Exhibit No. ___(KC-3)
Docket No. UE-051090
Witness: Ken Canon

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of the Joint Application of MIDAMERICAN ENERGY HOLDINGS COMPANY AND PACIFICORP, d/b/a PACIFIC POWER & LIGHT COMPANY For an Order Authorizing Proposed Transaction.	)	**Docket No. UE-051090**

EXHIBIT NO.___(KC-3)

EXCERPT OF OFFICE OF RATEPAYER ADVOCATES' REPORT ON THE PROPOSED ACQUISITION OF PACIFICORP BY MIDAMERICAN ENERGY HOLDING COMPANY (OCT. 19, 2005)

November 18, 2005

Docket:	:	A. 05-07-010
Exhibit Number	:	
Commissioner	:	Comm. J. Bohn
Admin. Law Judge	:	ALJ T. Kenney
Witnesses	:	M. K. Bumgardner
	:	

OFFICE OF RATEPAYER ADVOCATES
CALIFORNIA PUBLIC UTILITIES COMMISSION

Office of Ratepayer Advocates' Report on the Proposed Acquisition of PacifiCorp by MidAmerican Energy Holding Company

San Francisco, California
October 19, 2005

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1. EXECUTIVE SUMMARY

Applicants request an order exempting the proposed aquistion of PacifiCorp by MidAmerican Energy Holding Company (MEHC) from the approval requirements of Section 854(a) of the Public Utilities Code (P.U. Code). The Office of Ratepayer Advocates (ORA) has reviewed PacifiCorp/MEHC's Application (A.) 05-07-070[1] and finds the following.

- The acquisition would result in $1.3 billion more in capital investment, which would increase the costs California ratepayers pay PacifiCorp by $5.3 million every year.
- The acquisition would increase operating costs by $3.5 million per year, which would increase the costs California ratepayers pay PacifiCorp by an additional $70,000 each year.
- MEHC claims that ratepayers would save $7.3 million annually, which would result in a potential decrease of $145,000 a year for California ratepayers. The economic benefits to ratepayers associated with the proposed transaction are paltry.
- California ratepayers may ultimately have to pay an additional $121 a year per ratepayer based upon PacifiCorp/MEHC's application.
- The acquisition of PacifiCorp by MEHC may increase PacifiCorp's debt cost rather than decrease them based upon the evidence in the Commission's possession.
- MEHC has not recognized any other synergies inherent in its acquisition of another large utility in addition to the one it currently operates in the mid-West.
- The majority of the other conditions appear to keep PacifiCorp's California ratepayers neutral to the acquisition.

[1] Application of PacifiCorp and MidAmerican Energy Holdings Company for Exemption Under Section 853(b) From the Approval Requirements of Section 854(a) of the Public Utilities Code with Respect to the Acquisition of PacifiCorp by MidAmerican, filed July 15, 2005. (Application)

These results are contrary to ratepayer interest. In addition, PacifiCorp has currently expressed its intent to file a test year 2007 general rate case (GRC) application (presumably for higher rates.) Looking at these results in isolation warrants a denial of the Application. There are no net economic benefits to ratepayers associated with the acquisition, and the Applicants have not demonstrated that the request is in the public interest.

ORA recommends that this Commission reject the Applicants' request to have MEHC acquire PacifiCorp; but should the Commission authorize this acquisition, any approval needs to be conditioned on the implementation of the following requirements:

- PacifiCorp must postpone its planned general rate increase filing for one year to provide ratepayers sufficient guaranteed tangible benefits from the acquisition (rates would be held at current levels until January 1, 2008);

- Under no circumstances should ratepayers be required to pay the costs associated with acquisition premiums to a utility. Paying any part of the acquisition premium would make this transaction unbeneficial to ratepayers. Unless the Applicants agree that ratepayers will not pay any part of the acquisition premium, the proposed transaction should not be authorized.

- MEHC must pay all acquisition costs and will not allocate any of these costs to PacifiCorp's ratepayers.

- Upon completion of the transaction, PacifiCorp, its owners, and its affiliates will be governed by the California P.U. Code, the Commission's General Orders, Rules of Practice and Procedures, and all decisions and resolutions that PacifiCorp is currently required to follow.

- PacifiCorp and its new owners must provide California with the same operating and affiliate transaction reports that they will provide to the other states that it operates.

