1 **Q. Please state your name, business address and present position with**
2 **PacifiCorp (the Company).**
3 A. My name is Bruce N. Williams. My business address is PacifiCorp, 825 NE
4 Multnomah, Suite 1900, Portland, Oregon 97232. I was elected Treasurer by the
5 Board of Directors in February 2000. Prior to my election as Treasurer, I served
6 as Assistant Treasurer for several years.

7 **Qualifications**

8 **Q. Mr. Williams, please briefly describe your education and business**
9 **experience.**
10 A. I received a Bachelor of Science degree in Business Administration with a
11 concentration in Finance from Oregon State University in June 1980. I also
12 received the Chartered Financial Analyst designation upon passing the
13 examination in September 1986. I have been employed by PacifiCorp for 20
14 years. My business experience has included financing of PacifiCorp's electric
15 operations and non-utility activities, investment management, and investor
16 relations.

17 **Q. Please describe your present duties.**
18 A. I am responsible for the Company's treasury, pension and other investment
19 management activities. In this proceeding, I am responsible for the preparation of
20 the Company's embedded cost of debt and preferred equity and the testimony
21 related to the Company's capital structure.

22 Purpose of Testimony

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

24 A. I will first present a financing overview of the Company. Next, I will discuss the
25 planned amounts of common equity, debt, and preferred stock to be included in
26 the Company's planned capital structure. I will then analyze the embedded cost
27 of debt and preferred stock supporting PacifiCorp's electric operations in the state
28 of Utah. This analysis includes the use of forward interest rates, historical
29 relationship of security trading patterns, and known and measurable changes to
30 the debt and preferred stock portfolios.

31 **Q. What financial information is your analysis based on?**

32 A. The analysis supporting the capital structure, embedded cost of debt and preferred
33 stock calculations set forth below relies on the most recent information available
34 from the Company's financial planning process. At the time this filing was
35 prepared, however, the Company's most recent forecasted capital structure
36 numbers were available only through Fiscal Year ("FY") 2007 (the twelve-month
37 period ending March 31, 2007) and thus my testimony is based on FY 2007
38 financial data. As I discuss later, I have made changes to remove long-term debt
39 that will mature and to add new long-term debt issuances necessary to fund our
40 operations and to refinance the debt maturing through the mid-point of the test
41 year. It is my current expectation that capital structure and cost of capital at
42 September 30, 2007 will be in line with those at March 31, 2007. However, if
43 there are changes that affect my analysis, specifically including changes that
44 result from the closing of the MidAmerican Energy Holdings Company

45 transaction, those changes will be addressed in the supplemental testimony to be
46 filed in this proceeding.

47 **Q. What is the overall cost of capital that PacifiCorp is proposing in this**
48 **proceeding?**

49 A. PacifiCorp is proposing an overall cost of capital of 9.05 percent. This cost
50 includes the Return on Equity recommendation from Dr. Sam Hadaway and the
51 following capital structure and costs:

52 **PacifiCorp**

53 Overall Cost of Capital

	Component	Percent of Total	Percent of Cost	Weighted Average
54–55				
56	Long Term Debt	46.2%	6.41%	2.96%
57	Preferred Stock	1.0%	6.54%	.07%
58	Common Stock Equity	52.8%	11.40%	6.02%
59		100.0%		9.05%

60 Financing Overview

61 **Q. How does PacifiCorp finance its electric utility operations?**

62 A. PacifiCorp finances the cash flow requirements of its regulated utility operations
63 through a reasonable mix of debt and equity securities designed to provide a
64 competitive cost of capital and predictable capital market access.

