

**Exhibit No. ____ (BEG-8T)
Docket No. UE-051090
MEHC Acquisition of PacifiCorp
Witness: Brent E. Gale**

**BEFORE THE
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION**

**IN THE MATTER OF THE JOINT)
APPLICATION OF MIDAMERICAN)
ENERGY HOLDINGS COMPANY AND)
PACIFICORP DBA PACIFICORP POWER &)
LIGHT COMPANY FOR AN ORDER)
AUTHORIZING PROPOSED)
TRANSACTION)**

Docket No. UE-051090

Rebuttal Testimony of Brent E. Gale

December 2005

1 **Introduction**

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

3 A. My name is Brent E. Gale. My business address is 666 Grand Avenue, Suite
4 2600, Des Moines, Iowa 50309.

5 **Q. Are you the same Brent E. Gale who previously submitted prepared direct
6 and revised direct testimony in this docket?**

7 A. Yes, I am.

8 **Q. What is the purpose of your rebuttal testimony in this proceeding?**

9 A. The purpose of my testimony is to respond to issues raised by Staff and
10 intervenors related to the standard for transaction approval, the existence of
11 benefits related to the transaction, and perceived negative impacts of the
12 transaction. I am also sponsoring additional commitments responsive to the
13 testimony of some of the Staff and intervenor witnesses.

14 **Standard for Transaction Approval**

15 **Q. On page 3 beginning at line 14 and page 8 beginning at line 2, Staff witness
16 Elgin discusses the appropriate standard to be used in determining whether
17 the Commission should approve the transaction. What is your
18 understanding of the Commission's standard as compared to the standard
19 that Mr. Elgin is proposing?**

20 A. I understand that the Commission has previously determined that the standard
21 appropriate for approval of transactions changing the ownership of utilities is a
22 "no harm to the public interest" standard. In contrast, Mr. Elgin appears to be
23 suggesting that the Commission change the standard in this case to require a

1 showing of net benefits to customers. He premises the need for this new standard
2 on his belief that ScottishPower shareholders, MEHC shareholders and PacifiCorp
3 executives will benefit from the transaction.

4 **Q. Do you view his premise as a reasonable basis for applying a different**
5 **standard to this transaction?**

6 A. No. Assuming rational parties, any transaction that involves a price negotiated by
7 a willing seller and a willing buyer will be viewed as beneficial by both the seller
8 and the buyer. The benefits contemplated by Mr. Elgin are not unique to this
9 transaction, and there is nothing unusual about this transaction to suggest it should
10 be evaluated under a different regulatory standard than has consistently been
11 applied by the Commission in the past.¹

12 **MEHC/PacifiCorp Commitments**

13 **Q. At page 10, beginning at line 10, ICNU witness Canon expresses confusion**
14 **regarding the commitments made by MEHC and PacifiCorp. What is your**
15 **response?**

16 A. Mr. Canon is creating confusion where none exists. As I explained at page 4 of
17 my direct testimony, MEHC and PacifiCorp met with numerous groups that had
18 an interest in this transaction and asked them to identify their risks and concerns.
19 Some of the risks and concerns that they identified were similar to concerns that

¹ Moreover, it is not uncommon for critical members of management to receive incremental compensation or retention payments in exchange for foregoing other opportunities and remaining to operate the business as the transaction proceeds through the approval process. It should be noted that the retention payments in this transaction will be paid by ScottishPower and will not impact regulated revenue requirements.

1 had been raised and addressed in the ScottishPower transaction. Therefore,
2 MEHC and PacifiCorp, through my direct testimony, proposed adopting or
3 continuing commitments and conditions required by one or more of the regulatory
4 commissions in the ScottishPower transaction.² These Commitments (now
5 numbered for convenience) 1 through 34 are those referenced as the “existing
6 commitments.” Refer to my Exhibit No. ____ (BEG-10).

7 The commitments previously sponsored by MEHC witness Abel (now
8 numbered 35 through 50 in my Exhibit No. ____ (BEG-10)) were not commitments
9 or conditions in the ScottishPower transaction but are responsive to concerns
10 expressed in the meetings with interested groups. These represent “new
11 commitments” as compared to the ScottishPower transaction.

12 Mr. Canon implies that continuation of existing commitments is not a
13 benefit to customers. The fact that interested groups expressed concern for
14 continuation of the existing commitments suggests otherwise. Moreover, if
15 Mr. Canon were correct, there would seem to be no objection to eliminating all of
16 those commitments. But, as indicated by other witnesses in this case, many of
17 those commitments are critical to address concerns that are important to them.

18 Mr. Canon also suggests that some of the new commitments are existing
19 commitments. He is incorrect – these were not commitments in the
20 ScottishPower transaction. Most are completely new commitments. A few, such
21 as the renewable energy commitment, constitute an expansion of an existing

² It is important to recognize that no state commission in the ScottishPower transaction required all 34 of the commitments. Since MEHC and PacifiCorp are extending these commitments to *all* states, some of these 34 commitments will be “new” in each jurisdiction.

1 PacifiCorp goal. And still others, such as the commitment regarding customer
2 service standards, constitute an extension of existing commitments that might not
3 otherwise occur without this transaction.