- PacifiCorp and MEHC must provide California ratepayers with the same benefits that are provided to other jurisdictions (Most Favored Nation Treatment.)

Unless the Commission includes these provisions as part of the proposed transaction, the Application should be denied.

2. OVERVIEW

A) PacifiCorp

PacifiCorp is an electric utility, incorporated in Oregon, with substantial operations in six western states. The six states in which it conducts regulated electric utility operations are the states of Washington, Oregon, Idaho, Utah, Wyoming and California.

PacifiCorp's electric operations in California are by far the smallest of those in any of these states, consisting of approximately 43,000 customers, $65 million of annual revenue, and about 2% of its system sales. The generation used to serve California customers is primarily located in other states, as is the vast bulk of the transmission system used by PacifiCorp to serve its California customers.[2]

PacifiCorp stated that prior to negotiating the acquisition by MEHC, it had already planned to file a separate general rate application in the late fall for a test year beginning January 1, 2007. The application further states that PacifiCorp's rates were last increased in late 2003, citing D. 03-11-019, and that its California territory electric rates average approximately 7.7¢/KWh.[3]

B) MidAmerican Energy Holding Company

MEHC is a privately-held company engaged in the production and delivery of energy from a variety of sources, including coal, natural gas, geothermal, hydroelectric, nuclear, wind and biomass. MEHC's global assets total approximately $20 billion and its 2004 revenues totaled approximately $6.6

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[2] Application (A.) 05-07-010 p. 2.

[3] A. 05-07-010, p. 2, fn 4.

billion.[4] An Iowa corporation, MEHC's major ownership interest of 83.75% belongs to Berkshire Hathaway Inc. [5]

With the repeal of the Public Utility Holding Company Act of 1935 (PUHCA), Berkshire Hathaway will exchange its convertible preferred stock in MEHC into common shares, increasing Berkshire Hathaway's 9.9% voting interest in MEHC to a voting interest of approximately 83.75% (or 80.5% on a diluted basis) of the common stock of MEHC. The exchange of Berkshire Hathaway's convertible preferred stock does not change the owners of MEHC, only their respective voting interests. The result is the matching of Berkshire Hathaway's voting interest with its ownership interest. The conversion does not affect the PacifiCorp transaction since MEHC remains the acquiring entity.[6]

C) ScottishPower

ScottishPower's 2004/05 Annual Report and Accounts states that the sale of PacifiCorp to MEHC for $9.4 billion will bring net proceeds of $5.1 billion, of which $4.5 billion will be returned to shareholders. MEHC will assume net debt of approximately $4.3 billion.[7]

D. 99-06-049 dated June 10, 1999, stated that ScottishPower was "incorporated in Scotland in 1989," "is a multi-utility business in the United Kingdom (U.K.) with 5 million customers," has "activities that span electricity generation, transmission, distribution and supply," has "provided electric service to the public for over 100 years," "is among the 25 largest investor-owned electric utilities in the world", "had assets of approximately $9 billion" in 1998, maintain

[4] Revised Direct Testimony of Gregory E. Abel, PPL/100, p. Abel/7.

[5] A. 05-07-010, p. 5.

[6] August 24, 2005 letter from Andrea Kelly, Managing Director to ALJ Kenney, p. 2.

[7] ScottishPower 2004/05 Annual Report and Accounts, p. 5.

PacifiCorp's U.S. debt market, and "provide access to U.K. and European debt markets." ScottishPower claimed that the 1999 acquisition would:

- Enable PacifiCorp to become part of a large financially strong corporation group and will permit it to obtain needed capital on favorable terms.
- Stress standards of service which encompass a variety of areas, the object of which is to enhance performance within the business and increase customer satisfaction.[8]

D) Proposed Acquisition

On April 27, 2005, MEHC initiated the negations to acquire PacifiCorp from ScottishPower.[9] On or about May 23, 2005, MEHC and ScottishPower entered into an agreement to sell all of PacifiCorp's common stock to MEHC for approximately $9.4 billion. Approximately $5.1 billion is cash and the remaining $4.3 billion is net debt and preferred stock, which will remain outstanding at PacifiCorp.[10] The sale of PacifiCorp's common stock includes transfer of control of certain PacifiCorp subsidiaries that are associated with the regulated business.[11]

E) Commission's Role in Authorizing this Transaction

The Commission is charged with overseeing the acquisitions and mergers of public utilities that serve California ratepayers,[12] as well as the sale of utility

[8] D. 99-06-049

[9] MEHC's response to ORA 3rd Data Request 3.5.

