with the care and loyalty expected of a board. Even though the

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<sup>3</sup> Following completion of the Plan of Exchange, by which Avista Corporation would become an affiliate of the new holding company (AVA), the shares of stock of Avista Capital held currently by Avista Corporation would be distributed to AVA, and Avista Corporation’s name would be changed to Avista Utilities, (following the maturity of the 9.75% Senior Notes on June 1, 2008 unless consent is received prior).

1 members of the Avista Utilities board of directors may also be members of AVA's board, the two  
2 boards will exercise separate and independent functions and duties.

3 **Q. How would the Company's current cash management procedures be**  
4 **affected by any proposed "ring fencing" of the Utility after the Reorganization?**

5 A. Avista's current cash management procedures are designed to maintain  
6 segregation between the utility's cash flows and the cash flows of affiliates. These cash  
7 management guidelines have been filed with FERC pursuant to Docket No. RM02-14 and are in  
8 compliance with FERC requirements. Each company maintains separate bank accounts and our  
9 cash management guidelines are designed to prevent the commingling of funds. It is Avista's  
10 intention that when the holding company structure becomes effective, AVA will continue to  
11 maintain such separation, after reflecting the impact of the Reorganization.

12 **Q. How would the Company's current financing procedures be affected by the**  
13 **Reorganization?**

14 A. Avista Utilities currently issues, and will continue to issue upon completion of the  
15 Reorganization, its own debt and preferred stock, and would maintain its own credit facility for  
16 short-term funding needs. To issue such securities, Avista Utilities will continue to file for  
17 authorization from the commission for such issuances. Avista Utilities common stock will be  
18 solely owned by AVA. When AVA issues stock or debt securities, it would use the proceeds to  
19 fund, as necessary, the common equity requirements of all of its affiliates, including Avista  
20 Utilities. The other funding requirements of the non-regulated affiliates would be provided by  
21 their own cash flows or separate financing raised at the affiliate level.

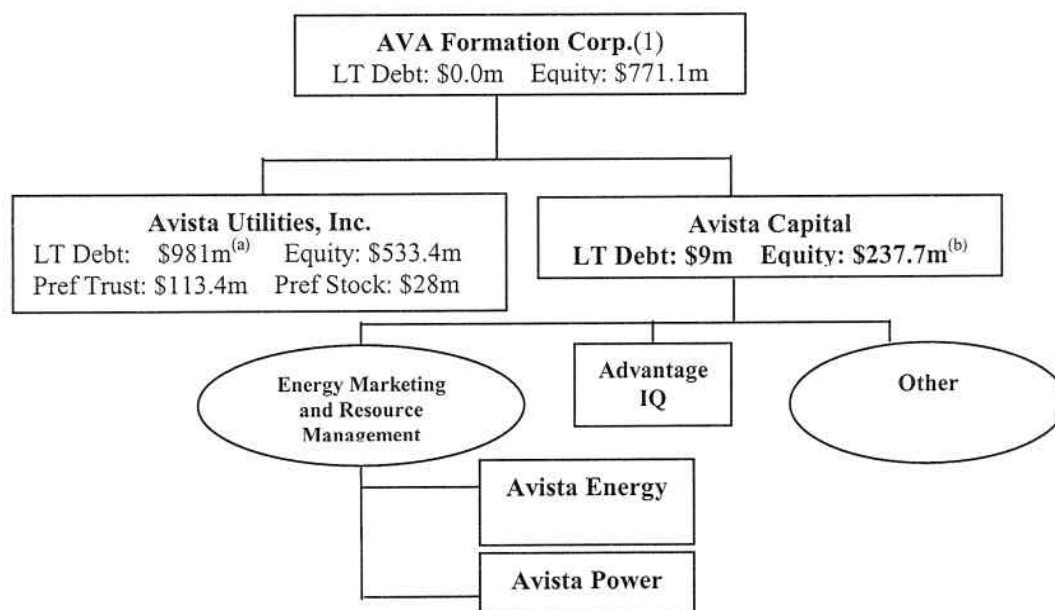


Each company will be responsible to pay for its liabilities from its own bank account and for the funding of its own obligations, either through the issuance of debt or, as appropriate, by funding from the holding company. Avista Utilities and AVA will each maintain separate credit ratings, as appropriate. As required by generally accepted accounting principles, liabilities of each company will continue to be recorded on the books and records of such individual company.

