Q. Are you the same Bruce N. Williams who previously filed direct testimony in this proceeding?

A. Yes.

Purpose of Testimony

Q. What is the purpose of your testimony?

A. I address certain adjustments to the Company's cost of debt proposed by Division witness Bart Croxford. I will also respond to the concerns expressed by UAE witness Dr. Richard M. Anderson over the equity portion of PacifiCorp's forecast test year capital structure. I will specifically address Dr. Anderson's proposal to use a hypothetical capital structure. I will also rebut the allegation made by UIEC witness Michael Gorman that PacifiCorp's affiliation with ScottishPower and other affiliates has likely increased the Company's cost of debt.

Capital Structure

Q. Do you agree with the adjustments that Mr. Croxford is proposing to the Company's cost of debt?

A. Yes, Mr. Croxford has made several adjustments to reflect debt that has been issued since my direct testimony was prepared. The Company agrees that these adjustments shown in DPU Exhibits 5.3.1 and 5.3.2 are appropriate.

Q. Which parties have suggested adjustments to the Company's proposed test year capital structure?

A. UAE witness Richard Anderson is the only witness now supporting an adjustment to the Company's proposed test year capital structure. Dr. Anderson proposes that the Commission use a hypothetical capital structure for determining the weighted average cost of capital, or alternatively, use only the projected equity portion for FY05. Although the Division originally proposed an adjustment in the prefiled direct testimony of Bart Croxford and Dr. William Powell, the Division has since filed the supplemental direct testimony of Dr. Powell withdrawing the proposed adjustment and supporting the Company's proposed capital structure. Committee witness Daniel Lawton proposed no adjustment, finding that the Company proposed 2006 capital structure estimate is "reasonable." (Direct Testimony of Daniel J. Lawton at 21, line 3).

Q. Do you agree with the adjustment that Dr. Anderson is proposing to the Company's capital structure?

A. No. The Company's proposed capital structure is intended to help maintain our existing long-term debt ratings (presently A- and A3 by Standard & Poor's and Moody's, respectively.) The increase in the common equity percentage is necessary to meet the financial targets published by Standard & Poor's Rating Service (S&P). Those targets are set forth in S&P's June 1, 2004 publication which is Exhibit UP&L___ (BNW-1R). PacifiCorp's recent results are below the targeted levels for an A rated Integrated Electric Utility with a Business Profile of "5" (such as PacifiCorp):

	"A"	PacifiCorp (12 mos ended 9/30/04)	Target Met?
FFO/Interest:	3.8 – 4.5x	4.0x	Yes
FFO/Total Debt:	22 – 30%	19.9%	No
Debt/Capitalization:	42 – 50%	54.8%	No

In fact, Dr. Powell filed supplemental testimony withdrawing the Division's proposed capital structure adjustment for this very reason: "Allowing PacifiCorp to decrease its debt ratio should enhance PacifiCorp's ability to maintain an A rating." (Powell Supplement Direct at page 3, lines 11-13). Without increasing the Company's common equity percentage, only one of our ratios met the target levels for an A rating. The rating agencies have noted this and commented as follows: "Company historical financial performance, while improving, has been weak for the rating category" Moody's Global Credit Research, June 5, 2004.

Q. How does the capital structure in this case compare with the adopted capitalization in the last rate case?

A. In Docket No. 03-2035-02 the Commission adopted a capital structure comprised of 51.55 percent debt, 1.41 percent preferred stock, and 47.04 percent common equity. In the current case the Company proposes a slight change in capital structure, which is comprised of 51.0 percent debt, 1.2 percent preferred stock, and 47.8 percent common equity. The change reflects accumulated earnings and a planned equity issue by the utility. As noted above, PacifiCorp financials are "weak for the credit rating." Yet, Dr. Anderson proposes a capital structure that that will further weaken the utility credit quality.

Q. Are there other reasons the Company is looking to increase its common equity percentage?

A. Yes. In addition to ratios that presently fall short of the "A" rating targets, the Company's results are even weaker when the impacts of purchased power agreements (PPAs) are included.

Q. Please explain what you mean by this.

A. Rating agencies and financial analysts consider PPAs to be debt like and will impute debt and related interest when calculating financial ratios. For example, S&P will adjust our published results and add in debt and interest resulting from PPAs when assessing PacifiCorp's credit worthiness. They do so in order to obtain a more accurate assessment of the financial commitments and fixed payments that a Company has. Exhibit UP&L___ (BNW-2R) is the May 12, 2003 publication by S&P detailing their view of the debt aspects of purchased power agreements.

Q. How does this impact PacifiCorp?

A. During our most recent ratings review, S&P evaluated our PPAs and other related long-term commitments. This resulted in approximately $520 million of additional debt and $52 million of interest expense being added to our debt and coverage tests.