[10] Direct Testimony of Gregory E. Abel, PPL/100, Abel/10.

[11] The following PacifiCorp subsidiaries which will be included in the transfer consist primarily of mining companies and companies created to handle environmental remediation and avoided deforestation carbon credits: Centralia Mining Company, Energy West Mining Company, Glenrock Coal Company, Interwest Mining Company, Pacific Minerals, Inc., Bridger Coal Company, PacifiCorp Environmental Remediation Company, PacifiCorp Future Generations, Inc., Canopy Botanicals, Inc., Canopy Botanicals, SRL, PacifiCorp Investment Management, Inc., and Trapper Mining, Inc. (A.05-07-010, p. 12).

[12] P.U. Code, Section 854. See Attachment A.

assets used for serving ratepayers,[13] and the purchase of utility stock.[14] The Applicants contend that because PacifiCorp is not a California corporation, Section 854(a) does not authorize the Commission to review the proposed acquisition under that Section.[15] Instead, Applicants claim that the Commission should exempt the transaction from review under Section 853(b)[16] of the P.U. Code.

Section 854(a) provides in part:

"No person or corporation, whether or not organized under the laws of this state, shall merge, acquire, or control either directly or indirectly any public utility organized and doing business in this state without first securing authorization to do so from the commission" Applicants argue that since PacifiCorp is a public utility "doing business in this state" but is not "organized under the laws of this state," Section 854(a) does not authorize this Commission to review the transaction. Such an interpretation of Section 854(a) is contrary to the results of over fifty reported cases in which the Commission has reviewed Section 854(a) applications filed by utilities notwithstanding the fact that the utility being acquired is incorporated in a state other than California.[17]

Most recently, the Commission reviewed the acquisition of Avista's California gas service territory by Southwest Gas Corporation. D. 05-03-031 approved Southwest's acquisition of Avista's South Lake Tahoe service territory of Avista pursuant to Sections 851 and 854 of the P.U. Code. As discussed further

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[13] Section 851. See Attachment A.

[14] Section 852. See Attachment A

[15] A. 05-07-010, p. 2 and note 2.

[16] The complete text of Section 853(b) is in Attachment A, but in part it states "the commission may….exempt any public utility….from this article if it finds that the application thereof with respect to the public utility is not necessary in the public interest."

[17] See Attachment B List of 854(a) applications and decisions involving utilities incorporated in other states.

in Section 4.E, the Commission approved a settlement between Avista, Southwest, and ORA that recognized significant synergies and ratepayer benefits that would result from the proposed transaction.

The Commission should exercise its authority pursuant to Sections 851 and 854 to review MEHC's proposed acquisition of PacifiCorp, as it did earlier this year for Avista, and for dozens of other similar transactions in the past.

3. FUTURE RATEPAYER IMPACTS

In its application, MEHC and PacifiCorp identify several capital projects, additional operating costs, and some cost savings that it would undertake. The following table shows the impacts of these changes and the impact on California's ratepayers.

PacifiCorp/MEHC Merger New Costs (Capital & Expense) (Dollars in thousands)			
Project Name Capital Costs	Expected Cost	Total Costs	Estimated California Allocation
Path C Upgrade	$ 78,000		
Mona-Oquirrh	$ 196,000		
Walla Walla-Yakima or Mid-C	$ 88,000		
Other Transmission and Distribution (Asset Risk Program)	$ 75,000		
Other Transmission and Distribution (Local Transmission Risk Projects)	$ 69,000		
Emission Reductions from Coal-Fueled Generating Plant	$ 812,000		
Total Expected Capital Plant Additions		$ 1,318,000	
Total California Future Expected Annual Impact			$ 5,272
Project Name Operating Costs			
Other Transmission and Distribution (Accelerated Distribution Circuit Fusing Program)	$ 1,500		
Other Transmission and Distribution (Saving SAIDI Initiative)	$ 2,000		
Total Expected Operating Expense Increase		$ 3,500	
Total California Future Expected Operating Effect			$ 70
Cost Savings			
Reduced Cost of Debt	$ (1,260)		
Corporate Overhead Charges	$ (6,000)		
Total Expected Cost Savings		$ (7,260)	
Total California Expected Cost Savings			$ (145)
Total Ultimate Expected Future Revenue Requirement in California			$ 5,197
Customer Expected Impact in California			$ 121

MEHC expects to add $1.3 billion in total system capital adds in the future, which has an impact of increasing California customer costs by $5 million.[18] It should be noted that none of the transmission or emission investment projects are currently required by federal or state law or any federal or state regulatory agency.[19] Assuming MEHC estimates its incremental capital additions, operating expense increases, and cost savings correctly, the cost to ratepayers will be to ultimately increase each customer's rates by potentially $121 per year. Based on this evidence, the proposed merger would not provide economic benefits to California ratepayers.

