BEFORE THE

PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of Rocky Mountain Power for Authority to Increase its Retail Electric Utility Service Rates in Utah and for Approval of its Proposed Electric Service Schedules and Electric Service Regulations	)))))))))	**Docket No. 11-035-200**

Direct Testimony and Exhibits of

Michael P. Gorman

on Cost of Capital Issues

On behalf of

The Federal Executive Agencies (FEA)

Project 9584
May 31, 2012

BRUBAKER & ASSOCIATES, INC.
CHESTERFIELD, MO 63017

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Table of Contents to the Direct Testimony of Michael P. Gorman

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Direct Testimony of Michael P. Gorman

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A Michael P. Gorman. My business address is 16690 Swingley Ridge Road, Suite 140, Chesterfield, MO 63017.

Q WHAT IS YOUR OCCUPATION?

A I am a consultant in the field of public utility regulation and a Managing Principal of Brubaker & Associates, Inc., energy, economic and regulatory consultants.

Q PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND EXPERIENCE.

A This information is included in Appendix A to my testimony.

Q ON WHOSE BEHALF ARE YOU APPEARING IN THIS PROCEEDING?

A I am appearing on behalf of the Federal Executive Agencies ("FEA"). The FEA operates several facilities within Utah, specifically Hill Air Force Base, which receive

service from Rocky Mountain Power ("RMP" or "Company"). The rate increase requested by RMP, if approved, would result in significant additional costs to the FEA.

Q WHAT IS THE SUBJECT OF YOUR DIRECT TESTIMONY?

A I will recommend a fair return on common equity, and overall rate of return for RMP.

SUMMARY

Q PLEASE SUMMARIZE YOUR RATE OF RETURN RECOMMENDATIONS.

A I recommend the Public Service Commission of Utah (the "Commission") award RMP a return on common equity of 9.25%, which is the midpoint of my recommended range of 9.00% to 9.50%, and an overall rate of return of 7.35% (Exhibit FEA-1 (MPG-1)).

I also recommend adjustments to the Company's proposed capital structure. I propose to remove common equity supporting non-utility assets from the capital structure used to develop the overall rate of return applied to RMP's utility cost of service. My capital structure removes the common equity supporting non-utility investments for the five-quarter period ending March 31, 2013, used to develop the ratemaking capital structure. In addition, I also reflected the new financing activities described in the rebuttal testimony of Mr. Williams in RMP's current Wyoming rate case filing.[1]

My recommended return on equity and proposed capital structure will provide RMP with an opportunity to realize cash flow financial coverages and balance sheet strength that conservatively support RMP's current bond rating. Consequently, my

[1]Wyoming Public Service Commission Docket No. 20000-405-ER-11, Rebuttal Testimony of Bruce N. Williams.

recommended return on equity represents fair compensation for RMP's investment risk, and it will preserve the Company's financial integrity and credit standing.

I will also respond to RMP witness Dr. Samuel Hadaway's proposed return on equity of 10.2%. For the reasons discussed below, Dr. Hadaway's recommended return on equity is excessive and should be rejected.

Q DOES YOUR RECOMMENDED RETURN ON EQUITY REFLECT RMP'S EXISTING INVESTMENT RISK?

A Yes. My recommended return on equity reflects fair compensation for RMP's existing investment risk including its regulatory mechanism used to recover its cost of service and financial position. These factors are reflected in RMP's existing bond rating and other risk factors used to select a comparable risk proxy group. If the Commission modified RMP's existing regulatory mechanisms to reduce RMP's investment risk, then any related risk reduction should be considered in determining a fair risk-adjusted return on equity for RMP.

Q HOW DID YOU ESTIMATE RMP'S CURRENT MARKET COST OF EQUITY?

A I performed analyses using three Discounted Cash Flow ("DCF") models, a Risk Premium ("RP") study, and a Capital Asset Pricing Model ("CAPM"). These analyses used a proxy group of publicly traded companies that have investment risk similar to RMP. Based on these assessments, I estimate RMP's current market cost of equity to be 9.25%.

Q HOW DOES YOUR RECOMMENDED RETURN ON EQUITY COMPARE TO RMP'S LAST AUTHORIZED RETURN ON EQUITY?

A On September 13, 2011, the Commission issued its final order in RMP's rate case (Docket No. 10-035-124) and approved a settlement, which included a return on equity of 10.00%.

My recommended return on equity is lower in this case than the return on equity included in the settlement to RMP's rate case from September 2011. However, this lower return on equity is justified based on clear evidence that capital market costs today are much lower than they were in 2011 when the rate settlement process took place and when the rate settlement was ultimately approved.

Q DO YOU BELIEVE MARKET COSTS OF CAPITAL ARE LOWER TODAY THAN THEY WERE IN RMP'S LAST RATE CASE?

A Yes. Market costs of capital declined since RMP's last rate case. This is illustrated by a comparison of bond yields in this case and the last case, and is evident from cost of capital estimates in this case versus the last case. In Table 1, I show the change in utility bond yields.

TABLE 1

Capital Costs – RMP Rate Cases

Description	Current Case[1]	Docket No. 10-035-124	Yield Change
"A" Rated Utility Bond Yields	4.40%	4.97%	0.57%
"Baa" Rated Utility Bond Yields	5.08%	5.39%	0.31%
13-Week Period Ending	05/04/2012	09/09/2011	

Source:
[1]Exhibit FEA-14 (MPG-14), Page 1.

As shown in the table above, the current market cost of debt for "A" (by Standard & Poor's, "S&P") and "Baa" (by Moody's) rated utility bond yields has decreased in this case relative to RMP's last rate case. The current "A" rated utility bond yield is 0.57 percentage points lower now than it was in RMP's last rate case. Also, the current "Baa" utility bond yield is 0.31 percentage points lower than during RMP's last rate case.

Utility bond yields have declined by approximately 50 basis points since RMP's last rate case. This decline in utility bond yields suggests that RMP's cost of capital is lower now than it was in its last rate case.

Q IS THERE OTHER EVIDENCE OF THE DECLINE IN MARKET COST OF EQUITY SINCE RMP'S LAST RATE CASE?

A Yes. This is evident from RMP's case itself. In RMP's last rate case, Dr. Hadaway proposed a return on equity of 10.5%[2] in his direct filing. In its current rate case, RMP is proposing a return on equity of 10.2%. Hence, the Company has acknowledged that the cost of capital has decreased by 30 basis points.

Similarly, in the last RMP rate case I recommended a return on equity of 9.80%.[3] This return on equity is 55 basis points above my recommended return on equity of 9.25% in this case.

[2]Docket No. 10-035-124, Direct Testimony of Dr. Hadaway at 2.
[3]Docket No. 10-035-124, Direct Testimony of Michael P. Gorman at 2.

RATE OF RETURN

Electric Utility Industry Market Outlook

Q PLEASE DESCRIBE THIS SECTION OF YOUR TESTIMONY.

A I begin my estimate of a fair return on equity for RMP by reviewing the market's assessment of electric utility industry investment risk, credit standing and stock price performance in general. I used this information to get a sense of the market's perception of the risk characteristics of electric utility investments in general, which is then used to produce a refined estimate of the market's return requirement for assuming investment risk similar to RMP's utility operations.

Based on the assessments described below, I find the credit rating outlook of the industry to be strong and supportive of the industry's financial integrity, and electric utilities' stocks have exhibited strong price performance over the last several years.

Based on this review of credit outlooks and stock price performance, I conclude that the market has again embraced the electric utility industry as a safe-haven investment, and views utility equity and debt investments as low-risk securities.

Q PLEASE DESCRIBE THE ELECTRIC UTILITIES' CREDIT RATING OUTLOOK.

A Electric utilities' credit rating outlook has improved over the recent past and is now stable. S&P recently provided an assessment of the credit rating of U.S. electric utilities. S&P's commentary included the following:

> **Solid Industry Fundamentals Support Stable Outlook**
>
> The U.S. electric utility sector performed well through 2011, and found it easier to access the capital markets than did most other corporate issuers.

> Investor appetite for electric utility debt remains healthy, and deals have been oversubscribed. Credit fundamentals indicate that most, if not all, electric utilities should continue to have ample access to funding sources and credit. Some firms may issue common stock to partially fund construction spending, which would help to support the capital structure balance. In addition, many utilities are accessing short-term credit markets through commercial paper programs at very low rates.[4]

Similarly, Fitch states:

> **Electric Utilities: Stable**
>
> Fitch's Outlook for the electric utility sector in 2012 remains stable. The sector benefits from low interest rates, modest inflationary pressures, open capital markets, and low natural gas and power prices. Fitch expects these conditions to persist into 2013.
>
> The favorable funding environment helps to offset any stress that would otherwise result during an extended period of high projected capital investment. Capex is expected to remain elevated, increasing 5%–6% over 2011 levels.[5]

Value Line also continues to characterize utility stock investments as a safe haven:

> **Conclusion**
>
> With most of 2011 completed, it seems almost certain that electric utility stocks will have outperformed the broader market averages when the year is over. As of mid-December, the Value Line Utility Average is up slightly, while the Value Line GeometricAverage is down about 14%. Electric utility stocks have long been viewed as a safe haven in volatile markets, due in large part to their generous dividend yields.[6]

The Edison Electric Institute ("EEI") also opined as follows:

> There was little change during 2011 in the industry's long-term outlook. Many regulated utilities are engaged in capital spending programs that should, according to Wall Street analysts, help drive slow but steady earnings growth over the next several years. New EPA regulations may boost capex by 30% in the years ahead, relative to EEI's latest capex survey estimates.[7]

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[4]Standard & Poor's RatingsDirect on the Global Credit Portal: "Industry Economic And Ratings Outlook: Continued Ratings Stability Expected For U.S. Regulated Electric Utilities In 2012," January 25, 2012 at 4-5.

[5]Fitch Ratings: "2012 Outlook: Utilities, Power, and Gas," December 5, 2011 at 10.

