Exhibit No.___(BNW-1T)
Docket No. UE-09___
Witness: Bruce N. Williams

BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION, Complainant, vs. PACIFICORP dba Pacific Power Respondent.	)	Docket No. UE-09______

PACIFICORP

DIRECT TESTIMONY OF BRUCE N. WILLIAMS

February 2009

1 **Q. Please state your name, business address and present position with**
2 **PacifiCorp (the Company).**
3 A. My name is Bruce N. Williams. My business address is 825 NE Multnomah,
4 Suite 1900, Portland, Oregon 97232. My present position is Vice President and
5 Treasurer.
6 **Qualifications**
7 **Q. Briefly describe your educational and professional background.**
8 A. I received a Bachelor of Science degree in Business Administration with a
9 concentration in Finance from Oregon State University in June 1980. I also
10 received the Chartered Financial Analyst designation upon passing the
11 examination in September 1986. I have been employed by the Company for 23
12 years. My business experience has included financing of the Company's electric
13 operations and non-utility activities, responsibility for the investment
14 management of the Company's qualified and non-qualified retirement plan assets,
15 and investor relations.
16 **Q. Please describe your present duties.**
17 A. I am responsible for the Company's treasury, credit risk management, pension
18 and other investment management activities. I am also responsible for the
19 preparation of PacifiCorp's embedded cost of debt and preferred equity and any
20 associated testimony related to capital structure for regulatory filings in all of
21 PacifiCorp's state and federal jurisdictions.

1 **Purpose of Testimony**

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

3 A. I first present a financing overview of the Company. Next, I discuss the amounts
4 of common equity, debt, and preferred stock to be included in the Company's
5 proposed capital structure. I then analyze the embedded cost of debt and
6 preferred stock supporting PacifiCorp's electric operations in the state of
7 Washington as of June 30, 2009. This analysis includes the use of forward
8 interest rates, the historical relationship of security trading patterns, and known
9 and measurable changes to the debt and preferred stock portfolios.

10 **Q. What time period does your analyses cover?**

11 A. The test period in this proceeding is the twelve months ending June 30, 2008 with
12 known and measurable adjustments. For cost of capital, the Company has used a
13 pro forma period through June 30, 2009. Therefore, the determination of the
14 embedded cost of debt and preferred stock was conducted using the Company's
15 actual costs adjusted for changes through June 30, 2009, as I later detail in this
16 filing.

17 **Q. Please explain the Company's requirements to generate new capital.**

18 A. As described in Company witness Mr. Richard P. Reiten's direct testimony, the
19 Company continues to acquire new generation resources, such as the Chehalis gas
20 plant and new renewable energy facilities. These and future capital additions and
21 investments will require the Company to raise funds by issuing significant
22 amounts of new long-term debt in the capital markets and obtaining new capital
23 contributions from its parent company. Funds will also be made available by the

1 continued absence of any dividends or distributions by PacifiCorp to its parent
2 company during the period. Since the acquisition of PacifiCorp by MidAmerican
3 Energy Holdings Company ("MEHC") in March 2006, there have been no
4 common stock dividends or distributions, PacifiCorp has received $865 million in
5 additional cash equity contributions from MEHC and $1.1 billion of earnings
6 have been retained in PacifiCorp. These actions help ensure that PacifiCorp
7 remains well-positioned to support the additional investments that have been and
8 will continue to be made in the system.

9 **Q. What is the overall cost of capital that you are proposing in this proceeding?**

10 A. PacifiCorp is proposing an overall cost of capital of 8.51 percent. This cost
11 includes the Return on Equity recommendation from Dr. Samuel C. Hadaway and
12 the following capital structure and costs:

13 Overall Cost of Capital

Line	Component	Percent of Total	% Cost	Weighted Average
14–15	Component	Percent of Total	% Cost	Weighted Average
16	Short Term Debt	0.4%	2.39%	0.01%
17	Long Term Debt	49.1%	6.05%	2.97%
18	Preferred Stock	0.4%	5.41%	0.02%
19	Common Stock Equity	50.1%	11.00%	5.51%
20	Total	100.0%		8.51%

