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. 13-035-184

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HEARING PROCEEDINGS

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TAKEN AT:	Public Service Commission Hearing Room 403 160 East 300 South Salt Lake City, Utah
DATE:	Thursday, May 29, 2014
TIME:	9:02 a.m.
REPORTED BY:	Scott M. Knight, RPR

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CHAIRMAN: RON ALLEN
COMMISSIONER: THAD LeVAR

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PROCEEDINGS

THE HEARING OFFICER: On the record.

Good morning, ladies and gentlemen. This is the time and date duly noticed for a hearing in Docket No. 13-035-184. It's Rocky Mountain Power's general rate case proceeding. The formal caption is 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.

I'm Commissioner David Clark. To my left is Commission Chairman Ron Allen. And to his left is Commissioner Thad LeVar. And we'll begin this morning by taking the appearances of counsel. And if you would also introduce witnesses that you have present to testify today, that would be helpful. We'll begin with the applicant, Mr. Monson.

MR. MONSON: Gregory Monson, Stoel Rives, appearing for Rocky Mountain Power. And with me today are Bruce Williams and Sam--Dr. Samuel Hadaway. Brought two witnesses.

THE HEARING OFFICER: Thank you.

MS. SCHMID: Patricia E. Schmid and Justin C. Jetter with the Utah Attorney General's Office on behalf of the

Division of Public Utilities. The witness today is Mr. Charles E. Peterson.

MR. COLEMAN: Brent Coleman with the Utah Attorney General's Office on behalf of the Office of Consumer Services. And with me at counsel table is Mr. Dan Lawton, who will be sponsoring the Office's testimony today.

THE HEARING OFFICER: Thank you.

CAPTAIN JERNIGAN: Captain Tom Jernigan with the Federal Executive Agencies. I'm here with Mr. Mike Gorman.

MR. DODGE: Gary Dodge on behalf of UAE. UAE does not have a witness in this phase of the proceedings. So, I will primarily be an observer.

THE HEARING OFFICER: Any other appearances?

I know that we have at least one person on the phone. If any on the phone intend to participate in any way in the proceeding, we would appreciate it if you would identify yourselves now by providing your name and the organization or client with whom you're associated.

MS. RHOADES: Yes. Thank you. Hi. This is Meshach Rhoades from Greenberg, Traurig on behalf of Wal-Mart.

THE HEARING OFFICER: Thank you very much.

Are there any preliminary matters before I describe the process that we propose for our hearing today?

There appear to be none. What we would intend to do today is to begin the presentation of evidence with the applicant followed by the Division and the Office and the federal executive agencies. And when we have the cross-examination of witnesses, we'll have the applicant go last, as it desires to cross-examine witnesses of the other parties, at least if that's what you would like to do, Mr. Monson.

MR. MONSON: That's fine.

THE HEARING OFFICER: Anything else that we should settle before we proceed?

Mr. Monson, please proceed.

MR. MONSON: We'll call Bruce Williams as our first witness.

THE HEARING OFFICER: All right.

Before you're seated, Mr. Williams, if you'd raise your right hand, please. Do you solemnly swear that the testimony you're about to give shall be the truth, the whole truth, and nothing but the truth?

THE WITNESS: I do.

THE HEARING OFFICER: Thank you. Please be seated.

BRUCE WILLIAMS, being first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY-MR.MONSON:

Q. Mr. Williams, could you please state your full name for the record?

A. My name is Bruce Williams.

Q. And by whom are you employed?

A. I am employed by PacifiCorp, or Rocky Mountain Power.

Q. In what capacity?

A. I am the vice president and treasurer.

Q. What's your business address?

A. 825 NE Multnomah, Portland, Oregon 97232.

Q. Thank you. Did you prepare direct testimony in this proceeding, which includes Exhibits 1 through 14?

A. Yes, I did.

Q. And do you have any corrections that you wish to make to that testimony?

A. No, I do not.

Q. Did you also prepare and file rebuttal testimony, which includes Exhibits 1R through 5R?

A. Yes, I did.

Q. Do you have any corrections you wish to make to that testimony?

A. No. There are no corrections to that testimony either.

Q. So, if I were to ask you the questions set forth in your direct and rebuttal testimony today, your answers would be the same as set forth therein?