**Q. How will the Reorganization change the Company's current capitalization structure?**

A. Illustration 1, below, based on December 31, 2005 levels of capitalization, shows where the debt and equity components will reside, after the reorganization:

**Illustration 1: Capitalization Structure**



(1) For illustrative purposes only, the table above shows a level of capitalization for the holding company structure, as of the date of its implementation, based on December 31, 2005 levels.

(a) Excludes short-term debt.

(b) Will occur on June 1, 2008 when the 9.75% Senior Notes mature, unless consent is received prior to June 1, 2008.

1           **Q.     Would the Company's business practices currently in place be adversely**  
2 **affected by the Reorganization?**

3           A.     No. In addition to the structural separations discussed above, both AVA and  
4 Avista Utilities would continue to operate in such a way as to protect utility customers from the  
5 risks associated with AVA's other subsidiaries or affiliates. Avista has exited those businesses  
6 that did not fit within Avista's strategy to focus on our energy and utility-related businesses.  
7 Avista's remaining affiliates are adequately funded. Avista has downsized its Energy Marketing  
8 and Resource Management business conducted at Avista Energy, as compared to prior years, and  
9 is increasing its focus on the generally lower risk activities related to resource management and  
10 energy services to industrial and large end use customers. And importantly, Avista has separate,  
11 very disciplined, risk management programs in place at both Avista Utilities and Avista Energy.