21 **Q. Why have you included short-term debt as part of the capital structure?**

22 A. The Company is doing so in this case to be consistent with the Washington
23 Utilities and Transportation Commission's ("Commission") final Order in Docket

1 UE-050684. However, the Company continues to believe that it is inappropriate
2 and inequitable to include short-term debt in the capital structure for PacifiCorp.
3 As it now stands, short-term debt is effectively being double-counted as financing
4 both rate base and construction work in progress. To remedy this inconsistency,
5 PacifiCorp would need to deviate from the Federal Energy Regulatory
6 Commission-prescribed method for determining the allowance for funds used
7 during construction. Unfortunately, this is not a practical solution for PacifiCorp
8 as it would result in assets that are allocated to more than one state having
9 multiple, different book values and depreciation rates.
10 Further, the percentage of short-term debt in the capital structure can be
11 more volatile than the permanent sources of financing. Short-term balances can
12 move dramatically and the Company often has periods of time when there is no
13 short-term debt outstanding. The fact that there are periods of time with no short-
14 term debt demonstrates that short-term debt is not a permanent source of
15 financing rate base. The Company will continue to evaluate this treatment of
16 short-term debt and may request the Commission to reconsider it in future cases.
17 **Financing Overview**
18 **Q. How does the Company finance its electric utility operations?**
19 A. The Company finances the cash flow requirements of its regulated utility
20 operations utilizing a reasonable mix of debt and equity designed to provide a
21 competitive cost of capital and predictable capital market access.

1 **Q. How does the Company meet its debt and preferred equity financing**
2 **requirements?**
3 A. The Company relies on a mix of first mortgage bonds, other secured debt, tax-
4 exempt debt, unsecured debt and preferred stock to meet its long-term debt and
5 preferred stock financing requirements.
6 The Company has completed the majority of its long-term financing
7 utilizing secured first mortgage bonds issued under the Mortgage Indenture dated
8 January 9, 1989. Exhibit No.___(BNW-2) shows that, as of June 30, 2009, the
9 Company is projected to have approximately $5.8 billion of first mortgage bonds
10 outstanding, with an average cost of 6.40 percent and average remaining maturity
11 of 19 years. Presently, all outstanding first mortgage bonds bear interest at fixed
12 rates. Proceeds from the issuance of the first mortgage bonds (and other financing
13 instruments) are used to finance the combined utility operation and are not
14 allocated on a divisional basis.
15 Another important source of financing has been the tax-exempt financing
16 associated with certain qualifying equipment at power generation plants. Under
17 arrangements with local counties and other tax-exempt entities, the Company
18 borrows the proceeds and guarantees the repayment of the long-term debt in order
19 to take advantage of their tax-exempt status in financings. As of June 30, 2009,
20 the Company's tax-exempt portfolio is projected to be $738 million in principal
21 amount with an average cost of 3.31 percent (which includes the cost of issuance
22 and credit enhancement).

1 **Capital Structure**

2 **Q. How did you determine the capital structure proposed in this proceeding?**

3 A. The Company used an average of the five quarter ends during the time period
4 ending June 30, 2009 to calculate its proposed capital structure. This approach
5 smoothes volatility in the percentage of short-term debt and other aspects of the
6 capital structure that may fluctuate as the Company expends capital, issues debt,
7 retains earnings or receives infusions of new equity. The Company calculated its
8 capital structure in this same manner in its last general rate case in Docket No.
9 UE-080220, ("2008 Rate Case"). This method is also consistent with the
10 approach to capital structure advocated by Commission Staff and Public Counsel
11 in Docket UE-050684.