65 **How does PacifiCorp meet its debt and preferred equity financing requirements?**

66 A. PacifiCorp relies on a mix of first mortgage bonds, other secured debt, tax exempt
67 debt and preferred stock to meet its long-term debt and preferred stock financing

68 requirements. The Company has concluded the majority of its long-term
69 financing utilizing secured first mortgage bonds issued under the PacifiCorp
70 Mortgage Indenture dated January 9, 1989. Exhibit UP&L___(BNW-1) shows
71 that, as of March 31, 2007, PacifiCorp is projected to have approximately $3.3
72 billion of first mortgage bonds outstanding, with an average cost of 6.71 percent
73 and average remaining maturity of 12.7 years. Presently, all of PacifiCorp's first
74 mortgage bonds bear interest at fixed rates. Proceeds from the issuance of the
75 first mortgage bonds (and other financing instruments) are used to finance the
76 combined utility operations across the Company's six-state service territory.
77 Another important source of financing has been the tax-exempt financing
78 associated with certain qualifying equipment at PacifiCorp's power generation
79 plants. Under arrangements with local counties and other tax-exempt entities,
80 PacifiCorp borrows the proceeds and guarantees the repayment of the long-term
81 debt in order to take advantage of their tax-exempt status in financings. As of
82 March 31, 2007, PacifiCorp's tax-exempt portfolio is projected to be $736 million
83 in principal amount with an average cost of 5.05 percent (which includes the cost
84 of issuance and credit enhancement).
85 **Q. Does PacifiCorp expect to require significant new financing to meet its**
86 **capital budget in the test period?**
87 A. Yes. As stated in Mr. Walje's testimony, PacifiCorp's budgeted level of
88 investment in the test period is approximately fifty percent higher than the
89 Company's net operating income and over two times the depreciation rate. New
90 financing will be required for these investments.

91 **Capital Structure**

92 **Q. How does the Company determine the amount of common equity, debt, and**
93 **preferred stock to be included in the Company's planned capital structure?**

94 A. As a regulated utility, PacifiCorp has a duty and an obligation to provide safe,
95 adequate and reliable service to customers in its Utah service territory while
96 balancing cost and risk. In order to fulfill this obligation, PacifiCorp must make
97 significant capital expenditures for plant and network maintenance, power
98 delivery infrastructure, clean air investments and hydro relicensing activities.
99 Through its planning process, PacifiCorp determined the amounts of new
100 financing needed to support these activities and calculated the required equity and
101 debt ratios required to maintain our current 'A-' credit rating for senior secured
102 debt. These determinations are then reflected in PacifiCorp's budget.

103 **Q. Have PacifiCorp's recent budgets reflected an expectation that PacifiCorp's**
104 **capital structure will include an increase in equity?**

105 A. Yes. PacifiCorp's FY 2006 budget reflected quarterly cash contributions of $125
106 million, for a total of $500 million in new equity. Similarly, PacifiCorp's FY
107 2007 budget includes quarterly cash contributions of $131.25 million, for a total
108 of $525 million in new equity. This will result in an additional $650 million of
109 new common equity in PacifiCorp on March 31, 2007. During this same period,
110 the Company will also secure additional debt financing.

111 **Q. Why do PacifiCorp's FY 2006 and FY 2007 budgets reflect the need for**
112 **additional equity in PacifiCorp's capital structure?**

113 A. The budgets reflect the cost increases described in this case, including investment

114 in utility plant, power costs and OMAG, especially plant maintenance. These cost
115 increases, coupled with the increasingly more rigorous expectations of the credit
116 rating agencies for credit metrics and balance sheet strength, mean that additional
117 equity will be required along with improved business results and other
118 considerations to support PacifiCorp's current 'A-' credit rating from Standard &
119 Poor's ("S&P") and an 'A3' from Moody's Investors Service ("Moody's") and to
120 prevent Fitch Ratings from further downgrading PacifiCorp.

121 **Q. How does this projected capital structure compare to comparable electric**
122 **utilities?**

123 A. The projected capital structure is consistent with the comparable group that Dr.
124 Hadaway has selected in his estimate of Return on Equity. Both PacifiCorp and
125 the group of comparable companies show an increasing percentage of common
126 equity in their capital structures. The Value Line estimate of common equity ratio
127 for the comparable group averages 51.4 percent. Exhibit UP&L___(BNW-2).