A. Yes. They would be the same.

Q. Okay. And do you have a summary of your testimony?

A. I have a brief summary.

Q. Would you please present that?

A. Certainly.

Mr. Chairman and Commissioners, thank you for the opportunity to be here today and discuss the cost of capital in this case. My testimony concerns capital structure and the cost of debt and preferred. Dr. Hadaway will talk about cost of equity, the other witnesses, as well.

The capital structure is relatively noncontroversial in this. The Company has proposed using the actual capital structure and actual cost of debt and preferred, which I believe has generally been accepted by all the parties in this case. But just to highlight, the common equity component of capital structure is 51.43 percent. That's a decrease from the last order for the Company here in Utah. And we hope to continue to lower that common equity component, much as Mr. Peterson suggests, but that will depend on financial ratios and results in rate cases here and other States, as well.

The cost of debt has also declined dramatically over the last four or five years. As recently as 2010, the cost of debt was about 6 percent. In this case today, it's--we're proposing 5.20. So, we've lowered the cost of debt approximately 80 basis points in four years or so. And that's been possible partially or primarily through the Company maintaining its ratings, which has allowed it to access the markets in favorable terms and rates. And we think that's important, because all those cost savings are passed directly to customers in terms of the revenue requirements.

I think in my direct testimony we estimated the reduction from the 6 percent to the 5.24 was in the direct testimony--that's about--I think it was $20 million revenue requirement savings for customers in this case. So, it does have a valuable impact on the customers here.

Finally, you'll hear a lot about ROEs, I'm sure, later this morning, this afternoon. The point I want to make is that the ROEs do have an effect on financial ratios and can impact ratings both quantitatively--and I'm sure there will be some discussion about that. And of those ratios are an important consideration by the rating agencies, that they provide the ratings on the Company. And lower--obviously, lower ratings will result in higher debt costs and higher cost to customers.

The other impact of the ROEs is also qualitative. And I think it's an important signal that the rating agencies look at as to how credit's afforded, commissions and other bodies are as to utilities. So, I would say it's both a combination of the quantitative, the model and results that come out of those, but also qualitative, especially if an ROE is significantly out of line with averages in other parts of the country.

So, that's it for my summary.

MR. MONSON: Thank you. So, we would offer Mr. Williams's direct and rebuttal testimony with our Company exhibits.

THE HEARING OFFICER: Any objections?

MS. SCHMID: None.

MR. COLEMAN: Nothing from the Office.

CAPTAIN JERNIGAN: No objections.

THE HEARING OFFICER: They're received in evidence.

MR. MONSON: Mr. Williams is available for cross-examination.

THE HEARING OFFICER: Ms. Schmid?

MS. SCHMID: Thank you.

CROSS-EXAMINATION

BY-MS.SCHMID:

Q. Good morning.

A. Good morning.

Q. My questions relate to credit and credit ratings. As vice president and treasurer, you are responsible for the Company's risk management and capital structure testimony in rate case filings. Is that right?

A. Yes. And the testimony, yes, there are-- excuse me--others who are obviously involved in setting capital structure, but in terms of testimony, yes, I'm the primary witness.

Q. Are you familiar with the things that they use in setting capital structure? Does your knowledge extend that far?

A. "They" being the Company when we're--

Q. Yes.

A. Yes. I'm very familiar with that. I'm one of the people that's heavily involved, but I didn't want to mislead you to think I'm the sole person that does that.

Q. Thank you.

Do rating agencies such as Fitch, Moody's, Standard & Poor, look at existing rate and regulatory treatment by State regulatory agencies?

A. Yes.

Q. When these credit agencies are looking at companies and assigning ratings, do you know if they look at return on equity, among other things?