12

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

14           A.     Yes it does.

BEFORE THE  
PUBLIC UTILITY COMMISSION OF OREGON

DOCKET NO. UM-1250

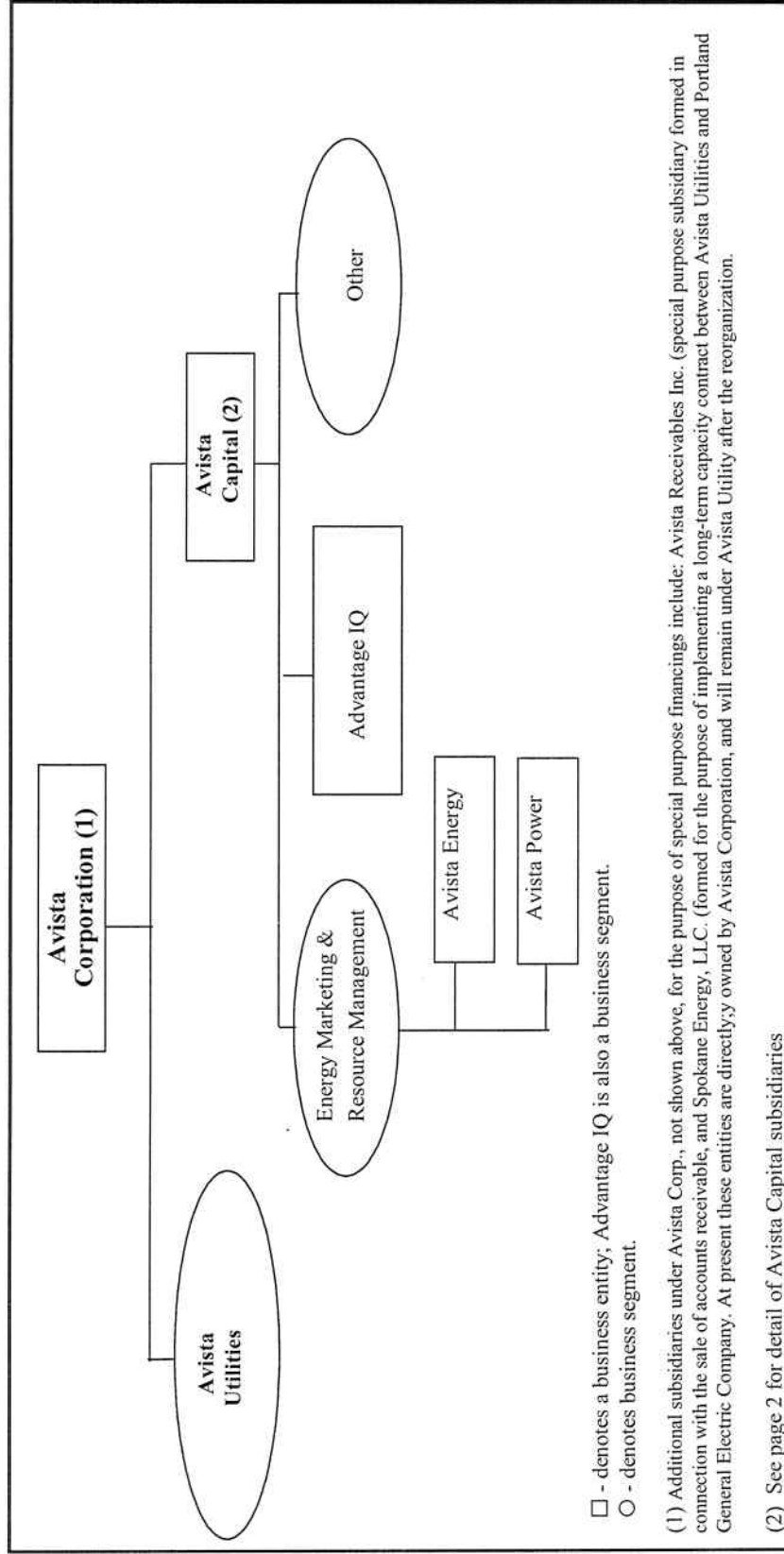
AVISTA CORP

MALYN K. MALQUIST  
**Exhibit No. 201**

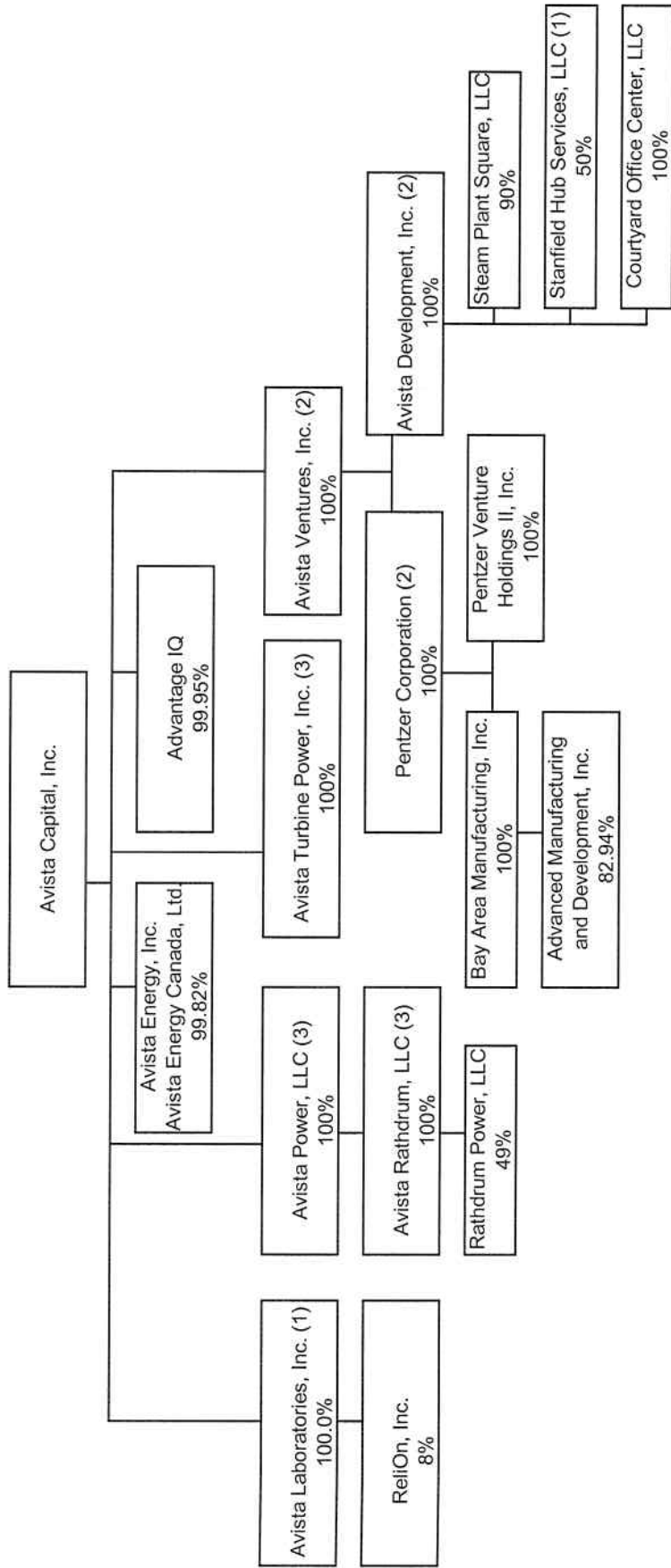
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Operations, Ratepayer Protection