4. RATEPAYER BENEFIT

A) Debt Financing

MEHC claims that PacifiCorp's incremental cost of long-term debt will be reduced as a result of the proposed transaction, due to the association with Berkshire Hathaway. According to MEHC its utility subsidiaries have been able to issue long-term debt at levels below their peers with similar credit ratings. MEHC commits that over the next five years it will demonstrate that PacifiCorp's incremental long-term debt issuances will be at a yield ten basis points below its similarly rated peers. It offers that if it is unsuccessful in demonstrating that PacifiCorp's long-term debt costs are ten basis points lower than similarly rated peers, PacifiCorp will accept up to a ten basis point reduction to the yield it actually incurred on any incremental long-term debt issuances for any revenue

[18] A. 05-07-010, Appendix No. 7, pp. 1, 2, 3, and 4, shows the support for the $1.3 billion in capital projects, 3.5 million in operating expenses, and 7.2 million cost savings. All costs were developed on an annual basis. Capital expenses were developed by multiplying capital costs by .2 as an approximation of return, taxes, and depreciation. California costs were calculated by multiplying total company expenses by .02, and per customer costs were calculated by dividing California costs by 43,000, the number of PacifiCorp customers living in California.

[19] MEHC's response to ORA 3rd Data Request 3.1.3.

requirement calculation effective for the five year period subsequent to the approval of the proposed acquisition.[20]

MEHC states that it has "access to significant financial and managerial resources thorough its relationship with Berkshire Hathaway, one of its owners, whose debt rating is AAA." MEHC adds that its "global assets are approximately $20 billion, with its 2004 revenues totaling $6.6 billion." Moreover, on a consolidated basis, "MEHC's pro forma combined assets would be approximately $34 billion, with combined revenues of about $9.6 billion." [21]

However, MEHC's credit rating from the various credit rating agencies are only a BBB- from Standard & Poor's (S&P); Baa3 from Moody's Investor Service (Moody's); and BBB from Fitch Ratings (Fitch).[22] These are significantly lower than ScottishPowers credit ratings as discussed below.

MEHC provided an analysis of the ratings by stating S&P placed MEHC's corporate rating and senior unsecured debt rating of BBB- on CreditWatch Positive; Moody's noted its senior unsecured debt rating of Baa3, a positive rating outlook; and, Fitch affirmed its senior unsecured debt rating at BBB, with a stable outlook.[23]

With regard to PacifiCorp's credit rating, immediately after the acquisition was announced, S&P placed PacifiCorp's secured debt on CreditWatch with negative implications, explaining its current rating for PacifiCorp reflects ScottishPower's consolidated credit profile and that the "negative implications"

[20] Revised page to Abel Exh. PPL/101, p. 2

[21] A.05-07-010, p. 16.

[22] Table 2, Crediting Ratings – July 2005, Direct Testimony of Patrick J. Goodman, Revised 8/25/05, PPL/400, Goodman/7.

[23] A. 05-07-010, pp. 16-17.

observation is based on PacifiCorp's "weaker stand-alone metrics." S&P states it will assess other factors as the transaction proceeds.[24]

Moody affirmed its rating of PacifiCorp's senior secured debt as A3 and senior unsecured debt as Baa1. It changed its ratings outlook from stable to developing. Moody did state it believed the acquisition would have positive long-term benefits, particularly on large capital expenditure over the next several years and that its "developing" rating outlook reflected short-term regulatory challenges faced by PacifiCorp as it litigates pending rate cases and seeks regulatory approval of the acquisition.[25]

Fitch declared PacifiCorp's debt rating of senior secured "A"; senior unsecured "A-", was stable. It also noted that MEHC has the financial capability to provide equity financing for PacifiCorp's ongoing capital expenditure program.[26]

ScottishPower's 2004-2005 Annual Report identified its S&P credit ratings as BBB+, Moody's Baa1, and Fitch BBB+. The Annual Report also stated that ScottishPower's U.K. (long-term) credit rating for S&P to be A-, Moody's A3, and Fitch A.

