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BEFORE THE WASHINGTON

UTILITIES AND TRANSPORTATION COMMISSION

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WASHINGTON UTILITIES AND)
TRANSPORTATION COMMISSION,)Docket UE-050684
Complainant,)Volume XIII
vs.)Pages 1613-1735
PACIFICORP d/b/a PACIFIC POWER &)
LIGHT COMPANY,)
Respondent.)
<hr/>	
In the Matter of)Docket UE-050412
PACIFIC POWER & LIGHT) (Consolidated)
Petition for an order approving)
deferral of costs relating to)
declining hydro generation.)
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A hearing in the above-entitled matter was held at 9:09 a.m. on Friday, February 3, 2006, at 1300 South Evergreen Park Drive, S.W., Olympia, Washington, before Administrative Law Judges ANN RENDAHL, Chairman MARK SIDRAN, Commissioner PATRICK OSHIE and Commissioner PHILIP JONES.

The parties present were as follows:

PACIFICORP, by Marcus Wood, Attorney at Law, Stoel Rives, LLP, 900 S.W. Fifth Avenue, Portland, Oregon 97229, and Jason B. Keyes, Attorney at Law, Stoel Rives, 600 University Street, Suite 3600, Seattle, Washington 98101.
Barbara L. Nelson, CCR
Court Reporter

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1 PUBLIC COUNSEL, by Simon ffitch,
Assistant Attorney General, 900 Fourth Avenue, Suite
2 2000, Seattle, Washington 98164.

3 COMMISSION STAFF, by Donald T. Trotter
and Robert Cedarbaum, Assistant Attorneys General,
4 1400 S.W. Evergreen Park Drive, S.W., P.O. Box 40128,
Olympia, Washington 98504-0128.

5 INDUSTRIAL CUSTOMERS OF NORTHWEST
6 UTILITIES, by Melinda Davison, Attorney at Law, 333
S.W. Taylor, Portland, Oregon 97204.

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1 JUDGE RENDAHL: Let's go on the record.
2 We're back on the record on the morning of Friday,
3 February 3rd, for our last day of hearing in this
4 proceeding in Docket Number UE-050684 and UE-050412.
5 And we're going to begin this morning with the
6 cross-examination of Mr. Vander Weide, and I hope I
7 have pronounced that correctly.

8 MR. VANDER WEIDE: You have.

9 JUDGE RENDAHL: Good. Mr. Vander Weide,
10 you're welcome to come up here to the witness stand.
11 Whereupon,

12 JAMES H. VANDER WEIDE,
13 having been first duly sworn, was called as a witness
14 herein and was examined and testified as follows:

15 JUDGE RENDAHL: Okay, thanks. Please be
16 seated. And just a tip on the microphone. When the
17 button is up, the microphone is on, and you need to
18 speak close to it, as I am, so that it projects, so
19 -- thank you. Mr. Wood.

20 MR. WOOD: Thank you.

21

22 D I R E C T E X A M I N A T I O N

23 BY MR. WOOD:

24 Q. Dr. Vander Weide, I want to identify your
25 pre-filed exhibits. 811-T is your pre-filed direct

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1 supplemental testimony; Exhibit 812 is your Exhibit
2 JHV-2, qualifications; Exhibit 813 is your Exhibit
3 JHV-3, capital structure pre and post-acquisition;
4 and Exhibit 814 is your Exhibit JHV-4, hypothetical
5 revenue requirement calculation, stand-alone
6 subsidiary versus double leverage subsidiary.

7 Were the documents I've identified prepared
8 by you or under your supervision and direction?

9 A. Yes, they were.

10 Q. Do you have any changes to make to any of
11 these documents?

12 A. No, I do not.

13 Q. Are the testimony and exhibits true and
14 correct, to the best of your knowledge?

15 A. Yes, they are.

16 MR. WOOD: Your Honor, I would offer these
17 pre-filed exhibits at this time.

18 JUDGE RENDAHL: Thank you. Are there any
19 objections to admitting what's been marked as
20 Exhibits 811-T through 814? Hearing nothing -- Mr.
21 ffitich, I'm sorry, are there any objections? I don't
22 want to overlook -- any objections to admitting 811-T
23 through 814?

24 MR. FFITCH: No, Your Honor. Thank you.

25 JUDGE RENDAHL: Okay. With that, those

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1 exhibits will be admitted. Mr. Wood.

2 MR. WOOD: Yes, I have a couple of
3 additional -- actually, one additional question for
4 Mr. Hill -- I mean, for Dr. Vander Weide.

5 Q. Dr. Vander Weide, Mr. Hill introduced in his
6 supplemental testimony two proposed means of
7 calculating the cost of equity for a parent company
8 and a double leveraged calculation. Are the numbers
9 arising from the two new calculations accurate and
10 reliable?

11 A. No. Mr. Hill's method for calculating the
12 parent's cost of equity, shown on page 14 of his
13 supplemental testimony, gets a low cost of equity
14 because Mr. Hill has misstated a well-documented
15 finance equation. Mr. Hill proposes using an
16 equation which is very similar to the one I presented
17 in my testimony. However, Mr. Hill incorrectly
18 writes the equation as $K_e = K_u + (K_u - I)(1 - T)B/S$.

19 The error in Mr. Hill's equation is that Mr.
20 Hill has incorrectly multiplied the entire term $K_u - I$
21 by the term $1 - T$, whereas only the interest component,
22 I , should be multiplied by the term $1 - T$. Because it
23 is only interest, not K_u , the unlevered firm's cost
24 of equity, that is tax deductible.

25 The correct equation is

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1 $K_e = K_u + (K_u - I(1-T))B/S$. If Mr. Hill had used the
2 correct equation to estimate the adjusted cost of
3 equity for the parent, he would have found that the
4 parent's cost of equity should be 14.02 percent when
5 the subsidiary's cost of equity is 9.125 percent, as
6 used in his example. If the subsidiary's cost of
7 equity were 11 percent, then the correct adjustment
8 process for the parent would produce a cost of equity
9 for the parent equal to 17.65 percent.

10 In addition, Mr. Hill's application of the
11 CAPM, or Capital Asset Pricing Model, and his process
12 for adjusting the beta component of the CAPM is
13 inconsistent with his own testimony in this
14 proceeding that, quote, There are three fundamental
15 problems with the key CAPM risk measure beta that
16 indicate that the CAPM analysis is not a reliable
17 primary indicator of equity capital costs.

18 Furthermore, Mr. Hill inconsistently mixes
19 up book value capital structures and market value
20 capital structures. In his calculation of the
21 weighted average cost of capital for the utility
22 subsidiary, Mr. Hill defines leverage using the book
23 value of equity. On the other hand, when he
24 calculates the adjusted cost of equity for the
25 parent, Mr. Hill defines leverage using the market

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1 value of equity. Market values of equity should be
2 used both for calculating the utility's weighted
3 average cost of capital and for calculating the cost
4 of equity.

5 However, because Mr. Hill has used the book
6 value of equity to calculate the subsidiary's
7 weighted average cost of capital and for defining
8 whether double leverage exists, consistency requires
9 that he also use the book value of equity to
10 calculate the cost of equity for the parent.

11 The effect of Mr. Hill's inconsistent
12 calculations causes him to significantly understate
13 the required rate of return on equity for the parent.

14 Q. Does this conclude your additional oral
15 testimony?

16 A. Yes, it does.

17 MR. WOOD: Dr. Vander Weide is available for
18 cross-examination, Your Honor.

19 JUDGE RENDAHL: Thank you, Mr. Wood. Mr.
20 Cedarbaum.

21 MR. CEDARBAUM: Thank you, Your Honor.

22

23 C R O S S - E X A M I N A T I O N

24 BY MR. CEDARBAUM:

25 Q. Good morning. My name is Robert Cedarbaum,

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1 I'm one of the Staff attorneys on this case.

2 A. Good morning, Mr. Cedarbaum.

3 Q. Good morning. I guess I should ask you, do
4 you prefer Dr. Vander Weide or Mr. Vander Weide?

5 A. Either one is fine with me.

6 Q. I'd like to start off by asking you to look
7 at what's been marked for identification as Exhibit
8 815. Counsel has provided that.

9 A. Yes.

10 Q. You have that. And looking at the exhibit,
11 Staff Data Request 384 asked you to provide all work
12 papers, studies, analyses that support the
13 calculations that appeared in your -- appearing in
14 your Exhibit JHV-4, which is Exhibit 814; is that
15 correct?

16 A. Yes.

17 Q. And the attachment to the second page of the
18 exhibit is your response to that Staff data request?

19 A. That's correct.

20 MR. CEDARBAUM: Your Honor, I would offer
21 Exhibit 815.

22 MR. WOOD: No objection.

23 JUDGE RENDAHL: With that, are there any
24 objections to this exhibit? Hearing none, then the
25 exhibit will be admitted.

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1 Q. Dr. Vander Weide, is it correct that you've
2 testified on the subject of double leverage in other
3 jurisdictions?

4 A. Yes, it is.

5 Q. And those other jurisdictions would include
6 two cases decided in 2003 by the Iowa Utilities
7 Board?

8 A. Yes.

9 Q. And those two cases involved rate filings by
10 the Interstate Power and Light Company; is that
11 correct?

12 A. Yes.

13 Q. And IPL, or Interstate Power and Light
14 Company, is a subsidiary of a holding company called
15 Alliant Energy; is that right?

16 A. Yes.

17 Q. Is it also correct that, in those two cases,
18 you testified on behalf of MidAmerican Energy
19 Company?

20 A. Yes, it is.

21 Q. MidAmerican Energy Company is one of the
22 utility subsidiaries of MidAmerican Energy Holdings
23 Company?

24 A. That's correct.

25 Q. And MidAmerican Energy Holding Company is

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1 the same company seeking to acquire PacifiCorp in
2 this jurisdiction; is that right?

3 A. Yes.

4 Q. Would you accept, subject to your check,
5 that one of those Iowa cases had Consolidated Docket
6 Numbers of RPU-02-3, RPU-02-8, and ARU-02-1?

7 A. Yes, I would.

8 Q. And would you also accept, subject to your
9 check, that the docket number in the other Iowa case
10 was RPU-02-7?

11 A. Yes.

12 Q. Is it correct that in those two Iowa cases,
13 you opposed a double leverage adjustment to determine
14 the cost of capital for IPL because you believed the
15 adjustment violates the financial principles set in
16 the Hope Natural Gas case?

17 A. Yes, it is.

18 Q. And is it also correct that the Iowa
19 Utilities Board accepted a double leverage adjustment
20 despite your argument?

21 A. It's correct that they accepted it as
22 applied to IPL, because they had a condition with
23 regard to accepting double leverage that the parent
24 must have invested equity capital, have made equity
25 infusions into the subsidiary. That condition

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1 applied to IPL, but it does not apply to MEHC, and so
2 that -- according to the Iowa Commission's own
3 conditions, it shouldn't be applied in this
4 proceeding.

5 MR. CEDARBAUM: If I could just have a
6 minute, Your Honor.

7 JUDGE RENDAHL: Sure.

8 MR. WOOD: Your Honor, someone listening in
9 indicated that Dr. Vander Weide's microphone is not
10 on, so they can't hear him. It's in the up position,
11 Doctor. That's it.

12 THE WITNESS: Okay. I'm sorry.

13 JUDGE RENDAHL: Your voice must carry well
14 enough in the room. We can hear you.

15 THE WITNESS: That's what my students
16 usually say.

17 Q. Let me ask you if you would accept, subject
18 to check, that in the RPU-02-7 case, that the Iowa
19 Utilities Board decision, which was issued on May
20 15th, 2003, stated in part as follows: The Board
21 adopted the use of double leverage in the electric
22 rate proceeding to account for the parent's
23 accessibility to lower cost debt to purchase equity
24 in a subsidiary upon which it may earn a higher rate
25 of return than it pays for the debt. Would you

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1 accept that, subject to your check?

2 MR. WOOD: Your Honor, if the witness is
3 going to be asked specific questions about language
4 in the order, I would request that he be given a copy
5 of the order so he could see that language.

6 MR. CEDARBAUM: Sure. It's my only copy,
7 though, so --

8 JUDGE RENDAHL: Let's be off the record for
9 a moment.

10 (Recess taken.)

11 JUDGE RENDAHL: Let's be back on the record.

12 Mr. Cedarbaum.

13 MR. CEDARBAUM: Thank you, Your Honor.

14 Q. Dr. Vander Weide, I've provided you a copy
15 of the Iowa Commission's decision in RPU-02-07, dated
16 May 15th, 2003. Do you have that?

17 A. Yes, I do. And I would -- just to --

18 Q. I'm sorry, if I could -- I just asked you if
19 you had a copy of it.

20 A. Yes, I do.

21 Q. And just for clarity purposes, the decision
22 that we're looking at is -- IPL is a combination
23 utility, electric and gas?

24 A. Yes.

25 Q. And the decision we're looking at was a gas

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1 rate filing and the other decision I asked you about
2 with the consolidated docket numbers was the electric
3 side?

4 A. Yes.

5 Q. Okay. So now, looking at the gas decision
6 that I provided you with in RPU-02-7, the language
7 that I quoted to you is on page 239; is that right?

8 A. I'm not sure. Would you quote it again,
9 please?

10 Q. On page 239, in the column furthest to the
11 right, I had quoted you language at the top that
12 says, The board adopted the use of double leverage in
13 the electric rate proceeding, referring to the
14 electric case, to account for the parent's
15 accessibility to lower cost debt to purchase equity
16 in its subsidiary upon which it may earn a higher
17 rate of return than it pays for the debt.

18 Then, to continue, The Board found that the
19 use of double leverage recognizes the true capital
20 structure at the subsidiary level and prevents the
21 parent company stockholders from earning a windfall
22 from regulated rates. In the electric rate
23 proceeding, the Board was not persuaded to disavow
24 the application of double leverage in all instances.
25 Do you see that language?

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1 A. Yes, I do.

2 MR. CEDARBAUM: Thank you. Those are all my
3 questions.

4 JUDGE RENDAHL: Thank you. Mr. ffitch.

5 MR. FFITCH: Thank you, Your Honor.

6

7 C R O S S - E X A M I N A T I O N

8 BY MR. FFITCH:

9 Q. Good morning, Dr. Vander Weide.

10 A. Good morning.

11 Q. Hope I don't massacre the pronunciation too
12 much. I'm Simon ffitch, from the Office of Public
13 Counsel. I just have a few questions this morning.

14 Would you please turn to your supplemental
15 testimony, which is Exhibit 811-T, go to page eight?

16 A. Yes.

17 Q. And please go to line five. And there you
18 give an example of double leverage -- starting there
19 you give an example of double leverage with two
20 companies, Company A and Company B, with identical
21 capital structures; correct?

22 A. That's correct.

23 Q. And they both have 50 percent equity and 50
24 percent debt; right?

25 A. Yes.

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1 Q. Are those book value capital structures?

2 A. Yes, they are.

3 Q. Isn't it true that standard regulatory
4 practice with electric utilities is to use book value
5 capital structures for rate-setting purposes?

6 A. Yes, it is, and that's why I suggest that
7 when one is going to use the parent's -- make an
8 adjustment to the parent's cost of equity using a
9 capital structure, one ought to also use a book value
10 capital structure there to be consistent.

11 Q. Okay. Now, PacifiCorp has filed its rate
12 request based on its book value capital structure in
13 this case, haven't they?

14 A. Yes.

15 Q. The company wasn't wrong to do that, were
16 they?

17 A. No.

18 Q. And the discussion regarding double leverage
19 in this proceeding has been predicated on book value
20 capital structures, hasn't it?

21 A. The discussion discussing whether double
22 leverage exists has been predicated on book value
23 capital structures.

24 Q. All right.

25 A. The discussion regarding a cost of equity

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1 adjustment to the parents has, at least in Mr. Hill's
2 testimony, was based on a market value capital
3 structure.