128 **Q. Does PacifiCorp's capital structure now reflect these planned cash**
129 **contributions?**

130 A. Yes, PacifiCorp is current on all FY 2006 budgeted cash contributions.
131 PacifiCorp's parent company, PacifiCorp Holdings, Inc. ("PHI"), made three
132 contributions of $125 million each in 2005 and will make an additional cash
133 infusion on March 31, 2006 or the date of the closing of the acquisition of
134 PacifiCorp by MidAmerican Energy Holdings Co. (MEHC), whichever comes
135 first.

136 **Q. Please describe the changes to the Company's levels of debt financing.**

137 A. Through the period ending March 31, 2007, the balance of the outstanding long-
138 term debt will change through maturities, principal amortization and sinking fund
139 requirements, and issuance of new securities. Based upon the long-term debt
140 outstanding on November 30, 2005, I have calculated the reduction to the
141 outstanding balances for maturities, principal amortization and sinking fund
142 requirements, which are scheduled to occur during the period ending March 31,
143 2007. The total long-term debt maturities and principal amortized over this period
144 is $316.3 million. Then I added $300 million of new long-term debt issuances
145 necessary to fund our operations and to refinance the debt maturing through FY
146 2007. This level of debt is consistent with PacifiCorp's budget and is necessary
147 to fund our ongoing operations. This level of debt financing is also consistent
148 with, and balanced by, the projected increase in equity provided through the series
149 of cash infusions discussed above, as well as increased retained earnings.

150 **Q. Please describe the changes to the Company's level of preferred equity**
151 **financing.**

152 A. For preferred stock, I started with the balance outstanding at November 30, 2005
153 and made a reduction of $3.75 million of preferred stock to reflect the sinking
154 fund requirements of the $7.48 Series No Par Serial Preferred stock. A
155 mandatory sinking fund payment of $3.75 million will occur on June 15, 2006.

156 **Q. What steps has the Company taken to implement the financings set forth in**
157 **its forecast?**

158 A. The Company has obtained the approvals of the PacifiCorp Board and the

159 necessary regulatory authorities for debt issuances included in the plan. The
160 Company will be submitting requests in the near future for the necessary
161 regulatory authorities for the equity issuances in FY 2007. The planned increased
162 levels of debt and equity have also been included in presentations to rating
163 agencies. These agencies have used this information as part of their
164 determination of PacifiCorp's credit ratings.

165 **Q. Is the proposed capital structure consistent with the Company's current**
166 **credit rating?**

167 A. Yes. This planned capital structure is intended to enable PacifiCorp to deliver its
168 budgeted capital expenditures while maintaining credit ratios that support the
169 continuance of our current 'A-' credit rating.

170 **Q. What is the relationship between a strong credit rating and customer**
171 **benefits?**

172 A. The credit rating assigned to a utility by the credit rating agencies directly affects
173 the price the utility pays to attract the capital necessary to support its current and
174 future operating needs. A strong credit rating directly benefits customers by
175 reducing immediate and future borrowing costs related to the financing needed to
176 support regulatory operations.

177 During periods of capital market disruptions, higher-rated companies are
178 more likely to have on-going, uninterrupted access to capital. This is not always
179 the case with lower-rated companies, which during such periods may find
180 themselves either unable to secure capital or able to secure capital only on
181 unfavorable terms and conditions.

182 In addition, higher-rated companies have greater access to the long-term
183 markets for power and fuel purchases and sales. Such access provides these
184 companies with more alternatives when attempting to meet the current and future
185 load requirements of their customers. Finally, a company with strong ratings will
186 often avoid having to meet costly collateral requirements that are typically
187 imposed on lower-rated companies when securing power or fuel in these markets.