4 **Benefits of the Transaction**

5 Infrastructure Investments

6 **Q. Several witnesses (Staff witness Elgin at page 10, lines 8-16, ICNU witness**
7 **Canon at pages 5 and 11-14 and Public Counsel witness Dittmer at page 7)**
8 **have suggested that many of the benefits cited by the Joint Applicants are**
9 **merely actions that would be required of a prudent utility or were already**
10 **planned by PacifiCorp. What is your response?**

11 A. I have three observations.

12 First, a utility, or any business, will (or should) perform the minimum
13 functions required by law, which in most cases will be deemed prudent. This
14 approach to conducting business focuses on the short-term horizon. As a
15 consequence, the approach may fail to identify opportunities where doing *more*
16 than the minimum will reduce long-term costs for customers or result in achieving
17 benefits sooner. The emissions control investments that MEHC is proposing are
18 an example of deploying investment dollars (actually somewhat fewer dollars
19 than PacifiCorp planned) in a manner that both reduces long-term costs and
20 achieves benefits (*e.g.*, emissions reductions) sooner than PacifiCorp's current,
21 prudent plans.

22 Second, although planning, assumptions and goal-setting may all be
23 accomplished in a prudent manner, the absence of available capital may thwart

1 the achievement of the goal. PacifiCorp's renewable energy goal of 1400 MW of
2 incremental supply by 2015 is an example. The planning, assumptions and goal
3 all appear reasonable and prudent for a capital-constrained utility. But the capital
4 constraint means that PacifiCorp's plan for achieving the goal depends upon
5 others building the renewable facilities and some of the necessary transmission.
6 MEHC believes that if the capital constraint can be removed (such as through this
7 acquisition), the achievement of the goal is more likely because PacifiCorp can
8 make firm plans to build the transmission needed for delivery of the renewable
9 energy. MEHC therefore committed to the Path C and Walla Walla transmission
10 projects. Moreover, by virtue of its extensive experience with renewable energy,
11 it is MEHC's view that having a utility own/operate option also increases the
12 likelihood of meeting the goal and doing so in a cost-effective manner. This
13 option becomes a possibility when the capital constraint is removed; it is not
14 available under current ScottishPower ownership. None of this means that
15 PacifiCorp's plans and goals are imprudent, but capital constraints may render
16 PacifiCorp unable to achieve the goal in the desired timeframe.

17 Third, in a particular situation, an action that is prudent for one utility
18 could be disastrous for another. Again using the renewable goal as an example, a
19 decision to deploy capital to own/operate a new wind resource might be a prudent
20 choice for a utility in a strong financial position capable of raising the upfront
21 capital needed at a relatively low cost, capable of using the production tax credit,
22 or able to wait to recoup its investment over a period of twenty years or more.
23 That same decision could be an undesirable choice for a company with a high

1 debt ratio, a need to recoup its investment quickly, or an inability to use the
2 production tax credit.

3 **Q. What about the claim that the infrastructure projects committed to by**
4 **MEHC were already planned by PacifiCorp?**

5 A. PacifiCorp's plans, as provided to MEHC, did not contain:

- 6 • the Walla Walla and Path C transmission investments,
- 7 • the full amount of Asset Risk Program investment,
- 8 • the local transmission risk project investment,
- 9 • the increase in the Accelerated Distribution Circuit program,
- 10 • the extension of the Saving SAIDI program,
- 11 • the DSM study, or
- 12 • the commitment for an incremental 100 MW of wind energy within one year
13 of closing.

14 Moreover, while PacifiCorp had expected expenditures in its plan for
15 emissions reductions at existing coal-fired generating plants, it had no definitive
16 plans for those expenditures. MEHC was able to develop those plans and, in the
17 process, refocus and reduce the expected expenditures while achieving results
18 sooner. This is an example of MEHC's approach to investment: focusing upon
19 ways to employ capital more efficiently to reduce long-term revenue
20 requirements, while having a positive (or at least no negative) impact upon
21 benefits.

22 The mix of infrastructure projects offered by MEHC also provides
23 regulators and parties a foreshadowing of the long-run perspective that MEHC

1 will bring to PacifiCorp. This is a perspective that cannot easily be achieved by a
2 company that must be concerned about the level of quarterly dividends. These are
3 projects that provide long-term benefits (including cost reductions) to customers,
4 but that might very well not be undertaken by a prudent utility with a capital
5 constraint or without an extended long-run perspective.

6 It is also important to recognize that many projects in PacifiCorp's capital
7 plan were just that: a *plan*. Inclusion of a project in the capital plan by no means
8 indicates that ScottishPower had committed to finance that project. Corporate
9 approval of "less than \$6 million" for a small aspect of a \$196 million project, as
10 cited by ICNU witness Canon at page 13, lines 8-17, can hardly be argued to
11 constitute a "commitment" to the entire project.