12 **Q. How does the Company determine the amount of common equity, debt, and**
13 **preferred stock to be included in its capital structure?**

14 A. As a regulated utility, PacifiCorp has a duty and an obligation to provide safe,
15 adequate and reliable service to customers in its Washington service territory
16 while balancing cost and risk. Significant capital expenditures for new plant
17 investment, including new renewable resources, operating and maintenance costs
18 for new and existing utility plant assets and environmental investments are
19 required for the Company to fulfill this obligation. Through its planning process,
20 the Company determined the amounts of necessary new financing needed to
21 support these activities and calculated the equity and debt ratios required to
22 maintain the Company's current 'A-' credit rating for senior secured debt.

1 **Q. Has the Company's capital structure demonstrated increased amounts of**
2 **equity?**
3 A. Yes. This is consistent with the "general trend of increasing equity capitalization
4 in the industry," noted by the Commission in its final Order in Docket UE-
5 050684, and reflects MEHC's significant capital contributions to PacifiCorp since
6 it acquired the Company.
7 **Q. Why is there the need for additional equity in the capital structure?**
8 A. The Company's capital structure reflects the cost increases described in this case,
9 including investment in utility plant and power costs. These cost increases,
10 coupled with the credit rating agencies' expectations for credit metrics and
11 balance sheet strength, mean that the Company cannot finance itself solely with
12 new debt. Additional equity is required along with improved business results and
13 other considerations to support our current 'A-' credit rating from Standard &
14 Poor's ("S&P"), 'A3' rating from Moody's Investors Service ("Moody's"), and
15 'A-'from Fitch Ratings.
16 **Q. How does this proposed capital structure compare to similarly-situated**
17 **electric utilities?**
18 A. The proposed capital structure is consistent with the comparable group that Dr.
19 Hadaway has selected in his estimate of Return on Equity. The Value Line
20 estimate of common equity ratio for the comparable group is 49.8 percent as
21 shown in Exhibit No. ___(SCH-3), in line with the 50.1 percent common equity
22 ratio PacifiCorp proposes in this case.

1 **Q. Please describe the changes to the Company's levels of debt financing.**

2 A. During the period ending June 30, 2009, the balance of the outstanding long-term
3 debt will change through maturities, principal amortization and issuance of new
4 securities. Based upon the long-term debt series outstanding at December 31,
5 2008, I have calculated the reduction to the outstanding balances for maturities,
6 principal amortization and sinking fund requirements which are scheduled to
7 occur during the period ending June 30, 2009. Additionally, the capital structure
8 reflects a $1.0 billion long-term debt issuance that occurred in January 2009, the
9 details of which I discuss later in this testimony.

10 **Q. Is the proposed capital structure consistent with the Company's current**
11 **credit rating?**

12 A. Yes. This capital structure is intended to enable the Company to deliver its
13 required capital expenditures while maintaining credit ratios that support the
14 continuance of our current 'A-' credit rating.

15 **Q. Are PacifiCorp's stand-alone credit metrics consistent with the Company's**
16 **current credit ratings?**

17 **A.** No. As stated by S&P, "While the…. utility's credit metrics are more consistent
18 on a standalone basis with a 'BBB' category rating, the ratings benefit from the
19 implicit and explicit support available to MEHC… from its parent, Berkshire
20 Hathaway… As a result, the ratings assigned to PacifiCorp are higher than would
21 be warranted….". Clearly, PacifiCorp and our customers benefit from the
22 ownership by MEHC and its parent, Berkshire Hathaway.

23 Another important element supporting the Company's current credit

1 ratings is the rating agencies expectations that PacifiCorp will receive supportive
2 regulatory treatment including reasonable outcomes in rate proceedings. Absent
3 ownership by MEHC or constructive regulatory treatment, PacifiCorp's credit
4 ratings would likely suffer at least a one rating level downgrade.

5 **Q. How does maintenance of the Company's current credit ratings benefit**
6 **customers?**

7 A. The credit ratings given to a utility have a direct impact on the price that a utility
8 pays to attract the capital necessary to support its current and future operating
9 needs. A solid credit rating directly benefits customers by reducing immediate
10 and future borrowing costs related to the financing needed to support regulatory
11 operations.