Q. What is the impact on the ratios when this adjustment is made?

A. The ratios would weaken and fall further short of the targets for an "A" rating. The adjusted ratios would be as follows:

	"A"	PacifiCorp (12 mos ended 9/30/04)	Target Met?
FFO/Interest:	3.8 – 4.5x	3.5x	No
FFO/Total Debt:	22 – 30%	17.6%	No
Debt/Capitalization:	42 – 50%	57.8%	No

Q. How would the inclusion of this PPA related debt impact the Company's capital structure?

A. By including the $520 million of imputed debt resulting from PPA's the Company's capital structure would have a lower equity percentage as debt has increased.

Q. Have you done a pro-forma calculation of this impact?

A. Yes. Using the capital structure submitted in my direct testimony the impact is as follows:

	FY05	FY06	Avg	%
Long-Term Debt	$4,419.8	$4,518.0	$4,468.9	54.1%
Preferred	94.0	90.2	92.1	1.1%
Common Equity	3,392.7	4,021.0	3706.8	44.8%

It is clear that the inclusion of the PPA related debt has a significant impact on the Company's capital structure. The Company has appropriately recognized this and intends to increase its equity component to offset the PPA related debt and for the other reasons discussed above in my testimony.

Q. Dr. Anderson proposed that the Commission use a hypothetical capital structure based on the average capital structure of the representative sample of utilities used by the Company in calculating its proposed ROE. Do you agree this is appropriate?

No. The Company has presented clear testimony about its capital structure and the reasons for the increased equity. The reasons support the use of the actual proposed structure rather than a hypothetical structure.

Further, the Value Line 2007 -2009 estimate of common equity ratio for the comparable group is 52.5 percent. This ratio is even greater than what the Company has requested in the current case. Clearly, the Company's capital structure is consistent with others in the utility industry and the expected trend to greater common equity percentages.

Cost of Debt

Q. Mr. Gorman alleges that PacifiCorp's affiliation with ScottishPower and other affiliates has likely increased PacifiCorp's cost of debt. Do you believe this to be true?

A. Absolutely not. If anything, PacifiCorp's cost of debt has benefited from ScottishPower. As I noted earlier, PacifiCorp financial results do not meet the 'A' rating benchmarks although the ratings remain at that level. The agencies have written that PacifiCorp's association with ScottishPower has been a benefit rather than a hindrance.

Q. What examples do you have of these rating agency opinions?

A. Moody's wrote in a December 2003 Opinion Update that "The A3 senior secured rating of PacifiCorp reflects a portfolio of low-cost generating assets, an extensive transmission network, and **an affiliation with parent Scottish Power, who has implemented significant cost reductions and operational efficiencies.**" (emphasis added). Further as early as September 1999, Moody's wrote that "The rating outlook is stable and factors in the expected operational and financial merger [with ScottishPower] benefits encompassed in the current ratings. **If the merger is not completed, PacifiCorp's ratings will be under pressure**."

(emphasis added). Moody's re-iterated the benefit of the association with ScottishPower in January, 2001 at which time the rating outlook was changed to negative from stable due to concerns about the ongoing high cost of wholesale power. "PacifiCorp continues to benefit from its affiliation with its financially strong parent, ScottishPower (senior unsecured debt at A1). However, the company's consolidated interest coverage and other cash flow measures although improving in recent years, remain weak relative to PacifiCorp's rating category."

Q. **Do you have more recent evidence that contradicts the allegation by Mr. Gorman that PacifiCorp's affiliation with ScottishPower and other affiliates has likely increased PacifiCorp's cost of debt?**

A. Recent assessments of PacifiCorp financial performance would suggest that just the opposite is true. In a recent research note dated November 17, 2004 Morgan Stanley states, "Although SPW's UK Business is growing strongly, this positive momentum is now offset by the stagnant Pacificorp business." In addition in a research note by Lehman Brothers dated November 19, 2004 they stated, "Confidence in PPW's capacity has been undermined for the third time – it will take consistent delivery to turn this around."

Moody's recently re-iterated their view, stating "Company's historical financial performance, while improving, has been weak for the rating category." Further, Moody's cited as a specific item under Credit Strength for PacifiCorp "Non-regulated affiliated businesses are relatively modest in size and narrowly focused." (Moody's Global Credit Research December 29, 2004.)

Q. What do you conclude from these assessments?

It is clear to me that absent the association with ScottishPower, PacifiCorp's ratings would be lower than they are today. This ratings benefit has resulted in a lower cost of debt and a benefit to customers.

Q. Does this conclude your rebuttal testimony?

A. Yes.