188 **Q. Is PacifiCorp subject to rating agency debt imputation associated with**
189 **Purchased Power Agreements?**

190 A. Yes. Rating agencies and financial analysts consider Purchased Power
191 Agreements ("PPAs") to be debt-like and will impute debt and related interest
192 when calculating financial ratios.

193 For example, S&P will adjust PacifiCorp's published results and add in debt and
194 interest resulting from PPAs when assessing PacifiCorp's creditworthiness. They
195 do so in order to obtain a more accurate assessment of a company's financial
196 commitments and fixed payments. Exhibit UP&L____(BNW-3) is the May 12,
197 2003 publication by S&P detailing its view of the debt aspects of PPAs.

198 **Q. How does this impact PacifiCorp?**

199 A. During a recent ratings review, S&P evaluated our PPAs and other related long-
200 term commitments. Following this review, S&P added approximately $520
201 million of additional debt and $52 million of interest expense to our debt and
202 coverage tests due to our PPA's.

203 **Q. What actions could the Commission take that would help reduce the impact**
204 **of these PPA's and have a favorable impact on the Company's overall credit**
205 **rating?**

206 A. Approval of a power cost recovery mechanism by this Commission, in
207 conjunction with the recent Wyoming commission approval of a mechanism and
208 favorable action by the Company's other jurisdictions on the Company's request
209 for a mechanism, would reduce the amount of debt imputed by credit rating
210 agencies and would favorably impact the company's overall credit rating. S&P
211 has indicated in recent public reports and in personal meetings with PacifiCorp
212 that the risk factor used when determining the debt impact of PPAs will be
213 significantly reduced if the Company has a reasonably structured power cost
214 recovery mechanism in place in its various jurisdictions. For example, if the risk
215 factor that S&P uses in determining PPA debt imputation for PacifiCorp was
216 reduced from the current 50 percent to 30 percent the amount of debt imputed
217 would be approximately $315 million,. This amount is more than $200 million
218 less than is currently imputed. Correspondingly, the interest imputation would
219 decline from the current $52 million to about $31 million.

220 **Q. What would be the effect of a power cost recovery mechanism for**
221 **PacifiCorp?**

222 A. With a power cost recovery mechanism in place, PacifiCorp would not be
223 required to issue as much equity to offset the imputed debt impacts of PPAs. This
224 would not only help PacifiCorp to maintain its credit rating under its current
225 supply portfolio, but would also facilitate the development of the independent

226 energy market by making PPAs less costly for customers.

227 When PacifiCorp acquires resources through its RFP process, debt imputation is a
228 factor associated with the evaluation of energy options. Because debt is imputed
229 for PPAs, the Company must also infuse a commensurate level of equity to
230 balance its ratios to maintain its credit rating. A lower risk factor associated with
231 PacifiCorp's portfolio of PPAs will help to make purchased power more attractive
232 relative to other options considered in the RFP process.

233 **Q. Has net power cost exposure been recognized and addressed by other**
234 **regulatory Commissions in the Western United States?**

235 A. Yes. In fact, the majority of investor owned electric utilities located in the
236 Western U.S. currently have some form of a power cost recovery mechanism. In
237 the recently settled PacifiCorp Wyoming General Rate Case (Docket No. 20000-
238 230-ER-05), a PCAM mechanism was approved on February 10, 2006.

239 **Financing Cost Calculation**

240 **Q. How did you calculate the Company's embedded costs of long-term debt and**
241 **preferred stock?**

242 A. I calculated the embedded costs of debt and preferred stock using the
243 methodology relied upon in the Company's previous rate cases in Utah and
244 elsewhere.

