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Credit Opinion: PacifiCorp

Global Credit Research - 07 May 2014

Portland, Oregon, United States

Ratings

Category	Moody's Rating
Outlook	Stable
Issuer Rating	A3
First Mortgage Bonds	A1
Senior Secured	A1
Sr Unsec Bank Credit Facility	A3
Senior Unsecured MTN	(P)A3
Pref. Stock	Baa2
Commercial Paper	P-2
Ult Parent: Berkshire Hathaway Inc.	
Outlook	Stable
Issuer Rating	Aa2
Senior Unsecured	Aa2
ST Issuer Rating	P-1
Parent: BERKSHIRE HATHAWAY ENERGY COMPANY	
Outlook	Stable
Sr Unsec Bank Credit Facility	A3
Senior Unsecured	A3
Commercial Paper	P-2

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Key Indicators

[1]PacifiCorp	12/31/2013	12/31/2012	12/31/2011	12/31/2010	12/31/2009
CFO pre-WC + Interest / Interest	5.0x	4.9x	4.8x	5.3x	5.2x
CFO pre-WC / Debt	22.8%	21.1%	21.0%	25.7%	26.0%
CFO pre-WC - Dividends / Debt	15.6%	18.4%	13.5%	25.7%	26.0%
Debt / Capitalization	36.7%	38.3%	39.8%	38.8%	42.4%

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. Source: Moody's Financial Metrics

Note: For definitions of Moody's most common ratio terms please see the accompanying [User's Guide](#).

Opinion

Rating Drivers

Reasonably supportive regulatory environment

Diversified generation portfolio and service territories

Solid credit metrics

Benefits from Berkshire Hathaway affiliation

Corporate Profile

PacifiCorp (A3 senior unsecured, stable) is a vertically integrated electric utility company headquartered in Portland, Oregon serving 1.8 million retail electric customers in six states, including Utah (44% of PacifiCorp's 2013 retail electricity volumes), Oregon (24%), Wyoming (17%), Washington (7%), Idaho (7%), and California (1%). PacifiCorp also has ancillary operations in wholesale power marketing (15% of 2013 electricity volumes, as a result of excess electricity generation or other system balancing activities) and coal mining services, both which support its core utility business.

PacifiCorp is the largest subsidiary of Berkshire Hathaway Energy Company (BHEC, formerly known as MidAmerican Energy Holdings Co.: A3 senior unsecured, stable), accounting for roughly 45% of BHEC's operating income in 2013. BHEC, in turn, is a consolidated subsidiary of Berkshire Hathaway Inc. (BRK: Aa2 Issuer Rating, stable).

SUMMARY RATING RATIONALE

PacifiCorp's ratings are supported by the stability of the utility's regulated cash flows, the geographically diverse and relatively constructive regulatory environments in which it operates, the diversification of its generation portfolio, and solid credit metrics. The rating also considers PacifiCorp's position as a subsidiary of BHEC, a holding company whose subsidiaries are primarily engaged in regulated activities, and the benefits from its affiliation with BRK.

DETAILED RATING CONSIDERATIONS

REASONABLY SUPPORTIVE REGULATORY ENVIRONMENT

PacifiCorp's rating recognizes the rate-regulated nature of its electric utility operations which generate stable and predictable cash flows. PacifiCorp operates in regulatory jurisdictions that we consider as average in terms of framework, consistency and predictability of decisions along with an expectation of timely recovery of costs and investments.

Revenues in 2014 will benefit from recent base rate increases in Oregon (\$24 million) and Washington (\$17 million) as well as step-ups under its two-year rate plans in Utah (\$54 million) and Wyoming (\$18 million). PacifiCorp is also currently pursuing a general rate case in Utah (\$71 million requested) and Wyoming (\$36 million request). Among its jurisdictions, the company's most challenging is Washington, where the allowed ROE is the lowest at 9.5% and where it is contesting its last rate decision, while filing for a new base rate increase (\$27 million request).