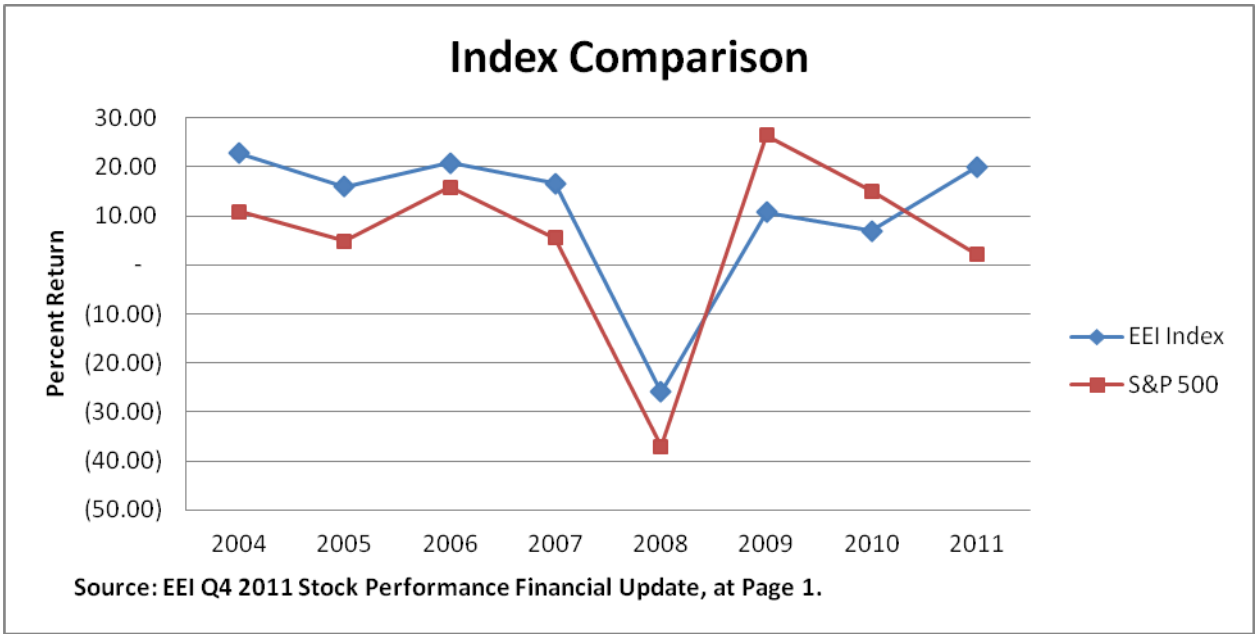
[6]*Value Line Investment Survey*, December 23, 2011 at 901.

[7]EEI Q4 2011 Stock Performance at 1.

Q PLEASE DESCRIBE ELECTRIC UTILITY STOCK PRICE PERFORMANCE OVER THE LAST SEVEN YEARS.

A As shown in Figure 1 below, the EEI has recorded electric utility stock price performance compared to the market. The EEI data shows that its Electric Utility Index has outperformed the market, with a few exceptions, triggered by the recent state of the economic environment.

Figure 1



During 2009 and 2010, the EEI Index underperformed the market, which is not unusual for stocks that are considered "safe havens" during periods of market turbulence.

In 2011, the EEI Index outperformed the market. EEI states the following:

Commentary

> The EEI Index produced a positive 20% return during 2011, its strongest annual gain since 2006, outperforming the broad market after two consecutive years of underperformance as stocks rebounded from the lows reached during 2008 financial crisis.

* * *

> The strength of the EEI Index in 2011 is no surprise, highlighting the industry's traditional role as a defensive investment following its reemphasis in recent years of core regulated businesses with slow but predictable earnings growth and steady dividends. In fact, the industry's average dividend yield exceeded 4% during the year, leading that of all other U.S. business sectors.[8]

RMP Investment Risk

Q PLEASE DESCRIBE THE MARKET'S ASSESSMENT OF THE INVESTMENT RISK OF RMP.

A The market assessment of RMP's investment risk is best described by credit rating analysts' reports. RMP's current senior secured bond ratings from S&P and Moody's are "A" and "A2," respectively.[9]

Specifically, S&P states the following:

> **Rationale**
>
> The 'A-' corporate credit rating (CCR) on PacifiCorp reflects what Standard & Poor's Ratings Services views as a significant financial profile and is supported by PacifiCorp's modest use of leverage to finance a large capital program and parent MidAmerican Energy Holdings Co.'s (MEHC; BBB+/Stable) willingness to deploy equity into PacifiCorp as needed to support the company's capital structure as it expands its rate base. Since acquiring the company in 2006, MEHC has provided $1.06 billion in equity support for the utility's capital needs.
>
> PacifiCorp's excellent business profile benefits from the geographical, market, and regulatory diversity provided by its six-state service territory. PacifiCorp provides power to retail customers under the name Rocky Mountain Power in Utah, Wyoming, and Idaho, and as Pacific Power in Oregon, Washington, and California. Utah and Oregon are the most important markets for the company, providing around 42% and 24% of annual retail sales, respectively, as of year-end 2010.[10]

[8] *EEI Q4 2011 Stock Performance* at 1 and 4-5.
[9] Hadaway Direct at 2.
[10] Standard & Poor's RatingsDirect on the Global Credit Portal: "PacifiCorp," October 3, 2011 at 2 and 3, provided by RMP in Mr. Williams' Exhibit RMP___(BNW-2).

Similarly, Moody's states:

> **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.
>
> * * *
>
> Reasonably supportive regulatory environment
>
> PacifiCorp's rating recognizes the rate-regulated nature of its electric utilities which generate stable and predictable cash flows. PacifiCorp operates in regulatory jurisdictions that Moody's considers as average in terms of framework, consistency and predictability of decisions along with an expectation of timely recovery of costs and investments. This "average" assessment is in line with Moody's views of most U.S. state jurisdictions compared to regulatory environments elsewhere in the world.[11]

Fitch states:

> **Key Rating Drivers**
>
> **Ratings Affirmed:** On Sept. 29, 2011, Fitch Ratings affirmed PacifiCorp's (PPW) ratings with a Stable Rating Outlook. PPW's ratings and outlook reflect the electric utility's solid credit-protection measures, a diversified service territory, a generally balanced regulatory environment, and relatively predictable operating earnings and cash flow characteristics.
>
> * * *
>
> **Ring-Fence Provisions:** Structural protections insulate PPW in the event of financial stress at intermediate holding company MidAmerican Energy Holdings Co. (MEHC, IDR 'BBB+'/Outlook Stable) without impeding the parent's ability to infuse capital into PPW.
>
> **Regulation Key:** Timely recovery of large capital investment program in rates is crucial to PPW's credit quality in Fitch's view. The ratings assume recovery of capital and operating costs in rates will support credit metrics consistent with the company's 'BBB' IDR and Stable Outlook.
>
> * * *

[11] Moody's Investors Service Credit Opinion: "PacifiCorp," May 9, 2011, provided by RMP in Attachment D.18a.

Improved Risk Profile: Since being acquired by MidAmerican Energy Holdings Company (MEHC) in 2006, the utility's business risk has been improved by the adoption of rate mechanisms designed to reduce regulatory lag and facilitate timely recovery of fuel and purchased power costs.[12]

RMP's Proposed Capital Structure

Q WHAT CAPITAL STRUCTURE IS THE COMPANY REQUESTING TO USE TO DEVELOP ITS OVERALL RATE OF RETURN FOR ELECTRIC OPERATIONS IN THIS PROCEEDING?

A RMP's 2010 forecasted capital structure, as supported by RMP witness Mr. Bruce N. Williams, is shown below in Table 2.

TABLE 2

RMP's Proposed Capital Structure

Description	Percent of Total Capital
Long-Term Debt	47.6%
Preferred Stock	0.3%
Common Equity	52.1%
Total Capital Structure	100.0%

Source: Williams Direct at 2.

.

RMP's proposed capital structure reflects common equity investments supporting non-utility assets. Specifically, RMP's balance sheet reflects significant investments in subsidiary companies and non-utility investments. It is not appropriate to include the equity capital supporting these non-utility assets in a regulated utility's capital structure. The cost associated with the capital supporting these non-regulated investments is not related to the cost of providing utility service in Utah or RMP's

[12] FitchRatings Corporates: "PacifiCorp," November 16, 2011, provided by RMP in Attachment D.18b.

other utility jurisdictions. Hence, the Company's proposed capital structure should be modified to remove the common equity supporting these non-utility investments.

Q PLEASE DESCRIBE YOUR PROPOSED ADJUSTMENT TO RMP'S CAPITAL STRUCTURE.

A I propose to remove the common equity supporting non-utility investments from RMP's proposed capital structure. Mr. Williams projected a capital structure described at page 2 of his testimony. At page 13 of his testimony, Mr. Williams described that he developed his proposed capital structure by averaging the five quarters ending March 31, 2013. From that capital structure, I propose to remove common equity investments recorded on PacifiCorp's FERC Form 1 balance sheet, that are non-utility related. These non-utility investments include net non-utility property and investments in subsidiary companies, and other investments. The amount of these investments has been relatively stable through calendar year 2011, and I assume that they will continue to be stable through the end of the test year. Removing this amount of equity investments from the Company's proposed capital structure, will reduce the amount of common equity to total capital ratio for the ratemaking capital structure.

Q WHY IS IT REASONABLE TO ASSUME THAT THE NON-REGULATED INVESTMENTS ARE SUPPORTED WITH ONLY COMMON EQUITY CAPITAL?

A It is not reasonable to assume that utility debt is being used to fund investments in non-utility assets. PacifiCorp has both secured and unsecured utility bond debt issuances recorded on its balance sheet and included in the development of its test year capital structure. It would increase the investment risk on these debt securities if

PacifiCorp was not dedicating these debt securities to its low-risk utility operations. If it was issuing utility debt to invest in non-regulated properties, that would likely increase its investment risk exposure and increase its cost of debt. I do not believe PacifiCorp has undertaken this, and I do not believe it would be appropriate for it to do so.

