

Avista Corporation 2009 Natural Gas Integrated Resource Plan Annual Update – Oregon

SUMMARY UPDATE

Avista is submitting this annual update as an informational filing. At this time, we have not noted any significant variances in actual demand relative to forecasted demand nor do we anticipate any near term significant changes in demand forecasts or resource needs from our previously acknowledged 2009 Integrated Resource Plan (IRP or plan) and therefore we are not requesting acknowledgement of any changes associated with this update.

Actual demand in our Oregon service territories has trended at or slightly below our plan's Expected Case which had forecasted slow near term demand growth heading into an economic recession. We anticipate this weak demand trend will continue in the near term given a still sluggish economic recovery plagued by high unemployment and anemic construction activity in the housing and commercial building sectors. Our first identified Oregon resource needs are still expected to occur within the timetable identified in the Expected Case in our 2009 plan (winter 2018-19).

The following discusses emerging planning issues we see for our next plan. If desired, we would be happy to present this information at a Commission public meeting.

EMERGING PLANNING ISSUES

The planning environment leading up to the 2009 IRP was filled with uncertainty. The shale gas revolution was just getting under way precipitating a dramatic drop in natural gas prices from a peak of over \$13/Dth in the summer of 2008. The United States and global economy were in upheaval stemming from an international credit crisis. Climate change legislation was a hot topic on Capitol Hill with the primary debate not whether it would be implemented, but rather when it would be implemented. With this backdrop of uncertainty, the focus of our plan was to analyze a wide range of potential outcomes.

Shale Gas

As we prepare for our next IRP, the game changing impacts of shale gas production looks to reshape numerous aspects of the industry. Foremost is a dramatically revised assessment of the amount of natural gas that can be economically produced, often at a lower cost than conventional natural gas production. This is achieved primarily as a result of economies of scale, near elimination of exploration risks and standardized, sophisticated production techniques that streamline costs and minimize the time from drilling to delivery to market. This change in production profile for shale gas could alter the price and volatility aspects of natural gas as production quickly responds to changing market conditions. This in turn could lead to numerous ripple effects such as longer term bilateral hedging transactions, new financing structures or vertical integration by utilities into natural gas reserves acquisition.

However, shale gas does not come free of controversy. State and federal agencies are reviewing the environmental impacts of this new production method. As a result of the environmental concerns production of natural gas in some areas has been halted. Increased environmental protections could drive costs up while uncertainty around environmental issues could precipitate increased price volatility.

Shale gas production has radically influenced the projected importation of LNG to the US and, at least temporarily, broken the link to global pricing. Numerous regasification terminals have been put on hold or cancelled while some facilities have sought approval for export authority. This may have ripple effects on storage and transportation infrastructure. The Kitimat LNG terminal in northern British Columbia in particular could have far reaching implications on Pacific Northwest supply and prices due to increased competition for Canadian production by Asian markets.

These are just some potential supply implications Avista will consider in its next IRP.

Demand

The United States and global economy are still looking for firm economic traction coming out of a global recession. There is continued debate and uncertainty about when and to what degree economic recovery, and by extension, natural gas demand will materialize. The economic turmoil has recently dampened demand in all rate classes.

Although not currently anticipated, recent muted demand growth risks masking a potentially rapid acceleration in demand either from rapid economic recovery or new incremental demand development. Compressed natural gas (CNG) vehicles and distributed electric generation are two areas that could propel increased new demand and warrant monitoring and scenario demand planning. Should natural gas benefit from a sustained relative energy price advantage, other incremental sources of demand could emerge. When and where this incremental demand might stress both supply and distribution infrastructure could create unforeseen challenges.

Climate Change Legislation

One area of fallout from the recession was a reconsideration of the potentially damaging economic implications climate change legislation could impose upon a vulnerable economy. Consequently, climate change legislation is effectively suspended with an uncertain future. Prior to the recession, it was generally viewed that climate change legislation would advantage natural gas-fired generation relative to coal-fired generation given its cleaner emissions and smaller carbon footprint. However, even without carbon legislation, the new lower natural gas price environment is making natural gas generation competitive with many coal plant facilities. The challenge is to assess whether significant additional gas demand for power will erode the current surplus production situation due to the shale boom. Correspondingly, once supply and demand rebalances, will there be upward pressure on prices as producers need to reach into their more expensive inventory?

Regional Infrastructure

In comparison to other parts of the country, the Pacific Northwest has significantly fewer pipeline options to bring supply from the producing basins to its various local service territories. Recent history (pre recession) shows that our regional supply infrastructure was strained prompting several new pipeline projects. For Avista, many of these pipeline projects did not facilitate bringing gas all the way to our service territory and were thus only a potential partial solution. As the recession began to impact regional demand, the need for these new pipelines waned. Should demand rebound quickly, the need could reassert itself again but with less time to respond.

The Pacific Northwest has historically been geographically well positioned to benefit from an Alaskan natural gas pipeline. However, shale gas production has made the future of an Alaskan natural gas

pipeline more uncertain than ever. With plentiful low cost shale gas available numerous locations in the lower 48 states, these resources have a geographic advantage of being much closer to markets, making for very challenging economics to support Alaska pipeline project development at this time.