12 **Q. Are there other benefits?**

13 A. Yes. During periods of capital market disruptions, higher-rated companies are
14 more likely to have on-going, uninterrupted access to capital. This is not always
15 the case with lower-rated companies, which during such periods find themselves
16 either unable to secure capital or able to secure capital only on unfavorable terms
17 and conditions. I will discuss how PacifiCorp's current ratings have assisted it in
18 recently accessing the market for new long-term debt at attractive levels later in
19 my testimony.

20 In addition, higher-rated companies have greater access to the long-term
21 markets for power purchases and sales. Such access provides these companies
22 with more alternatives when attempting to meet the current and future load
23 requirements of their customers. Finally, a company with strong ratings will often

1 avoid having to meet costly collateral requirements that are typically imposed on
2 lower-rated companies when securing power in these markets.

3 **Impacts of Economic Crisis on PacifiCorp**

4 **Q. How has the recent liquidity or credit crisis impacted PacifiCorp?**

5 A. Very significantly. Although the Company has been able to continue to fund its
6 working capital and long-term needs, it has been anything but "business as usual."
7 For example, at times during October 2008, the Company was unable to find
8 investors for its commercial paper. Fortunately, the Company had previously
9 arranged multi-year, committed revolving credit agreements and was able to
10 borrow under those facilities in order to provide liquidity and daily cash needs
11 normally met by the commercial paper markets. At the times when the
12 commercial paper market was available, rates were significantly higher than just a
13 few months earlier. During November 2008, the Company's commercial paper
14 rates were at an average spread of approximately 250 basis points (2.50 percent)
15 higher than issuances through the middle of July 2008. While recent short-term
16 funding for the Company has modestly improved from these harsh conditions, the
17 Company is largely limited to overnight commercial paper issuances rather than a
18 range of maturities of up to 270 days as in prior markets.

19 Similar to the commercial paper market, the market for tax-exempt debt
20 was also "frozen" for a period of time. As I discussed earlier in this testimony,
21 the Company has arranged over $700 million of low-cost tax-exempt financing.
22 A portion of this debt is variable rate and re-prices through periodic remarketings.
23 However, this market also was shaken by the credit crisis resulting in extremely

1 high resets of interest rates or failed remarketings when there was insufficient
2 investor demand. PacifiCorp chose to acquire approximately $216 million of
3 these obligations to avoid paying rates that were unimaginable just a few months
4 earlier. The Company recently completed the remarketing of these bonds
5 following a change to their credit enhancements including the addition of letters
6 of credit for the benefit of investors. Other utilities have found this market is
7 now totally closed to them and are delaying previously scheduled tax-exempt
8 bond offerings. Fortunately, PacifiCorp enjoys the benefits of sound credit
9 ratings and was able to lessen the impact on customers by temporarily acquiring
10 the bonds, arranging for these letters of credit despite extremely difficult
11 conditions for the banks themselves and then remarketing the bonds.

12 **Q. Was PacifiCorp able to issue new long-term debt during this period?**

13 A. Yes. In early January 2009, the Company issued $350 million of first mortgage
14 bonds with a ten-year maturity at a coupon rate of 5.50 percent and $650 million
15 of thirty-year first mortgage bonds with a coupon of 6.00 percent.

16 **Q. What are your observations about this long-term debt issuance?**

17 A. First, the issuance demonstrated the importance of PacifiCorp's solid investment
18 grade credit ratings during a period of time in which the markets have been
19 extremely volatile. Many lower rated issuers have not been able to access the
20 debt markets or have found the terms and conditions prohibitive. The
21 Company's sound investment grade rating has allowed it continued access to the
22 credit markets, although at credit spreads higher than historical levels.

23 Second, as noted in Dr. Hadaway's direct testimony, recent increases in

1 credit spreads have impacted the Company's cost of equity and debt. His
2 testimony includes a table that shows recent utility debt issuances and their
3 corresponding credit spreads. While the Company's credit spread of 3.10 percent
4 on its recent long term debt issuance is better than the range seen in recent
5 issuances by other utilities, it is still among the highest credit spreads the
6 Company has experienced.