4 Q. All right. You've been testifying on the
5 subject of utility finance and cost of capital since
6 1975; correct?

7 A. Yes.

8 Q. And we can see that if we look at your
9 Exhibit 812, pages eight through 15; correct?

10 A. Correct.

11 Q. And that shows all the proceedings where
12 you've testified over the last 29 years; is that
13 right?

14 A. Yes.

15 Q. And in that period, from 1975 to 2004, when
16 testifying for electric utilities, you recommended
17 the use of book value capital structures in setting
18 rates; correct?

19 A. I usually did not recommend a capital
20 structure. Generally, my testimony regarded the cost
21 of equity and the company presented the capital
22 structure. I recognize that there was a fundamental
23 inconsistency between the way leverage is defined in
24 economics and finance, which uses market value
25 capital structures to define leverage, and the way it

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1 has been defined in regulatory practice, which has
2 relied on book values.

3 I believe that one ought to use market
4 values both for the regulatory practice and for the
5 cost of equity, but at the very least, one shouldn't
6 be inconsistent and apply book value capital
7 structures for estimating the weighted average cost
8 of capital and then use a market value capital
9 structure to estimate the adjustment in booked debt.

10 In both of those instances, the use of the
11 book value produces a lower number in the case of the
12 average weighted cost of capital and the use of a
13 market value produces a lower number in the case of
14 the adjustment. So that inconsistency undoubtedly
15 produces a bias downward in the estimate of the cost
16 of capital.

17 Q. Well, let's go back to my original question,
18 Dr. Vander Weide, and that is that during a period
19 from 1975 up through 2004, your cost of capital and
20 capital structure testimony relied on the use of book
21 value capital structures, didn't it, until 2004?

22 A. I'm not entirely sure what you mean by the
23 word relies. I've just testified, I normally did not
24 recommend a capital structure; I recommended a cost
25 of equity.

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1 Q. All right. When -- were the capital
2 structures that were used in those cases based on
3 book value?

4 A. Yes.

5 Q. When utility stock market prices are above
6 book value, like they are now, all else equal, the
7 cost of market value capital structures, rather than
8 book value capital structures, will result in higher
9 overall return recommendations, won't it?

10 A. If one were dealing only with a stand-alone
11 utility in calculating a weighted average cost of
12 capital, a market value capital structure would
13 produce a higher number.

14 Q. All right.

15 A. If, however, one is also, for the regulatory
16 process, attempting to adjust the parent's cost of
17 equity for the purpose of doing a double leverage
18 calculation and one would, inconsistent with the
19 regulatory practice, use a market value capital
20 structure in that calculation, one would get a lower
21 cost of equity and hence a lower weighted average
22 cost of capital for the utility.

23 Q. Okay. But I didn't ask you about your
24 double leverage theory or testimony in this case. I
25 understand you have a theory that you're propounding

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1 in this case.

2 What I asked you was, as a matter of
3 rate-making practice and theory, when utility stock
4 market prices are above book value, like they are
5 now, all else being equal, the use of market value
6 capital structures, rather than book value capital
7 structures, will result in higher overall return
8 recommendations; isn't that correct?

9 A. Again, I don't understand the question. Are
10 you addressing the question only to a stand-alone
11 utility that has no parent with leverage?

12 Q. That's correct. I'm not asking you to
13 repeat your theory of double leverage in this case.
14 I'm asking you a question about a stand-alone
15 utility.

16 A. For a stand-alone utility, that's correct,
17 it would.

18 Q. Okay. Now, let's turn to your third
19 exhibit, Exhibit 813. That's your JHV-3. Do you
20 have that?

21 A. I do. There it is. I got it.

22 Q. There you show PacifiCorp's requested
23 capital structure, the bottom portion of the page, of
24 49.4 percent equity, 1.1 percent preferred stock and
25 49.5 percent debt; correct?

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1 A. Yes.

2 Q. All right. Is that a projected capital
3 structure or a current actual capital structure?

4 A. I don't know the answer to that question,
5 since I wasn't the one that prepared a requested
6 capital structure.

7 Q. Okay. It is a book value capital structure;
8 isn't that correct?

9 A. Again, I didn't prepare it, so I don't know
10 what is behind that number.

11 Q. All right. And do you know the current
12 consolidated book value capital structure of MEHC,
13 Dr. Vander Weide?

14 MR. WOOD: Clarification. Is he asking does
15 he know what it is literally today, or does he know
16 what it has been in recent times?

17 JUDGE RENDAHL: Mr. ffitch.

18 MR. FFITCH: That will be an acceptable
19 answer.

20 JUDGE RENDAHL: The latter?

21 MR. FFITCH: The latter.

22 THE WITNESS: I don't have a copy of their
23 book value capital structure in front of me. If you
24 would like to hand me a copy, I'd be happy to discuss
25 it.

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1 Q. Would you accept, subject to check, that
2 it's approximately 20 percent common and 80 percent
3 debt, 20 percent common equity and 80 percent debt?

4 A. This is as of what date?

5 Q. Recent -- recent evidence that's in the
6 record in the proceeding.

7 A. I don't know how I could accept it without
8 seeing what is in it.

9 JUDGE RENDAHL: Mr. ffitch, if it's based on
10 evidence, is there an exhibit number we can refer to
11 or --

12 MR. FFITCH: Yes, it is, but -- it's in the
13 record. We don't really need to pursue this. If he
14 doesn't know, he doesn't know.

15 JUDGE RENDAHL: All right. Okay.

16 MR. FFITCH: Those are all the questions I
17 have, Your Honor. Thank you, Dr. Vander Weide.

18 JUDGE RENDAHL: All right.

19 MR. FFITCH: I'd like to offer Public
20 Counsel Cross Exhibits 816 and 817 at this time.

21 JUDGE RENDAHL: Are there any objections?

22 MR. WOOD: No objection, Your Honor.

23 JUDGE RENDAHL: With that, Exhibits 816 and
24 817 will be admitted. Ms. Davison, do you have
25 anything for this witness?

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1 MS. DAVISON: No, Your Honor.

2 JUDGE RENDAHL: All right. Are there any
3 questions for Dr. Vander Weide from the Bench? I'm
4 sorry. Is there any redirect, Mr. Wood?

5 MR. WOOD: Yes, there is, Your Honor.

6

7 R E D I R E C T E X A M I N A T I O N

8 BY MR. WOOD:

9 Q. Dr. Vander Weide, Mr. Cedarbaum read to you
10 language from the decision of the Iowa Utilities
11 Board in re: Interstate Power and Light Company,
12 Docket RPU-02-7, and he stopped his question after
13 asking you, I believe, about one paragraph.

14 I believe you, in your introductory
15 comments, stated that the Iowa cases would not
16 justify double leverage here. Is there anything in
17 the very order he cited you that so states?

18 A. Yes, there is. And just for clarification,
19 I would point out that I did not testify in this
20 proceeding, although I did testify in the RPU-02-3
21 and RPU-02-8. But on page 240, there's a paragraph
22 that begins, The evidence in this proceeding supports
23 the same findings on this issue as were made in the
24 electric rate proceeding. The Board based its
25 decision on the failure of IPL to meet all four of

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1 the factors for disproving the reasonableness of
2 double leverage established in Iowa Electric Light
3 and Power Company Docket Numbers RPU-89-3 and
4 RPU-89-9. The Board found that IPL failed to satisfy
5 the fourth criteria, that the only increase to common
6 equity since inception had been through an increase
7 in the Utility's retained earnings. AEC has infused
8 capital into IPL since the merger, and this activity
9 at the parent level supports the utility's capital
10 structure.

11 So that paragraph supports precisely the
12 statement that I made earlier that, in this case,
13 since there has not been an equity infusion into the
14 subsidiary, this order does not support the use of
15 double leverage in this particular case that we're in
16 right now.

17 Q. And the electric case that Mr. Cedarbaum
18 cited, does it state the same thing?

19 A. Yes, on page 58 of the order in the electric
20 case, the Board states, The Board found the use of
21 double leverage was not appropriate in calculating
22 the capital structure for Iowa Electric because the
23 facts warranted an exception. Iowa Electric
24 demonstrated that IE Industries' debt does not result
25 in an increase in Iowa Electric's common equity. The

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1 parent's debt was shown by the specific facts not to
2 support the utility's capital structure.

3 MR. WOOD: Thank you. Those are all the
4 questions I have, Your Honor.

5 JUDGE RENDAHL: Anything further for Dr.
6 Vander Weide? Any questions from the Bench? I'm
7 sorry, Mr. Cedarbaum.

8 MR. CEDARBAUM: I'm sorry, I was distracted.
9 Were you asking if I had --

10 JUDGE RENDAHL: Yes, is there anything in
11 response?

12 MR. CEDARBAUM: Yes, if I may have just have
13 one moment.

14 JUDGE RENDAHL: Dr. Vander Weide, do you
15 have a cite, a similar public utilities reports
16 citation to the last case you were just referring to?

17 THE WITNESS: I don't. I don't know if
18 Counsel does.

19 JUDGE RENDAHL: All right. I'll get it from
20 Mr. Cedarbaum later.

21 MR. CEDARBAUM: Your Honor, I can give you
22 the -- you want me to state that on the record now?

23 JUDGE RENDAHL: That would be useful. Thank
24 you.

25 MR. CEDARBAUM: There was actually a final

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1 decision, a decision on rehearing. The first
2 decision in that case is 225 PUR 4th at 165, and the
3 rehearing order is 225 PUR 4th 487.

4 JUDGE RENDAHL: Thank you.

5

6 R E C R O S S - E X A M I N A T I O N

7 BY MR. CEDARBAUM:

8 Q. Dr. Vander Weide, you said that you didn't
9 testify in the gas case, which surprised me, quite
10 frankly, because in Staff Data Requests 379, we asked
11 the company to provide copies of all testimony and
12 exhibits prepared by Dr. Vander Weide in any other
13 proceeding on the issue of double leverage. Please
14 include all Commission orders that resolved the issue
15 of double leverage in those proceedings.

16 And then the answer we got included a CD
17 that had some testimony of yours, which I thought was
18 in RPU-02-07, which was the gas case.

19 A. It was -- at the time I prepared that, it
20 was my recall that I'd been in both cases. This
21 morning, I reviewed that case and, as of this time, I
22 do not believe I was in the first case, although the
23 two cases were very close in time, and so I was
24 thinking about both of the cases at the same time,
25 but I didn't, best of my knowledge, I did not

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1 actually testify in the 07 case.

2 Q. Well, would you accept, subject to your
3 check, that in response to that Staff Data Request
4 379, Staff was provided with direct testimony of Dr.
5 James H. Vander Weide in Docket RPU-02-07? If that's
6 just inaccurate, your counsel will let us know, but
7 that's what we got.

8 A. All right. Well, if I provided it, then I
9 did testify in both cases, if you have the testimony.
10 It's a little difficult to recall at this time.

11 Q. Just a couple of other questions. Are you
12 familiar with the current financing plan for MEHC to
13 acquire PacifiCorp?

14 A. I'm vaguely familiar with it. Not in
15 detail.

16 Q. Do you understand that there's a purchase
17 price for PacifiCorp of \$5.1 billion, or would you
18 accept that, subject to your check?

19 A. Yes.

20 Q. Would you also accept, or do you just know
21 that of that 5.1 billion, \$1.7 billion will come from
22 debt issued by MEHC and \$3.4 billion will come from
23 equity, an equity investment from Berkshire Hathaway?

24 A. I'm not entirely sure. It was my
25 understanding that the final financing had not yet

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1 been decided.

2 Q. I'm just talking about the current plan that
3 we've all been talking about. I understand that that
4 may change, but what we currently know would be
5 accurately stated in my question?

6 A. It's my understanding that that was an
7 initial plan. I don't know whether that still is the
8 plan.

9 MR. CEDARBAUM: Thank you. Those are all my
10 questions.

11 JUDGE RENDAHL: Okay. Thank you, Mr.
12 Cedarbaum. Are there any questions for Dr. Vander
13 Weide? Commissioner Jones.

14

15 E X A M I N A T I O N

16 BY COMMISSIONER JONES:

17 Q. Good morning, Dr. Vander Weide.

18 A. Good morning, Mr. Jones.

19 Q. You have a Dutchname, don't you?

20 A. Yeah, I sure do.

21 Q. What part of Holland do you come from?

22 A. I come -- well, it was my parents who
23 actually came, and my father came from Friesland,
24 which is in the northern part of Holland.

25 Q. Could you turn to pages five through seven

1642

1 of your --

2 A. Yes.

3 Q. -- supplemental testimony? These are your
4 summary of objections to the double leverage
5 approach. I just want to understand very succinctly
6 at a higher level why you say that this violates
7 three fundamental principles of financial economics.
8 Could you just run -- the way I understand those
9 objections is that the expected or required rate of
10 return should be equal to the expected or required
11 rate of return investments of the same risk, it
12 should not get into the issues of the risk of the
13 owner's other business activities at the holding
14 company level --

15 A. Yes.

16 Q. -- and the third point you make is it should
17 not get into the analysis of how the owner, the
18 holding company, finances its equity investment. Is
19 that a fair understanding?

20 A. That's correct. If you'd like me to explain
21 those --

22 Q. Briefly.

23 A. -- briefly, I will.

24 Q. Yeah.

25 A. The first one is, in finance, is frequently

1643

1 called the law of one price. That means if you have
2 two things that are exactly the same, they ought to
3 sell for the same price. And if you have two things
4 in the -- that have the same risk in the capital
5 markets, both business and financial risk, then they
6 ought to have the same required return, that being
7 the price of capital.

8 And as I demonstrate, if you have two
9 utilities, one of which is a stand-alone utility and
10 the other is owned by a parent company that has
11 leverage, the proponents of double leverage would
12 give a different allowed rate of return to two
13 entities that are exactly the same with regard to
14 business risk and financial risk.

15 So if the ownership changed or if there was
16 no parent, the cost of capital would be higher and
17 utility rates would be higher than if there is a
18 parent. That just doesn't make sense in economics or
19 finance, and it would lead to a misallocation of
20 society's resources, because capital would move
21 toward the utility with the higher return, the one
22 that didn't have a parent, it would move away.
23 Capital would move out of the utility that had the
24 lower return for the same level of risk. That's the
25 first principle.

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1 The second principle says that the return on
2 a project shouldn't depend on the risk of the owner's
3 other business activities. In double leverage, what
4 is done is you take the weighted average cost of
5 capital for the parent and you assign it as the cost
6 of equity for the subsidiary, but if the parent has
7 investments in a lot of other subsidiaries, some of
8 which may be riskier than this one, the parent's
9 weighted average cost of capital will reflect the
10 risk of all of its subsidiaries, including the more
11 risky ones.

12 Q. Could I interrupt you for a minute? And as
13 you do this analysis, could you apply it to the case
14 of MEHC, and specifically with -- I'm sure you've
15 looked at the others --

16 A. Yes.

17 Q. -- Kern River, Northern Natural Gas --

18 A. Right.

19 Q. Thank you.

20 A. In the case of MEHC, they have investments
21 in gas pipelines, they have investments in electric
22 plants in England, and they have investments in
23 merchant electric plants, where the electricity's
24 sold in an unregulated environment. So the weighted
25 average cost of capital for MEHC will reflect the

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1 risk of all of its businesses, including Kern River
2 and Northern Natural Gas, including the electric
3 utilities in England, including the risk of the
4 merchant electric plants that are unregulated, and
5 then, as well, MidAmerican Energy, and if it were to
6 be applied to PacifiCorp, it would also reflect the
7 risk of PacifiCorp.

8 So in this case, then, applying double
9 leverage would mean that you're reflecting the risk
10 of each of the other subsidiaries in the weighted
11 average cost of capital of the parent and applying
12 that as the cost of equity for the -- for PacifiCorp,
13 which means that PacifiCorp's cost of equity would
14 depend not only on its own risk, but also the risk of
15 all of the parent's other subsidiaries, including the
16 merchant power plants. Okay.