# Avista Corporation Organizational Structure September 2006



**Avista Capital Organizational Structure  
 September 2006**



(1) Inactive - see note a) below  
 (2) No employees, passive income  
 (3) Ceased active development of additional projects  
note a) Other Inactive Subsidiaries under Avista Capital, not shown above, include: Coyote Springs 2, LLC

BEFORE THE  
PUBLIC UTILITY COMMISSION OF OREGON

DOCKET NO. UM-1250

AVISTA CORP

MALYN K. MALQUIST  
**Exhibit No. 202**

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Operations, Ratepayer Protection

PLAN OF SHARE EXCHANGE

THIS PLAN OF SHARE EXCHANGE (the "Plan of Exchange"), dated as of February 13, 2006, is between Avista Corporation, a Washington corporation ("Avista"), the corporation whose shares of common stock will be acquired pursuant to the exchange provided for in this Plan of Exchange (the "Exchange"), and AVA Formation Corp., a Washington corporation ("AVA"), the acquiring corporation. Avista and AVA, together, are referred to in this Plan of Exchange as the "Companies."

RECITALS:

A. The authorized capital of Avista consists of (a) 200,000,000 shares of common stock, without nominal or par value ("Avista Common Stock"), of which 48,593,873 shares were issued and outstanding as of January 15, 2006, and (b) 10,000,000 shares of preferred stock, without nominal or par value ("Avista Preferred Stock"), of which 262,500 shares were issued and outstanding as of December 31, 2005. The number of issued and outstanding shares of Avista Common Stock is subject to increase to the extent that additional shares are issued prior to the Effective Time (as defined below).

B. AVA is a wholly-owned subsidiary of Avista, with authorized capital of (a) 200,000,000 common shares, without nominal or par value ("AVA Common Stock"), of which one hundred (100) shares are issued and outstanding and owned by Avista, and (b) 10,000,000 preferred shares, without nominal or par value, none of which are issued.

C. The Boards of Directors of the Companies deem it desirable and in the best interests of the Companies and the shareholders of Avista that, at the Effective Time, each share of Avista Common Stock be exchanged for one share of AVA Common Stock, with the result that AVA becomes the owner of all outstanding shares of Avista Common Stock and that each holder of shares of Avista Common Stock shall automatically become the holder of an identical number of shares of AVA Common Stock, all on the terms and subject to the conditions set forth below.

D. The Boards of Directors of the Companies have each adopted this Plan of Exchange. The Board of Directors of Avista has voted Avista's shares of AVA Common Stock to approve, and recommended that the shareholders of Avista approve, this Plan of Exchange pursuant to the Washington Business Corporation Act, Title 23B, Revised Code of Washington, as amended (the "Act"), and specifically Section 23B.11.030 of the Act.

NOW, THEREFORE, the Companies agree as follows:

ARTICLE I

This Plan of Exchange shall be submitted to the holders of Avista Common Stock for approval as provided by Section 23B.11.030 of the Act. The affirmative vote of at least two-thirds ( 2/3) of the outstanding shares of Avista Common Stock shall be necessary to approve the Plan of Exchange.

ARTICLE II

Subject to the terms and conditions of this Plan of Exchange, the Exchange shall become effective immediately following the close of business on the date of filing with the Secretary of State of the State of Washington (the "Secretary of State") of articles of share exchange pursuant to Section

23B.11.050 of the Act (the “Articles”), or at such later time and date as may be stated in the Articles (the time and date at and on which the Exchange becomes effective, the “Effective Time”).

### ARTICLE III

A. At the Effective Time:

(1) Each share of Avista Common Stock issued and outstanding immediately prior to the Effective Time shall be automatically exchanged for one share of AVA Common Stock, which share shall be fully paid and nonassessable.

(2) AVA shall acquire and become the owner and holder of each issued and outstanding share of Avista Common Stock so exchanged.

(3) Each share of AVA Common Stock issued and outstanding immediately prior to the Effective Time shall be canceled and shall constitute an authorized but unissued share of AVA Common Stock.