Q HOW DID YOU ADJUST THE LONG-TERM DEBT BALANCE AND THE EMBEDDED COST OF DEBT?

A In his rebuttal testimony in RMP's Wyoming rate case filing, Mr. Williams described several new financing activities that were not reflected in his direct testimony in this regulatory proceeding. Therefore, including the new $100 million debt issuance used to refinance some of the outstanding pollution control bonds increases the long-term debt balance and reduces the embedded cost of debt from 5.41% down to 5.36%.[13]

Q WHAT IS YOUR PROPOSED CAPITAL STRUCTURE IN THIS PROCEEDING?

A My proposed capital structure is shown below in Table 3.

TABLE 3

Proposed Capital Structure

Description	Percent of Total Capital
Long-Term Debt	48.7%
Preferred Stock	0.3%
Common Equity	51.0%
Total Capital Structure	100.0%

Source: Exhibit FEA-1 (MPG-1).

[13]Wyoming Public Service Commission Docket No. 20000-405-ER-11, Exhibit RMP___ (BNW-1R).

Q WHY IS YOUR PROPOSED CAPITAL STRUCTURE GENERALLY CONSISTENT WITH RMP'S TARGET CAPITAL STRUCTURE FOR UTILITY OPERATIONS?

A Mr. Williams has stated a capital structure target for utility operations of 50%/50% debt/equity. The capital structure outlined in Table 3 approximates this targeted utility capitalization mix.

Q WILL YOUR PROPOSED CAPITAL STRUCTURE SUPPORT RMP'S FINANCIAL INTEGRITY AND CREDIT RATING?

A Yes. As I will discuss later in my testimony, my proposed capital structure is consistent with RMP's current credit rating and will support RMP's financial integrity.

RETURN ON EQUITY

Q PLEASE DESCRIBE WHAT IS MEANT BY A "UTILITY'S COST OF COMMON EQUITY."

A A utility's cost of common equity is the return investors require on an investment in the utility. Investors expect to achieve their return requirement from receiving dividends and stock price appreciation.

Q PLEASE DESCRIBE THE FRAMEWORK FOR DETERMINING A REGULATED UTILITY'S COST OF COMMON EQUITY.

A In general, determining a fair cost of common equity for a regulated utility has been framed by two hallmark decisions of the U.S. Supreme Court: *Bluefield Water Works & Improvement Co. v. Public Serv. Commission of West Virginia,* 262 U.S. 679 (1923) and *Federal Power Commission v. Hope Natural Gas Co.*, 320 U.S. 591 (1944).

These decisions identify the general standards to be considered in establishing the cost of common equity for a public utility. Those general standards provide that the authorized return should: (1) be sufficient to maintain financial integrity; (2) attract capital under reasonable terms; and (3) be commensurate with returns investors could earn by investing in other enterprises of comparable risk.

Q PLEASE DESCRIBE THE METHODS YOU HAVE USED TO ESTIMATE THE COST OF COMMON EQUITY FOR RMP.

A I have used several models based on financial theory to estimate RMP's cost of common equity. These models are: (1) a constant growth Discounted Cash Flow ("DCF") model using analyst growth data; (2) a sustainable growth DCF model; (3) a multi-stage growth DCF model; (4) a risk premium ("RP") model; and (5) a Capital Asset Pricing Model ("CAPM"). I have applied these models to a group of publicly traded utilities that I have determined share investment risk similar to RMP's.

Q HOW DID YOU SELECT A UTILITY PROXY GROUP SIMILAR IN INVESTMENT RISK TO RMP TO ESTIMATE ITS CURRENT MARKET COST OF EQUITY?

A I relied on the same utility proxy group used by RMP witness Dr. Hadaway to estimate RMP's return on equity.

Q HOW DOES THE PROXY GROUP INVESTMENT RISK COMPARE TO RMP'S INVESTMENT RISK?

A The proxy group is shown on Exhibit FEA-2 (MPG-2). This proxy group has an average senior secured credit rating from S&P of "A-," which is a notch lower than S&P's senior secured credit rating for RMP. The proxy group's senior secured credit

rating from Moody's is "A2," which is identical to RMP's senior secured credit rating from Moody's of "A2." The proxy group has comparable investment risk to RMP.

The proxy group has an average common equity ratio of 46.3% (including short-term debt) from *AUS Utility Reports* ("AUS") and 48.8% (excluding short-term debt) from *Value Line* in 2011. The proxy group's common equity ratio is slightly lower but comparable to my proposed common equity ratio of 51.0% excluding short-term debt.

I also compared RMP's business risk to the business risk of the proxy group based on S&P's ranking methodology. RMP has an S&P business risk profile of "Excellent," which is identical to the S&P business risk profile of the proxy group. The S&P business risk profile score indicates that RMP's business risk is comparable to that of the proxy group.[14]

Based on these proxy group selection criteria, I believe that my proxy group reasonably approximates the investment risk of RMP, and can be used to estimate a fair return on equity for RMP.

Discounted Cash Flow Model

Q PLEASE DESCRIBE THE DCF MODEL.

A The DCF model posits that a stock price is valued by summing the present value of expected future cash flows discounted at the investor's required rate of return or cost of capital. This model is expressed mathematically as follows:

[14]S&P ranks the business risk of a utility company as part of its corporate credit rating review. S&P considers total investment risk in assigning bond ratings to issuers, including utility companies. In analyzing total investment risk, S&P considers both the business risk and the financial risk of a corporate entity, including a utility company. S&P's business risk profile score is based on a six-notch credit rating starting with "Vulnerable" (highest risk) to "Excellent" (lowest risk). The business risk of most utility companies falls within the lowest risk category, "Excellent," or the category one notch lower (more risk), "Strong." Standard & Poor's: "Criteria Methodology: Business Risk/Financial Risk Matrix Expanded," May 27, 2009.

$$P_0 = \frac{D_1}{(1+K)^1} + \frac{D_2}{(1+K)^2} \ldots . \frac{D_\infty}{(1+K)^\infty} \quad \text{where} \qquad \text{(Equation 1)}$$

P_0 = Current stock price
D = Dividends in periods 1 - ∞
K = Investor's required return

This model can be rearranged in order to estimate the discount rate or investor-required return, "K." If it is reasonable to assume that earnings and dividends will grow at a constant rate, then Equation 1 can be rearranged as follows:

$$K = D_1/P_0 + G \qquad \text{(Equation 2)}$$

K = Investor's required return
D_1 = Dividend in first year
P_0 = Current stock price
G = Expected constant dividend growth rate

Equation 2 is referred to as the annual "constant growth" DCF model.

Q PLEASE DESCRIBE THE INPUTS TO YOUR CONSTANT GROWTH DCF MODEL.

A As shown in Equation 2 above, the DCF model requires a current stock price, expected dividend, and expected growth rate in dividends.

Q WHAT STOCK PRICE HAVE YOU RELIED ON IN YOUR CONSTANT GROWTH DCF MODEL?

A I relied on the average of the weekly high and low stock prices of the utilities in the proxy group over a 13-week period ended May 4, 2012. An average stock price is less susceptible to market price variations than a spot price. Therefore, an average stock price is less susceptible to aberrant market price movements, which may not be reflective of the stock's long-term value.

A 13-week average stock price reflects a period that is still short enough to contain data that reasonably reflect current market expectations, but the period is not so short as to be susceptible to market price variations that may not reflect the stock's

long-term value. In my judgment, a 13-week average stock price is a reasonable balance between the need to reflect current market expectations and the need to capture sufficient data to smooth out aberrant market movements.

Q WHAT DIVIDEND DID YOU USE IN YOUR CONSTANT GROWTH DCF MODEL?

A I used the most recently paid quarterly dividend, as reported in *The Value Line Investment Survey*.[15] This dividend was annualized (multiplied by 4) and adjusted for next year's growth to produce the D_1 factor for use in Equation 2 above.

Q WHAT DIVIDEND GROWTH RATES HAVE YOU USED IN YOUR CONSTANT GROWTH DCF MODEL?

A There are several methods that can be used to estimate the expected growth in dividends. However, regardless of the method, for purposes of determining the market-required return on common equity, one must attempt to estimate investors' consensus about what the dividend or earnings growth rate will be, and not what an individual investor or analyst may use to make individual investment decisions.

As predictors of future returns, security analysts' growth estimates have been shown to be more accurate than growth rates derived from historical data.[16] That is, assuming the market generally makes rational investment decisions, analysts' growth projections are more likely to influence observable stock prices than growth rates derived only from historical data.

For my constant growth DCF analysis, I have relied on a consensus, or mean, of professional security analysts' earnings growth estimates as a proxy for investor consensus dividend growth rate expectations. I used the average of analysts' growth

[15] *The Value Line Investment Survey*, February 24, March 23, and May 4, 2012.

[16] See, e.g., David Gordon, Myron Gordon, and Lawrence Gould, "Choice Among Methods of Estimating Share Yield," *The Journal of Portfolio Management*, Spring 1989.

rate estimates from three sources: Zacks, SNL Financial, and Reuters. All such projections were available on May 7, 2012, and all were reported online.

Each consensus growth rate projection is based on a survey of security analysts. The consensus estimate is a simple arithmetic average, or mean, of surveyed analysts' earnings growth forecasts. A simple average of the growth forecasts gives equal weight to all surveyed analysts' projections. It is problematic as to whether any particular analyst's forecast is more representative of general market expectations. Therefore, a simple average, or arithmetic mean, of analyst forecasts is a good proxy for market consensus expectations.

Q WHAT ARE THE GROWTH RATES YOU USED IN YOUR CONSTANT GROWTH DCF MODEL?

A The growth rates I used in my DCF analysis are shown in Exhibit FEA-3 (MPG-3). The average growth rate for my proxy group is 5.03%.

Q WHAT ARE THE RESULTS OF YOUR CONSTANT GROWTH DCF MODEL?