Although PacifiCorp has been filing rate cases every year or so in its largest jurisdictions and getting reasonable outcomes, regulatory lag is still evident. Rate relief has improved its actual ROE from the 7% range in 2011 and 2012 to 8.9% in 2013. Nevertheless, these returns are still below the upper 9% range that the company has been allowed in its recent rate cases and below the industry-average allowed ROEs of roughly 10%.

Expecting flat load growth over the next decade, the company has curtailed its annual capital expenditures to about \$1.1 billion, about half what it spent in 2009. It is also keeping operating and maintenance expenses down in order to reduce the need for rate relief and, consequently, regulatory lag.

Future rate filings will arise from its \$6 billion Energy Gateway transmission program, with the Sigurd-Red Butte segment currently under construction, and its 645-megawatt Lake Side 2 gas plant, which is expected to come online in May 2014. The ability to use a forward test year in its rate requests helps to limit regulatory lag in Utah, Oregon, Wyoming, and California. The company has been successful in getting approvals for its major projects; however, it is exposed to some disallowances in most of its jurisdictions, where pre-approvals on projects or cash

returns on construction work in progress are not granted.

The company has obtained energy cost adjustment mechanisms in all its jurisdictions now except Washington. Such mechanisms to recover fuel and purchased power costs -- a large, volatile expense --are more established in other parts of the country. While this development is supportive of credit quality, there remains some lag in recovering portions of energy costs. For example, in Utah, Wyoming, and Idaho, the majority of the difference between the actual power costs and costs established in its base rates is deferred. This difference is then recovered or refunded after an annual filing.

DIVERSIFIED GENERATION PORTFOLIO AND SERVICE TERRITORIES

PacifiCorp benefits from a well diversified generation portfolio. Its 11,240 MW of net generating capacity is comprised primarily of its low cost base-load coal plants (55% of the company's generation), along with 25% from its gas assets, 10% from hydro, and the remaining 10% from wind and other sources.

With coal accounting for a slight majority of its generation capacity, PacifiCorp is subject to numerous emissions standards, but the company is well positioned to comply, with the vast majority of its plants already equipped with sulfur dioxide and nitrogen oxide controls. PacifiCorp can well afford its annual environmental expenditures in the \$100 million range.

The market and customer diversity of PacifiCorp's six-state service territory is favorable, because it mitigates the economic and regulatory impacts in any one jurisdiction. For example, the decline in the retail load in the Pacific Northwest over the last several years was offset by the commercial and industrial growth in the Rocky Mountain states from the tech and energy sectors. Load growth in the Pacific Northwest is now recovering, and we expect flat sales growth overall for the company.

SOLID CREDIT METRICS

PacifiCorp produces solid credit metrics. In 2013, the ratio of cash from operations before changes in working capital (CFO pre-W/C)/Debt was 23% (up from 21% in 2011-2012) and CFO pre-W/C plus Interest/Interest was 5.0x. We expect that these ratios will remain at around these levels over the near term, as the decrease in the deferred tax portion of CFO as a result of the expiration of bonus depreciation in 2013 is offset by increased earnings from rate relief and cost control. The company's Debt/Book Capitalization was 37% at year-end 2013, due to a substantial amount of deferred taxes on its balance sheet.

BENEFITS FROM BERKSHIRE HATHAWAY AFFILIATION

PacifiCorp benefits from its affiliation with BRK, which requires no regular dividends from PacifiCorp or BHEC. From a credit perspective, the company's ability to retain its earnings as an entity that is privately held, particularly by a deep-pocketed sponsor like BRK, is an advantage over most other investor owned utilities that are typically held to a regular dividend to their shareholders.

As an example, PacifiCorp did not pay dividends for the first five years after being acquired by BHEC in 2006, and during that time received equity contributions totaling \$1.1 billion from BHEC to help PacifiCorp finance its capital expenditures. Its balance sheet has strengthened from this financial policy, and PacifiCorp now makes irregular dividends that are sized to manage PacifiCorp's equity ratio (as measured by unadjusted equity to equity plus debt) to about 50%.