(4) Each right to receive shares of Avista Common Stock and each unexpired and unexercised option to purchase shares of Avista Common Stock (each, an “Avista Grant”) under an Avista executive compensation or employee benefit plan (each, an “Avista Plan”), whether vested or unvested, shall, pursuant to an amendment to each such Avista Plan, become the right to receive an equal number of shares of AVA Common Stock or an option to purchase, at the same price per share specified in such Avista Grant, that number of shares of AVA Common Stock equal to the number of shares of Avista Common Stock that could have been purchased immediately prior to the Effective Time (assuming full vesting), as the case may be, under the Avista Plans. Each Avista Grant shall be subject to the same terms and conditions as are set forth in the Avista Plans.

(5) Each share of Avista Common Stock held under the Avista Direct Stock Purchase and Dividend Reinvestment Plan (the “Dividend Reinvestment Plan”) immediately prior to the Effective Time shall automatically be exchanged for an equal number (including fractional and uncertificated shares) of shares of AVA Common Stock, and shall continue to be held under the Dividend Reinvestment Plan.

B. Each former holder of shares of Avista Common Stock shall be entitled to receive only (1) shares of AVA Common Stock in exchange for such Avista Common Stock as provided in this Plan of Exchange or (2) payment of the fair value of such shares of Avista Common Stock under Chapter 23B.13 of the Act.

C. As of the Effective Time, AVA shall adopt any of the Avista Plans as in effect immediately prior to the Effective Time under which Avista Grants are outstanding or that continues to provide for new Avista Grants. The Avista Plans shall be appropriately amended to provide for the issuance and delivery of AVA Common Stock on and after the Effective Time on substantially the same terms as Avista Common Stock would have been issuable thereunder immediately prior to the Effective Time.

D. As of the Effective Time, AVA shall succeed to the Dividend Reinvestment Plan as in effect immediately prior to the Effective Time, and the Dividend Reinvestment Plan shall be appropriately amended to provide for the issuance and delivery of AVA Common Stock on and after the Effective Time.



E. As of the Effective Time, each and every preferred share purchase right granted pursuant to the Rights Agreement, dated as of November 15, 1999, between Avista and the Bank of New York as successor Rights Agent, as amended, shall expire and no further rights shall be granted.

#### ARTICLE IV

The filing of the Articles with the Secretary of State and the consummation of the Exchange are subject to satisfaction of each of the following conditions precedent:

A. The approval by the holders of Avista Common Stock provided for in Article I of this Plan of Exchange;

B. the receipt of such orders, authorizations, approvals, waivers or disclaimers of jurisdiction from the Washington Utilities and Transportation Commission, the Idaho Public Utility Commission, the Montana Public Service Commission, the Oregon Public Utility Commission, the Federal Energy Regulatory Commission, and all other regulatory bodies, boards or agencies as are or may be required in connection with the Exchange and related transactions, which orders, authorizations, approvals, waivers and disclaimers shall remain in full force and effect, and shall not include, in the sole judgment of the Board of Director of Avista, unacceptable conditions;

C. the effectiveness of a registration statement under the Securities Act of 1933, as amended, relating to AVA Common Stock to be issued in the Exchange;

D. the approval by the New York Stock Exchange for the listing of the AVA Common Stock to be issued in the Exchange; and

E. the receipt by Avista of a favorable opinion of Heller Ehrman LLP covering certain United States federal income tax matters.

#### ARTICLE V

Following the Effective Time, each holder of an outstanding certificate or certificates that represented shares of Avista Common Stock immediately prior to the Effective Time may, but shall not be required to, surrender such certificates to AVA's transfer agent for cancellation and reissuance of a new certificate or certificates in such holder's name or for cancellation and transfer, and each such holder or transferee shall be entitled to receive a certificate or certificates representing the same number of shares of AVA Common Stock as the shares of Avista Common Stock previously represented by the certificate or certificates surrendered. Until so surrendered or presented for exchange or transfer, each outstanding certificate that, immediately prior to the Effective Time, represented Avista Common Stock shall be deemed and shall be treated for all purposes to represent the ownership of the same number of shares of AVA Common Stock as though such surrender or exchange or transfer had taken place. The holders of Avista Common Stock at the Effective Time shall have no right at and after the Effective Time to have any shares of Avista Common Stock transferred on the stock transfer books of Avista (such stock transfer books being deemed closed for this purpose at the Effective Time), and each record of a holder of outstanding certificate(s) that represented shares of Avista Common Stock immediately prior to the Effective Time shall be recorded as representing the ownership by such holder of the same number of shares of AVA Common Stock in the stock transfer books of AVA at the Effective Time.