A As shown in Exhibit FEA-4 (MPG-4), the average and median constant growth DCF returns for my proxy group are 9.32% and 9.38%, respectively.

Even though the average and median results are relatively close, there are wide variations in the results of the proxy group estimates. I believe some of the estimates seem to be unreasonably low. Therefore, I conclude that the group median represents a more reasonable assessment of the central tendency of all the estimates within the proxy group. As such, I believe my constant growth DCF model, using analysts' growth rate estimates, supports a return on equity of 9.38%.

Q DO YOU HAVE ANY COMMENTS ON THE RESULTS OF YOUR CONSTANT GROWTH DCF ANALYSIS?

A Yes. The three- to five-year growth rates are in line with the long-term sustainable growth rate. Therefore, I believe my constant growth DCF analysis using analysts' three- to five-year growth rates reflects reasonable growth outlooks and the DCF results are also reasonable. Nevertheless, I consider other DCF methodologies in order to enhance the information available to accurately estimate RMP's current market return on common equity.

Sustainable Growth DCF

Q PLEASE DESCRIBE HOW YOU ESTIMATED A SUSTAINABLE LONG-TERM GROWTH RATE FOR YOUR SUSTAINABLE GROWTH DCF MODEL.

A A sustainable growth rate is based on the percentage of the utility's earnings that is retained and reinvested in utility plant and equipment. These reinvested earnings increase the earnings base (rate base). Earnings grow when plant funded by reinvested earnings is put into service, and the utility is allowed to earn its authorized return on such additional rate base investment.

The internal growth methodology is tied to the percentage of earnings retained in the company and not paid out as dividends. The earnings retention ratio is 1 minus the dividend payout ratio. As the payout ratio declines, the earnings retention ratio increases. An increased earnings retention ratio will fuel stronger growth because the business funds more investments with retained earnings. The payout ratios of the proxy group are shown on my Exhibit FEA-5 (MPG-5). These dividend payout ratios and earnings retention ratios then can be used to develop a sustainable long-term earnings retention growth rate. A sustainable long-term retention ratio will help gauge

whether analysts' current three- to five-year growth rate projections can be sustained over an indefinite period of time.

The data used to estimate the long-term sustainable growth rate is based on the Company's current market to book ratio and on *Value Line's* three- to five-year projections of earnings, dividends, earned returns on book equity, and stock issuances.

As shown in Exhibit FEA-6 (MPG-6), page 1, the average sustainable growth rate for the proxy group using this internal growth rate model is 4.90%.

Q WHAT IS THE DCF ESTIMATE USING THESE SUSTAINABLE LONG-TERM GROWTH RATES?

A A DCF estimate based on these sustainable growth rates is developed in Exhibit FEA-7 (MPG-7). As shown there, a sustainable growth DCF analysis produces proxy group average and median DCF results of 9.18% and 8.91%, respectively. Considering the central tendency of my proxy group, I will rely on the median DCF result. Therefore, I believe my constant growth DCF analysis using a sustainable growth rate produces a return on equity estimate of 8.91% for RMP in this case.

Multi-Stage Growth DCF Model

Q HAVE YOU CONDUCTED ANY OTHER DCF STUDIES?

A Yes. My first constant growth DCF is based on consensus analysts' growth rate projections, so it is a reasonable reflection of rational investment expectations over the next three to five years. The limitation on the constant growth DCF model is that it cannot reflect a rational expectation that a period of high/low short-term growth can be followed by a change in growth to a rate that is more reflective of long-term

sustainable growth. Hence, I performed a multi-stage growth DCF analysis to reflect this outlook of changing growth expectations.

Q PLEASE DESCRIBE YOUR MULTI-STAGE GROWTH DCF MODEL.

A The multi-stage growth DCF model reflects the possibility of non-constant growth for a company over time. The multi-stage growth DCF model reflects three growth periods: (1) a short-term growth period, which consists of the first five years; (2) a transition period, which consists of the next five years (6 through 10); and (3) a long-term growth period, starting in year 11 through perpetuity.

For the short-term growth period, I relied on the consensus analysts' growth projections described above in relationship to my constant growth DCF model. For the transition period, the growth rates were reduced or increased by an equal factor, which reflects the difference between the analysts' growth rates and the GDP growth rate. For the long-term growth period, I assumed each company's growth would converge to the maximum sustainable growth rate for a utility company as proxied by the consensus analysts' projected growth for the U.S. GDP of 5.0%.

Q WHY IS THE GDP GROWTH PROJECTION A REASONABLE PROXY FOR THE MAXIMUM SUSTAINABLE GROWTH RATE FOR A UTILITY?

A Utilities cannot indefinitely sustain a growth rate that exceeds the growth rate of the overall economy. Utilities' earnings/dividend growth is created by increased utility investment or rate base. Such investment, in turn, is driven by service area economic growth and demand for utility service. In other words, utilities invest in plant to meet sales demand growth, and sales growth, in turn, is tied to economic growth in their service areas. The Energy Information Administration ("EIA") has observed that utility

sales growth is less than U.S. GDP growth, as shown in Exhibit FEA-8 (MPG-8). Utility sales growth has lagged behind GDP growth for more than a decade. As a result, nominal GDP growth is a very conservative, albeit overstated, proxy for electric utility sales growth, rate base growth, and earnings growth. Therefore, GDP growth is a conservative proxy for the highest sustainable long-term growth rate of a utility.

Q IS THERE RESEARCH THAT SUPPORTS YOUR POSITION THAT, OVER THE LONG TERM, A COMPANY'S EARNINGS AND DIVIDENDS CANNOT GROW AT A RATE GREATER THAN THE GROWTH OF THE U.S. GDP?

A Yes. This concept is supported in both published analyst literature and academic work. Specifically, in a textbook entitled "Fundamentals of Financial Management," published by Eugene Brigham and Joel F. Houston, the authors state as follows:

> The constant growth model is most appropriate for mature companies with a stable history of growth and stable future expectations. Expected growth rates vary somewhat among companies, but dividends for mature firms are often expected to grow in the future at about the same rate as nominal gross domestic product (real GDP plus inflation).[17]

Q HOW DID YOU DETERMINE THE CONSENSUS REASONABLE, SUSTAINABLE LONG-TERM GROWTH RATE?

A I relied on the consensus analysts' projections of long-term GDP growth. *The Blue Chip Economic Indicators* publishes consensus economists' GDP growth projections

[17]"Fundamentals of Financial Management," Eugene F. Brigham and Joel F. Houston, Eleventh Edition 2007, Thomson South-Western, a Division of Thomson Corporation at 298.

twice a year. Based on its latest issue, the consensus economists' published GDP growth rate outlook is 5.1% to 4.8% over the next ten years.[18]

Therefore, I propose to use the consensus economists' projected 10-year average GDP consensus growth rate of 5.0% (4.95% rounded to 5.0%), as published by *Blue Chip Economic Indicators,* as an estimate of long-term sustainable growth. *Blue Chip Economic Indicators'* projections provide real GDP growth projections of 2.9% and 2.5%, and GDP inflation of 2.1% and 2.2%[19] over the five-year and 10-year projection periods, respectively. This consensus GDP growth forecast represents the most likely views of market participants because it is based on published consensus economist projections.

Q DO YOU CONSIDER OTHER SOURCES OF PROJECTED LONG-TERM GDP GROWTH?

A Yes. The U.S. EIA in its Annual Energy Outlook projects the real GDP out until 2035. In its 2011 Annual Report, the EIA projects real GDP through 2035 to be in the range of 2.1% to 3.2%, with a midpoint or reference case of 2.7%.[20]

Also, the Congressional Budget Office ("CBO") makes long-term economic projections. The CBO is projecting real GDP growth of 3.8% to 2.5% during the next five and 10 years, respectively, with GDP price inflation of 1.7% to 2.0%.[21] The CBO's real GDP projections are higher than the consensus but its GDP inflation is lower than the consensus economists.

The real GDP and nominal GDP growth projections made by the U.S. EIA and those made by the CBO support the use of the consensus analyst five-year and 10-

[18] *Blue Chip Economic Indicators*, March 10, 2012 at 15.
[19] GDP growth is the product of real and inflation GDP growth.
[20] DOE/EIA Annual Energy Outlook 2011 With Projections to 2035, April 2011.
[21] *Blue Chip Economic Indicators*, March 10, 2012 at 15.

year projected GDP growth outlooks as a reasonable market assessment of long-term prospective GDP growth.

Q WHAT STOCK PRICE, DIVIDEND AND GROWTH RATES DID YOU USE IN YOUR MULTI-STAGE GROWTH DCF ANALYSIS?

A I relied on the same 13-week stock price and the most recent quarterly dividend payment data discussed above. For stage one growth, I used the consensus analysts' growth rate projections discussed above in my constant growth DCF model. The transition period begins in year six and ends in year ten. For the long-term sustainable growth rate starting in year 11, I used 5.0%, the average of the consensus economists' five-year and 10-year projected nominal GDP growth rates.

Q WHAT ARE THE RESULTS OF YOUR MULTI-STAGE GROWTH DCF MODEL?

A As shown in Exhibit FEA-9 (MPG-9), the average and median DCF returns on equity for my proxy group are 9.31% and 9.50%, respectively. Again, for consistency I would rely on the median DCF return estimate.

Q PLEASE SUMMARIZE THE RESULTS FROM YOUR DCF ANALYSES.

A The results from my DCF analyses are summarized in Table 4 below:

TABLE 4

Summary of DCF Results

Description	Median Estimates
Constant Growth DCF Model (Analysts' Growth)	9.38%
Constant Growth DCF Model (Sustainable Growth)	8.91%
Multi-Stage Growth DCF Model	9.50%

I am placing less emphasis on the results of my sustainable growth DCF result, because the growth rates implied in that model are lower than the consensus analysts' three- to five-year projected growth rates, and the implied growth in my multi-growth DCF, both of which I believe are reasonable estimates of long-term sustainable growth. Based on this assessment, I believe a fair point estimate based on my DCF studies for RMP is 9.45%, which is the approximate average of my constant growth analysts, 9.38%, and multi-growth DCF, 9.50%.