17 And the third principle is just the simple
18 idea that if I buy an equity investment, if I buy the
19 stock of a company, my required return on that
20 investment, it depends only on the risk of my equity
21 investment. If I decide to buy that on leverage, I
22 decide to borrow in order to buy that stock, the
23 required return for the company doesn't change,
24 because its risk didn't change.

25 So for instance, if I were to buy the stock

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1 in, say, General Electric, and I borrowed the money
2 to do that, bought that stock on margin, General
3 Electric's required return wouldn't change just
4 because I bought its stock on margin. However, my
5 required return would go up considerably if I bought
6 it on margin. In fact, I normally wouldn't do that.

7 But the point is is I would have a higher
8 required return because I had a higher level of risk,
9 but the rate of return on General Electric would not
10 change one iota because of how I financed it. And
11 that would be the same for PacifiCorp. The rate of
12 return of PacifiCorp should depend on the risk of its
13 assets, not how a parent company or an investor in
14 the equity of PacifiCorp financed that investment.

15 Q. Do any of these principles of financial
16 economics -- thank you for that summary. That
17 helped. But we are faced with a somewhat unique
18 situation here, I think, in which the ultimate source
19 of equity to be put at risk is Berkshire Hathaway?

20 A. Yes.

21 Q. Okay. Berkshire Hathaway is a
22 publicly-traded company?

23 A. That's correct.

24 Q. Injecting capital, as we understand, of \$3.7
25 billion of cash equity, 1.7 billion of debt equity to

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1 be issued by MEHC. That's the plan, it's not final
2 yet, but that's what we understand it to be. MEHC is
3 not a publicly-traded company, so we have a situation
4 where we have, if you will, a sole and exclusive
5 owner of the equity capital and we have common
6 equity, at least at the MEHC level, that is not
7 publicly traded. It's not liquid.

8 A. Right.

9 Q. You can't go into the market and establish a
10 market price?

11 A. That's correct.

12 Q. So do these two factors affect these three
13 principles of financial economics at all?

14 A. They don't affect it in any way whatsoever.
15 Whether it's a publicly-traded company or not a
16 publicly-traded company, the principles are still
17 exactly the same.

18 Q. Let's go to page six and seven of your
19 testimony. We get into this issue of the
20 hypothetical that if the Commission were to apply a
21 double leverage approach, on page six, in statement
22 number five of your critique, you say, It would be
23 important for the Commission to recognize that the
24 1.2 billion of the amount financed represents
25 investment that the Commission would not be included

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1 in regulated rates, and then, point number six, you
2 say MEHC has not sought recovery in rates of its
3 acquisition, but has reserved the right to seek
4 recovery if the issuance of any MEHC debt to finance
5 the acquisition premium is improperly used as a
6 justification of reducing the revenue requirement of
7 PacifiCorp.

8 So here you are saying, and I think this
9 reflects the company's position in one of the
10 stipulations in the acquisition, that if double
11 leverage were to be applied, that you would recommend
12 that the Commission consider an approach that would
13 seek some recovery of that acquisition premium; is
14 that correct?

15 A. That's correct. If they cannot recover it
16 in some fashion because they're the ones that
17 accepted the risk of the investment, they wouldn't
18 continue to make -- they wouldn't continue to invest
19 in the utility if they can't recover the cost of
20 their investment. Now, the nice thing about the way
21 they've done it, by ring fencing the utility and by
22 not putting in rate base, is that the ratepayers
23 don't really pay anything for that premium. The only
24 way ratepayers can pay for the premium is if the
25 premium is included in rate base, because then rates

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1 would go up with a higher rate base.

2 The way that MEHC could attempt to recover
3 its premium is by taking on more risk with greater
4 leverage. There's no magic that all of a sudden you
5 can recover this without any cost on your part. They
6 would take on greater risk and get a higher return
7 and maybe that would or would not cover the
8 acquisition premium. It's mainly a compensation for
9 the greater risk.

10 On the other hand, if it were to go into
11 rate base, then it would reflect -- it would cost
12 something to the ratepayers, because rate base is a
13 fundamental element in determining rates. So the
14 main point there is that it -- ratepayers don't pay
15 for it the way it is right now, because there's no
16 increase in rate base.

17 Q. If the Commission were to adopt a double
18 leverage adjustment, either by the Staff or another
19 one, is there any specific method by which you would
20 recommend the Commission recover the acquisition
21 premium?

22 A. Yes, I would think that if they were to use
23 the double leverage approach, as they have
24 recommended in their testimony, that the acquisition
25 premium should be included in rate base. That would

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1 be the only fair way to do it.

2 Q. Final question. Is there unanimous --
3 you're a financial economist and you've been at this
4 for some time, haven't you?

5 A. Yes, I have.

6 Q. Is there, either with Dr. Morin's text that
7 was the subject of this morning's flurry of activity,
8 or Mr. Fama or yourself, is there agreement in the
9 financial economics community about double leveraging
10 adjustments or is it a fairly contentious subject?

11 A. It undoubtedly is contentious in regulatory
12 proceedings. In the finance literature, I think it's
13 pretty clear that one shouldn't consider a double
14 leverage. For instance, the Morin book is very clear
15 about the flaws in the double leverage approach. He
16 discusses double leverage and basically rejects it in
17 his book. There's a -- there's also several
18 articles, one was by Petway and Jordan, I believe,
19 that rejected the double leverage approach, and there
20 was also a very good article by an economist whose
21 name forgets me right now who had been at the Iowa
22 Utility Commission, and he basically shows an
23 approach that leads to the same equation that I have,
24 that if you're going to apply double leverage, you
25 have to adjust the cost of equity at the parent

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1 level, and if you do it right, it's not going to make
2 a difference. That is, the cost of equity for the
3 parent goes up by enough because of the higher
4 leverage and the cost of debt would go up by enough
5 that when you take the weighted average cost of
6 capital for the parent, it turns out to be the same
7 as the cost of equity for the subsidiary. It doesn't
8 lead to a magic reduction in the cost of capital.

9 And it makes common sense. If a utility
10 already has a capital structure, as PacifiCorp does,
11 that is similar to the capital structures of other
12 utilities and have been approved by utility
13 commissions around the country as being a reasonable
14 capital structure, that suggests that that's a
15 minimal cost capital structure. The fact that the
16 other utility commissions approved those capital
17 structures indicated that they found rates to be just
18 and reasonable based on the capital structures used
19 by those other stand-alone utilities.

20 You don't get anything for free. You can't
21 all of a sudden get lower rates or get a lower cost
22 of capital by adding more leverage to the utility's
23 capital structure when the rest of the world has
24 recognized that a correct capital structure is one of
25 the comparable companies. If that would have been

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1 the correct capital structure, the other companies
2 would have done it, as well, and they haven't. Nor
3 have capital structures with 20 percent equity or
4 such low levels been approved by other commissions,
5 and certainly not by the financial community. If the
6 company were to have a capital structure, a utility
7 with that kind of leverage, their bond rating would
8 undoubtedly be affected.

9 COMMISSIONER JONES: Thank you. That's all
10 I have.

11 JUDGE RENDAHL: Are there any other
12 questions for Dr. Vander Weide? All right. Well,
13 thank you very much, Dr. Vander Weide. You may step
14 down. Be off the record for a moment.

15 (Recess taken.)

16 JUDGE RENDAHL: Let's be on the record.
17 We're back after a brief break, and I understand,
18 before we bring Mr. Gorman up, we have a few
19 clarifications. Mr. Cedarbaum.

20 MR. CEDARBAUM: Yes, Your Honor. In my
21 questions of Dr. Vander Weide, I had asked him
22 subject to check that he had testified in the gas
23 rate case of Interstate Power and Light Company, and
24 he didn't think he had, and he was actually correct.
25 So he did testify in only the electric side of that

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1 case, so that -- in terms of our discussion of those
2 cases, that was the case that had the Consolidated
3 Docket Numbers RPU-02-3, 02-8, and ARJ 02-1, and that
4 was the case in PUR citation 225 PUR 4th 165 and 487.

5 JUDGE RENDAHL: Okay. Well, thank you for
6 that clarification. Good morning, Ms. Davison.

7 MS. DAVISON: Good morning.

8 JUDGE RENDAHL: I understand we have Mr.
9 Gorman on the line. Mr. Gorman, are you there?

10 MR. GORMAN: I am.

11 JUDGE RENDAHL: Okay. Thank you. I'm going
12 to turn up the volume here. Just a moment. Okay.
13 Can you raise your right hand in cyberspace?

14 Whereupon,

15 MICHAEL P. GORMAN,
16 having been first duly sworn, was called as a witness
17 herein and was examined and testified as follows:

18 JUDGE RENDAHL: Thank you. Ms. Davison.

19 MS. DAVISON: Thank you, Your Honor.

20

21 D I R E C T E X A M I N A T I O N

22 BY MS. DAVISON:

23 Q. Mr. Gorman, are you the same Mr. Gorman who
24 has submitted pre-filed testimony in this docket on
25 behalf of the Industrial Customers of Northwest

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1 Utilities?

2 A. I am.

3 Q. And do you have any corrections to your
4 testimony?

5 A. I do not.

6 JUDGE RENDAHL: Okay. Mr. Gorman, can you
7 speak directly into the phone, if you're using a
8 speaker phone, so that we can hear you more clearly?

9 THE WITNESS: I'm sorry. I do not have any
10 corrections.

11 JUDGE RENDAHL: Okay. Thank you. That's
12 better.

13 MS. DAVISON: Your Honor, I would like to
14 move the admission of Exhibits 121-T through 139, as
15 well as Exhibit 142 and 144 into the record.

16 JUDGE RENDAHL: And not 143?

17 MS. DAVISON: Oh, I'm sorry, 142 through
18 144.

19 JUDGE RENDAHL: Okay. Are there any
20 objections to admitting what's been marked as
21 Exhibits 121-T through 139 and 142 through 144, Mr.
22 Gorman's pre-filed testimony and exhibits?

23 MR. WOOD: No objection, Your Honor. I was
24 just checking to see if we had cross-examination
25 exhibits that we were stipulating to the record.

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1 JUDGE RENDAHL: On my list, I have one
2 cross-examination exhibit from PacifiCorp, what's
3 been marked as Exhibit 140, and one for Staff,
4 Exhibit 141, and none for the supplemental testimony.

5 MR. WOOD: I would move Cross-examination
6 Exhibit 140.

7 JUDGE RENDAHL: Okay. Well, since there's
8 no objection to Exhibits 121-T through 139 and 142
9 through 144, those are admitted. Is there any
10 objection to admitting PacifiCorp's Cross Exhibit
11 140?

12 MS. DAVISON: No, Your Honor.

13 JUDGE RENDAHL: Okay. No objection. That
14 will be admitted. And Mr. Cedarbaum, do you wish to
15 offer Exhibit 141 for Staff?

16 MR. CEDARBAUM: Yes.

17 JUDGE RENDAHL: All right. Is there any
18 objection to admitting that exhibit?

19 MS. DAVISON: No.

20 JUDGE RENDAHL: All right. With that, all
21 of those exhibits will be admitted into the record.

22 MS. DAVISON: Thank you, Your Honor.

23 Q. Mr. Gorman, did you listen in on the WUTC
24 bridge line yesterday to the testimony of PacifiCorp
25 Witness Williams?

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1 A. I did.

2 Q. And can you -- again, you're a little faint.

3 A. I'm sorry. Yes, I did.

4 Q. That's much better. Thank you. Do you have
5 any response to Witness Williams' comments concerning
6 the impact on PacifiCorp's off-balance sheet debt
7 equivalent after the MEHC acquisition?

8 A. I do. I have two comments concerning his
9 response to my testimony. First, he indicated -- my
10 testimony discusses a potential for a change in the
11 off-balance sheet debt equivalent because of the
12 reduction to the West Valley lease payment and issues
13 related to -- pardon me. I'm looking for the page in
14 my testimony. The facility that is currently owned
15 by MEHC and PacifiCorp is under contract with that
16 facility. That is --

17 JUDGE RENDAHL: Can you speak up again, Mr.
18 Gorman?

19 THE WITNESS: I'm sorry. I'm looking for
20 the page in my testimony. I apologize. I should
21 have had this marked. It's on page four and five of
22 my supplemental testimony that's discussed, the
23 Blundell plant, which is currently under contract to
24 PacifiCorp, a subsidiary of MEHC. After this
25 transaction takes place, it's my understanding that

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1 MEHC intends to make an equity contribution to
2 PacifiCorp for this plant. Consequently, that
3 contract will be converted from an off-balance sheet
4 financial obligation of PacifiCorp to essentially an
5 on-balance sheet asset of PacifiCorp, at which point
6 it would be just worried about PacifiCorp's debt and
7 equity capital structure.

8 The contribution of that plant would lower
9 PacifiCorp's off-balance sheet debt obligations
10 because it simply would no longer be an off-balance
11 sheet obligation. Mr. Williams did not respond to
12 that portion of my testimony.

13 His statements concerning West Valley lease
14 were issues I attempted to validate or discover in
15 the discovery process. I specifically asked
16 questions concerning which of their financial
17 obligations were included in the determination of
18 their off-balance sheet debt equivalent in our Data
19 Request 16-10.

20 And the company provided that number in
21 aggregate, but, however, the information was
22 requested on a per contract and per plant basis. We
23 didn't get the detail to validate whether or not West
24 Valley was included in that number or not.

25 So I can't refute or confirm Mr. Williams'

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1 contention that West Valley is indeed not included in
2 the off-balance sheet debt obligations by the
3 Standard and Poor's evaluations.

4 Finally, and probably most importantly, I
5 would like to briefly respond to his evaluations of
6 the credit metric calculations considering
7 off-balance sheet debt obligations. In all of his
8 evaluations, Mr. Williams compared those credit
9 rating metrics to Standard & Poor's benchmarks for a
10 single A utility. His argument was that PacifiCorp's
11 current corporate bond rating from Standard & Poor's
12 is A minus. While that's true, he didn't point out
13 that PacifiCorp's unsecured bond rating from Standard
14 & Poor's is triple B plus.

15 Off-balance sheet debt obligations are
16 subordinate obligations; they're not secured
17 obligations. So when one compares the financial
18 credit metric calculations that I've calculated or
19 even that the company's calculated, it's important to
20 consider that what PacifiCorp's actual bond rating
21 is, reflecting all of its debt obligation, including
22 its unsecured obligations, which is what off-balance
23 sheet debt obligations are.

24 So comparing my return on equity to capital
25 structure recommendation, those ratios, either those

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1 calculated by myself or largely those calculated by
2 Dr. Hadaway do support either a very weak single A
3 bond rating or a solid triple B bond rating. In
4 other words, they support PacifiCorp's current credit
5 rating.

6 That concludes my response to that aspect of
7 Mr. Williams' rebuttal.

8 MS. DAVISON: Your Honor, I have no further
9 questions of Mr. Gorman.

10 JUDGE RENDAHL: Okay. Thank you.

11 MR. WOOD: May I ask a follow-up to that?
12 Are we at the right time?

13 JUDGE RENDAHL: Yes, please go ahead, Mr.
14 Wood.

15

16 C R O S S - E X A M I N A T I O N

17 BY MR. WOOD:

18 Q. Mr. Gorman, I realize that you've been at a
19 disadvantage in that you were listening in and didn't
20 necessarily have the written material in front of
21 you. Did you understand that, in his oral comments,
22 Mr. Williams referenced both the West Valley lease
23 cost and the Blundell 30-year steam purchase
24 agreement, and that he said that changes with respect
25 to these two contracts, both contracts, however,

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1 cannot reduce the 570 million in debt equivalence
2 currently assigned to PacifiCorp's contractual
3 payment obligations for the simple reason that the
4 contracts referenced by Mr. Gorman were not --

5 JUDGE RENDAHL: Mr. Wood, I'm sorry, when
6 you read, you need to slow down for the court
7 reporter.

8 MR. WOOD: I'm sorry, I'm sorry.

9 Q. For the simple reason that the contracts
10 referenced by Mr. Gorman were not included in the
11 list of contractual obligations provided to Standard
12 & Poor's for its debt equivalence evaluation.