ARTICLE VI

A. This Plan of Exchange may be amended, modified or supplemented, or compliance with any provision of this Plan of Exchange may be waived, at any time prior to the Effective Time (including, without limitation, after receipt of the affirmative vote of holders of Avista Common Stock as provided in Article I above), by the mutual consent of the Boards of Directors of Avista and AVA, so long as such amendment, modification, supplement or waiver would not, in the sole judgment of the Board of Directors of Avista, materially and adversely affect the shareholders of Avista.

B. This Plan of Exchange may be terminated and the Exchange and related transactions abandoned at any time prior to the Effective Time (including, without limitation, after receipt of the affirmative vote of holders of Avista Common Stock as provided in Article I above), if the Board of Directors of Avista determines, in its sole judgment, that consummation of the Exchange would for any reason be inadvisable or not in the best interests of Avista or its shareholders.

EXECUTED by each of the Companies, pursuant to authorization and approval given by its Board of Directors, as of the date first above written.

AVISTA CORPORATION

AVA FORMATION CORP.

By: /s/ Gary G. Ely  
Gary G. Ely  
Its Chairman, President & CEO

By: /s/ Gary G. Ely  
Gary G. Ely  
Its President

BEFORE THE  
PUBLIC UTILITY COMMISSION OF OREGON

DOCKET NO. UM-1250

DIRECT TESTIMONY OF ELIZABETH M. ANDREWS  
REPRESENTING THE AVISTA CORPORATION

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Cost Allocations

1 **I. INTRODUCTION**

2 **Q. Please state your name, business address, and present position with Avista**  
3 **Corporation.**

4 A. My name is Elizabeth M. Andrews. I am employed by Avista Corporation as a  
5 Senior Regulatory Analyst in the State and Federal Regulation Department. My business address  
6 is 1411 East Mission, Spokane, Washington.

7 **Q. Would you please describe your education and business experience?**

8 A. I am a 1990 graduate of Eastern Washington University with a Bachelor of Arts  
9 Degree in Business Administration, majoring in Accounting. That same year, I passed the  
10 November Certified Public Accountant exam, earning my CPA License in August 1991. I  
11 worked for Lemaster & Daniels, CPAs from 1990 to 1993, before joining the Company in  
12 August 1993. I served in various positions within the sections of the Finance Department,  
13 including General Ledger Accountant and Systems Support Analyst until 2000. For the past six  
14 years, I have served in the State and Federal Regulation Department. I have also attended several  
15 utility accounting and ratemaking courses.

16 **Q. As a Senior Regulatory Analyst, what are your responsibilities?**

17 A. Aside from special projects, I am responsible for the preparation of normalized  
18 revenue requirement and pro forma studies for the various jurisdictions in which the Company  
19 provides utility services. During the last six years I have assisted in the Company's electric and  
20 natural gas general rate filings in Washington and Idaho.

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

1           A.     My testimony in this proceeding will generally cover Avista's current  
2     accounting policies and procedures used by Avista and its regulated and non-regulated businesses  
3     to charge costs or services between the Utility and its affiliates. As discussed within my  
4     testimony, these policies and procedures will not change with the formation of the proposed  
5     holding company structure.

6

7

## **II. COST ALLOCATIONS**

8           **Q.     Regarding regulated Utility operations and accounting for such, have there**  
9     **been any changes to the Company's system and jurisdictional procedures as approved in**  
10    **the Company's previous rate proceedings?**

11          A.     No. For ratemaking purposes, the Company allocates revenues, expenses and rate  
12    base between electric and gas services and between Washington, Idaho, and Oregon jurisdictions  
13    where electric and/or gas service is provided. The current methodology was implemented in  
14    1994 and has not changed, with one exception. Consistent with the accepted allocation  
15    methodology, the Company has reflected the reallocation of costs resulting from the sale of the  
16    Company's California gas distribution properties in April 2005. This accepted allocation  
17    methodology for the regulated Utility operations will not be impacted by the proposed holding  
18    company structure.