Risk Premium Model

Q PLEASE DESCRIBE YOUR BOND YIELD PLUS RISK PREMIUM MODEL.

A This model is based on the principle that investors require a higher return to assume greater risk. Common equity investments have greater risk than bonds because bonds have more security of payment in bankruptcy proceedings than common equity and the coupon payments on bonds represent contractual obligations. In contrast, companies are not required to pay dividends or guarantee returns on common equity investments. Therefore, common equity securities are considered to be more risky than bond securities.

This risk premium model is based on two estimates of an equity risk premium. First, I estimated the difference between the required return on utility common equity investments and U.S. Treasury bonds. The difference between the required return on common equity and the Treasury bond yield is the risk premium. I estimated the risk premium on an annual basis for each year over the period 1986 through 2011. The common equity required returns were based on regulatory commission-authorized returns for electric utility companies. Authorized returns are typically based on expert witnesses' estimates of the contemporary investor-required return.

The second equity risk premium estimate is based on the difference between regulatory commission-authorized returns on common equity and contemporary "A" rated utility bond yields. I selected the period 1986 through 2011 because public utility stocks consistently traded at a premium to book value during that period. This is illustrated in Exhibit FEA-10 (MPG-10), which shows that the market to book ratio since 1986 for the electric utility industry was consistently above 1.0. Over this period, regulatory authorized returns were sufficient to support market prices that at least exceeded book value. This is an indication that regulatory authorized returns on common equity supported a utility's ability to issue additional common stock without diluting existing shares. It further demonstrates that utilities were able to access equity markets without a detrimental impact on current shareholders.

Based on this analysis, as shown in Exhibit FEA-11 (MPG-11), the average indicated equity risk premium over U.S. Treasury bond yields has been 5.23%. Of the 26 observations, 20 indicated risk premiums fall in the range of 4.41% to 6.13%. Since the risk premium can vary depending upon market conditions and changing investor risk perceptions, I believe using an estimated range of risk premiums provides the best method to measure the current return on common equity using this methodology.

As shown in Exhibit FEA-12 (MPG-12), the average indicated equity risk premium over contemporary Moody's utility bond yields was 3.81% over the period 1986 through 2011. The indicated equity risk premium estimates based on this analysis primarily fall in the range of 3.03% to 4.62% over this time period.

Q DO YOU BELIEVE THAT THESE EQUITY RISK PREMIUM ESTIMATES ARE BASED ON A TIME PERIOD THAT IS TOO LONG OR TOO SHORT TO DRAW ACCURATE RESULTS CONCERNING CONTEMPORARY MARKET CONDITIONS?

A No. Contemporary market conditions can change dramatically during the period that rates determined in this proceeding will be in effect. A relatively long period of time where stock valuations reflect premiums to book value is an indication that the authorized returns on equity and the corresponding equity risk premiums were supportive of investors' return expectations and provided utilities access to the equity markets under reasonable terms and conditions. Further, this time period is long enough to smooth abnormal market movement that might distort equity risk premiums. While market conditions and risk premiums do vary over time, this historical time period is a reasonable period to estimate contemporary risk premiums.

The time period I use in this risk premium study is a generally accepted period to develop a risk premium study using "expectational" data. Conversely, studies have recommended that use of "actual achieved return data" should be based on very long historical time periods. The studies find that achieved returns over short time periods may not reflect investors' expected returns due to unexpected and abnormal stock price performance. However, these short-term abnormal actual returns would be smoothed over time and the achieved actual returns over long time periods would approximate investors' expected returns. Therefore, it is reasonable to assume that averages of annual achieved returns over long time periods will generally converge on the investors' expected returns.

My risk premium study is based on expectational data, not actual returns, and, thus, need not encompass very long time periods.

Q BASED ON HISTORICAL DATA, WHAT RISK PREMIUM HAVE YOU USED TO ESTIMATE RMP'S COST OF EQUITY IN THIS PROCEEDING?

A The equity risk premium should reflect the relative market perception of risk in the utility industry today. I have gauged investor perceptions in utility risk today in Exhibit FEA-13 (MPG-13). On that exhibit, I show the yield spread between utility bonds and Treasury bonds over the last 32 years. As shown in this exhibit, the 2008 utility bond yield spreads over Treasury bonds for "A" rated and "Baa" rated utility bonds are 2.25% and 2.97%, respectively. The utility bond yield spreads over Treasury bonds for "A" and "Baa" rated utility bonds for 2009 are 1.97% and 2.99%, respectively. In 2010, these spreads declined to 1.21% and 1.71%, respectively. In 2011, they declined further to 1.13% and 1.65%, respectively. These utility bond yield spreads over Treasury bond yields are now lower than the 32-year average spreads of 1.58% and 1.98%, respectively.

A current 13-week average "A" rated utility bond yield of 4.40%, when compared to the current Treasury bond yield of 3.18% as shown in Exhibit FEA-14 (MPG-14), page 1 of 3, implies a yield spread of around 1.22%. This current utility bond yield spread is lower than the 32-year average spread for "A" utility bonds of 1.58%. The current spread for the "Baa" utility yields of 1.90 is also lower than the 32-year average spread of 1.98%.

These utility bond yield spreads are clear evidence that the market considers the utility industry to be a relatively low risk investment and demonstrates that utilities continue to have strong access to capital.

Q HOW DID YOU ESTIMATE RMP'S COST OF COMMON EQUITY WITH THIS RISK PREMIUM MODEL?

A I added a projected long-term Treasury bond yield to my estimated equity risk premium over Treasury yields. The 13-week average 30-year Treasury bond yield, ending May 4, 2012 was 3.18%, as shown in Exhibit FEA-14 (MPG-14), page 1 of 3. *Blue Chip Financial Forecasts* projects the 30-year Treasury bond yield to be 3.90%, and a 10-year Treasury bond yield to be 2.90%.[22] Using the projected 30-year bond yield of 3.90%, and a Treasury bond risk premium of 4.41% to 6.13%, as developed above, produces an estimated common equity return in the range of 8.31% (3.90% + 4.41%) to 10.03% (3.90% + 6.13%). I recommend an equity risk premium of 9.46%, rounded to 9.50%. This estimate is based on giving two-thirds weight to my high-end risk premium estimate of 10.03%, and one-third weight to my low-end risk premium estimate of 8.31%. I believe this weighting is appropriate given the unusually large yield spreads between Treasury bond and "Baa" utility bond yields.

I next added my equity risk premium over utility bond yields to a current 13-week average yield on "A" rated utility bonds for the period ending May 4, 2012 of 4.40%. Adding the utility equity risk premium of 3.03% to 4.62%, as developed above, to an "A" rated bond yield of 4.40%, produces a cost of equity in the range of 7.43% (4.40% + 3.03%) to 9.02% (4.40% + 4.62%). Again, recognizing the unusually low Treasury yield and wide Treasury to utility bond yield spreads, I recommend two-thirds weight to the high-end risk premium, and one-third weight to the low-end risk premium. This produces a risk premium return of 8.49%,[23] rounded to 8.50%.

My risk premium analyses produce a return estimate in the range of 8.50% to 9.50%, with a midpoint estimate of approximately 9.00%.

[22] *Blue Chip Financial Forecasts*, May 1, 2012 at 2.
[23] 1/3 x 7.43% + 2/3 x 9.02% = 8.49%.

Capital Asset Pricing Model ("CAPM")

Q PLEASE DESCRIBE THE CAPM.

A The CAPM method of analysis is based upon the theory that the market-required rate of return for a security is equal to the risk-free rate, plus a risk premium associated with the specific security. This relationship between risk and return can be expressed mathematically as follows:

$R_i = R_f + B_i \times (R_m - R_f)$ where:

R_i = Required return for stock i
R_f = Risk-free rate
R_m = Expected return for the market portfolio
B_i = Beta - Measure of the risk for stock

The stock-specific risk term in the above equation is beta. Beta represents the investment risk that cannot be diversified away when the security is held in a diversified portfolio. When stocks are held in a diversified portfolio, firm-specific risks can be eliminated by balancing the portfolio with securities that react in the opposite direction to firm-specific risk factors (e.g., business cycle, competition, product mix, and production limitations).

The risks that cannot be eliminated when held in a diversified portfolio are non-diversifiable risks. Non-diversifiable risks are related to the market in general and are referred to as systematic risks. Risks that can be eliminated by diversification are regarded as non-systematic risks. In a broad sense, systematic risks are market risks, and non-systematic risks are business risks. The CAPM theory suggests that the market will not compensate investors for assuming risks that can be diversified away. Therefore, the only risk that investors will be compensated for are systematic or non-diversifiable risks. The beta is a measure of the systematic or non-diversifiable risks.

Q PLEASE DESCRIBE THE INPUTS TO YOUR CAPM.

A The CAPM requires an estimate of the market risk-free rate, the company's beta, and the market risk premium.

Q WHAT DID YOU USE AS AN ESTIMATE OF THE MARKET RISK-FREE RATE?

A As previously noted, *Blue Chip Financial Forecasts*' projected 30-year Treasury bond yield is 3.90%.[24] The current 30-year Treasury bond yield is 3.20%. I used *Blue Chip Financial Forecasts*' projected 30-year Treasury bond yield of 3.90% for my CAPM analysis.

Q WHY DID YOU USE LONG-TERM TREASURY BOND YIELDS AS AN ESTIMATE OF THE RISK-FREE RATE?

A Treasury securities are backed by the full faith and credit of the United States government, so long-term Treasury bonds are considered to have negligible credit risk. Also, long-term Treasury bonds have an investment horizon similar to that of common stock. As a result, investor-anticipated long-run inflation expectations are reflected in both common-stock required returns and long-term bond yields. Therefore, the nominal risk-free rate (or expected inflation rate and real risk-free rate) included in a long-term bond yield is a reasonable estimate of the nominal risk-free rate included in common stock returns.