The basis for MEHC's claim that its subsidiaries obtain less expensive credit is a three-page report, based on market data independently obtained from JP Morgan and ABN AMRO. The report compares the September 2004 debt issuance of MidAmerican Energy Company to debt issuances[27] of eight other utilities, including PacifiCorp, between February 2003 and September 2004 and

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[24] A. 05-07-010, p. 17.
[25] A. 05-07-010, p. 17.
[26] A. 05-07-010, p. 17.
[27] MidAmerican Energy issued Notes. The other debt issuances included Notes, First Mortgage Bonds, Senior Notes, and Secured.

concludes that MEHC's cost of debt was 10 basis points lower.[28] MEHC needs far more support to prove its claim that Berkshire Hathaway subsidiaries enjoy lower credit costs than a single affiliated debt issuance compared to a small sample of companies' debt issuances spanning 18 months and including four different types of debt.

MEHC provided information about one debt issuance over a year ago of a single Berkshire Hathaway subsidiary. ORA requested a list of all debt issuances from Berkshire Hathaway associated businesses by company for the last five years, but MEHC indicated that it "is not in possession of any of the data requested."[29]

ORA was therefore unable to substantiate MEHC's claim that its subsidiaries were able to garner lower debt costs because of their affiliation with Berkshire Hathaway. The strongest evidence before the Commission shows that PacifiCorp's association with MEHC will raise its debt costs (S&P's CreditWatch negative)[30] since MEHC's debt rating (BBB-)[31] is lower than ScottishPower's debt rating (A-).[32] MEHC's offer that for the five year period subsequent to the approval of the proposed acquisition PacifiCorp will accept up to a ten basis point reduction for any revenue requirement calculation, if its incremental long-term debt issuances are not ten basis points lower than that of similarly rated peers will be difficult, if not impossible, to enforce.

B) Corporate Overhead Charges

MEHC commits that the corporate charges to PacifiCorp from MEHC and MEC will not exceed $9 million annually for a period of five years after the

[28] MEHC's response to ORA 3rd Data Request 3.1.1.
[29] MEHC's response to ORA 3rd Data Request 3.1.3.
[30] A. 05-07-010, p. 17.
[31] A. 05-07-010, p. 16.
[32] A. 05-07-010, p. 17.

closing on the proposed transaction.[33] This results in a savings of $6 million per year on a total company basis if the holding company provides the same services as PacifiCorp Holding Inc. However, it is MEHC's plan to change the mix of services. This change in mix will cause the shifting of costs from MEHC to PacifiCorp such that the change in the holding company cost alone will not provide an accurate indication of the costs/savings caused by the new owner. An example of some of the services that may be reassigned to PacifiCorp could be Strategic Planning and Environmental services.[34]

C) Most Favored Nation Treatment

Applicants have stated that they would include "Most Favored Nation" treatment for agreements reached with other jurisdictions. With the exception of commitments that are clearly state specific, MEHC has stated that it intends to apply each commitment made in any of the state jurisdictions to all six states.[35]

D) Traditional Holding Company Efficiencies

When businesses merge or are acquired synergies may be acquired by performing the same functions more efficiently. These efficiencies (synergies) are obtained by allocating the fixed costs of an operation over a larger base while maintaining marginal costs. Some areas where typical synergies occur for like companies include consolidation and removal of duplicate facilities pertaining to:

- Accounting services;
- Administrative costs and services;
- Advertising costs;

[33] Revised page to Abel Exh. PPL/101, p. 2

[34] Strategic Planning and Environmental services were identified as services provided by ScottishPower (PacifiCorp's response to ORA 3rd Data Request 3.11.2) which were not identified as services MEHC will provide to PacifiCorp (MEHC's response to ORA 3rd Data Request 3.11.1.

[35] MEHC's and PacifiCorp's response to ORA 2nd set of data requests, question 2.1.