13 Did you understand that Mr. Williams
14 testified that neither the Blundell nor the West
15 Valley lease contracts were included in such
16 evaluation?

17 A. It was my understanding, from hearing his
18 testimony yesterday, that he clearly made that
19 statement concerning West Valley. But my
20 understanding of his comments concerning the Blundell
21 facility was that it was -- that the conversion from
22 a contract from a non-affiliated company to an
23 affiliated company would not change the debt
24 equivalent of that facility.

25 Q. The record will speak for itself, but if Mr.

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1 Williams had testified that the Blundell contract, as
2 well, was not considered and the debt equivalence of
3 570 million was not provided to Standard & Poor's, do
4 you have -- are you suggesting any evidence to the
5 contrary?

6 A. Well, again, that is information I attempted
7 to gain through discovery with the company to
8 actually identify which purchase power agreements and
9 lease generation facility agreements were considered
10 in the debt equivalent calculation with Standard &
11 Poor's. I very clearly asked for it by purchase
12 power agreement and by the name of the lease
13 generating facility. They gave it to me in
14 aggregate; they did not give me a breakout of the
15 individual components that comprise the aggregate.
16 So I'm not able to validate Mr. Williams' statements.
17 But, importantly, we attempted to validate that
18 through appropriate discovery.

19 MR. WOOD: Thank you.

20 JUDGE RENDAHL: All right. Ms. Davison,
21 anything further?

22 MS. DAVISON: No, Your Honor.

23 JUDGE RENDAHL: All right. Anything further
24 from the parties for this witness, Mr. Gorman? All
25 right. Are there any questions from the Bench for

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1 Mr. Gorman? Commissioner Jones.

2

3 E X A M I N A T I O N

4 BY COMMISSIONER JONES:

5 Q. Good morning, Mr. Gorman, this is

6 Commissioner Jones.

7 A. Good morning.

8 Q. Do you have both your direct testimony,
9 Exhibit 121-T and the supplemental -- I don't have a
10 number on that.

11 JUDGE RENDAHL: It's -- the supplemental is
12 Exhibit 142-T.

13 Q. Do you have both of those in front of you
14 now?

15 A. I do.

16 Q. Okay. Could we go to your direct testimony
17 first?

18 A. Okay.

19 Q. I'll just start with some basic questions.
20 On pages one and two, you summarize your
21 recommendations on cost of capital. And I just want
22 to confirm that in your review of the evidence on the
23 MEHC acquisition for the supplemental testimony, you
24 didn't address specifically the issue of any changes
25 in your recommended return, either on the return on

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1 equity or overall cost of capital.

2 So I take it -- could you just confirm for
3 the record that you still support the recommendations
4 in your direct testimony of 9.8 percent return on
5 common equity and an overall cost of capital for
6 PacifiCorp of 8.02 percent?

7 A. I do support that, yes.

8 Q. Okay. Let's go to your supplemental
9 testimony, pages -- page two.

10 JUDGE RENDAHL: That's Exhibit 142.

11 COMMISSIONER JONES: Yes.

12 JUDGE RENDAHL: All right. And Mr. Gorman,
13 if you can speak up again, the court reporter's
14 having some difficulty hearing you.

15 THE WITNESS: I apologize.

16 Q. We are grappling with the precision of the
17 impact of the MEHC acquisition on cost of capital, as
18 you know. And I would just like to state a couple of
19 sentences that you state in your supplemental and
20 state them for the record and see if you still agree
21 with them.

22 On lines 20 and 21 of page two, you say,
23 quote, While it is not precisely known at this time,
24 it is likely that PacifiCorp's capital structure and
25 capital structure management could change after the

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1 acquisition. Then, on page three, line 11, you say,
2 quote, PacifiCorp's actual financing decisions after
3 the acquisition are not yet known. And then you go
4 on about some possible impacts.

5 Do you still stand by those statements to
6 the effect that we, with precision and exactness, do
7 not exactly know at this time what the capital
8 structure will be after the acquisition?

9 A. Yes, I think it is not absolutely certain
10 what PacifiCorp's capital structure or overall
11 leverage risk is going to be after the acquisition
12 takes place.

13 Q. Okay. With that as a fundamental, I'd like
14 to ask you about short-term debt. On pages -- I
15 think on page three, three and four of your
16 testimony, you get into the issue of the -- that
17 PacifiCorp --

18 JUDGE RENDAHL: Is this the direct, original
19 direct or --

20 COMMISSIONER JONES: No, this is the
21 supplemental, Judge.

22 Q. Excuse me, on page two, lines 22 and 23, you
23 say, quote, MEHC will have the incentive to require
24 PacifiCorp to place a greater reliance on short-term
25 borrowings in the future than it has in the past,

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1 thus potentially driving down its ratio of common
2 equity to total capital.

3 How likely -- have you read the stipulations
4 in detail on the acquisition of PacifiCorp by MEHC,
5 specifically 18, Stipulation 18, I think it is?

6 A. Yes.

7 Q. And could you just summarize your theory
8 here or your proposition that you think there will be
9 a much greater reliance on short-term borrowings?

10 A. Well, I tried to explain that in my
11 testimony, and again, it's my expectation that the
12 reality will be as it is after the acquisition takes
13 place. But because MEHC will have a great incentive
14 to receive dividends from PacifiCorp, I would expect
15 that it would require PacifiCorp to take actions
16 which improve the probability that it will receive
17 those dividends.

18 MEHC needs the dividends because those are
19 its dividends from PacifiCorp, and its other utility
20 affiliates are its only source of cash available to
21 service a significant debt obligation at the parent
22 company level, MEHC level. One potential restriction
23 on PacifiCorp paying MEHC dividends is if its equity
24 ratio, as prescribed in the stipulation, falls below
25 specific levels. Importantly, in those equity ratio

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1 calculations, short-term debt is not included as a
2 component of total capital in establishing what the
3 common equity ratio is and whether or not PacifiCorp,
4 the entity, pays dividends to MEHC.

5 Because of that, it's my expectation that,
6 in any event, because PacifiCorp's common equity
7 ratio is very near those right now, that MEHC will
8 require PacifiCorp to rely more on short-term debt
9 than it potentially has during the test year in this
10 case in order to protect PacifiCorp's ability to pay
11 dividends.

12 Q. I understand that. Is there also the other
13 factor? Do you think that current market conditions
14 in the bond markets are favorable for issuing
15 short-term debt?

16 A. Well, they certainly aren't in the fact that
17 short-term debt interest rates are cheaper than
18 long-term interest rates, but there's a risk that
19 goes along with that lower interest rate. Short-term
20 -- extensive amount of short-term borrowing subjects
21 the utility to a lot of interest rate risk.
22 Conversely, locking in the long-term interest rate
23 essentially takes the utility out of the interest
24 rate market, but allows the utility, if there's
25 reasonable terms and conditions on the bond issue, to

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1 refinance the long-term securities if interest rates
2 move in their favor.

3 So in short, there is an opportunity for
4 reduced interest cost by using short-term debt
5 financing, but there is risk that corresponds to that
6 lower cost.

7 Q. Could you turn to page six of your
8 supplemental testimony, lines ten through 14? This
9 gets into the issue of how, both on the short-term
10 debt issue and the debt equivalence issue, the
11 off-balance sheet issue, the ratings agencies are
12 going to look at the post acquisition cap structure.
13 Are you -- do you think -- my question is simply do
14 you think there is a potential for a rating agency
15 upgrade for both PacifiCorp and MEHC after the
16 acquisition based on some of the following factors:
17 For PacifiCorp, there will be decreased operational
18 risk through the elimination of the high-risk
19 affiliates, such as PPM Energy. For MEHC, there will
20 be, as you know, a consolidation with the balance
21 sheet. With Berkshire Hathaway, after PUHCA repeal
22 is implemented, stronger consolidated financial
23 ratios, et cetera.

24 So do you think -- you talk about the
25 likelihood of certain things happening on the debt

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1 equivalent side and the short-term debt side, but do
2 you think there is a potential, and rate the
3 potential of a credit agency upgrade for these two
4 companies.

5 A. There's certainly the potential for it, but
6 I think one thing that seems clear is, to the extent
7 that PacifiCorp's affiliation with PHI's other
8 affiliates has caused some credit rating concern,
9 that will be eliminated by the acquisition. That's a
10 certainty. The opportunity for improved credit
11 ratings is there, of course, depending on the impact
12 of MEHC's leveraged capital structures impact on
13 PacifiCorp's stand-alone credit rating, if it does,
14 in fact, achieve a stand-alone credit rating, and any
15 changes Berkshire Hathaway may make to its financing
16 of MEHC as a result of changes to federal law.

17 So the opportunity is there, but what the
18 actual outcome will be is yet to be determined. With
19 everything except for the elimination of PacifiCorp's
20 risk in relationship to PHI (inaudible).

21 JUDGE RENDAHL: Mr. Gorman.

22 THE WITNESS: Yes.

23 JUDGE RENDAHL: I think we missed that last
24 bit, the last sentence.

25 THE WITNESS: I concluded by saying, again,

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1 I just repeated myself. There is one element of
2 PacifiCorp's risk that will be eliminated, and that
3 is to the extent PacifiCorp's risk has been impacted
4 by its affiliation with PHI's not-regulated
5 higher-risk affiliates, that risk will go away after
6 the acquisition.

7 Q. Back to short-term debt, is there any
8 recommendation -- I think in your direct testimony,
9 you proposed a short-term debt level of 2.55 percent
10 in the cap structure, and then you proposed some
11 other alternatives. But based on your testimony in
12 the supplemental of this incentive to issue
13 additional short-term debt, is there any recommended
14 capital structure with an increased percentage of
15 short-term debt that you recommend the Commission
16 consider?

17 A. I have not made that kind of recommendation
18 at this point, no. The recommendation I have is my
19 best assessment of what PacifiCorp's costs will be,
20 but with my expectation that rates determined in this
21 proceeding will be in effect. I did not say that
22 that capital structure accurately reflects its
23 capital structure mix.

24 JUDGE RENDAHL: Its capital structure mix?

25 THE WITNESS: Yeah, PacifiCorp's actual

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1 capital structure that will be in effect during this
2 period, the rates determined in this proceeding are
3 in effect.

4 Q. Would you go to page two? I'm going to
5 address the issue of equity infusions now. Could you
6 go to page two, lines five through 12 of your direct?

7 A. Okay.

8 Q. Are you there?

9 A. I am.

10 Q. Do you still stand by the statement in that
11 testimony that, in your estimations of capital
12 structure, that you are only including one infusion
13 of equity from Scottish Power via PHI to PacifiCorp
14 of 125 million, and you are excluding two additional
15 payments that had been made through December 30th,
16 2005, of approximately 250 million?

17 A. I did exclude those simply because I was not
18 able to reconcile both the actual equity infusions
19 that have been made and, second, you know, what
20 portion of those equity infusions was actually given
21 back to Scottish Power in the form of dividend
22 distributions.

23 Q. Is it known and measurable at this point
24 that the additional equity infusions have been made
25 based on data requests and what has been presented in

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1 the record, in your view?

2 A. Yes, it is known the equity infusions has
3 been made, but it is not known the actual impact on
4 common equity, because the record is not clear on the
5 amount of dividend distributions that have been made
6 along with those equity infusions.

7 Q. I see. Final question. What, in your view,
8 would be -- if the Commission were to include a PCAM,
9 power cost adjustment mechanism, A, and B, a
10 decoupling mechanism, either on a trial basis or a
11 permanent basis, what would be the impact on the ROE
12 and the overall cost of capital in your analysis?

13 A. Well, there would be potentially a
14 significant impact on the capital structure. If you
15 read the Standard & Poor's report attached to the
16 direct testimony of Mr. Williams, there is a
17 discussion of Standard & Poor's methodology for
18 establishing off-balance sheet debt equivalence. One
19 of the thresholds is the actual risk factors Standard
20 & Poor's assigns to the Utility's risk of fully
21 recovering purchased power firm commitment cost.

22 With the PCAM, it is likely, if not nearly a
23 certainty, that Standard & Poor's would reduce the
24 risk factor to PacifiCorp, and that would
25 significantly -- potentially significantly drive down

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1 the off-balance sheet debt equivalent. What that
2 would mean is that PacifiCorp's proposed capital
3 structure in this case would be much too heavily
4 weighted with common equity.

5 The potential return on equity consideration
6 is also heavily impacted by the implementation of
7 that kind of mechanism. All the witnesses in this
8 proceeding looked at the reasonableness of
9 PacifiCorp's proposed capital structure in assessing
10 the risk in developing a return on equity
11 recommendation in this case. PacifiCorp's capital
12 structure is a key financial component that goes into
13 establishing what its risks are in selection of other
14 companies with comparable risks to PacifiCorp.

15 If a PCAM is implemented, PacifiCorp's risk
16 would be reduced, its capital structure would no
17 longer be appropriate for the operating risk
18 PacifiCorp undertakes, and the return on equity
19 recommendation that I've made would be much too high
20 to reflect a much lower operating risk exposure of
21 PacifiCorp.

22 So the bottom line effect is that kind of
23 mechanism can have a meaningful reduction in
24 PacifiCorp's risk and it needs to be captured in the
25 return on equity and, probably as importantly, that

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1 the appropriate capital structure for developing the
2 overall rate of return.

3 Q. Thank you. So am -- I take it -- is my
4 understanding correct that in your analysis for the
5 direct testimony, where you came up with an overall
6 cost of capital for 8.02 percent, that neither the
7 PCAM, a consideration of the PCAM, nor the decoupling
8 mechanism was included in your analysis?

9 A. That's right. (Inaudible)

10 Q. Could you repeat that?

11 A. My recommended return on equity was based on
12 my assessment of PacifiCorp's risk as it currently
13 stands.

14 Q. Risk as currently stands?

15 A. Yes.

16 Q. Have you been involved in other
17 jurisdictions in considerations of PCAMs, power cost
18 adjustment mechanisms, and the impact on ROE?

19 A. Yes.

20 Q. Okay. Could you quantify for the record
21 what you mean by much too high, quote, end quote?
22 What range, and a range would be acceptable, because
23 this is what Commissions like ours deal with. What
24 would be a range of percentages that we should
25 consider if we were to include a PCAM?

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1 A. Well, of course it depends on the PCAM that
2 is implemented. The transfer of risk.

3 Q. Well, for that, have you reviewed the
4 company's proposal for a PCAM in this case?

5 A. I have not in this case, but I've
6 (inaudible).

7 Q. Okay. Are you familiar --

8 JUDGE RENDAHL: I'm sorry, Mr. Gorman, your
9 last comment dropped off there. I understood you
10 hadn't looked at the PCAM proposal in this case, but
11 I missed the last comment.

12 THE WITNESS: I reviewed their proposal in
13 other cases, but I have not reviewed the one in
14 Washington, proposed in Washington.

15 JUDGE RENDAHL: Thank you.

16 MS. DAVISON: Mr. Gorman, we're having --
17 still having difficulty hearing you. Could you pick
18 up your handset and just talk directly into the phone
19 instead of using a speaker phone?

20 THE WITNESS: I have already done that. I
21 apologize. I just need to talk --

22 MS. DAVISON: Just talk louder. Thank you.

23 JUDGE RENDAHL: Go ahead, Commissioner
24 Jones. Sorry about that.

25 Q. Well, I can't pursue that much further if he

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1 hasn't reviewed the PCAM proposal in detail, but if
2 -- yeah, well, I'll just leave it at that.

3 My last question relates to -- I just want
4 to confirm that there are no changes in your
5 testimony for an overall -- you looked at a -- in
6 your analysis at a DCF, a risk premium, and CAPM
7 approaches to estimate the cost -- the return on
8 common equity of 9.8 percent; correct?

9 A. Yes.

10 Q. And you criticized Dr. Hadaway for use of
11 projected -- for his weight in giving projected
12 interest rates, rather than you using currently
13 observed utility bond rates in the risk premium
14 methodology; correct?