Liquidity Profile

PacifiCorp has good near-term liquidity, with \$172 million in cash and two \$600 million revolvers expiring in 2017 and 2018, of which about \$788 million was available as of March 31, 2014. The company generates CFO pre-W/C at a run-rate of roughly \$1.5 billion which will more than cover the \$1.1 billion a year it plans on capital expenditures. Excluding minor amounts of revenue bonds, the only debt maturity over the next 12 months is the \$200 million due on 15 August 2014.

PacifiCorp uses its credit facilities to backstop its commercial paper program and to support its variable rate tax-exempt bonds. These credit agreements do not require a MAC representation for borrowings, which we view positively. The sole financial covenant is a limitation on debt to 65% of total capitalization. As of March 31, 2014, PacifiCorp had ample headroom under that covenant with that ratio at 49% as defined in the agreement.

Rating Outlook

The stable outlook incorporates our expectation that PacifiCorp will continue to receive reasonable regulatory treatment for the recovery of its capital expenditures, and that the funding requirements will be financed in a manner consistent with management's commitment to maintain a healthy financial profile. We anticipate that PacifiCorp's credit metrics will be sustained at about current levels, for example, CFO pre-W/C/Debt in the low 20% range.

What Could Change the Rating - Up

Although its flat financial outlook limits the prospects for a rating upgrade in the foreseeable future, the rating could be upgraded longer term if reasonable regulatory support and a conservatively financed capital expenditure program results in a sustained improvement in credit metrics. This would include, for example, PacifiCorp's ratios of CFO pre-W/C/Debt sustained in the mid 20% range.

What Could Change the Rating - Down

The ratings could be adjusted downward if PacifiCorp's planned capital expenditures are funded in a manner inconsistent with its current financial profile, or if there were to be adverse regulatory rulings on current and future rate cases such that we would anticipate a sustained deterioration in financial metrics as demonstrated, for example, by a ratio of CFO pre-W/C/Debt falling to the mid teens.

Rating Factors

PacifiCorp

Regulated Electric and Gas Utilities Industry Grid [1][2]	Current LTM 12/31/2013		[3]Moody's 12-18 Month Forward ViewAs of May 2014	
Factor 1 : Regulatory Framework (25%)	Measure	Score	Measure	Score
a) Legislative and Judicial Underpinnings of the Regulatory Framework	A	A	A	A
b) Consistency and Predictability of Regulation	A	A	A	A
Factor 2 : Ability to Recover Costs and Earn Returns (25%)				
a) Timeliness of Recovery of Operating and Capital Costs	A	A	A	A
b) Sufficiency of Rates and Returns	Ba	Ba	Ba	Ba
Factor 3 : Diversification (10%)				
a) Market Position	A	A	A	A
b) Generation and Fuel Diversity	Baa	Baa	Baa	Baa
Factor 4 : Financial Strength (40%)				
a) CFO pre-WC + Interest / Interest (3 Year Avg)	4.9x	A	4.8x - 5.0x	A
b) CFO pre-WC / Debt (3 Year Avg)	21.6%	Baa	20%- 22%	Baa
c) CFO pre-WC - Dividends / Debt (3 Year Avg)	15.8%	Baa	15% - 16%	Baa
d) Debt / Capitalization (3 Year Avg)	38.3%	A	38% - 40%	A
Rating:				
Grid-Indicated Rating Before Notching Adjustment		A3		A3
HoldCo Structural Subordination Notching	na	na	na	na
a) Indicated Rating from Grid		A3		A3
b) Actual Rating Assigned		A3		A3

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] As of 12/31/2013; Source: Moody's Financial Metrics [3] This represents Moody's forward view; not the view of the issuer; and unless noted in the text, does not incorporate significant acquisitions

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