19          **Q.     Please explain the Company's current cost allocation procedures for charges**  
20    **of costs or services between the Utility and its affiliates.**

1           A.     Avista's current cost allocation procedures for transactions or costs for services  
2 between the Utility and its affiliates are accounted for appropriately under applicable statutes and  
3 rules established by each Commission.

4           All charges that relate to corporate services provided to affiliates and costs incurred,  
5 including labor costs loaded for benefits, are directly billed to affiliates at cost. No allocation of  
6 expenses occurs, no additional margin or profit is included, and no assets are allocated.  
7 Examples of these charges are salaries of general office employees who spend time on corporate  
8 support, such as managerial functions, accounting, federal income tax filing, payroll, etc. Their  
9 time is charged directly to suspense accounts (Deferred Debit 186), loaded for benefits and then  
10 established as a receivable (Account 146) when billed to the affiliate. If other resources are  
11 expended during the course of this work such as travel or consulting services, these costs are also  
12 charged to suspense accounts and billed to the affiliate. Suspense and capture of Avista  
13 Corporation employee costs, which are then billed back to the affiliates at cost, serve to reduce  
14 the expenses that must be borne by the utility.

15           The revenues and expenses associated with the types of transactions listed above are  
16 reviewed by Commission staff and other interested parties during rate cases and through existing  
17 Commission reporting requirements, such as the Subsidiary Transaction Report filed with the  
18 Washington Utility and Transportation Commission (WUTC) and the Affiliated Interest Report  
19 filed with the Public Utility Commission of Oregon (OPUC) annually.

20           **Q.     Will the Company's proposed Reorganization change the current**  
21 **accounting policies or procedures with respect to its regulated and non-regulated affiliates?**

1           A.     No. Avista’s current cost allocation procedures and the basis of assigning costs  
2 between the Utility and any of Avista’s affiliates would remain unchanged through the approval  
3 of the Reorganization.

4           For example, Avista employees currently reporting to Avista Corporation (dba Avista  
5 Utilities) would not change after the Reorganization, with the exception of the five senior  
6 Officers who would also report to the new AVA holding company. These Officers’ salaries and  
7 expenses would be allocated as appropriate between Avista’s regulated and non-regulated  
8 businesses and the allocation would follow the same procedures as under the Company’s current  
9 structure.

10          The proposed Reorganization also would not entail the transfer of Utility assets, nor, as  
11 discussed further by Company witness Mr. Norwood, would it adversely affect the financial,  
12 technical, and managerial abilities of Avista Utilities. Avista customers would see no change in  
13 the Utility or its operations, because the Utility would continue to provide the same high-quality  
14 service as before the Reorganization. In addition, after the Reorganization, Avista Utilities  
15 would continue to be subject to the same regulatory jurisdiction of the Commission as to rates,  
16 service, accounting and other general matters of utility operations.

17

18

### **III. PROTECTIONS FOR CUSTOMERS**

19          **Q.     Has the Company proposed any other protections for customers?**

20          A.     Yes. As mentioned above, there will be little if any effect on Avista customers,  
21 employees, or the Company’s current accounting policies and procedures. To ensure this, as  
22 described further by Mr. Norwood, Avista’s Reorganization proposal includes protections for

1 customers, such as the continuation of internal controls that preclude cross-subsidization among  
2 Avista's businesses, assuring segregation of operations to prevent the co-mingling of assets  
3 between the regulated and non-regulated businesses, the fair allocation of Holding Company  
4 costs among the utility and other affiliates, and the fact that customers will see no change in rates  
5 resulting from the cost of forming the holding company. Avista would also continue to comply  
6 with all applicable statutes, rules, and Commission practices regarding property transfers,  
7 affiliated or subsidiary transactions, and securities transactions

8 **Q. Has the Company agreed to develop an Intercompany Administrative**  
9 **Services Agreement to address cost allocation methodologies?**

10 A. Yes. Stipulation No.9-f, recently approved by the Idaho Public Utilities  
11 Commission in Order No. 30091, Case Nos. AVU-E-06-1 and AVU-G-06-1, as set forth in the  
12 Stipulation reproduced in Exhibit No. 102, requires Avista to prepare an Intercompany  
13 Administrative Services Agreement (IASA) that will memorialize the corporate and affiliate cost  
14 allocation methodologies discussed above. The IASA will be filed with the Commission as soon  
15 as practicable after the closing of the transaction.

16

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

18 A. Yes, it does.