15 A. Yes.

16 Q. And you quoted in your testimony that the
17 blue chip economic indicators continue to decline in
18 their estimation of a long-term treasury bond. I
19 think you said 5.8 percent to 5.0 percent. Do you
20 still stand by that testimony today? Because I think
21 treasury bond rates today are in the range of 4.5 or
22 4.6 percent.

23 A. Yes, treasury bond rates have not increased,
24 as Dr. Hadaway suggested, and I point out that more
25 recent projections of interest rates have continued

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1 to fall below projections that were made just a few
2 months ago. So there is not a general consensus that
3 interest rates are going to increase, as Dr. Hadaway
4 seems to assume in his analysis.

5 Q. But has there been a recent quarterly
6 forecast by the blue chip economic indicators on
7 their projection of T-bond rates that you are aware
8 of, other than what's provided in your testimony? I
9 think the latest one you have is 5.0 percent?

10 A. The latest projection on T-bond rates is 5.1
11 percent by the blue chip financial forecast. I
12 believe the projected -- projection used in my
13 analysis -- let me refer you to a page.

14 JUDGE RENDAHL: You'll have to speak up
15 again, Mr. Gorman.

16 THE WITNESS: Sorry, the most -- at page 26
17 of my direct testimony, I refer to the 20-year
18 projected treasury bond yield by the blue chip
19 financial forecast was 5.2 percent in October of
20 2005. February of 2006, the two-year-out projection
21 of 20-year treasury bond yield is 5.1 percent. So
22 the projected yields are going down, not up, and
23 current cash yields are staying relatively stable, on
24 the long end of the interest rate yield curve.

25 Q. And just for the record, again, since we're

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1 examining so much data from four capital witnesses in
2 this case, what was the range that you suggested
3 under the risk premium approach in your analysis?
4 Was it -- here it is, 9.4 to 10.3 percent, with a
5 mid-point estimate of 9.9 percent; is that correct?

6 A. It is.

7 Q. That's on page 25. So if anything, with the
8 downward change in interest rates of the long-term
9 T-bond, this would move these estimates in a downward
10 direction; correct?

11 A. They would.

12 COMMISSIONER JONES: Thank you. That's all
13 I have.

14 JUDGE RENDAHL: All right. Is there
15 anything further for Mr. Gorman?

16 MR. WOOD: I have just two questions, Your
17 Honor, if I might follow-up to one of his responses
18 to Commissioner Jones?

19 JUDGE RENDAHL: Okay. Go ahead, Mr. Wood.
20 Mr. Gorman, can you hear Mr. Wood?

21 THE WITNESS: I can.

22

23 R E C R O S S - E X A M I N A T I O N

24 BY MR. WOOD:

25 Q. My two questions relate to your Exhibit

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1 MPG-6, which is Exhibit --

2 JUDGE RENDAHL: -- 126.

3 Q. Thank you, 126. You list a series of
4 comparable companies. Most of these companies
5 currently have some form of PCA, don't they, Mr.
6 Gorman?

7 A. Most of them do, yes. Not all of them.

8 Q. And is it correct from your exhibit that the
9 Value Line common equity ratios for these companies
10 average 49 percent?

11 A. It is.

12 MR. WOOD: Thank you.

13 JUDGE RENDAHL: All right. Is there
14 anything further for Mr. Gorman? Thank you very much
15 for calling in, Mr. Gorman. We appreciate your being
16 flexible and appearing this morning. So you can
17 continue to listen in if you'd like or go on with
18 whatever you wish to do today.

19 And our next witness will be Mr. Selecky,
20 it's my understanding, so let's be off the record for
21 a moment while we change witnesses.

22 (Recess taken.)

23 JUDGE RENDAHL: Let's be back on the record.
24 Again, good morning, Mr. Selecky. If you could raise
25 your right hand.

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1 Whereupon,

2 JAMES T. SELECKY,

3 having been first duly sworn, was called as a witness

4 herein and was examined and testified as follows:

5 JUDGE RENDAHL: Please go ahead, Ms.

6 Davison.

7 MS. DAVISON: Thank you, Your Honor.

8

9 D I R E C T E X A M I N A T I O N

10 BY MS. DAVISON:

11 Q. Could you state your name for the record,
12 please?

13 A. My name is James T. Selecky.

14 Q. And are you the same Mr. Selecky that has
15 submitted pre-filed testimony in this proceeding on
16 behalf of the Industrial Customers of Northwest
17 Utilities?

18 A. Yes.

19 Q. Do you have any corrections to your
20 testimony?

21 A. On my direct testimony, which is 301-T, I
22 had a change on page four, line 14. There's a number
23 there that is 27.6 million. That should be 7.967
24 million.

25 JUDGE RENDAHL: 7.96 million?

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1 THE WITNESS: Yes, 967. 7.967.

2 JUDGE RENDAHL: All right, thank you.

3 Q. Do you have any other corrections?

4 A. No.

5 MS. DAVISON: Your Honor, I would like to
6 move the admission of Exhibits 301-T through 318,
7 Exhibits 821-T and 822-T into the record.

8 JUDGE RENDAHL: Are there any objections to
9 admitting what's been marked as Exhibits 301-T
10 through 318 and 821-T and 822?

11 MR. WOOD: No objections, Your Honor.

12 JUDGE RENDAHL: All right. With that, those
13 exhibits will be admitted into the record.

14 MR. WOOD: Your Honor, should I offer the
15 cross-examination exhibits at this time, also?

16 JUDGE RENDAHL: I don't see why not.

17 MR. WOOD: I would identify
18 cross-examination exhibits to the direct testimony,
19 Numbers 320 through 328, plus the cross-examination
20 exhibits to the supplemental testimony, 823 and 824,
21 and would offer those exhibits.

22 JUDGE RENDAHL: Ms. Davison, is there any
23 objection?

24 MS. DAVISON: No, Your Honor.

25 JUDGE RENDAHL: All right. Hearing no

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1 objection, what's been marked as Exhibits 320 through
2 328 and Exhibits 823 through 824 will be admitted
3 into the record.

4 MS. DAVISON: Mr. Selecky is available for
5 cross-examination. When I arrived this morning, I
6 did not get an extra copy of the exhibits, the
7 supplemental cross exhibits for Mr. Selecky, so if I
8 could get a copy of that, that would be helpful.

9 MR. WOOD: Could we go off the record a
10 moment, Your Honor?

11 JUDGE RENDAHL: Let's go off the record for
12 a moment.

13 (Discussion off the record.)

14 JUDGE RENDAHL: Let's be back on the record.
15 Ms. Davison. I'm sorry, Mr. Wood.

16 MR. WOOD: Thank you.

17

18 C R O S S - E X A M I N A T I O N

19 BY MR. WOOD:

20 Q. Mr. Selecky, Marcus Wood. I'm representing
21 PacifiCorp in this proceeding. I have just a few
22 questions for you. They relate to your direct
23 testimony, which is Exhibit 820 -- no.

24 A. 301-T.

25 Q. 301-T. Thank you. I've been chronically

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1 bad at this in this proceeding.

2 A. That's okay.

3 Q. In pages 17 through 22, you discuss what you
4 referred to as your consolidated tax adjustment; is
5 that correct?

6 A. Yes, sir.

7 Q. That adjustment involves attributing to this
8 rate case tax deductions earned at the parent levels,
9 interest deductions at the parent level of
10 PacifiCorp; correct?

11 A. Correct.

12 Q. And on page 20, you have a question, which
13 was, Would PHI receive excessive compensation for its
14 investment in PacifiCorp if PacifiCorp's income tax
15 expense is not adjusted to more accurately reflect
16 actual payments to taxing authorities. And you
17 respond yes?

18 A. That's correct.

19 Q. Okay. Just a few questions related to that.
20 Prior to the acquisition by Scottish Power,
21 PacifiCorp was publicly traded; correct?

22 A. Yes.

23 Q. And right after the acquisition, Scottish
24 Power reduced the previous dividend payments that had
25 been made by the publicly-traded company; correct?

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1 A. I would have to accept that subject to
2 check. I don't recall that specifically.

3 Q. Do you recall that, after the energy crisis
4 or as a result of the energy crisis, Scottish Power's
5 -- the dividend to Scottish Power was wholly
6 suspended for a year?

7 A. Again, I would have to check that. I would
8 accept that subject to check, but I don't have
9 specific knowledge of that, because I didn't pursue
10 that.

11 Q. Okay. Are you aware that Scottish Power, in
12 response to the same power stresses, pumped an
13 additional \$150 million into PacifiCorp equity in
14 2002?

15 MS. DAVISON: Your Honor, Mr. Wood has been
16 asking a series of questions about Scottish Power
17 infusion of equity and other suspension of dividend,
18 and this has been going on subject to check. I
19 thought if it was just one question, we'd just kind
20 of let it slide, but since there's a series of
21 questions, is there a document that Mr. Wood could
22 produce or identify that we should be looking to so
23 that we do not have to do extensive research on these
24 broad issues?

25 JUDGE RENDAHL: Mr. Wood.

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1 MR. WOOD: Yeah, we can confirm and the
2 record already identifies for Mr. Williams these
3 infusions. That can be confirmed in the record.

4 MS. DAVISON: Well, perhaps it would be
5 helpful if you could ask your questions with
6 reference to Mr. Williams' testimony, so we could
7 refer to that.

8 MR. WOOD: Fine.

9 Q. My question is would you accept, subject to
10 check, that Mr. Williams identified that Scottish
11 Power, in 2002, was required to or did infuse 150
12 million in additional equity capital into PacifiCorp?

13 A. Yes, I would accept that, subject to check.

14 Q. And this is one you probably are quite aware
15 of, that Scottish Power committed, between March of
16 2005 and March of 2006, to infuse an additional \$500
17 million in equity capital into PacifiCorp?

18 A. Yes, they committed to do that.

19 Q. And the last question in that area actually
20 can be -- if you'll turn to Exhibit 824.

21 A. I have that.

22 Q. Okay. And to the second page and the third
23 paragraph, would you acknowledge that, at the time of
24 the sale, after holding PacifiCorp, making the
25 infusions, at the time of sale to MEHC, Scottish

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1 Power was required to take a \$927 million write-off
2 on its PacifiCorp investment -- 927 million pound
3 write-off?

4 A. Right.

5 Q. And that would be approximately 1.5 billion
6 U.S., or slightly higher, wouldn't it?

7 A. I know it would be above 927 million U.S. I
8 don't know the exact conversion.

9 Q. Fine.

10 A. But that's what that document does state.

11 Q. Fine. And if Scottish Power's intention had
12 been to receive excessive compensation, it's probably
13 been, so far, a little disappointed, hasn't it?

14 A. I guess it depends what its expectations
15 were. I don't know the source of the write-off, if
16 the write-off had to do with the acquisition premium.
17 What I was referring to in my testimony was their
18 returns on an ongoing basis.

19 MR. WOOD: Thank you. I have no other
20 questions.

21 JUDGE RENDAHL: Ms. Davison, anything in
22 redirect?

23 MS. DAVISON: No, Your Honor.

24 JUDGE RENDAHL: Are there any questions for
25 Mr. Selecky from the Bench? I do have a few, Mr.

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1 Selecky, just to clarify.

2 THE WITNESS: Sure.

3

4 E X A M I N A T I O N

5 BY JUDGE RENDAHL:

6 Q. And this is focused on your testimony, your
7 supplemental testimony, having to do with the
8 adjustments relating to the stipulation recently
9 entered in Docket UE-051090, the acquisition
10 proceeding. On pages two and three of your
11 testimony, Exhibit 821, you talk about three of these
12 adjustments, and I'm just seeking to clarify whether
13 you're intending to include these adjustments and --
14 whether ICNU is planning to include these adjustments
15 in its case.

16 For example, the first one, on page two,
17 starting on line ten, would be the captive insurance
18 adjustment. Are you intending -- is it your
19 recommendation that ICNU include a revenue
20 requirement reduction of \$125,000 for that
21 adjustment? I'm just trying to clarify what your
22 recommendation is.

23 A. Yes, but I think the adjustment you're
24 talking about is not the captive insurance
25 adjustment. I think that's the cost assigned to the

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1 affiliates.

2 Q. All right.

3 A. Okay. Essentially, what I'm recommending is
4 that if it cannot be demonstrated that indeed these
5 costs are reflected in the development of
6 PacifiCorp's revenue requirement, then yes, those
7 adjustments should be included in the revenue
8 requirement.

9 I have not been satisfied yet and I realize
10 Mr. Wrigley, from the company, has indicated that, as
11 I understand his testimony and some of his
12 documentation, that that information has been
13 supplied to, I guess, the Commission and the Staff.
14 If the Commission and the Staff is convinced that
15 indeed that adjustment is already included in
16 PacifiCorp's revenue requirement, then I would not be
17 recommending a reduction of an additional \$125,000.
18 I have not been able to satisfy myself yet that all
19 of those adjustments are included.

20 Q. So if you can't be satisfied, then you would
21 recommend a reduction of 125,000?

22 A. Yes.

23 Q. All right. For the next page, starting on
24 line 22nd MEHC, and this does refer to the captive
25 insurance adjustment. Going on to page three, your

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1 recommendation on line six is a revenue requirement
2 reduction of 357,000; is that correct?

3 A. Yes.

4 Q. And is this, again, a situation where you
5 can't assure yourself that you understand the
6 numbers?

7 A. That's correct. My explanation's the same
8 as the previous one I've given. It's not clear to me
9 yet that this captive insurance adjustment is truly
10 reflected in their case.

11 Q. All right. And is the same true for the
12 third adjustment, starting on line seven of page
13 three and ending on line 13? Unless you can be clear
14 from the numbers what's happening, that you would
15 recommend a reduction of 658,000?

16 A. That's correct.

17 Q. Now, is the information that you refer to
18 that Staff and -- Staff has from the company, was
19 that through data requests?

20 A. I believe there was a data response.

21 Q. Is ICNU able to -- does ICNU receive copies
22 of data request responses from the company to Staff?

23 A. I think that was a data -- let me back up.
24 I think there was a data response to a question that
25 we had asked, if my memory serves me right.

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1 Q. I guess my question is, is it possible
2 before the brief that you're likely to get this
3 information?

4 A. I would say I think some of it, yes.

5 Q. Okay. And are you likely to include in the
6 -- do you believe ICNU will likely include by the
7 brief a clarification of the other three MEHC
8 adjustments discussed in Mr. Wrigley's testimony, the
9 West Valley lease, the affiliated management fee
10 issue, and the A&G stretch adjustment? Are you
11 familiar with those adjustments?

12 A. Yes.

13 Q. So are you likely to be able to take a
14 position on that before briefing?

15 A. Yes.

16 JUDGE RENDAHL: Okay. With that, I don't
17 have any other questions for you, Mr. Selecky. Thank
18 you very much. Is there anything further for this
19 witness? With that, Mr. Selecky, thank you very much
20 for being here. You may step down.

21 THE WITNESS: Thank you.

22 JUDGE RENDAHL: All right. We don't -- is
23 Mr. Hill here?

24 MR. FFITCH: Mr. Hill is in the building,
25 Your Honor.

1690

1 JUDGE RENDAHL: All right. Well, why don't
2 we take a brief break while we find him? I think
3 we'll just stay here and --

4 MR. FFITCH: Your Honor, sorry to interrupt,
5 but I did want to make a request for a recess to
6 confer with Mr. Hill. Obviously, he's been presented
7 with some new direct testimony this morning to
8 respond to, and I haven't had a chance to confer with
9 him about that. I would request, if possible, 15
10 minutes or a shorter period at the Bench's
11 discretion.

12 JUDGE RENDAHL: How much time do you
13 anticipate in oral redirect to Mr. Hill?

14 MR. FFITCH: I don't think it's going to be
15 longer than 15 or 20 minutes. Again, I haven't had a
16 chance to talk to him about Mr. Vander Weide's direct
17 --

18 JUDGE RENDAHL: All right.

19 MR. FFITCH: -- in any detail.

20 JUDGE RENDAHL: Why don't we take a
21 ten-minute break. We'll back at 11:20, and that
22 means we'll probably get started a few minutes after
23 that. So let's aim for 20 after 11:00. So let's be
24 off the record.