12 **Q. Could you provide an example of a project subject to a MEHC commitment**
13 **that was not included in the plan previously provided to MEHC by**
14 **PacifiCorp?**

15 A. Yes. The Path C transmission project was not included in PacifiCorp's capital
16 plan as provided to MEHC. After reviewing PacifiCorp's planned generation
17 additions, the potential transmission projects that were not included in
18 PacifiCorp's plan, and the likelihood of PacifiCorp achieving its 1400 MW
19 renewable energy goal, MEHC, in consultation with the PacifiCorp management
20 team, concluded that the Path C investment would provide desirable long-term
21 benefits.

22 This project is a perfect example of the type of investment MEHC will
23 support at PacifiCorp. It is a project that provides future benefits to PacifiCorp

1 customers, but also requires a significant upfront expenditure. The Path C project
2 will not only increase transfer capability between the eastern and western portions
3 of PacifiCorp's system, it will also (1) allow two future generation additions to be
4 delayed or eliminated at significant reduction in expected revenue requirements,
5 (2) provide increased access to Idaho wind resources, and (3) increase reliability.
6 Indeed, when PacifiCorp evaluated this project in its November 2005 IRP Update,
7 it was determined the project had a twenty-year present value of revenue
8 requirement benefit of approximately \$186 million.

9 **Q. What benefits are provided by MEHC regarding those infrastructure**
10 **investments that were already included in PacifiCorp's capital plan?**

11 A. As I mentioned, the investments MEHC has committed to make to reduce
12 emissions at PacifiCorp's coal-fired plants provide a good example. Although
13 PacifiCorp had included expenditure amounts in its capital plan related to
14 assumed future emissions reductions, no definitive equipment plan had been
15 developed and no approval had been given by ScottishPower for the expenditures.

16 MEHC's investment commitment is based on specific equipment additions
17 on a specific timeline, providing much more certainty that the needed investments
18 will actually occur on a timely basis. MEHC's plan for compliance with
19 anticipated federal requirements should also minimize the cost of that compliance
20 by (1) allowing for purchase of equipment at lower costs because the demand for
21 that equipment will not be as great as it will be when industry is confronted with a
22 legislated or regulatory deadline, and (2) minimizing related outages through

1 scheduling equipment installation during already scheduled outages or
2 maintenance.

3 Indeed, purchasing and installing the equipment now provides greater
4 assurance that compliance will occur in a timely fashion. If the current demand
5 for and lack of availability of wind turbines are any indication, it is reasonable to
6 believe that sufficient emissions reduction equipment may not be available when
7 it is in highest demand.

8 Because MEHC takes a long-run view, its long-term planning tends to be
9 more definitive than that of many other companies. The net present value of the
10 benefits of reduced purchase power costs resulting from the minimization of
11 outages is \$80 million, as shown in Exhibit No. ____ (BEG-9).

12 **Q. At page 11, beginning at line 20, ICNU witness Canon states that the lack of a**
13 **timeline related to MEHC's investment commitments indicates they are not**
14 **firm, enforceable commitments. Is MEHC willing to provide a timeline for**
15 **these investments?**

16 A. Yes. MEHC has provided target completion dates for the proposed transmission
17 projects in the Consolidated List of Commitments included as part of the
18 Stipulation filed in Utah Docket No. 05-035-54 on November 18, 2005, which is
19 my previously referenced Exhibit No. ____ (BEG-10). The Path C project target
20 date included in those commitments is 2010, the Mona-Oquirrh project date is
21 2011, and the Walla Walla-Yakima project date is 2010.

22 **Q. ICNU witness Canon also expresses concern at page 14, lines 12-20 that**
23 **accepting an investment as a customer benefit creates the impression that the**

1 **investment has been found to be appropriate. Do MEHC and PacifiCorp**
2 **regard approval of the transaction as also approving its investment**
3 **commitments?**

4 A. No. The commitments are binding only upon MEHC, PacifiCorp and, where
5 noted, their affiliates. We have not asked for, and are not seeking, Commission
6 approval of the prudence of the investments or the ratemaking treatment. Those
7 approvals will be sought in appropriate proceedings after approval of the
8 transaction.

9 The commitments have been offered by MEHC and PacifiCorp to ensure
10 that the transaction provides benefits to customers, addresses identified concerns
11 and risks, creates no harm to the public interest, and otherwise satisfies the
12 regulatory requirements for approval of the transaction. The purpose of the
13 investment commitments is to provide evidence of MEHC's process for assessing,
14 and willingness to make, investments in PacifiCorp's infrastructure. Although
15 our preliminary analysis indicates that the investments do provide net benefits
16 (*i.e.*, reduce net revenue requirements, as noted in Exhibit No. ___(BEG-9)), final
17 analysis of the benefits and the authorization of the recovery of the costs will be
18 the subject of rate and other proceedings where a full record will be made.

19 MEHC and PacifiCorp will not allege in any future proceeding before the
20 Commission or the courts that by approving the transaction the Commission or
21 any party has agreed to waive any right to assert or adopt any position regarding
22 the prudence, just and reasonable character, rate or ratemaking impact or

1 treatment, or public interest as they deem appropriate pertaining to the
2 commitments.