- Billing services;
- Financing services;
- Human resource costs and services;
- Legal costs and services;
- Medical costs and services;
- Purchasing functions;
- Regulatory functions, costs, and services;
- Research; and,
- Strategic Planning services;

MEHC has not provide any documents that support the existence of any synergies, efficiencies, or cost savings other than the decrease in debt cost and minor corporate service costs. When asked to identify whether MEHC has evaluated these items for synergies and cost savings MEHC stated that it "has not performed a study of potential savings from the transaction.[36] With a proposed purchase price in excess of book value, and only minor savings identified by MEHC, ORA concludes that there must be synergies, efficiencies, and cost savings that MEHC will pursue that it is not identifying to justify the acquisition cost paid by MEHC. Without additional synergies this acquisition must be denied because the application has failed to show net economic benefits associated with the acquisition. However, these potential synergies can be recognized by delaying PacifiCorp's next general rate increase proceeding one year. This would also ensure some credible and definitive economic benefits are realized by ratepayers through this transaction.

[36] MEHC's response to ORA 3rd Data Request 3.12.

E) Delay in PacifiCorp's next GRC

PacifiCorp is currently in the process of preparing a Test Year 2007 general rate case. The rate case will not incorporate any of the future costs/savings of the new owner. California uses a forward looking test year and calculates the rates based upon a utility's estimated future operation. It is ORA's expectation that PacifiCorp will be proposing a rate increase in its GRC application.

ORA is concerned that MEHC may recognize consolidation savings during the next several years (benefits that they will not be identified in its application), while demonstrating only diminutive benefits (which will be offset by sizable capital costs in the future because of the expected future capital additions.) ORA's experience is that merged companies have substantial savings after merging.

In the SDG&E/SoCalGas merger the Commission found that the five year savings from the merger to be $288 million which were to be distributed to ratepayers and shareholders, 50/50, over a five year period.[37] Additionally, in the sixth year, all such merger benefits were allocated to ratepayers.[38]

The most recent energy acquisition involved the acquisition of Avista Corporation's (Avista) South Lake Tahoe district by Southwest Gas Corporation (Southwest). On July 21, 2004, Southwest and Avista entered into a purchase and sale agreement, subject to regulatory approval, by which Southwest would acquire Avista's South Lake Tahoe natural gas assets for approximately $15 million. On September 3, 2004, Avista and Southwest filed a Joint Application[39] requesting Commission authorization for the transaction. Among other things, Southwest proposed that it not be foreclosed from seeking in a future rate case the opportunity to recover the acquisition premium related to the transaction. A settlement was negotiated in the case between ORA, Avista, and Southwest.

[37] D. 98-03-073, p. 2, Summary.
[38] D. 98-03-073, Finding of Fact 8.
[39] A. 04-09-009

Among other things, the settlement provided that: 1) the base margin rates for the South Lake Tahoe district being purchased by Southwest would remain unchanged for the years 2005, 2006, 2007, and 2008 and 2) Southwest will not seek Commission authority to recover the acquisition premium associated with the transaction in that case or in any future regulatory proceeding. On March 17, 2005, the Commission approved the settlement and granted authority for the proposed transaction.[40] In that decision, the Commission concluded that P.U. Code Sections 851 and 854 governed the transaction.

In light of the decision in the Southwest acquisition case in which base margin rates were frozen for a four-year period, ORA has offered an extremely reasonable and modest proposal of a one-year rate deferral for the Northern California service territory of PacifiCorp in this case.

5. COMPANY SAFEGUARDS

A) MEHC's and PacifiCorp's Proposed Regulatory Safeguards

Applicants' application contains a copy of the regulatory safeguards proposed by Applicants in this proceeding.[41] All but two of these safeguards are designed to keep California ratepayers neutral to the proposed transaction. The two safeguards that provide minimal benefit are offset over 35-fold by new planned costs that are not currently required by any federal or state regulatory agency or law.

B) ORA's Additional Proposed Safeguards

ORA's additional safeguards were developed mindful that California is only two percent of PacifiCorp's operation.

[40] D. 05-03-010

[41] A. 05-07-010, Appendix 7.

1) Acquisition Premium

In MEHC's and PacifiCorp's proposed safeguards, the Applicants threaten to propose recovery of the acquisition premium in PacifiCorp's regulated retail rates *if* the Commission in a rate order issued subsequent to the closing of the transaction reduces PacifiCorp's retailed revenue requirement through the imputation of benefits other than those benefits committed to in this transaction[42]

This proposal of Applicants is not a safeguard but an inappropriate attempt by Applicants to force ratepayers to compensate shareholders for its acquisition premium costs should the Commission recognize the acquisition's expected benefits. This is contrary to the Commission's long standing policies.