7 **Q. How do the terms of PacifiCorp's debt issuance compare to other recent**
8 **utility debt issuances?**

9 A. PacifiCorp was able to issue debt at interest rates below rates that other borrowers
10 have achieved. For example, Nevada Power (rated Baa3/BBB) issued new debt
11 two days following PacifiCorp and was required by investors to pay a coupon of
12 7.375 percent for a five-year maturity. More recently, Puget Sound Energy (rated
13 Baa2/A-) issued new seven year debt at a spread of Treasuries plus 480.3 basis
14 points resulting in a coupon of 6.75 percent. In addition, lower rated borrowers
15 appear to be shut out entirely of the market. For example, Arizona Public Service
16 Company (rated Baa2/BBB-) recently filed a letter with the Arizona Corporation
17 Commission explaining that the commercial paper market is completely closed to
18 them and, they likely could not successfully issue long-term debt. See Exhibit
19 No.___(BNW-3).

20 **Q. What do you conclude from this comparison?**

21 A. This recent period of market volatility has underscored the critical importance to
22 utilities of maintaining solid credit ratings. Lower-rated utilities are now paying
23 dearly for their more tenuous credit positions because they cannot access capital

1 or can do so only at very high prices. This confirms the importance of
2 PacifiCorp's ongoing plan to maintain a balanced capital structure. It also
3 highlights PacifiCorp's need for supportive and constructive treatment from its
4 regulatory commissions.

5 **Purchase Power Agreements**

6 **Q. Is the Company subject to rating agency debt imputation associated with**
7 **Purchase Power Agreements?**

8 A. Yes. Rating agencies and financial analysts consider Purchase Power Agreements
9 ("PPAs") to be debt-like and will impute debt and related interest when
10 calculating financial ratios. For example, S&P will adjust the Company's
11 published financial results and impute debt balances and interest expense related
12 to PPAs when assessing creditworthiness. They do so in order to obtain a more
13 accurate assessment of a company's financial commitments and fixed payments.
14 Exhibit No.___(BNW-4) is the May 12, 2003 publication by S&P detailing its
15 view of the debt aspects of PPAs which was refined in the March 30, 2007
16 publication (Exhibit No.___(BNW-5)).

17 **Q. How does this impact the Company?**

18 A. During a recent ratings review, S&P evaluated the Company's PPAs and other
19 related long-term commitments. Approximately $450 million of additional debt
20 and related interest expense were added to the Company's debt and coverage tests
21 as a result of PPAs.

1 **Q. How would the inclusion of this PPA related debt affect the Company's**
2 **capital structure?**
3 A. By including the $450 million imputed debt resulting from PPAs, the Company's
4 capital structure would have a lower equity component as a corollary to the higher
5 debt component.
6 **Financing Cost Calculations**
7 **Q. How did you calculate the Company's embedded costs of long-term debt and**
8 **preferred stock?**
9 A. I calculated the embedded costs of debt and preferred stock using the
10 methodology relied upon in the 2008 Rate Case and previous rate cases in
11 Washington and other jurisdictions.
12 **Q. Please explain the cost of long-term debt calculation.**
13 A. I calculated the cost of debt by issue, based on each debt series' interest rate and
14 net proceeds at the issuance date, to produce a bond yield to maturity for each
15 series of debt. It should be noted that in the event a bond was issued to refinance
16 a higher cost bond, the pre-tax premium and unamortized costs, if any, associated
17 with the refinancing were subtracted from the net proceeds of the bonds that were
18 issued. The bond yield was then multiplied by the principal amount outstanding
19 of each debt issue, resulting in an annualized cost of each debt issue. Aggregating
20 the annual cost of each debt issue produces the total annualized cost of debt.
21 Dividing the total annualized cost of debt by the total principal amount of debt
22 outstanding produces the weighted average cost for all debt issues. This is the
23 Company's embedded cost of long-term debt.