245 **Q. Please explain the cost of debt calculation.**

246 A. I calculated the cost of debt by issue, based on each debt series' interest rate and
247 net proceeds at the issuance date, to produce a bond yield to maturity for each
248 series of debt. It should be noted that in the event a bond was issued to refinance

249 a higher cost bond, the pre-tax premium and unamortized costs, if any, associated

250 with the refinancing were subtracted from the net proceeds of the bonds that were

251 issued. The bond yield was then multiplied by the principal amount outstanding of

252 each debt issue, resulting in an annualized cost of each debt issue. Aggregating

253 the annual cost of each debt issue produces the total annualized cost of debt.

254 Dividing the total annualized cost of debt by the total principal amount of debt

255 outstanding produces the weighted average cost for all debt issues. This is the

256 Company's embedded cost of long-term debt.

257 **Q. How did you calculate the embedded cost of preferred stock?**

258 A. The embedded cost of preferred stock was calculated by first determining the cost

259 of money for each issue. This is the result of dividing the annual dividend rate by

260 the per share net proceeds for each series of preferred stock. The cost associated

261 with each series was then multiplied by the stated value or principal amount

262 outstanding for each issue to yield the annualized cost for each issue. The sum of

263 annualized costs for each issue produces the total annual cost for the entire

264 preferred stock portfolio. I then divided the total annual cost by the total amount

265 of preferred stock outstanding to produce the weighted average cost of all issues.

266 This is the Company's embedded cost of preferred stock.

267 **Q. A portion of the securities in the Company's debt portfolio bears variable**

268 **rates. What is the basis for the projected interest rates used by the**

269 **Company?**

270 A. The majority of the Company's variable rate debt is in the form of tax-exempt

271 debt. Exhibit UP&L____(BNW-4) shows that these securities had been trading at

272 approximately 87 percent of the 30-day LIBOR (London Inter Bank Offer Rate)
273 for the period December 1999 through November 2005. Therefore, the Company
274 has applied a factor of 87 percent to the forward 30-day LIBOR Rate for March
275 31, 2007 and added the respective credit enhancement and remarketing fees for
276 each floating rate tax-exempt bond. Credit enhancement and remarketing fees are
277 included in the interest component because these are costs which contribute
278 directly to the interest rate on the securities.

279 **Q. Regarding the $300 million of new long-term debt issuances mentioned**
280 **above, how did you determine the interest rate for this new long-term debt?**

281 A. I projected that this debt would be issued at the Company's estimated
282 November 2005 credit spreads over the forward twenty-year Treasury rates as of
283 March 31, 2007. Finally, I added in the effect of issuance costs.

284 This reflects the Company's best estimate of the cost of new debt, assuming the
285 Company's senior secured long-term debt ratings remain unchanged. Currently
286 the Company's senior secured long-term debt is rated 'A-' and 'A3' by S&P and
287 Moody's respectively.

288 **Q. What is the resulting estimated interest rate for this new long-term debt?**

289 A. The Company's estimated November 2005 credit spread for twenty-year notes
290 was 1.10 percent. The forward twenty-year Treasury rate for March 31, 2007 is
291 4.84 percent. Issuance costs for this type of note add approximately 9 basis points
292 (*i.e.*, 0.09 percent) to the all-in cost. Therefore the projected cost of replacement
293 debt is (1.10 + 4.84 +.09) = 6.03 percent.

294 **Q. How does this compare to the cost of the debt that is maturing through**
295 **March 31, 2007?**
296 A. That debt has an average cost of 6.47 percent.
297 **Embedded Cost of Long-Term Debt**
298 **Q. What is the Company's embedded cost of long-term debt?**
299 A. Exhibit UP&L___(BNW-1) shows the embedded cost of long-term debt at March
300 31, 2007 at 6.41 percent.
301 **Embedded Cost of Preferred Stock**
302 **Q. What is the Company's embedded cost of preferred stock?**
303 A. Exhibit UP&L____(BNW-5) shows the embedded cost of preferred stock at
304 March 31, 2007 at 6.54 percent.
305 **Q. Does this conclude your testimony?**
306 A. Yes