3 **Q. At page 15 of his testimony, ICNU witness Canon suggests that the renewable**
4 **energy commitment is simply committing to a plan that is already in place.**
5 **Is he correct?**

6 A. No, he is not. As I have already explained, PacifiCorp had a goal of 1400 MW of
7 cost-effective renewable energy by 2015. A goal is not an executable plan,
8 however. MEHC has made commitments to invest in transmission, to analyze
9 utility own/operate options for renewables, and to have 100 MW of incremental
10 renewables in place within one year after closing – all to turn the goal into a
11 concrete executable plan to achieve the objective.

12 It should also be noted that MEHC modified PacifiCorp's goal to be *at*
13 *least* 1400 MW and to clarify that not all of the renewable energy will come from
14 wind. This is reflected in Commitment 40 of Exhibit No. ___(BEG-10).

15 **Q. Mr. Canon also complains that the advanced coal technology commitment is**
16 **nebulous. What is your response?**

17 A. The use of any coal technology is controversial and the use of advanced coal
18 technology such as IGCC is only now approaching commercial viability. As a
19 result, MEHC did not believe it appropriate to presume how it should approach
20 the use of advanced coal technology in PacifiCorp's service territory until it
21 received more input from interested parties. After conducting two formal IGCC
22 information sessions with interested parties and after receiving input in all states,
23 MEHC and PacifiCorp have been able to develop more definitive commitments

1 regarding IGCC. Those are Commitments U 15 and U 16 of Exhibit
2 No. ___(BEG-10).

3 Extension of Customer Service Standards

4 **Q. Public Counsel witness Dittmer at page 7, lines 25-28 states that he does not**
5 **consider the extension of “existing” customer service standards and**
6 **performance guarantees a benefit.**

7 A. As clarified by Exhibit No. ___(BEG-10), Commitments 1 and 46, MEHC and
8 PacifiCorp are committing not to seek changes to the standards and guarantees
9 prior to March 31, 2008. This is a benefit to all those who value the standards and
10 guarantees as they exist and were concerned that the standards and guarantees
11 would be modified by MEHC. Moreover, MEHC and PacifiCorp, through
12 Commitment 46, are committing to a nearly 4-year extension of the standards and
13 guarantees with modifications only as approved by the Commission and no
14 elimination without Commission approval. This is a commitment that did not,
15 and perhaps would not, exist without this transaction. It is a benefit to those who
16 value the standards and guarantees and provides for Commission control over the
17 elimination of the standards and guarantees – in essence, an extension as long as
18 the Commission determines the standards and guarantees to be reasonable.

19 Indeed, the implication of Mr. Dittmer’s testimony is that the standards
20 and guarantees themselves have no value. If there is no value to a commitment to
21 continue the customer service standards and performance guarantees, then, *ipso*
22 *facto*, there would be no value to having them in the first place.

1 Rate Stability Issues

2 **Q. ICNU witness Canon, beginning at line 18 on page 3 of his testimony,**
3 **concludes that because it may be difficult to ensure that commitments are**
4 **actually honored after a transaction is approved, rate credits or rate freezes**
5 **are the preferred method for providing benefits to customers associated with**
6 **a change in utility ownership. Why has MEHC elected not to offer rates**
7 **credits or freezes?**

8 A. As PacifiCorp witness Johansen has testified, PacifiCorp is in a situation where it
9 will need to make significant investments over the next several years. In order for
10 PacifiCorp to be in a position to provide rate credits or even rate freezes,
11 substantial synergies and cost reductions would need to be realized. Such
12 synergies are not expected from this transaction since the transaction is an
13 acquisition and continuation of an on-going business, not a merger.

14 **Q. Please explain.**

15 A. Most utility transactions involve mergers of two utilities, either with or without
16 holding companies. The transacting utilities almost universally attempt to justify
17 the transaction on the basis of cost savings through “synergies” or “best
18 practices.” What this typically means is that the merging utilities claim to be able
19 to reduce costs through elimination of personnel, functions or service providers.
20 These cost reductions may or may not be realized. What is realized, however, is
21 the effective elimination of both merging utilities and the creation of a new entity,
22 regardless of the name selected for that entity. The consequence of creating a

1 new entity is almost unavoidably a period of dislocation and sub-optimum
2 operation.

3 MEHC does not engage in utility mergers. Instead, MEHC *acquires* a
4 utility and does not merge it with an existing MEHC business platform. An
5 acquisition permits MEHC to keep the utility's existing management and
6 operations largely in place and avoids the period of dislocation and sub-optimum
7 operation. In other words, the acquisition approach facilitates business continuity,
8 which is a desirable objective when the acquired company has good management
9 and good customer satisfaction. MEHC believes that this approach also facilitates
10 the acquired utility having a more local focus, responsive to its particular
11 constituency and customers.

12 The tradeoff for this business continuity, however, is that there are few
13 apparent opportunities for cost reductions. It is therefore not anticipated that
14 significant synergies will be realized. Even if MEHC and PacifiCorp are able to
15 accomplish greater cost reductions than those guaranteed in the Joint Application,
16 it is not likely they would be large enough to allow for rate reductions or even rate
17 freezes, if PacifiCorp is to be allowed to earn a reasonable return.