Treasury bond yields, however, do include risk premiums related to unanticipated future inflation and interest rates. A Treasury bond yield is not a risk-free rate. Risk premiums related to unanticipated inflation and interest rates are systematic or market risks. Consequently, for companies with betas less than 1.0,

[24] *Blue Chip Financial Forecasts*, May 1, 2012 at 2.

using the Treasury bond yield as a proxy for the risk-free rate in the CAPM analysis can produce an overstated estimate of the CAPM return.

Q WHAT BETA DID YOU USE IN YOUR ANALYSIS?

A As shown in Exhibit FEA-15 (MPG-15), the proxy group average *Value Line* beta estimate is 0.72.

Q HOW DID YOU DERIVE YOUR MARKET RISK PREMIUM ESTIMATE?

A I derived two market risk premium estimates, a forward-looking estimate and one based on a long-term historical average.

The forward-looking estimate was derived by estimating the expected return on the market (as represented by the S&P 500) and subtracting the risk-free rate from this estimate. I estimated the expected return on the S&P 500 by adding an expected inflation rate to the long-term historical arithmetic average real return on the market. The real return on the market represents the achieved return above the rate of inflation.

Morningstar's *Stocks, Bonds, Bills and Inflation 2012 Classic Yearbook* publication estimates the historical arithmetic average real market return over the period 1926 to 2011 as 8.6%.[25] A current consensus analysts' inflation projection, as measured by the Consumer Price Index, is 2.4%.[26] Using these estimates, the expected market return is 11.21%.[27] The market risk premium then is the difference between the 11.21% expected market return, and my 3.90% risk-free rate estimate, or 7.30%.

[25]Morningstar, Inc. Ibbotson *SBBI 2012 Classic Yearbook* at 84.
[26]*Blue Chip Financial Forecasts*, May 1, 2012 at 2.
[27]{ [(1 + 0.086) ∗ (1 + 0.024)] – 1 } ∗ 100.

The historical estimate of the market risk premium was also estimated by Morningstar in *Stocks, Bonds, Bills and Inflation 2012 Classic Yearbook*. Over the period 1926 through 2011, Morningstar's study estimated that the arithmetic average of the achieved total return on the S&P 500 was 11.8%,[28] and the total return on long-term Treasury bonds was 6.1%.[29] The indicated market risk premium is 5.7% (11.8% - 6.1% = 5.7%).

Q HOW DOES YOUR ESTIMATED MARKET RISK PREMIUM RANGE COMPARE TO THAT ESTIMATED BY MORNINGSTAR?

A Morningstar's analysis indicates that a market risk premium falls somewhere in the range of 5.9% to 6.6%. My market risk premium falls in the range of 5.7% to 7.3%. My average market risk premium of 6.5% is at the high end of Morningstar's range.

Morningstar estimates a forward-looking market risk premium based on actual achieved data from the historical period of 1926 through 2011. Using this data, Morningstar estimates a market risk premium derived from the total return on large company stocks (S&P 500), less the income return on Treasury bonds. The total return includes capital appreciation, dividend or coupon reinvestment returns, and annual yields received from coupons and/or dividend payments. The income return, in contrast, only reflects the income return received from dividend payments or coupon yields. Morningstar argues that the income return is the only true risk-free rate associated with Treasury bonds and is the best approximation of a truly risk-free rate. I disagree with this assessment from Morningstar, because it does not reflect a true investment option available to the marketplace and therefore does not produce a legitimate estimate of the expected premium of investing in the stock market versus

[28]Morningstar, Inc. Ibbotson *SBBI 2012 Classic Yearbook* at 83.
[29]*Id.*

that of Treasury bonds. Nevertheless, I will use Morningstar's conclusion to show the reasonableness of my market risk premium estimates.

Morningstar's range is based on several methodologies. First, Morningstar estimates a market risk premium of 6.6% based on the difference between the total market return on common stocks (S&P 500) less the income return on Treasury bond investments. Second, Morningstar found that if the New York Stock Exchange (the "NYSE") was used as the market index rather than the S&P 500, that the market risk premium would be 6.4% and not 6.6%. Third, if only the two deciles of the largest companies included in the NYSE were considered, the market risk premium would be 5.9%.[30]

Finally, Morningstar found that the 6.6% market risk premium based on the S&P 500 was influenced by an abnormal expansion of price-to-earnings ("P/E") ratios relative to earnings and dividend growth during the period 1980 through 2001. Morningstar believes this abnormal P/E expansion is not sustainable. Therefore, Morningstar adjusted this market risk premium estimate to normalize the growth in the P/E ratio to be more in line with the growth in dividends and earnings. Based on this alternative methodology, Morningstar published a long-horizon supply-side market risk premium of 6.1%.[31]

Q WHAT ARE THE RESULTS OF YOUR CAPM ANALYSIS?

A As shown in Exhibit FEA-16 (MPG-16), based on Morningstar's high-end market risk premium of 6.6%, a risk-free rate of 3.9%, and a beta of 0.72, my CAPM analysis produces a return of 8.65% (rounded to 8.70%).

[30]Morningstar observes that the S&P 500 and the NYSE Decile 1-2 are both large capitalization benchmarks. Morningstar, Inc. *Ibbotson SBBI 2012 Valuation Yearbook* at 54.

[31]*Id.* at 66.

Return on Equity Summary

Q BASED ON THE RESULTS OF YOUR RETURN ON COMMON EQUITY ANALYSES DESCRIBED ABOVE, WHAT RETURN ON COMMON EQUITY DO YOU RECOMMEND FOR RMP?

A Based on my analyses, I estimate RMP's current market cost of equity to be 9.25%.

TABLE 5

Return on Common Equity Summary

Description	Results
DCF	9.45%
Risk Premium	9.00%
CAPM	8.70%

My recommended return on common equity of 9.25% is approximately at the midpoint of my recommended range of 9.00% to 9.50%. The high-end of my range is based on my DCF studies, and the low-end is based on my risk premium estimate. I am placing less weight on the results of CAPM studies reflecting today's very low Treasury bond yields. My concern is whether these low Treasury bond yields will be sustained over time, or will eventually return to more normal levels than those experienced over the last few years.

Financial Integrity

Q WILL YOUR RECOMMENDED OVERALL RATE OF RETURN SUPPORT AN INVESTMENT GRADE BOND RATING FOR RMP?

A Yes. I have reached this conclusion by comparing the key credit rating financial ratios for RMP, at my proposed return on equity and capital structure, to S&P's benchmark financial ratios using S&P's new credit metric ranges.

Q PLEASE DESCRIBE THE MOST RECENT S&P FINANCIAL RATIO CREDIT METRIC METHODOLOGY.

A S&P publishes a matrix of financial ratios that correspond to its assessment of the business risk of the utility company and related bond rating. On May 27, 2009, S&P expanded its matrix criteria[32] by including additional business and financial risk categories. Based on S&P's most recent credit matrix, the business risk profile categories are "Excellent," "Strong," "Satisfactory," "Fair," "Weak," and "Vulnerable." Most electric utilities have a business risk profile of "Excellent" or "Strong." The financial risk profile categories are "Minimal," "Modest," "Intermediate," "Significant," "Aggressive," and "Highly Leveraged." Most of the electric utilities have a financial risk profile of "Aggressive." RMP has an "Excellent" business risk profile and a "Significant" financial risk profile.

Q PLEASE DESCRIBE S&P'S USE OF THE FINANCIAL BENCHMARK RATIOS IN ITS CREDIT RATING REVIEW.

A S&P evaluates a utility's credit rating based on an assessment of its financial and business risks. A combination of financial and business risks equates to the overall assessment of RMP's total credit risk exposure. S&P publishes a matrix of financial ratios that defines the level of financial risk as a function of the level of business risk.

S&P publishes ranges for three primary financial ratios that it uses as guidance in its credit review for utility companies. The three primary financial ratio benchmarks it relies on in its credit rating process include: (1) Total Debt to Total Capital; (2) Debt to Earnings Before Interest, Taxes, Depreciation and Amortization ("EBITDA"); and (3) Funds From Operations ("FFO") to Total Debt.

[32]S&P updated its original 2007 credit metric guidelines in 2009, and incorporated utility metric benchmarks with the general corporate rating metrics.

Q HOW DID YOU APPLY S&P'S FINANCIAL RATIOS TO TEST THE REASONABLENESS OF YOUR RATE OF RETURN RECOMMENDATIONS?

A I calculated each of S&P's financial ratios based on RMP's cost of service for its Utah jurisdictional electric operations. While S&P would normally look at total consolidated PacifiCorp financial ratios in its credit review process, my investigation in this proceeding is not the same as S&P's. I am attempting to judge the reasonableness of my proposed cost of capital for rate-setting in RMP's Utah regulated utility operations. Hence, I am attempting to determine whether my proposed rate of return will in turn support cash flow metrics, balance sheet strength, and earnings that will support an investment grade bond rating and RMP's financial integrity.

Q DID YOU INCLUDE ANY OFF-BALANCE SHEET DEBT ("OBSD")?

A Yes. As shown in Exhibit FEA-17 (MPG-17), I estimated off-balance sheet debt equivalents of $275.8 million attributed to RMP's operating leases and purchased power agreements ("PPA") as available online from Standard & Poor's RatingsDirect. S&P includes other off-balance sheet debt adjustments which I did not include in my analysis. S&P's inclusion of intermediate hybrids,[33] post-retirement benefits, and accrued interest not reported on the Company's debt and asset retirement obligations, were not included in my analysis. Each of these factors are either reflected in PacifiCorp's cost of service, or I could not find evidence that they relate to regulated utility operations. As such, I did not include them in the metrics to judge the reasonableness of my rate of return for retail operations in Utah in this proceeding.

[33]This was included but not in the OBS calculation. Refer to Exhibit FEA-17 (MPG-17), where the 50% of Preferred was included as debt-like instruments,

Q PLEASE DESCRIBE THE RESULTS OF THIS CREDIT METRIC ANALYSIS FOR RMP.