25 (Recess taken.)

1691

1 JUDGE RENDAHL: Let's be back on the record.
2 Commissioner Jones is on a conference call and will
3 join us when he's finished. Good morning, Mr. Hill.

4 MR. HILL: Good morning.

5 Whereupon,

6 STEPHEN G. HILL,
7 having been first duly sworn, was called as a witness
8 herein and was examined and testified as follows:

9 JUDGE RENDAHL: Okay. Please sit down. Mr.
10 Ffitch.

11 MR. FFITCH: Thank you, Your Honor.

12

13 DIRECT EXAMINATION

14 BY MR. FFITCH:

15 Q. Mr. Hill, could you please state your full
16 name for the record?

17 A. My name is Stephen G. Hill. How are we
18 doing? There we go.

19 Q. All right.

20 A. My name is Stephen G. Hill.

21 Q. And by whom are you employed?

22 A. I'm self-employed.

23 Q. And were you retained by Public Counsel in
24 this case to examine the cost of capital and capital
25 structure issues?

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1 A. Yes, I was.

2 Q. And to provide expert testimony on those
3 matters?

4 A. Yes.

5 Q. And have you prepared testimony in this
6 proceeding that has been marked -- just wait one
7 moment, Your Honor. I'm just recalling that we
8 haven't --

9 JUDGE RENDAHL: 91-T.

10 MR. FFITCH: -- gone with the originals. I
11 wasn't ready to wade into the supplemental, but --
12 thank you.

13 JUDGE RENDAHL: It starts on page five of my
14 exhibit list at 91-T.

15 MR. FFITCH: Thank you.

16 Q. Okay. Mr. Hill, you prepared in this case
17 direct testimony that's been marked as Exhibit 91-T,
18 and then exhibits that are marked as Exhibits 92
19 through 107; is that correct?

20 A. Yes.

21 Q. And then you also prepared supplemental
22 direct testimony, marked as Exhibits 114, 115 and
23 116?

24 A. That's correct.

25 Q. Do you have any changes or corrections to

1693

1 the testimony?

2 A. No, I don't.

3 Q. And are the answers and exhibits true and
4 correct, to the best of your knowledge?

5 A. Yes.

6 Q. If I were to ask you these questions today,
7 would your answers be the same?

8 A. Yes, they would.

9 MR. FFITCH: Your Honor, I'd like to offer
10 Exhibits 91-T through Exhibit 107, and then Exhibits
11 114, 115 and 116.

12 JUDGE RENDAHL: Are there any objections,
13 Mr. Wood?

14 MR. WOOD: No objections.

15 JUDGE RENDAHL: All right. With that,
16 what's been marked as Exhibits 91-T through 107 and
17 Exhibits 114 through 116 will be admitted. Mr. Wood,
18 did you want to offer the cross exhibits? There are
19 -- I'm sorry.

20 MR. KEYES: Yes, we'd like to offer the
21 cross exhibits, 108 through 113, please.

22 JUDGE RENDAHL: Thank you, Mr. Keyes. Is
23 there any objection, Mr. ffitch, to admitting what's
24 been marked as Exhibits 108 through 113?

25 MR. FFITCH: No objection.

1694

1 JUDGE RENDAHL: All right.

2 MR. FFITCH: Your Honor, at this time,
3 pursuant to the prior permission of the Bench, I
4 would like to ask Mr. Hill some direct examination
5 questions with regard to the oral testimony of Dr.
6 Vander Weide and also Mr. Williams.

7 JUDGE RENDAHL: Please go ahead.

8 Q. Mr. Hill, you analyzed the impact of the
9 additional leverage at the parent company level in
10 this case using a couple of methodologies, did you
11 not?

12 A. That's correct.

13 Q. And this morning, Dr. Vander Weide stated
14 that, with respect to one of those methods, you
15 presented the formula incorrectly; is that true?

16 A. That was his testimony, and that is, in
17 fact, correct. There was a parenthesis out of place
18 in the formula.

19 Q. All right. Now, Dr. Vander Weide stated
20 that if you corrected your formula, the result would
21 be a relevered cost of equity of 14 percent. Was
22 that his testimony?

23 A. Yes.

24 Q. And do you agree with that?

25 A. No, I don't. My calculation of the

1695

1 corrected formula indicates a new number of 11.5
2 percent, not 14 percent. But that doesn't change my
3 recommendation that the increment above PacifiCorp's
4 9.125 cost of equity in a double leverage adjustment
5 ought to be a hundred basis points for several
6 reasons.

7 First of all, the beta adjustment is my
8 primary adjustment to the cost of equity. Dr. Vander
9 Weide takes a theoretical exception to that
10 adjustment. He only complains or brings out the point
11 that I note in my testimony that beta is a relatively
12 inaccurate measure of risk.

13 While that is true, both Dr. Vander Weide
14 and I use capital asset pricing level analyses which
15 are predicated on the ability of beta. Beta is a
16 widely-recognized risk measure and, therefore, I
17 believe that the methodology that's my primary
18 methodology, which indicates a range of about 60
19 basis points to 120 basispoints, is reliable.

20 Also, I would note that Mr. Elgin, if
21 relying on studies by Dr. Rothschild, has indicated
22 that the relationship between the cost of equity and
23 capital structure is that, for every one percentage
24 increase in the -- or decrease in the equity ratio,
25 excuse me, for every one percent decrease in the

1 equity ratio, the cost of equity increases by four
2 basis points, or .04 percent. So we're talking about
3 a difference in equity ratio here between PacifiCorp
4 and MEHC post-acquisition of 45 percent to 29
5 percent. That's a 16 percent decrease in equity
6 ratio, and times four basis points would be about 64
7 basis points.

8 So my recommendation of a hundred basis
9 point increase is almost double that of Mr.
10 Rothschild and Mr. Elgin.

11 Finally, Dr. Vander Weide said something
12 about if I had used book value capital structures, I
13 would have gotten a different result. Well, the
14 leverage adjustment that I've made are not designed
15 to use book value capital structures. They come out
16 of the Miller and Modigliani papers that originated
17 in the 1950s, and those papers don't discuss book
18 values. They're only about the theoretical market
19 value equity. So the proper measure of capital
20 structure for that theoretical analysis is market
21 value. But that's not inconsistent with using book
22 value as a regulation, not at all inconsistent.

23 Also, my calculations show that if you use
24 the right formula, with parentheses in the right
25 place, you use book value capital structures and you

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1 use embedded cost rates, which you have to use if you
2 use book value capital structures, the differential,
3 the cost of equity differential falls back to a
4 hundred and -- in my calculation, shows 110 basis
5 points. Once again, my recommendation is a hundred.
6 I think that's reasonable.

7 Q. Does that conclude your responsive testimony
8 to Dr. Vander Weide's testimony?

9 A. Yes.

10 Q. Now, Mr. Hill, were you present during the
11 additional oral rebuttal testimony provided by
12 Company Witness Williams yesterday in this
13 proceeding?

14 A. Yes.

15 Q. And Mr. Williams testified that your
16 proposal regarding double leverage and the resulting
17 capital structure and cost of equity would be
18 inconsistent with the current A minus bond rating for
19 Pacific; isn't that right?

20 A. That was his testimony.

21 Q. All right. And do you agree with that?

22 A. No, I don't agree with that, and there are
23 two general reasons why that's the case. First, I
24 believe there are problems with his analysis, the
25 numerical part of the analysis. And second of all,

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1 even if his analysis is exactly right, the
2 recommendation Public Counsel has made actually
3 improves the bond rating metrics for PacifiCorp.

4 Q. All right. So could you please address the
5 analytical issues first?

6 MR. FFITCH: And Your Honor, I'll just note
7 for the record that during the break, we distributed
8 for the Bench and for parties a copy of the company's
9 response to Staff Data Request Number 22, with -- the
10 relevant page has a red tab marking that.

11 JUDGE RENDAHL: And is it your intent to
12 offer this as an additional exhibit?

13 MR. FFITCH: We would like to offer it as an
14 additional exhibit. We'd be happy to do that, Your
15 Honor, but I believe Mr. Hill would like to refer to
16 it in his answer.

17 JUDGE RENDAHL: All right. Well, let's mark
18 it as Exhibit 117.

19 MR. FFITCH: Thank you, Your Honor.

20 THE WITNESS: Well, the first thing I did in
21 checking Mr. Williams' analysis was compare it to the
22 analysis that he did of his -- PacifiCorp's
23 recommendation in this proceeding that was contained
24 in his response to Bench Request 13. And the
25 methodology is consistent, so his calculations are

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1 credible in that way. In other words, he didn't --
2 there was no funny business going on. He didn't try
3 to change anything there.

4 But looking at the actual calculation, I
5 noted several problems, one of which Mr. Elgin
6 alluded to yesterday, and that was the fact that much
7 of the costs that are attributed to the Washington
8 operations are ratioed down from whole company
9 numbers using a allocation of 8.3282 percent.

10 Well, we know that Washington is a
11 relatively small part of a very big company and a
12 disagreement about what that allocation number will
13 make a very big difference in the results. So I
14 think there's -- that adds a sense of volatility to
15 those results.

16 And I would like to note, also, about that
17 point, when Public Counsel asked Mr. Williams
18 yesterday on the witness stand about the fact that
19 Washington operations were a small part of
20 PacifiCorp, we weren't trying to say that we're doing
21 something bad here and that everybody else will make
22 up for it, not at all; we were simply trying to point
23 out the fact that, in his calculation, he's using a
24 particular allocation factor, which, if it's slightly
25 inaccurate, will make a big difference in the

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1 results. We believe that our recommendation for
2 double leverage here is legitimate and something that
3 ought to be implemented by this Commission in order
4 to ensure that MEHC doesn't over-earn its -- the
5 return it's allowed in this proceeding, return that's
6 appropriate for the risk it faces.

7 Second of all, one of the factors contained
8 in Mr. Williams' metrics is debt imputed by Standard
9 & Poor's corporation for purchased power. And he
10 references Staff DR 22, which I believe now has been
11 labeled Exhibit 117.

12 JUDGE RENDAHL: Yes, that's correct.

13 THE WITNESS: Right. He uses a figure in
14 there of \$570 million for Standard & Poor's
15 attribution for ultimate cost of purchase power.

16 Q. And Mr. Hill, are you referring now to the
17 page that's been marked with the red tab on the
18 exhibit?

19 A. Right, right. What he doesn't say is that
20 Standard & Poor's attributes a 50 percent risk factor
21 to those dollars. So instead of using 570 million,
22 he should use half that number to calculate the
23 interest cost related to purchased power. So that's
24 going to make his metrics downward biased to some
25 degree.

1701

1 Q. Mr. Hill, again, just to assist the people
2 in the hearing room, you're referring to the last
3 paragraph on that page in the exhibit?

4 A. Right. I'm sorry, I'm not looking at it,
5 but I believe that's correct. Right, it's the May 5,
6 2005 report by Standard & Poor's Ratings Direct, and
7 it's the third page, last paragraph.

8 So in that way, I believe his metrics are a
9 little understated because he's included too much
10 interest related to purchased power. Also, I would
11 note that he does use a ten percent interest cost --
12 pseudo interest cost, I'll call it, which is normally
13 attributed to purchased power expenses by Standard &
14 Poor's. However, this adjustment was first
15 instituted by Standard & Poor's some years ago when
16 debt costs were significantly higher than they are
17 now, and ten percent was an approximation of what
18 marginal debt costs are. They're much lower today,
19 so if you used a more reasonable discount factor, I
20 think the interest cost would go down even more.

21 Also, the other point I would note about the
22 actual math included in this calculations is that
23 there are some cash flow items that Standard & Poor's
24 considers for their coverage ratios that are not
25 included in Mr. Williams' calculations, but which are

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1 included and referenced in his response to Bench
2 Request 13. In Bench Request 13, he includes a PDF
3 file of several portions of 10-Qs and 10-Ks for
4 PacifiCorp. In those cash flow projections, he
5 points out that Standard & Poor's includes unrealized
6 gain on derivative contracts and on amortization of
7 regulatory assets as part of the cash flow to the
8 company. Those things aren't included in his
9 calculation, which would also tend to bias those
10 numbers downward.

11 Q. Now, Mr. Hill, let's assume that those
12 problems don't exist and Mr. Williams' numbers are
13 exactly right. Do you agree that the result of this
14 Commission's adoption of your recommendation would be
15 a downgrade of PacifiCorp's bond rating?

16 A. No, I don't, for several reasons. First of
17 all, the bond rating process doesn't boil down to a
18 few ratios. There are two major kinds of risks that
19 are considered in the bond rating process, and this
20 goes to the Commissioner's question yesterday about
21 bond rating 101.

22 There's business risk, which is the most
23 fundamental, then there's financial risks, which are
24 measures -- the ratio measures such as the ones that
25 Mr. Williams presented. They're separate. Business

1703

1 risk is the most fundamental, it's considered first.
2 You know, when I say business risk, I'm including
3 things like service territory, and that's where the
4 bond rating agency looks at the actual economics of
5 the service territory that the company covers.

6 By that, I mean what's the employment in the
7 region, what kind of wages do these people make
8 compared to the national average. High wages,
9 obviously good for a utility; low wages creates more
10 risk. What kind of competition is there, what is the
11 customer mix, a high ratio of industrial customers is
12 not good for risk, because industrial customers, if
13 business goes sour, they can pack up and move away.
14 Residential customers usually don't do that.

15 There are other operational issues that are
16 considered in business risk. What is the generation
17 mix, how much purchased power do they have, do they
18 have nuclear generation.

19 MR. WOOD: I'm going to object at this time,
20 Your Honor. I think we're going awfully far afield.
21 Mr. Williams only addressed changes in metrics, not
22 rate-making 101. This is all direct testimony stuff
23 that is not responsive to the question about whether
24 the -- about what the effect on the rating matrixes
25 would be. I didn't object at all to the broad

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1 questioning and challenges to the calculations of the
2 matrixes, but I think we've gone far beyond that at
3 this point.

4 JUDGE RENDAHL: Mr. ffitch?

5 MR. FFITCH: Well, Your Honor, I have two
6 responses. One is that these questions are -- or
7 this question is directly asking Mr. Hill to respond
8 to Mr. Williams' assertion that his recommendations
9 would result in a downgrade of PacifiCorp's bond
10 rating, and Mr. Hill's explaining why we believe
11 that's incorrect, and he's providing the background
12 for that.

13 Secondly, there's no question that Mr.
14 Williams testified yesterday morning with regard to
15 these matters at some length, so we think it's a
16 legitimate area to cover.

17 JUDGE RENDAHL: Mr. Wood.

18 MR. WOOD: Mr. Williams simply -- the only
19 thing he said about the rating was that the ratios
20 that are produced are inconsistent with the ratios
21 for an A minus credit rating, and Mr. Hill has talked
22 about why he believes that the ratios should be
23 calculated differently.

24 I believe what he's doing now is giving
25 direct testimony about all the factors that one might

1705

1 consider. Mr. Williams was very careful not to do
2 that. We even struck the last Q and A about the
3 importance of -- the significance of the bond rating
4 ratios following the MEHC acquisition. I just
5 believe that we're going beyond responding to what
6 was done in oral testimony.

7 JUDGE RENDAHL: So you're objecting to the
8 -- now the extent of what Mr. Hill is testifying to?

9 MR. WOOD: That he's gone beyond the scope
10 of the testimony that he was allowed to address.

11 MR. FFITCH: Well, Your Honor, if I can make
12 an offer, we could ask Mr. Hill to, you know,
13 summarize these concerns and sort of get to the nub
14 of the answer, which is to respond to this assertion
15 by Mr. Williams in his oral direct that Mr. Hill's
16 recommendation would result in a downgrade of
17 PacifiCorp's bond rating.

18 And if there's too much background being
19 provided, we can certainly ask Mr. Hill to, you know,
20 move through that or summarize that or skip through
21 that to the ultimate question that I would ask him.