18 **Q. Public Counsel witness Dittmer at page 11 of his testimony refers to a**
19 **number of potentially shared services. Given your discussion of business**
20 **continuity as an objective, please discuss the functions that will continue to**
21 **be performed at PacifiCorp.**

22 A. PacifiCorp will have its own management team, accounting function,
23 administrative services function, advertising function, billing/call center/customer

1 services function, financial staff, human resources personnel, legal services,
2 medical benefit plans, purchasing function, regulatory/legislative functions, and
3 strategic planning function. PacifiCorp will also have its own environmental and
4 tax personnel.

5 MEHC will provide oversight for many of these functions; coordinate
6 functions such as environmental, tax and corporate strategy; and provide
7 assistance/support.

8 **Q. Mr. Dittmer at pages 31 and 32 of his testimony expresses surprise that**
9 **MEHC is not claiming synergies from this transaction. What is your**
10 **response?**

11 A. I have previously noted that this transaction is not a merger; it is an acquisition
12 where business continuity is an objective. In utility mergers, particularly those
13 involving utilities located in the same state or otherwise with overlapping
14 territories, it is often possible to reduce or eliminate the costs of some facilities,
15 personnel and service providers without impacting service quality or
16 responsiveness to local conditions. For example, in such mergers, accounting,
17 administrative, legal, human resources, and regulatory services can be combined
18 in the merged company. As the costs of these services would then be spread over
19 a larger amount of output, these costs could properly be considered a factor in
20 determining economies of scale resulting from the merger.

21 In the case of the proposed acquisition of PacifiCorp, however,
22 MidAmerican Energy Company (“MEC”) and PacifiCorp do not have
23 overlapping, or even contiguous, franchises. Accordingly, MEHC believes that

1 the two utility subsidiaries will need to maintain their current separate facilities,
2 personnel and service providers in order to maintain service quality and
3 responsiveness to local conditions. In this sense, the respective facilities of the
4 two utilities are not duplicative, and economies of scale would not be expected to
5 result from the acquisition as the underlying costs of providing electric service
6 will not substantially change as a result of the acquisition.

7 **Q. Will PacifiCorp be the first acquisition by MEHC where the acquired**
8 **company was not merged with another subsidiary providing similar**
9 **services?**

10 A. No. For example, Kern River Gas Transmission Company is an interstate natural
11 gas pipeline that provides transportation services from the Rocky Mountain area
12 to California. That subsidiary of MEHC has not been merged with Northern
13 Natural Gas Company, an interstate natural gas pipeline subsidiary that provides
14 transportation services primarily in and around the Mississippi River area. Each
15 of these interstate pipeline subsidiaries serves different geographic areas with
16 differing customer characteristics. Each has its own management team,
17 administrative services staff and operations staff. The two pipelines exchange
18 ideas and information, as we would expect PacifiCorp and MEC to do, but do not
19 share physical or customer synergies that would yield material benefits if the
20 organizations were merged.

21 MEHC prefers to acquire companies that are well run and well managed,
22 where the business can continue seamlessly after the acquisition, and existing
23 management can remain in place to continue to operate the business. That was

1 the situation with Kern River and Northern Natural, and it is how we view the
2 situation with PacifiCorp.

3 **Q. Does the fact that MEHC is not claiming synergies to justify this acquisition**
4 **constitute an acknowledgement that there will be none?**

5 A. No. There may be some cost savings possible in the acquisition of common
6 services, materials and supplies. We would also expect cost savings and
7 efficiency improvements as a result of the information exchange. But we cannot
8 quantify these opportunities until after MEHC better understands the operations
9 and circumstances of PacifiCorp, and that cannot occur until MEHC owns
10 PacifiCorp. Regulatory credibility is extremely important to MEHC, as MEHC
11 witness Abel testified, and we try not to make claims that we cannot substantiate
12 or commitments that we cannot keep. (In this regard, it is worth noting
13 Mr. Dittmer's own professed skepticism regarding the overstated claims of
14 synergistic savings in other merger transactions.) Until we can be more certain
15 what, if any, synergies can be achieved, we will not make a commitment
16 regarding that achievement.

17 **Q. Mr. Dittmer also mentions savings attributable to best practices. Why has**
18 **MEHC not quantified expected savings from this source?**

19 A. As I testified above, there may be cost savings from the exchange of information
20 between MEC and PacifiCorp. But as I also noted in my direct testimony, both
21 utilities are very highly rated in terms of customer satisfaction, have among the
22 lowest delivered coal costs, and rank well in other important practices. Without

1 the experience that can only be gained by operating the businesses, MEHC is not
2 able to quantify savings that can be gained by changes in business practices.