A The S&P financial metric calculations for RMP at a 9.25% return are developed on Exhibit FEA-17 (MPG-17), page 1 of 4.

RMP's adjusted total debt ratio is 50%. This is at the high end of S&P's "Significant" range of 45% to 50%, and at the low end of the "Aggressive" utility guideline range of 50% to 60%. This total debt ratio will support an investment grade bond rating.

As shown on Exhibit FEA-17 (MPG-17), page 1 of 4, column 1, based on an equity return of 9.25%, RMP will be provided an opportunity to produce a debt to EBITDA ratio of 3.3x. This is at the low end of S&P's "Significant" guideline range of 3.0x to 4.0x.[34] This ratio also supports an investment grade credit rating.

Finally, RMP's retail operations FFO to total debt coverage at a 9.25% equity return would be 22%, which is at the low end of the "Significant" metric guideline range of 20% to 30%. The FFO/total debt ratio will support an investment grade bond rating.

At my recommended return on equity of 9.25% and proposed capital structure, RMP's financial credit metrics are supportive of its current "A" utility bond rating.

[34]Standard & Poor's RatingsDirect: "Criteria Methodology: Business Risk/Financial Risk Matrix Expanded," May 27, 2009.

RESPONSE TO RMP WITNESS DR. SAMUEL HADAWAY

Q WHAT RETURN ON COMMON EQUITY IS RMP PROPOSING FOR THIS PROCEEDING?

A RMP is proposing to set rates based on a return on equity of 10.20%. RMP's return on equity proposal is based on the analysis and judgment of Dr. Samuel Hadaway. Dr. Hadaway's results are summarized at page 31 of his direct testimony.

Q DO DR. HADAWAY'S METHODOLOGIES SUPPORT HIS 10.20% RETURN ON EQUITY FOR HIS PROXY GROUP?

A No. As discussed in detail below, Dr. Hadaway's own analyses would support a return on equity in the range of 9.0% to 10.0% if it is adjusted to reflect current market data and his models are properly applied. These adjustments to Dr. Hadaway's return on equity estimates support my recommended return on equity.

Q PLEASE DESCRIBE THE METHODOLOGY USED BY DR. HADAWAY TO SUPPORT HIS RETURN ON COMMON EQUITY RECOMMENDATION.

A Dr. Hadaway develops his return on common equity recommendation using three versions of the DCF model, and two utility risk premium analyses. I have summarized Dr. Hadaway's results in Table 6 under column 1. Under column 2, I show the results of Dr. Hadaway's analyses adjusted for updated data and more reasonable application of the models.

As shown in Table 6, using consensus economists' projection of GDP growth rather than Dr. Hadaway's inflated GDP growth estimates, his own DCF analyses would support a return on equity for RMP in the range of 9.2% to 10.0%. Proper adjustments to Dr. Hadaway's utility risk premium estimates to reflect the unadjusted

878 equity risk premium would reduce this estimate from 9.6% to 9.0%. Therefore,
879 Dr. Hadaway's return on equity estimate with reasonable adjustments will produce a
880 return on equity for RMP in the range of 9.0% to 10.0%. However, a majority of the
881 adjusted results fall in the range of 9.6% to 9.2%.

TABLE 6

Summary of Dr. Hadaway's ROE Estimate

Description	Hadaway Results[1] (1)	Adjusted Hadaway Results[2] (2)
DCF Analysis		
Constant Growth (Analysts' Growth)	9.6% - 10.0%	9.6% - 10.0%
Constant Growth (GDP Growth)	10.1% - 10.2%	9.3% - 9.4%
Multi-Stage Growth Model	9.9% - 10.0%	9.2% - 9.3%
Indicated DCF Range	9.6% - 10.2%	9.2% - 10.0%
Risk Premium Analysis		
Forecasted Utility Debt + Equity Risk Premium	9.7%	Reject
Current Utility Debt + Equity Risk Premium	9.6%	9.0%
Risk Premium Estimate	9.6%	9.0%
Recommended ROE	10.2%	
Adjusted ROE Range		9.0% - 10.0%

Sources:
[1]Hadaway Direct at 31.
[2] Exhibit FEA-18 (MPG-18).

882 **Q PLEASE DESCRIBE DR. HADAWAY'S CONSTANT GROWTH DCF ANALYSIS.**

883 A Dr. Hadaway's adjusted constant growth DCF analysis is shown on his Exhibit RMP
884 ___(SCH-4). As shown on that exhibit, Dr. Hadaway's constant growth DCF analysis
885 is based on a recent stock price, an annualized dividend and an average of three
886 growth rates: (1) *Value Line*; (2) Zacks; and (3) Thomson.

Q ARE DR. HADAWAY'S DCF ESTIMATES RELIABLE?

A No. His GDP growth rate used in his constant growth and multi-stage growth models is based on an inflated GDP growth rate of 5.8%. This GDP growth is excessive and not reflective of current market expectations.

Q HOW DID DR. HADAWAY DEVELOP HIS GDP GROWTH RATE?

A He states that the GDP growth rate is based on the achieved GDP growth over the last 10, 20, 30, 40, 50, and 60-year periods. Dr. Hadaway's projected GDP growth rate is unreasonable. Historical GDP growth over the last 20 and 40-year periods was strongly influenced by the actual inflation rate experienced over that time period.

Q WHY IS DR. HADAWAY'S DCF ESTIMATE EXCESSIVE IN COMPARISON TO THAT OF PUBLISHED MARKET ANALYSTS?

A The consensus economists' projected GDP growth rate is much lower than the GDP growth rate used by Dr. Hadaway in his DCF analysis. A comparison of Dr. Hadaway's GDP growth rate and consensus economists' projected GDP growth over the next five and 10 years is shown in Table 7. As shown in this table, Dr. Hadaway's GDP rate of 5.8% reflects real GDP of 2.7% and an inflation adjusted GDP of 3.0%. However, consensus economists' projections of nominal GDP include GDP inflation projections over the next five and 10 years of 2.1% and 2.2%, respectively.[35]

As is clearly evident in Table 7, Dr. Hadaway's historical GDP growth reflects historical inflation, which is much higher than, and not representative of, consensus market expected forward-looking inflation.

[35] *Blue Chip Economic Indicators*, March 10, 2012 at 15.

TABLE 7

GDP Projections

Description	GDP Inflation	Real GDP	Nominal GDP
Dr. Hadaway	3.0%	2.7%	5.8%
Consensus Five-Year Projection	2.1%	2.9%	5.1%
Consensus 10-Year Projection	2.2%	2.5%	4.8%

Source: *Blue Chip Economic Indicators*, March 10, 2012 at 15.

As such, Dr. Hadaway's 5.8% nominal GDP growth rate is not reflective of consensus market expectations and should be rejected. Indeed, Dr. Hadaway's 5.8% GDP growth rate outlook is inconsistent with the consensus of economists' independent projections of future long-term GDP growth, and also inconsistent with projections made by the U.S. Energy Information Administration, and Congressional Budget Office as referenced in my testimony above where I describe the parameters used in my own multi-stage growth DCF analyses. Those agencies also project real GDP in line with what Dr. Hadaway and his consensus projections include, however their outlook for future inflation is much lower than Dr. Hadaway, and much more consistent with the consensus independent economists' projections discussed in Table 7 above. For all these reasons, Dr. Hadaway's GDP growth outlook rate projections are simply out of line and out of touch with the consensus market outlooks.

Q HOW WOULD DR. HADAWAY'S DCF ANALYSES CHANGE IF CURRENT MARKET-BASED GDP GROWTH RATE PROJECTIONS ARE INCLUDED IN HIS ANALYSIS RATHER THAN HIS EXCESSIVE GDP GROWTH RATE?

A As shown in Exhibit FEA-18 (MPG-18), I updated Dr. Hadaway's DCF analyses using more recent market data and a GDP growth rate of 5.0%. This GDP growth rate is the consensus economists' five- and 10-year projected growth rate of the GDP as published in the *Blue Chip Economic Indicators*. As shown in Exhibit FEA-18 (MPG-18), using this consensus economists' projected GDP growth rate, reduces Dr. Hadaway's long-term GDP growth DCF result from 10.2% to 9.4% and his multi-stage DCF from 10.0% to 9.3%.

Q PLEASE SUMMARIZE YOUR ADJUSTMENTS TO DR. HADAWAY'S DCF STUDIES.

A Using a more reasonable GDP growth rate reduces the average DCF result produced by Dr. Hadaway's studies from 10.0% down to 9.5%. Dr. Hadaway's original estimates and these updated and adjusted results are shown below in Table 8.

TABLE 8

Adjusted Hadaway DCF

Description	Range Average Hadaway DCF	Range Average Adjusted DCF
Constant Growth (Analysts' Growth)	9.8%	9.8%
Constant Growth (GDP Growth)	10.2%	9.4%
Multi-Stage Growth Model	10.0%	9.3%
Average	10.0%	9.5%

As shown above in Table 8, using a consensus economists' GDP forecast, rather than the GDP forecast derived by Dr. Hadaway, would support a return on equity no higher than 9.5%.

Q PLEASE DESCRIBE DR. HADAWAY'S UTILITY RISK PREMIUM ANALYSIS.

A Dr. Hadaway's utility bond yield versus authorized return on common equity risk premium is shown in Exhibit RMP ___(SCH-5). As shown in this exhibit, Dr. Hadaway estimated an annual equity risk premium by subtracting Moody's average bond yield from the electric utility regulatory commission authorized return on common equity over the period 1980 through 2011. Based on this analysis, Dr. Hadaway estimates an average indicated equity risk premium over current utility bond yields of 3.33%.

Dr. Hadaway then adjusts this average equity risk premium using a regression analysis based on an expectation that there is an ongoing inverse relationship between interest rates and equity risk premiums. Based on this regression analysis, Dr. Hadaway increases his equity risk premium from 3.33%, up to 5.08% and 5.18% relative to projected and current "A" bond yield of 4.62% and 4.37%, respectively. He then adds these inflated equity risk premiums to the projected and current "A" rated utility bond yield of 4.62% and 4.37% to produce a return on equity of 9.70% and 9.55%, respectively.