> "It has been the policy of this Commission, for accounting and rate making purposes, to recognize the original cost of operating systems acquired by purchase and to disregard the purchase price paid by the transferees. Under such policy the consumers' rates reflect those costs associated with the actual cost of constructing the facilities devoted to their use and will not be subject to variations which might otherwise result in the event the purchase price, whether less than or in excess of the actual installed cost, were to be recognized in rate making purposes."[43]

A more recent decision, involving a different utility, amplified and clarified this statement of policy:

> "If a regulated utility purchasing dedicated property were allowed to pass on to its customers a price higher than original cost, the parties to the transaction would be in a position to frustrate the application of the original cost standard by arranging a transfer of ownership at a premium. The seller would receive, at the expense of future ratepayers, more than his original cost and yet the willingness of the purchaser to pay such a premium would have little significance since he himself would not bear the burden. On the other hand, the willingness of a seller to accept a price below the depreciated original cost can be persuasive evidence that the property has suffered deterioration in value and is no longer worth depreciated original

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[42] Revised pages to Gale Exh. PPL/301, pg. 3, Financial Integrity item C.

[43] D. 69490, quoting D. 63581. The Supreme Court of California denied a writ of review of D. 63581.

cost. The Commission may consider such evidence in establishing a rate base for ratemaking purposes."[44]

If the Commission ever allowed a utility to recover an acquisition adjustment in rates it would force the ratepayers to assume shareholder cost and risks, and force ratepayers to pay a premium that has no relation to the original cost of the system. Acquisition premiums are made by shareholders after they have evaluated the risk of acquiring the utility, and should never be charged to utility ratepayers. Furthermore, in this specific case, Applicants have failed to even request that the Commission even consider the reasonableness of the premium.

- Ratepayers should never be required to finance MEHC's acquisition premium. To do otherwise would make this transaction unbeneficial to ratepayers. The Commission should not approve the transaction unless Applicants agree that under no circumstances will ratepayers be forced to bear the cost of the acquisition premium.

2) Compliance with California's Decisions, Rules, and Laws

Article 12 of the California Constitution created the California Public Utilities Commission, subject to the control of the legislature, to fix rates and rules for public utilities operating inside the state of California. The Commission is governed by the California Constitution and the P.U. Code. Utilities are required to comply with the California P.U. Code, the Commission's General Orders, Rules of Practice and Procedures, and the Commission's resolutions and decisions that impact each utility. Upon completion PacifiCorp, the businesses that own it, and its affiliates need to be governed by California's Laws, Rules, and Decisions.

- Upon completion of the transaction, PacifiCorp, its owners, and its affiliates will be governed by the California P.U. Code, the

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[44] D. 69490, citing D. 68841 (April 6, 1965.)

Commission's General Orders, Rules of Practice and Procedures, and all decisions and resolutions that PacifiCorp is currently required to follow.

3) Reporting Requirements

As stated earlier, California is only 2% of PacifiCorp's operation. However, the Commission and ORA have a long history of monitoring the impacts of acquisitions to ensure that ratepayers are not negatively impacted by the owner. ORA is not proposing additional reporting requirements specifically for California but recommends the following:

- PacifiCorp and its new owners provide the Commission with the same operating and affiliate transaction reports that it will provide to the other states in which it operates.

6. SYSTEM RELIABILITY

MEHC and PacifiCorp affirmed that it would continue to provide existing customer service guarantees and performance standards in each jurisdiction through 2009.[45]

Further, MEHC and PacifiCorp agreed that penalties for noncompliance with performance standards and customer guarantees shall be paid as designated by the Commission and shall be excluded from results of operations. PacifiCorp will abide by the Commission's decision regarding payments.[46]

MEHC and PacifiCorp further commit to extend through 2011, the commitment in Exhibit PPL/301 regarding customer service guarantees and performance standards as established in each jurisdiction, a two-year extension.[47] ORA is not opposed to this proposal.

[45] A. 05-07-010, Appendix 7, Customer Service, item A, p. 6.
[46] A. 05-07-010, Appendix 7, Customer Service, item B, p. 6.
[47] A. 05-07-010, Appendix 7, Customer Service Standards, p. 5.