3 Reduced Cost of Debt & DSM Study

4 **Q. Both Public Counsel witness Dittmer and Staff witness Elgin attempt to**
5 **characterize MEHC benefits (such as the reduced cost of debt and**
6 **shareholder funding of the DSM study) as de minimus. How do you**
7 **respond?**

8 A. As I noted above, with the acquisition of a well-managed utility, it is unrealistic to
9 assume that large amounts of costs can be eliminated without negatively
10 impacting operations, reliability, safety, or customer satisfaction. We have
11 identified the areas of debt issuance costs and corporate overheads as areas where
12 we can bring cost reductions without negatively impacting operations or customer
13 satisfaction. While those cost reductions may not be as large as reductions
14 *claimed (i.e., hoped for)* by utilities engaged in mergers, they are cost reductions
15 that MEHC is confident of delivering. They are also cost reductions that can be
16 delivered without disrupting management's ability to continue with reliable
17 service and strong customer relations, which is itself a significant benefit.

18 **Potential Harms Addressed**

19 Holding Company Concerns

20 **Q. Public Counsel witness Dittmer offers a lengthy discussion regarding the**
21 ***potential* detriment to customers that could occur as a result of the economic**
22 **and political influence that could be wielded by an entity of the size and**

1 **diversity of Berkshire Hathaway. His resulting proposal at page 14, lines 19-**
2 **21 is that Berkshire Hathaway be subject to the same commitments**
3 **regarding reporting, notification and access that have been offered by**
4 **MEHC. Is his proposal acceptable to MEHC?**

5 A. By definition, any of the commitments made by MEHC or PacifiCorp with
6 respect to the affiliates of either will apply to Berkshire Hathaway after the close
7 of the transaction. Nevertheless, recognizing the importance of this issue to the
8 parties here and in other states, Exhibit No. ___(BEG-10) reflects modifications
9 to previously filed Commitment 4 that specifically apply the commitment to
10 Berkshire Hathaway. Commitment 4 pertains to access to books and records and
11 the preservation of those records.

12 Please also note that Commitment 5 by its terms also applies to make
13 Berkshire Hathaway personnel available to testify before the Commission.
14 Commitment 7 ensures compliance with applicable statutes and regulations
15 regarding affiliate transaction reporting. Commitment U 20, regarding the filing
16 of a letter by Berkshire Hathaway committing to be bound by the applicable
17 commitments, could also be adopted in Washington, if desired by the parties.

18 MEHC Lack of Operational Capability

19 **Q. ICNU witnesses Canon and Gorman both express concern regarding**
20 **MEHC's capability to operate an electric utility. Is that concern justified?**

21 A. No. Although MEHC has been in the regulated utility business in the United
22 States for only six years (about the same level of experience as ScottishPower
23 currently), it also has experience in the regulated utility business in the United

1 Kingdom and as an independent power producer both in the United States and
2 abroad.

3 MEHC is also able to draw upon the extensive experience of the
4 management of the regulated utilities it has already acquired. MEHC's vertically
5 integrated utility MEC and its predecessors, for example, have been in the utility
6 business in the United States for over one hundred years. (Included among the
7 states served is Illinois, where Mr. Gorman was employed by the Illinois
8 Commerce Commission for several years.)

9 Mr. Gorman's expressed concern is particularly surprising in light of the
10 inclusion in his Exhibit No. ____ (MPG-4) of a report by Standard and Poor's that
11 cites as a factor in its credit rating "MEHC's history of strong operations and
12 regulatory management at its only U.S.-based regulated utility."

13 Corporate Presence Commitments

14 **Q. ICNU witness Canon at page 16, lines 7-11 speculates that MEHC's**
15 **commitment to increase corporate and senior management positions in Utah**
16 **will be harmful to customers in the Pacific Northwest because such a split in**
17 **corporate executives and management may not be workable. Is this a valid**
18 **concern?**

19 A. No. MEHC has no intention of creating redundancies, overlapping
20 responsibilities or internal management jurisdictional conflicts. Corporate
21 executives certainly do not need to be located in the same office or same city or
22 same state in order to function efficiently. Conversely, being located in the same
23 office is not a guarantee of efficiency.

1 MEHC understands the concern that Washington's ability to regulate
2 PacifiCorp not be diminished by these commitments. MEHC also understands the
3 concerns that the commitments not diminish local control or PacifiCorp's
4 responsiveness to its regulators, elected officials and customers. The
5 commitments are fully consistent with these understandings. Indeed, the
6 commitments are designed to address these same concerns in each of the six
7 states.

8 MEHC expects that two or three additional senior executive positions will
9 be located in Utah, along with those support personnel deemed necessary by those
10 senior executives. This does not necessarily mean a concomitant reduction in
11 positions in the Pacific Northwest. Until the transaction has closed, vacancies are
12 identified, and economic analyses are performed, MEHC cannot identify the
13 additional senior executive positions to be relocated in Utah. Regardless of what
14 those positions are, however, this relocation will not diminish PacifiCorp's
15 responsiveness to Washington issues and concerns.

16 As demonstrated by Commitment U 7 of Exhibit No. ____ (BEG-10), the
17 focus of the corporate presence commitments is primarily upon allowing local
18 decisions to be made locally. Accomplishing this does not require significant or
19 uneconomic relocation of personnel. It is essentially a matter of having sufficient
20 personnel with adequate and clear authority (and ability) to make sound decisions.
21 Each of the states needs appropriate levels of decision making on a local level and
22 staffing to reflect a commitment to safe, reliable and cost-effective service
23 consistent with cost-effective operations.