22 JUDGE RENDAHL: Why don't we do that also in
23 the interest of time.

24 Q. So Mr. Hill, can you -- do you have the
25 ultimate question in mind?

1706

1 A. Yes.

2 Q. Do you want me to repeat it?

3 A. No, I understand.

4 Q. All right.

5 A. All I was doing by going through the fact
6 that there is something to be considered besides
7 financial ratios is to underscore the fact that
8 financial ratios alone are not determinative of bond
9 ratings, and we were focused also only on Standard &
10 Poor's bond ratings, the ratios. Standard & Poor's
11 is the only company that publishes financial ratios.

12 Moody's, I think probably equal to Standard
13 & Poor's in stature as bond rating agencies, doesn't
14 publish those financial metrics because they claim
15 that it's impossible to assign an accurate credit
16 rating based on financial ratio analysis alone.

17 My point in mentioning that is it's simply
18 -- financial ratio analysis is a second tier part of
19 the analysis.

20 Now, what Moody's does publish is a range of
21 financial metrics that exist, for example, for
22 medium-risk A-rated utilities and for high-risk
23 B-rated utilities, and those ranges are much broader
24 than the ranges that are published by Standard &
25 Poor's.

1707

1 For example, with the metric of FFO to
2 interest, which is funds from operation, basically
3 it's a measure of cash flow, funds from operation to
4 interest, the Standard & Poor's metric that Mr.
5 Williams cites for an A-rated utility is 3.8 to 4.5.
6 Moody's publishes a range that exists currently with
7 medium risk A-rated utilities of 3.5 to 6. So it
8 goes lower and higher. It's a much broader range,
9 and the public advocate's recommendation falls within
10 that range.

11 With regard to funds from operations to debt
12 ratios, Moody's to Standard & Poor's are the same,
13 but with regard to debt to capital ratios, Standard &
14 Poor's range for an A-rated is 42 percent to 50
15 percent debt. Moody's, for A-rated medium-risk
16 utilities, shows a range of 40 to 60 percent. Public
17 Counsel's recommendation falls within that for
18 A-rating.

19 My point simply is that you can't make a
20 decision about what's going to happen to bond rating
21 by looking at a couple of financial ratios. It's a
22 much bigger process than that, and other equally
23 weighty, if you will, institutions that rate bonds
24 have differing views than that of Standard & Poor's.

25 Q. Mr. Hill, do PacifiCorp's historical results

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1 for these specific financial ratios support Public
2 Counsel's recommendation?

3 A. Yes, they do. If you'll look at Exhibit 74,
4 which I believe has been passed out.

5 MR. FFITCH: Your Honor, if I can just
6 indicate, we do have copies of Exhibit 74, which is
7 already in the record, if it's not immediately
8 available to the Bench. I have some additional
9 copies here I can pass out.

10 JUDGE RENDAHL: This is the Staff data
11 request response to the -- the response to Staff's
12 Data Request 313?

13 MR. FFITCH: Correct. Do you need copies at
14 the Bench for reference?

15 JUDGE RENDAHL: I think we may need one.

16 MR. FFITCH: All right.

17 Q. You may go ahead, Mr. Hill. I believe the
18 exhibit is now available.

19 A. All right. If we look at, for example, at
20 the top line there, starting on the right-hand side
21 of the page with 2001, we'll see the funds from
22 operation divided by interest have gone from 2.5
23 times to three in 2002; 3.5 in 2003; 3.7, 2004; 3.4,
24 2005; and as recently as September of 2005, we're at
25 3.3.

1709

1 According to Mr. Williams' calculation,
2 Public Counsel's double leverage recommendation would
3 result in a funds from operation to interest coverage
4 of 3.9 times, higher than anything that they've had
5 over the past five years. We look at funds from
6 operation average total debt and we see the
7 progression of 9.5, 12.1, 16.6, I'm not going to read
8 all the numbers, all the way to September of '05, at
9 16.5.

10 Public Counsel's recommendation results,
11 according to Mr. Williams, in a funds from operations
12 to debt coverage of 19.60, higher than all the rest.
13 The only one of these recommendations that, for
14 Public Counsel, that is slightly higher is the debt
15 to capital. Historically, once again, this is
16 looking only at PacifiCorp, it goes from 55 percent
17 in 2001 to 58 percent in September of 2005. The
18 Public Counsel's recommendation of double leverage,
19 including parent company debt, is 58.2. Not very
20 different than the stand-alone PacifiCorp debt to
21 capital ratio.

22 So I think, looking at the historical
23 results, these financial metrics for PacifiCorp,
24 which over this time period has been an A-rated
25 company, and given the fact that according to Mr.

1710

1 Williams' calculations, which I believe are a little
2 bit depressed, a little low, Public Counsel's
3 recommendation in this proceeding exceeds the
4 historical average for all of these metrics except
5 one.

6 Q. Do you agree that it's likely that the
7 results of this Commission's adoption of Public
8 Counsel's double leverage cost of capital
9 recommendation would be an increase or would mean an
10 increase in the Standard & Poor's business risk
11 position from the five level to the six level?

12 A. No, I don't. I believe that the
13 Commission's recognition of the manner in which MEHC
14 has elected to finance its purchase of the equity of
15 PacifiCorp is a reasonable rate-making methodology
16 and would not be seen as harmful to the company, it
17 will not result in a change of the business position.

18 The business position, as I said earlier, is
19 a function -- maybe I didn't say earlier, but the
20 business position is a function directly of a
21 company's business risk, which is separate from the
22 financial risk. It depends on all those things that
23 I almost got through talking about, which are related
24 to the service territory, et cetera, of the company.

25 And Mr. Williams noted yesterday, in

1711

1 discussing that the company's business risks changed
2 from three to four as a result of the power
3 difficulties in the Pacific Northwest in the early
4 part of this decade. He also noted that, in 2004,
5 the business risk changed from four to five. What he
6 didn't say was that that was due to a --

7 MR. WOOD: Your Honor, I'm going to object
8 again. There is nothing about this testimony that
9 relates to the oral supplemental. I wasn't aware
10 that witnesses got to say who's going to be last and
11 let me comment on every answer on cross-examination
12 that somebody raised. Mr. Williams did not talk
13 about the changes to the risk profile in his oral
14 supplemental testimony.

15 JUDGE RENDAHL: Mr. ffitch.

16 MR. FFITCH: Your Honor, it's my
17 recollection this issue was addressed by Mr.
18 Williams. We did not intend to go beyond the scope
19 of his testimony. I think it's related to his
20 testimony. I could take another look at it right
21 now, but --

22 JUDGE RENDAHL: I recall the discussion of
23 the change in the business risk profile in response
24 to Bench questions, not in the oral rebuttal.

25 MR. FFITCH: Well, I'm looking at sort of

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1 the informal written handout that we received from
2 PacifiCorp with respect to Mr. Williams' testimony.
3 It certainly addresses business profile.

4 JUDGE RENDAHL: But I think the specific
5 testimony that Mr. Hill is giving relates to some
6 Bench questions, not to the general topic of risk
7 profile.

8 MR. FFITCH: I guess our view, Your Honor,
9 would be that this is part of the answer to whether
10 Public Counsel's recommendation would result in a
11 bond rating downgrade. This is sort of a follow on
12 to that, which was the gist of Mr. Williams'
13 testimony. He does talk about business profile
14 rankings in the context of making that assertion
15 about our recommendation, so I think it's legitimate
16 for Mr. Hill to address this and I think it's helpful
17 to the Commission. And I don't think these sort of
18 hypertechnical objections from Mr. Wood are helpful
19 to the record. These issues have been discussed,
20 they're going to be considered by the Commission, and
21 I think it's within the scope and the general thrust
22 of Mr. Williams' direct testimony.

23 JUDGE RENDAHL: Thank you. We'll be off the
24 record for a moment.

25 (Discussion off the record.)

1713

1 JUDGE RENDAHL: All right. The company's
2 objection is overruled. Mr. Williams did address the
3 broad area of risk profile in his oral rebuttal and,
4 in a sense, opened the door to this questioning.

5 But we do have a timing question for the
6 parties. That is, how much -- how much farther, Mr.
7 Ffitch, how much more do you have for this witness,
8 and Mr. Wood, how much -- or Mr. Keyes, how much
9 cross would you have for this witness? Whether we
10 need to take a lunch break and come back? Do we have
11 an hour's worth? I understand there's some questions
12 from the Bench and I don't want to tax the court
13 reporter at this point.

14 MR. FFITCH: Your Honor, I believe we were
15 just getting to the end of that section. I had a
16 couple more questions after that.

17 JUDGE RENDAHL: So another 15 minutes or so?

18 MR. FFITCH: Probably at the most, Your
19 Honor.

20 JUDGE RENDAHL: All right. And for the
21 company, about how much cross do you estimate at this
22 point?

23 MR. WOOD: Probably 10 or 15 minutes, Your
24 Honor.

25 JUDGE RENDAHL: So a good half hour, and

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1 then we have questions from the Bench. No questions
2 from the Bench? So should we just -- Barbara, can
3 you make it for another half an hour? Okay. Let's
4 keep going, Mr. ffitch.

5 MR. FFITCH: Okay. I'll try to be
6 efficient, Your Honor.

7 Q. Mr. Hill, there was an objection when you
8 were discussing the business risk ratings of Standard
9 & Poor's. Would you -- do you want to complete your
10 answer?

11 A. The only point I was trying to make, and
12 I'll be brief, is that the business risk changed from
13 four to five was not the result of any sort of change
14 in the business risk of PacifiCorp. Rather, it was a
15 change in the way that Standard & Poor's calculates
16 the business risk. They had been using this one to
17 ten scale for a number of years, and prior to 2004,
18 they realized that the bell-shaped -- the curve for
19 the industry was skewed to the low side. In other
20 words, it was -- it wasn't a bell-shaped curve. Most
21 of the business profiles they found were below five,
22 and they said this doesn't make any sense, we should
23 rejigger this so this distribution looks more
24 normalized, the risky companies are indeed of a ten
25 and the lowest companies are down at one.

1715

1 So when they did that, quite a few
2 companies, especially the integrated,
3 fully-integrated electricians moved from three to four
4 or four to five, but that was because of Standard &
5 Poor's sort of reevaluating where their numbers ought
6 to be, rather than any change in business risk. And
7 they make that very clear in their publication of
8 June 2nd, 2004. So I just didn't want the Commission
9 to be of a mind that PacifiCorp's sliding downhill as
10 far as business risk goes. That's not the case.

11 Q. Now, Mr. Hill, you've referred to some
12 testimony by Mr. Williams yesterday regarding the
13 benchmark measurements, financial measurements for
14 business profile five for setting bond ratings?

15 A. Yes.

16 Q. Do the company's own numbers presented in
17 this case meet those financial benchmarks that Mr.
18 Williams discussed yesterday?

19 A. No, again, in response to Bench Request 13,
20 Mr. Williams calculates in the same fashion the three
21 financial metrics that he calculated for both the
22 Staff and for Public Counsel, and the company's rate
23 request passes two of those tests and fails one.

24 Q. Can you specify which of those measurements?

25 A. I believe the debt to capital ratio, it

1716

1 fails.

2 MR. FFITCH: All right. May I have a
3 moment, Your Honor?

4 JUDGE RENDAHL: You may. Be off the record
5 for a moment.

6 (Recess taken.)

7 JUDGE RENDAHL: Let's be back on the record.

8 MR. FFITCH: Your Honor, those are all the
9 questions we have on oral direct for Mr. Hill. I
10 wanted to offer, if I haven't already, Exhibit 117,
11 which is Staff Data Request 22, it's the company
12 response to Staff Data Request 22.

13 JUDGE RENDAHL: Mr. Wood or Mr. Keyes, is
14 there any objection to admitting what's been marked
15 as Exhibit 117?

16 MR. KEYES: No objection.

17 JUDGE RENDAHL: All right. Exhibit 117 will
18 be admitted.

19 MR. FFITCH: Mr. Hill's available for
20 cross-examination.

21 JUDGE RENDAHL: All right.

22

23 C R O S S - E X A M I N A T I O N

24 BY MR. WOOD:

25 Q. Mr. Hill, I'll try to keep this short,

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1 because I suspect that will make everyone happy.
2 First, you made a couple of criticisms of Mr.
3 Williams' calculations of credit matrixes, and I
4 wanted to touch on a couple that I'm in a position to
5 verify at this time.

6 Could you turn back to your Exhibit 117, the
7 tab that you have picked for off-balance sheet
8 imputed debt?

9 A. I'm there.

10 Q. Okay. You acknowledge there that Standard &
11 Poor's does apply off-balance sheet imputed debt in
12 its matrixes; correct?

13 A. It says it does. It's not clear to me what
14 the actual result of that is. I think it's, to use
15 vernacular, it's kind of a wiggly adjustment.

16 Q. Let's turn to the language that you have
17 marked. Your contention, I take it, is that Standard
18 & Poor's has added to the balance sheet not \$570
19 million in imputed debt, but only one-half of that
20 amount; is that your testimony?

21 A. That's my understanding of what Standard &
22 Poor's means when they say it has a 50 percent risk
23 factor.

24 Q. Okay. Let me read very slowly something
25 from that very paragraph. Does it say that Standard

1718

1 & Poor's rating services has added about 570 million
2 to the utility's balance sheet that predominantly
3 reflects the long-term power purchase agreements and
4 operating leases?

5 A. Yes.

6 Q. And does the next sentence explain how that
7 balance sheet addition was computed?

8 A. Well, you could read it that way. I read it
9 the other way.

10 Q. Okay. I assume the company ought to be in a
11 good position to know how much was added, shouldn't
12 it?

13 A. Ought to be.

14 Q. Okay. You also testified that the
15 calculations by Mr. Williams were sensitive to the
16 allocation percentage that he applied to Washington;
17 correct?

18 A. Right.

19 Q. Didn't Mr. Williams, in fact, in his metrics
20 calculations, apply the same percentage allocation to
21 Washington as in the company's testimony to assure
22 that the Washington results would be applied to an
23 entire 100 percent of the company's rate base, rather
24 than having a hole in the rate base?

25 A. I don't know what his intent was.

1719

1 Q. Okay. Is it quite possible that if the --
2 if the -- if throughout -- through differing
3 allocation approaches the return is allowed on less
4 than 100 percent of rate base, that the metrics could
5 actually be worse?

6 A. Well, I think that's certainly true, and the
7 opposite is true, also.

8 Q. Okay. Discussing Exhibit 73, you note that
9 the company, during a period starting in 2001, I
10 believe --

11 MR. FFITCH: Excuse me, Your Honor. I want
12 to check whether Counsel's referring to Exhibit 74,
13 or actually to 73, which I don't think was discussed
14 earlier.

15 MR. WOOD: I'm sorry, I'm referring to 74,
16 which is PacifiCorp response to Staff Data Request
17 Number 113. Thank you.

18 Q. You discussed the company's ratios during
19 the period beginning 2001. Was this the same period
20 in which Scottish Power had to suspend the dividend
21 payment from PacifiCorp?

22 A. Yes, there were financial difficulties in
23 the early part of the decade, I believe I refer to
24 that, but it's also noteworthy to note that the
25 latest numbers are September 2005, and Public

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1 Counsel's metrics are above those.

2 Q. Is this the period in which Scottish Power
3 is pumping one-half billion dollars of additional
4 equity into the company?

5 A. Is what the period?

6 Q. The 2005 period you're referring to?

7 A. In part.

8 Q. And do the credit reports not indicate that
9 PacifiCorp's bond rating has been supported in
10 substantial part by the good bond rating and metrics
11 of Scottish Power?

12 A. Right, and that's a concern that Public
13 Counsel has about the not so good bond rating of
14 MEHC.

15 Q. And would it be your testimony that the
16 Commission should, in setting its rates and
17 considering rating metrics, assume that PacifiCorp
18 should continue to be supported by other companies to
19 maintain their credit ratings?

20 A. I don't know what you mean.

21 Q. Should the Commission set rates assuming
22 that Scottish Power or somebody else will continue to
23 assist the company to remain -- to maintain high
24 credit ratings?