Q ARE DR. HADAWAY'S UTILITY RISK PREMIUM ANALYSES REASONABLE?

A No. Dr. Hadaway develops a forward-looking risk premium model, relying on forecasted interest rates and volatile utility spreads, which are highly uncertain and produce inaccurate results. Further, Dr. Hadaway's proposal to adjust the actual

equity risk premium of 3.33% to reflect the inverse relationship between interest rates and utility risk premiums to 5.08% and 5.18% is unreasonable. This adjustment is inappropriate and not consistent with academic literature that finds that this relationship should change with risk changes and not simply changes to interest rates.

Q DO YOU HAVE ANY COMMENTS CONCERNING DR. HADAWAY'S FORECASTED UTILITY BOND YIELD OF 4.62%?

A Yes. Dr. Hadaway develops his forecasted utility bond yield based on the 3-month historical spread of A-rated utility bond yields and 30-year Treasury yields of 1.32% added to his projected long-term Treasury yield of 3.3%. This approach is unreasonable because Dr. Hadaway relies on projected interest rates with historical yield spreads. The accuracy of his interest rate projections are highly problematic, and he provides no support for his assumption that yield spreads will stay flat if Treasury yields increase. This yield spread relationship is volatile and uncertain as are interest rate projections. Indeed, while interest rates have been projected to increase over the last several years, those increased interest rate projections have turned out to be wrong.

Q WHY DO YOU BELIEVE THAT THE ACCURACY OF FORECASTED INTEREST RATES IS HIGHLY PROBLEMATIC?

A Over the last several years, observable current interest rates have been a more accurate predictor of future interest rates than economists' consensus projections. Exhibit FEA-19 (MPG-19) illustrates this point. On this exhibit, under Columns 1 and 2, I show the actual market yield at the time a projection is made for Treasury bond

yields two years in the future. In Column 1, I show the actual Treasury yield and, in Column 2, I show the projected yield two years out.

As shown in Columns 1 and 2, over the last several years Treasury yields were projected to increase relative to the actual Treasury yields at the time of the projection. In Column 4, I show what the Treasury yield actually turned out to be two years after the forecast. Under Column 5, I show the actual yield change at the time of the projections relative to the projected yield change.

As shown in this exhibit, over the last several years, economists consistently have been projecting that interest rates will increase. However, as demonstrated under Column 5, those yield projections have turned out to be overstated in virtually every case. Indeed, actual Treasury yields have decreased or remained flat over the last five years, rather than increase as the economists' projections indicated. As such, current observable interest rates are just as likely to predict future interest rates as are economists' projections.

Q WHY IS DR. HADAWAY'S USE OF A SIMPLE INVERSE RELATIONSHIP BETWEEN INTEREST RATES AND EQUITY RISK PREMIUMS NOT REASONABLE?

A Dr. Hadaway's belief that there is a simplistic inverse relationship between equity risk premiums and interest rates is not supported by academic research. While academic studies have shown that, in the past, there has been an inverse relationship between these variables, researchers have found that the relationship changes over time and

is influenced by changes in perception of the risk of bond investments relative to equity investments, and not simply changes to interest rates.[36]

In the 1980s, equity risk premiums were inversely related to interest rates, but that was likely attributable to the interest rate volatility that existed at that time. Interest rate volatility currently is much lower than it was in the 1980s.[37] As such, when interest rates were more volatile, the relative perception of bond investment risk increased relative to the investment risk of equities. This changing investment risk perception caused changes in equity risk premiums.

In today's marketplace, interest rate variability is not as extreme as it was during the 1980s. Nevertheless, changes in the perceived risk of bond investments relative to equity investments still drive changes in equity premiums. However, a relative investment risk differential cannot be measured simply by observing nominal interest rates. Changes in nominal interest rates are highly influenced by changes to inflation outlooks, which also change equity return expectations. As such, the relevant factor needed to explain changes in equity risk premiums is the relative changes to the risk of equity versus debt securities investments, not simply changes to interest rates.

Importantly, Dr. Hadaway's analysis simply ignores investment risk differentials. He bases his adjustment to the equity risk premium exclusively on changes in nominal interest rates. This is a flawed methodology that does not produce accurate or reliable risk premium estimates. His results should be rejected by the Commission.

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[36]"The Market Risk Premium: Expectational Estimates Using Analysts' Forecasts," Robert S. Harris and Felicia C. Marston, *Journal of Applied Finance*, Volume 11, No. 1, 2001 and "The Risk Premium Approach to Measuring a Utility's Cost of Equity," Eugene F. Brigham, Dilip K. Shome, and Steve R. Vinson, *Financial Management*, Spring 1985.

[37]Morningstar SBBI, 2009 Yearbook at 95-96.

Using Dr. Hadaway's projected equity risk premium adjusted for an inverse relationship of 5.08%, relative to the current observable "A" rated utility bond yield of 4.40%, would indicate a return on equity of 9.48%. This return estimate largely supports my recommended return on equity for RMP. Alternatively, modifying his equity risk premiums to consider yield spreads, rather than simply the inverse relationship between equity risk premiums and interest rates, would also reduce the level of equity risk premium estimated by Dr. Hadaway. Simply observing the highest equity risk premiums authorized over the last five years would indicate an average equity risk premium of 4.57%. (This is based on the last five years, excluding 2008, which had an abnormally low equity risk premium.) Relying on an equity risk premium of 4.40%, relative to current observable utility bond yields of 4.57%, or Dr. Hadaway's projected "A" rated utility bond yield of 4.62%, would indicate a return on common equity for RMP in the range of 8.97% to 9.02%, or 9.0%.

Q DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?

A Yes, it does.

Qualifications of Michael P. Gorman

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A Michael P. Gorman. My business address is 16690 Swingley Ridge Road, Suite 140, Chesterfield, MO 63017.

Q PLEASE STATE YOUR OCCUPATION.

A I am a consultant in the field of public utility regulation and a Managing Principal with Brubaker & Associates, Inc., energy, economic and regulatory consultants.

Q PLEASE SUMMARIZE YOUR EDUCATIONAL BACKGROUND AND WORK EXPERIENCE.

A In 1983 I received a Bachelors of Science Degree in Electrical Engineering from Southern Illinois University, and in 1986, I received a Masters Degree in Business Administration with a concentration in Finance from the University of Illinois at Springfield. I have also completed several graduate level economics courses.

In August of 1983, I accepted an analyst position with the Illinois Commerce Commission ("ICC"). In this position, I performed a variety of analyses for both formal and informal investigations before the ICC, including: marginal cost of energy, central dispatch, avoided cost of energy, annual system production costs, and working capital. In October of 1986, I was promoted to the position of Senior Analyst. In this position, I assumed the additional responsibilities of technical leader on projects, and my areas of responsibility were expanded to include utility financial modeling and financial analyses.

In 1987, I was promoted to Director of the Financial Analysis Department. In this position, I was responsible for all financial analyses conducted by the staff. Among other things, I conducted analyses and sponsored testimony before the ICC on rate of return, financial integrity, financial modeling and related issues. I also supervised the development of all Staff analyses and testimony on these same issues. In addition, I supervised the Staff's review and recommendations to the Commission concerning utility plans to issue debt and equity securities.

In August of 1989, I accepted a position with Merrill-Lynch as a financial consultant. After receiving all required securities licenses, I worked with individual investors and small businesses in evaluating and selecting investments suitable to their requirements.

In September of 1990, I accepted a position with Drazen-Brubaker & Associates, Inc. In April 1995, the firm of Brubaker & Associates, Inc. ("BAI") was formed. It includes most of the former DBA principals and Staff. Since 1990, I have performed various analyses and sponsored testimony on cost of capital, cost/benefits of utility mergers and acquisitions, utility reorganizations, level of operating expenses and rate base, cost of service studies, and analyses relating industrial jobs and economic development. I also participated in a study used to revise the financial policy for the municipal utility in Kansas City, Kansas.

At BAI, I also have extensive experience working with large energy users to distribute and critically evaluate responses to requests for proposals ("RFPs") for electric, steam, and gas energy supply from competitive energy suppliers. These analyses include the evaluation of gas supply and delivery charges, cogeneration and/or combined cycle unit feasibility studies, and the evaluation of third-party asset/supply management agreements. I have also analyzed commodity pricing

indices and forward pricing methods for third party supply agreements, and have also conducted regional electric market price forecasts.

In addition to our main office in St. Louis, the firm also has branch offices in Phoenix, Arizona and Corpus Christi, Texas.

Q HAVE YOU EVER TESTIFIED BEFORE A REGULATORY BODY?

A Yes. I have sponsored testimony on cost of capital, revenue requirements, cost of service and other issues before the Federal Energy Regulatory Commission and numerous state regulatory commissions including: Arkansas, Arizona, California, Colorado, Delaware, Florida, Georgia, Idaho, Illinois, Indiana, Iowa, Kansas, Louisiana, Michigan, Missouri, Montana, New Jersey, New Mexico, New York, North Carolina, Oklahoma, Oregon, South Carolina, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, Wyoming, and before the provincial regulatory boards in Alberta and Nova Scotia, Canada. I have also sponsored testimony before the Board of Public Utilities in Kansas City, Kansas; presented rate setting position reports to the regulatory board of the municipal utility in Austin, Texas, and Salt River Project, Arizona, on behalf of industrial customers; and negotiated rate disputes for industrial customers of the Municipal Electric Authority of Georgia in the LaGrange, Georgia district.

Q PLEASE DESCRIBE ANY PROFESSIONAL REGISTRATIONS OR ORGANIZATIONS TO WHICH YOU BELONG.

A I earned the designation of Chartered Financial Analyst (“CFA”) from the CFA Institute. The CFA charter was awarded after successfully completing three examinations which covered the subject areas of financial accounting, economics,

fixed income and equity valuation and professional and ethical conduct. I am a member of the CFA Institute's Financial Analyst Society.

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