1 Rate-making Treatment of Acquisition Premium

2 **Q. At page 6, lines 9-14, ICNU witness Canon portrays MEHC's Application as**
3 **"uniquely harmful in that MEHC has committed to recover its Acquisition**
4 **Premium in rates in certain circumstances." Public Counsel witness Dittmer**
5 **goes a step further at page 37, lines 8-12 to recommend that as a condition**
6 **for approval of the transaction, MEHC/PacifiCorp agree to never seek direct**
7 **or indirect recovery of the acquisition premium being paid. Do you have a**
8 **response?**

9 A. Yes. MEHC and PacifiCorp have no objection to completely deleting all
10 commitments regarding the acquisition premium and being silent on the issue.
11 However, as evidenced by the testimony, several parties want a commitment
12 regarding the premium. MEHC and PacifiCorp are willing to commit to
13 recording the premium at the holding company level, but only with the express
14 reservation of their right to present an argument to the Commission in the future if
15 one circumstance should occur. That circumstance is described later in my
16 testimony.

17 **Q. Please explain MEHC's position regarding inclusion of the acquisition**
18 **premium in regulated retail rates.**

19 A. There appear to be two sources of confusion regarding MEHC's position on the
20 acquisition premium. The first relates to the intent of the commitment. The
21 second relates to what situation would trigger a PacifiCorp request to include the
22 premium in rates. I will attempt to clarify MEHC's intent regarding both of these
23 points.

1 **Q. What exactly does the commitment language allow PacifiCorp/MEHC to do?**

2 A. The commitment language is not intended to allow PacifiCorp/MEHC to
3 unilaterally decide at some future point to include the acquisition premium in the
4 retail rates of PacifiCorp customers. Because the premium will be recorded at the
5 holding company level, the only way that the acquisition premium could ever be
6 included in PacifiCorp's rates would be if PacifiCorp affirmatively proposed to
7 include the premium in retail rates and the Commission agreed.

8 The intent of the commitment language is merely to preserve the right to
9 make an argument to the Commission that the acquisition premium should be
10 included in retail rates under one limited condition. MEHC is concerned that if it
11 agrees to a commitment not to include the acquisition premium in rates and if it
12 does so without a clear reservation of its rights, it would be denied the opportunity
13 in a future rate case to even point out a potential violation of the matching
14 principle, as discussed below.

15 The commitment leaves it up to the Commission, not PacifiCorp or
16 MEHC, as to whether the inclusion of a premium should be allowed. MEHC is
17 seeking only to retain the right to make a future argument, if necessary, and
18 nothing more.

19 **Q. Under what limited condition would MEHC expect this right to be exercised?**

20 A. In order for MEHC and PacifiCorp to exercise their right to present their
21 argument to the Commission regarding inclusion in rates of the acquisition
22 premium, PacifiCorp must be confronted with a potential violation of the
23 matching principle of original cost ratemaking that (1) imputes to PacifiCorp

1 customers (*i.e.*, reduces the regulated revenue requirement on the basis of) a
2 benefit associated with the premium accruing from a company above PacifiCorp
3 in the holding company system, while (2) failing to recognize in rates the cost
4 associated with achieving that benefit.

5 Such a situation would occur, for example, if the Commission were to
6 attribute a lower cost of capital to PacifiCorp's regulated operations based upon
7 substitution of debt costs from the holding company for the cost of utility equity,
8 without recognizing the additional risk (higher cost of equity) to the holding
9 company of its higher leverage. In this instance, PacifiCorp's regulated
10 customers would benefit from a lower cost of capital that assumes a greater
11 percentage of debt, which is typically lower cost than equity, without recognizing
12 the increase in the cost of common equity (due to increased risk) that occurs as a
13 result of that more leveraged financial structure.

14 No request for inclusion of the acquisition premium in rates would be
15 triggered, however, in situations where benefits obtained at the holding company
16 level are appropriately allocated to PacifiCorp, along with the costs of achieving
17 those benefits. For example, if MEHC were able to achieve lower insurance costs
18 post acquisition as a result of combining the insurance needs of itself and
19 PacifiCorp, a portion of such savings (along with the costs related to achieving
20 them) would be properly allocated to PacifiCorp. MEHC expects the lower net
21 costs would be included in retail rates (reducing the regulated revenue
22 requirement). MEHC would not consider this a situation that would allow
23 PacifiCorp to argue for inclusion of the acquisition premium in retail rates.

1 **Q. Is the distinction between a merger and an acquisition that you previously**
2 **discussed relevant to MEHC's position regarding the treatment of the**
3 **acquisition premium?**

4 A. The distinction between a merger and an acquisition is critical with respect to the
5 expectations for regulatory treatment of the acquisition premium. Merged utilities
6 may expect to recover the acquisition premium if they are able to demonstrate
7 cost reductions or other benefits to customers exceeding the cost to customers of
8 providing a return on the acquisition premium. This potential for a return on the
9 premium may or may not impact the size of the premium that the merging utilities
10 are willing to negotiate.