25 A. I think that's probably outside the scope of

1721

1 what the Commission ought to do. They ought to set
2 rates based on cost. And in order to do that, they
3 need to use a double leverage capital structure.

4 Q. Okay. You referred to -- you talked about
5 your formula and the correction of your formula. Was
6 that -- I take it you went back and looked at Dr.
7 Morin's text?

8 A. Yes, I did.

9 Q. Do you have a copy with you?

10 A. I do not. I believe the Commissioner does.

11 Q. I think I do here. Let me ask you first --

12 MR. FFITCH: Your Honor, if the witness is
13 going to be asked about this text, could he be
14 provided with a copy?

15 MR. WOOD: Absolutely. I wasn't immediately
16 going to ask him.

17 COMMISSIONER JONES: I reluctantly give up
18 my only copy of Mr. Morin's text, okay. This is the
19 only time I'm going to do it.

20 MR. FFITCH: Thank you, Your Honor.

21 Q. As an alternative to your formula, I should
22 just ask, you mentioned Mr. Rothschild's computation
23 of equity adders. Are you claiming that you have
24 reviewed those studies and adopt them as your own?

25 A. No, I'm not making that claim at all, but I

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1 understand that to be Mr. Elgin's testimony, and I've
2 done studies on my own in the Texas restructuring in
3 2000, which came up with similar results, four basis
4 points for one percent equity.

5 Q. You're not in a position to vouch for or
6 against the actual work of Mr. Rothschild on this
7 issue? Excuse me. You don't know whether he did it
8 -- you've never seen his work on that and his
9 background, have you?

10 A. That's correct.

11 Q. Okay. You stated that the company changed
12 from a rating position four to five was the result of
13 a change in standards by Standard & Poor's; is that
14 correct?

15 A. Not exactly. It was a result of a change in
16 the way that Standard & Poor's displayed the business
17 ranking for the entire utility industry.

18 Q. Okay. You couldn't make a similar claim
19 about its additional downgrade from three to four,
20 could you?

21 A. No.

22 Q. Okay. And finally, you stated, I believe,
23 that there should be no reduction in the business
24 risk of PacifiCorp for double leveraging, because
25 that was a reasonable methodology; correct?

1 A. Generally, I would agree with that.

2 Q. Okay. I just wanted to ask you, because
3 we've looked at this, the book that you went and
4 checked your formula in, Dr. Morin, and could you
5 turn to page 41, where he discusses double leverage?

6 A. Forty-one?

7 Q. Four-eighty-one. I'm sorry. I hope your
8 edition has the same pagination.

9 A. I'm sure it does.

10 Q. Is this the end of the chapter, at 481?

11 A. I'm sorry. Yes.

12 Q. Okay. Unlike some economists, he gets to
13 the point. He does summarize the conclusion. Would
14 you read the summary paragraph?

15 A. Quoting from Dr. Morin's book, Chapter 20,
16 Double Leverage, end of chapter: In summary, the
17 double leverage adjustment has serious conceptual and
18 practical limitations.

19 JUDGE RENDAHL: When you're reading, if you
20 could slow down, that would be great.

21 THE WITNESS: Okay. And violates basic
22 notions of finance, economics and fairness. The
23 assumptions which underlie its use are questionable,
24 if not unrealistic. The approach should not be used
25 in regulatory proceedings.

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1 MR. WOOD: I have no other questions, Your
2 Honor.

3 JUDGE RENDAHL: Is there anything further
4 for this witness, Mr. ffitch?

5 MR. FFITCH: Just one question.

6

7 R E D I R E C T E X A M I N A T I O N

8 BY MR. FFITCH:

9 Q. Mr. Hill, do you agree with Dr. Morin's
10 conclusion that you were just asked to read?

11 A. I certainly do not. There are many things
12 in this book what I think are useful. There are many
13 things with which I disagree. Dr. Morin and I have
14 testified against each other a number of times, and
15 we do disagree on many things. This is one of them.

16 Q. And can you summarize the basis for your
17 disagreement?

18 A. The basis for the disagreement is that, like
19 Dr. Vander Weide, Dr. Morin makes the broad
20 assumption that the DOTs, quote, unquote, of double
21 leverage don't attribute any higher risk to the
22 additional leverage at the parent company, and that
23 is not what my testimony says, although that's what
24 Dr. Vander Weide and Dr. Morin talk about.

25 I recognize that a 20 percent equity ratio

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1 does indeed impart additional risk, and if you're
2 going to have additional risk, you need a higher cost
3 of equity capital to recognize that risk. That was
4 what that whole beta analysis was all about. If
5 PacifiCorp was continued to be owned by Scottish
6 Power, there's not a double leverage issue in that
7 situation, we should regulate PacifiCorp as a
8 stand-alone entity, its cost of equity ought to be
9 set at 9.125.

10 If PacifiCorp goes to MEHC, there's a
11 definite double leverage issue. Its cost of equity
12 on the equity portion of its capital structure should
13 be 10.125, 100 basis points higher to recognize that
14 additional risk. And when you do that, you still
15 wind up with a lower cost of capital. So that's the
16 basis of the difference.

17 Both Dr. Vander Weide and Dr. Morin make the
18 broad assumption that folks like me are not going to
19 recognize additional risk at the parent company
20 level. That's not what I've done.

21 MR. FFITCH: Thank you. Those are all my
22 questions, Your Honor.

23 JUDGE RENDAHL: Mr. Hill, can you state into
24 the record the title of the book by Mr. Morin?

25 THE WITNESS: Dr. Morin's text is entitled

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1 Regulatory Finance Utilities Cost Of Capital.

2 JUDGE RENDAHL: And is there an edition
3 number?

4 THE WITNESS: It's Public Utilities Reports
5 1994. There's only one previous edition, that was
6 '84. And he says there's a new one coming out.

7 JUDGE RENDAHL: We'll just have to wait with
8 bated breath for that one.

9 THE WITNESS: With bated breath.

10 MR. WOOD: In the meanwhile, it's important
11 that Commissioner Jones recover his copy.

12 JUDGE RENDAHL: That's right.

13 THE WITNESS: I'll tear out that one page.

14 COMMISSIONER JONES: I have no questions,
15 but that's all I'm interested in, is getting my copy
16 back.

17 JUDGE RENDAHL: Is there anything further
18 for Mr. Hill? All right. With that, Mr. Hill, thank
19 you very much for appearing today.

20 THE WITNESS: Yes, ma'am.

21 JUDGE RENDAHL: And you may step down.

22 Before we go off the record, we have a few
23 housekeeping details. The company has waived cross
24 for Mr. Effron and Mr. Falkenberg, and we do have to
25 address Mr. Effron's supplemental testimony. Is

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1 there any opposition to admitting into the record Mr.
2 Effron's supplemental testimony, marked as 296-T and
3 297?

4 MR. KEYES: No, there is not.

5 JUDGE RENDAHL: All right. And in addition,
6 Mr. Falkenberg's testimony begins at 491-TC. There
7 is a errata that was filed yesterday with the
8 Commission, and so with the errata, 491-T through
9 508, and then the supplemental testimony of 522 and
10 523, is there any objection?

11 MR. KEYES: No, there's not.

12 JUDGE RENDAHL: And the company had proposed
13 cross exhibits for Mr. Falkenberg for the original
14 set of 509 through 521. Is there any objection to
15 admitting those into the record?

16 MS. DAVISON: No, Your Honor.

17 JUDGE RENDAHL: All right. So with that, I
18 have two other details for the record. And Public
19 Counsel had circulated some additional exhibits for
20 Mr. Duvall, which were marked as Exhibits 357 through
21 359. Is there any objection to admitting those?

22 MR. KEYES: No, there isn't.

23 JUDGE RENDAHL: All right. Those will be
24 admitted. And then I had noticed this morning, in
25 going through my exhibit list that I'm not sure that

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1 we resolved admitting Exhibit 646, which is
2 PacifiCorp's cross exhibit for Mr. Schooley. Is
3 there any objection? That's the Staff response to
4 Bench Request Number 25. And I do note that's not a
5 full and complete copy of the bench request, and that
6 is marked as a later exhibit. Mr. Trotter.

7 MR. TROTTER: I don't have any problem with
8 that exhibit going in. The bench request, I assume,
9 will go in. We're going to take a look and see if we
10 ought to supplement that to have all the Washington
11 Utilities columns look the same. But till we do
12 that, it's fine.

13 JUDGE RENDAHL: All right. And if you do
14 choose to update that, then we'll probably have to
15 include an updated version of 646.

16 MR. TROTTER: Well, I assume it would just
17 be an updated version of the bench request. It would
18 be your choice.

19 JUDGE RENDAHL: All right.

20 MR. WOOD: I'll make just a request of Staff
21 on that, as I think has been already done. If that's
22 going to be updated, I would appreciate it if Mr.
23 Schooley could review that before submission with Mr.
24 -- at PacifiCorp, so that we won't have any wrangling
25 about the numbers at all. I believe they've been

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1 doing that to date.

2 MR. TROTTER: Well, we don't have a problem
3 with that, but we do have some questions of the
4 company's response to Bench Request 25, and we have
5 asked the company for the backup, so we're hopeful
6 that that will be provided.

7 JUDGE RENDAHL: Okay. And to the extent
8 that there are changes, I expect you all will be
9 supplementing your responses and will include those
10 in the list.

11 So in terms of exhibits, those were the
12 witness exhibits that I needed to add in. I think
13 with that, the only marked exhibits on the list are
14 the bench request responses, and we had talked about
15 deferring a date -- talking about a date later.

16 MR. TROTTER: Your Honor, Staff can commit
17 to stating objections to bench requests that have
18 been received by today by a week from today, and if
19 you can give us like three business days on ones that
20 come in after today, I think that's reasonable. If
21 we can't make that, then we'll let you know.

22 JUDGE RENDAHL: Okay. So you will identify
23 any concerns you have with bench requests that have
24 been submitted up through today by next Friday, the
25 10th?

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1 MR. TROTTER: Yes.

2 JUDGE RENDAHL: And then, what was the other
3 part of that proposal?

4 MR. TROTTER: There are still some
5 outstanding, and we'll just do a three calendar-day
6 turnaround on those.

7 JUDGE RENDAHL: So you will let the parties
8 --

9 MR. TROTTER: Excuse me, business day.
10 Sorry, three business days turnaround on those.

11 JUDGE RENDAHL: So you will let the parties
12 and the Commission know within three business days if
13 you have any objections to other --

14 MR. TROTTER: Yes, and I assume that would
15 apply to -- I'm assuming other parties will need
16 that, as well.

17 JUDGE RENDAHL: Is that an acceptable time
18 frame for the bench request responses?

19 MR. FFITCH: Yes, Your Honor.

20 MR. KEYES: Yes, Your Honor.

21 JUDGE RENDAHL: All right. So that's what
22 we'll do with bench requests, and after that time
23 period, barring any objections, we'll admit the bench
24 requests that have been submitted by all the parties.

25 And I do have a clarification on the bench

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1 requests before I go to you, Mr. ffitch. I had
2 understood, from hearings last week or the week
3 before, that ICNU and Public Counsel and Staff wished
4 to respond to the two bench requests, 22 and 23,
5 having to do with PCAM comparisons. That was my
6 understanding, and I had reserved spots in the
7 exhibit list for that, but I'm not sure if that is
8 actually correct or not.

9 MR. TROTTER: I think the time for
10 responding may be passed. What Staff was going to do
11 was look at the company's response and then, if
12 additional information was necessary, we would file
13 it.

14 JUDGE RENDAHL: All right. So you would
15 include that within your --

16 MR. TROTTER: By next Friday.

17 JUDGE RENDAHL: -- response by next Friday?

18 MR. TROTTER: Yes.

19 JUDGE RENDAHL: And Mr. ffitch, is that your
20 proposal?

21 MR. FFITCH: Yes, Your Honor. In other
22 words, as I understand it, we're saying that we would
23 either object or file our own response, which would
24 -- to those bench requests within that same -- so
25 that would be by the 10th, since that one's already

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1 in, we would owe that one by the 10th.

2 MR. WOOD: Your Honor, I'll make the same
3 request, but because I think it will assist the
4 record and the Commission, which is that if there's a
5 concern with these data requests, and prior to the
6 parties making an objection or supplementing, if they
7 could confer and see if the parties would agree on
8 any change, this would avoid more wrangling.

9 JUDGE RENDAHL: I guess I would tend to
10 agree. I think if there are issues, if they're
11 philosophical differences, I don't know that those
12 can be resolved, but if there are data differences,
13 if you have questions about the data that the company
14 uses in its response, I would encourage the parties
15 to first work with each other before raising
16 objections.

17 But, again, if there are philosophical
18 differences, those aren't going to be resolved and
19 that's a different matter entirely, and you can also
20 argue on brief.

21 MR. FFITCH: So Your Honor, we'd be
22 perfectly happy to do that. I guess I would just add
23 a request that this procedure be available for other
24 bench requests. We're still reviewing them. Our
25 consultants are reviewing them and there may be two

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1 or three others where we might want to either object
2 or file a response that would, we believe, more --
3 well, provide our perspective on the question.

4 JUDGE RENDAHL: Okay. Well, as I understand
5 Staff's proposal, anything that has been filed up
6 through today, any bench request filed up through
7 today, you would have to confer with the company and
8 provide either your response or objection to those
9 responses by the 10th, and I guess that would go for
10 the company, to any responses by any other party to
11 bench requests that were directed to them. And then,
12 for any other outstanding bench request responses
13 after today, all parties would have three days to
14 either raise an objection or try to confer with one
15 another to come up with some agreed-to response.

16 MR. TROTTER: Your Honor, that latter time
17 limit I proposed before this consultation requirement
18 has been put in, so maybe we should just say five
19 calendar days for the second set?

20 JUDGE RENDAHL: Can the parties agree with
21 that, five calendar days after the bench request
22 response has been filed with the Commission? All
23 right. With that, I see nodding of heads and no
24 shaking, so we'll say five days.

25 The last bench request at this point on my

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1 list was Number 35. Does that correspond with all of
2 your lists? That was mine to Mr. Wrigley yesterday.

3 MR. KEYES: Yes, it does.

4 JUDGE RENDAHL: All right. And the one to
5 Mr. Schooley was withdrawn. So with that, the only
6 other item I'd like to discuss with all of you, and
7 we can do this off the record first, and then maybe
8 go back on quickly before we go off the record.

9 MS. DAVISON: Your Honor, before you do
10 that, I just had one thing to request on the bench
11 response very quickly.

12 JUDGE RENDAHL: All right. Stay on the
13 record.

14 MS. DAVISON: Regarding Bench Response 21,
15 we wanted to make the request of the company to
16 remove the months from June 2000 through June 2001 in
17 order to more accurately reflect the essentially
18 removing the effect of the Western Energy Crisis and
19 --

20 JUDGE RENDAHL: Is that the request to
21 modify Exhibit 384, or something like that?

22 MS. DAVISON: It's Mr. Widmer's Exhibit 4.
23 I'm not sure what the exact exhibit number is as it's
24 renumbered, but it's MTW-4, which was intended to
25 provide, you know, in effect, a redo with the Western

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1 Energy Crisis removed. And it's our view that the
2 company has identified those as being the months in
3 which the impacts of the energy crisis occurred.

4 And the problem is that our consultant has
5 reviewed this and he cannot make any sense of the
6 numbers. And we can talk about this and I can give
7 you his analysis, but essentially it is something
8 that is extremely difficult to do and we think that
9 it produces a cleaner response to remove the data
10 from that time period.

11 JUDGE RENDAHL: I guess I would just suggest
12 that you all work together. If you can't come up
13 with a solution, then your option is to file an
14 objection within the time period that we've stated.

15 MS. DAVISON: Thank you, Your Honor.

16 JUDGE RENDAHL: Okay. So let's be off the
17 record for a moment.

18 (Discussion off the record.)

19 (Proceedings adjourned at 12:36 p.m.)

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