1 **Q. How did you calculate the embedded cost of preferred stock?**
2 A. The embedded cost of preferred stock was calculated by first determining the cost
3 of money for each issue. This is the result of dividing the annual dividend rate by
4 the per share net proceeds for each series of preferred stock. The cost associated
5 with each series was then multiplied by the total par or stated value outstanding
6 for each issue to yield the annualized cost for each issue. The sum of annualized
7 costs for each issue produces the total annual cost for the entire preferred stock
8 portfolio. I then divided the total annual cost by the total amount of preferred
9 stock outstanding to produce the weighted average cost for all issues. This is the
10 Company's embedded cost of preferred stock.
11 **Q. A portion of the securities in the Company's debt portfolio bears variable**
12 **rates. What is the basis for the projected interest rates used by the Company?**
13 A. The majority of the Company's variable rate long-term debt is in the form of tax-
14 exempt debt. Exhibit No.___(BNW-6) shows that these securities on average had
15 been trading at approximately 85 percent of the 30-day London Inter Bank Offer
16 Rate ("LIBOR") for the period January 2000 through December 2008. Therefore,
17 the Company has applied a factor of 85 percent to the forward 30-day LIBOR
18 Rate at June 30, 2009 of 2.23 percent and then added the respective credit
19 enhancement and remarketing fees for each floating rate tax-exempt bond. Credit
20 enhancement and remarketing fees are included in the interest component because
21 these are costs which contribute directly to the interest rate on the securities and
22 are charged to interest expense. This method is consistent with the Company's
23 past practices when determining the cost of debt in previous Washington general

1 rate cases as well as the other states that regulate PacifiCorp.

2 **Embedded Cost of Long-Term Debt**

3 **Q. What is the Company's embedded cost of long-term debt?**

4 A. The cost of long-term debt is 6.05 percent, at June 30, 2009 as shown in Exhibit
5 No.___(BNW-2). As noted above, this includes the Company's January 2009,
6 debt issuance. The Company does not expect to issue any significant new debt
7 between the time of the filing and June 30, 2009.

8 **Embedded Cost of Preferred Stock**

9 **Q. What is the Company's embedded cost of preferred stock?**

10 A. Exhibit No.___(BNW-7) shows the embedded cost of preferred stock at June 30,
11 2009 at 5.41 percent.

12 **Fulfillment of MEHC Commitment**

13 **Q. Did PacifiCorp and MEHC make certain commitments concerning cost of**
14 **incremental long-term debt?**

15 A. Yes. During the regulatory approval process related to the acquisition of the
16 Company, MEHC stated that the incremental cost of long-term debt would be
17 reduced as a result of the acquisition by MEHC, due to the association with
18 Berkshire Hathaway. In Docket UE-051090, MEHC and PacifiCorp made a
19 formal commitment (General Commitment 37) that over the five years following
20 the closing of the transaction, they would demonstrate that incremental long-term
21 debt issuances would be at a spread ten basis points below PacifiCorp's similarly
22 rated peers.

1 **Q. Has the Company issued any long-term debt that has not been previously**
2 **assessed as to whether it satisfied General Commitment 37?**
3 A. Yes. On July 14, 2008, the Company issued $800 million of new long-term debt.
4 Additionally, the Company just completed an issuance in January 2009, as
5 discussed earlier in my testimony.
6 **Q. Have you assessed whether the MEHC commitment was fulfilled with respect**
7 **to this long-term debt issuance?**
8 A. Yes. Based on separate studies by banks knowledgeable about the Company's
9 debt issuances, market conditions and long-term debt issuances by other market
10 participants, the Company's issuances of long-term debt not only met, but
11 exceeded, the promised level of savings. Confidential Exhibit No.___(BNW-8C)
12 and Confidential Exhibit No.___(BNW-9C) demonstrates that each of the
13 respective issuances of long-term debt fulfilled the requirements of General
14 Commitment 37.
15 **Q. Does this conclude your direct testimony?**
16 A. Yes.