11 In contrast, because MEHC transactions are acquisitions and because
12 MEHC will not claim cost reductions that it does not believe it can deliver,
13 MEHC recognizes that it is unlikely that it will ever recover the acquisition
14 premium. Accordingly, MEHC is reluctant to negotiate a price for an acquisition
15 that is significantly in excess of book value. For example, the prices negotiated
16 for both MEC and PacifiCorp were approximately 130% of book value.

17 MEHC recognizes that the inability to earn a regulated return on the
18 acquisition premium is simply the price paid by shareholders for the opportunity
19 to earn a regulated return on the remainder – the book value or original cost (less
20 depreciation) used for ratemaking purposes. MEHC accepts that regulatory
21 treatment as long as the regulators apply original cost ratemaking fairly and
22 equitably. But if regulators attempt to asymmetrically vary from original cost
23 ratemaking by seeking to capture benefits not associated with the book value of

1 the utility (such as imputing cost reductions to regulated operations from other
2 companies within a holding company structure), MEHC believes it has the duty to
3 its shareholders to point out the asymmetrical treatment to regulators. This does
4 not mean that customers cannot benefit from cost reductions at the corporate level
5 that should accrue to regulated customers, but it does mean that regulators must
6 match costs and benefits, or risks and opportunities.

7 MEHC Eagerness to Invest

8 **Q. Public Counsel witness Dittmer suggests at pages 41 and 42 that the**
9 **Commission should be wary of MEHC's eagerness to invest because MEHC**
10 **is predicting it will invest more in infrastructure than is in PacifiCorp's**
11 **current business plan. What is your response?**

12 A. Mr. Dittmer is mistaken in his belief that MEHC's proposed investments are in
13 excess of the capital requirements in PacifiCorp's long term business plan.

14 With or without the transaction, PacifiCorp plans to invest approximately
15 \$1 billion annually for the next several years, resulting in rate increases averaging
16 4% each year. As I indicated in my direct testimony, MEHC's \$1.3 billion of
17 proposed investments will not result in greater rate increases than projected by
18 PacifiCorp; in fact, MEHC expects that the rate increases over time should be
19 reduced as a consequence of its incremental investments.

20 First, the \$1.3 billion of investments will not be made in a single year but
21 rather over a multi-year period. In addition, not all of the \$1.3 billion is
22 incremental to PacifiCorp's plan (somewhat over \$400 million is incremental).

23 Moreover, MEHC's proposed investments result in the avoidance (or deferral

1 beyond the plan period) of somewhat more than \$400 million of PacifiCorp's
2 planned expenditures. As a result, MEHC's investments do not increase the
3 amount of PacifiCorp's planned investments on a net basis.

4 At the same time, MEHC's investments do produce net benefits (*i.e.*,
5 revenue requirements reductions over time) as compared to PacifiCorp's plan.
6 Our current estimate of the net benefits, on an NPV basis, exceeds \$200 million
7 through 2015, even without recognition of the value of the incremental
8 renewables that are made possible by the transmission investments. This is
9 demonstrated in Exhibit No. ____ (BEG-9). As a result, revenue requirements over
10 the long term are expected to be lower with MEHC's proposed investments than
11 without those investments.

12 Allocation Issues

13 **Q. ICNU witness Wolverton beginning on page 3, line 5 expresses concern**
14 **regarding PacifiCorp's protections for slower-growing states from costs**
15 **associated with Utah load growth, as does Mr. Eberdt of The Energy Project**
16 **at page 5. They both opine that the MEHC proposed investments will**
17 **worsen this problem. Is that the case?**

18 A. No. While PacifiCorp witness Johansen will address the existing allocation
19 issues, I can offer assurance that the investments proposed by MEHC will not
20 have the impact that these witnesses fear. As I stated in my direct testimony,
21 MEHC's investments are not expected to result in rate increases beyond those
22 already incorporated in PacifiCorp's plan. MEHC, in selecting the investments
23 for its commitments, took care to select projects that would benefit customers in

1 all jurisdictions. All three major transmission project commitments include
2 system benefits, either through delay of future generation resources, lower
3 purchased power costs or better access to wind resources.

4 **Q. At page 6, lines 10-11, Mr. Wolverton suggests that approval of the**
5 **transaction should include a condition that shareholders will bear the cost**
6 **responsibility of differing allocation methodologies. Is this an appropriate**
7 **condition?**

8 A. It certainly is not. Placing the cost responsibility on the utility for regulators'
9 inability to agree on a way to allocate common costs would remove an important
10 incentive for regulatory comity. Such a condition would also provide a
11 disincentive to PacifiCorp to make needed investments, and would almost
12 certainly be regarded unfavorably by rating agencies, which would increase the
13 cost of capital to PacifiCorp and its customers.

14 Low Income Issues

15 **Q. Mr. Eberdt at page 8 of his testimony makes several proposals designed to**
16 **address his concerns regarding impacts of PacifiCorp rate increases on low**
17 **income customers. What is your response?**

18 A. Mr. Eberdt's proposals are addressed in the testimony of PacifiCorp witness
19 Johansen.

20 **Conclusion**

21 **Q. Does that conclude your rebuttal testimony?**

22 A. Yes, it does.