A. They--yes, they will look at return on equity authorized as well as earned. There are a number of criteria that go into the ratings. That is certainly one of them, but there are many others, as well.

Q. When a company such as Moody's is assigning a rate--a rating to a company, do they also look at the Company's capital structure?

A. Yes, that's certainly one of their components.

Q. And in combination with the capital structure, does Moody's assign a value or a rating based on the Company's--let me start again.

When Moody's assigns a rating to a company and is looking at the Company's capital structure, does--is there a range at which capital structures fit into to get a particular rating? For, like, a capital structure of 45 to 55 percent equity would get an A, for example, just hypothetically, and something else would get a B or is it--or is it a point thing?

A. I'm going to answer your question maybe a little bit differently. And if it's insufficient, please ask follow-up. But it's not quite that simple. They look at capital structure. They look at other measures. They also look at the financial results and ratios that are produced by that capital structure and by the financial decisions that the company makes. They will also look at other kind of quantitative and qualitative measures as well--you know, diversity, fuel source, things like that.

So, it's not quite as simple as your capital structure directly drives the ratings. It's certainly an important determinant, but there are other things, as well. But it's--to the extent the capital structure then influences the resulting financial ratios and credit metrics, you know, yes, but it's not quite that exact of a science.

Q. And you may have answered this question generally, but I'd like a specific answer, please. Have any of the rating agencies told you that PacifiCorp would be downgraded if its equity percentage dropped below 50 percent?

A. I think if you read some of the S&P reports, and Moody's as well, there's usually a section about what could lead to ratings changes, up and down.

Q. Uh-huh (affirmative).

A. And, typically, the downgrade, they will talk about--downgrade scenario, what could lead to that, they'll talk about excess leverage or increase in leverage, things like that, that would kind of correspond to a decrease in equity component. But to be clear, they haven't said, If you go to 50.1, we're going to downgrade you. It doesn't quite work quite that way. It's more, again, the quantitative assessments. But certainly, you know, the more leverage, the greater the chance for a downgrade.

Q. So, in conjunction with your role at PacifiCorp dealing with credit, credit agencies, ratings, and the like, do you know if PacifiCorp prepares or uses things like a business plan or other like documents?

A. Oh, yes. We have a very extensive business planning process and a very detailed business plan.

Q. And these are for internal review.

A. Internal. They're also shared with the parent companies, Berkshire Hathaway Energy, and I presume

Berkshire Hathaway, as well. And, then, portions of it, not the full ten years, but typically the first five years are presented to the rating agencies.

Q. In these business reports, is there often a section on credit agency ratings?

A. Yes.

Q. You said that return on equity is one of the things that is examined when a company is--a rating agency is looking at assigning a rating to a company. And I know that Dr. Hadaway is the Company's ROE witness, but I have some questions relating to internal company functions associated with ROE, so I'm going to ask you those.

A. Okay. I'll try to answer the best I can.

Q. Do you know if the business plans that we've previously referenced sometimes contain estimates, forecasts for projections of what ROE will be awarded in rate cases?

A. I believe that's a component of that, yes.

Q. Did you see a business plan or similar document that discussed the ROE that might be awarded in this case?

A. I've seen the plan. I cannot recall what the ROE that the plan assumed would be awarded in this case is. I would expect it's probably in the line of 9.8 to 10 percent, kind of consistent of where the ROE is today. But I can't tell you with certainty what was in the plan for the ROE in this case.

Q. And do the plans generally just look at, for example, this rate case or do they go and project into the next rate case, too?

A. The plan is a ten-year plan. So, it'll--depending on what the company anticipates for rate cases, it'll have, you know, as many rate cases as a company expects to file during that ten-year period.

MS. SCHMID: Thank you. Those are all my questions.

THE HEARING OFFICER: Mr. Coleman.

MR. COLEMAN: I have no questions for Mr. Williams.

THE HEARING OFFICER: Captain Jernigan.

CAPTAIN JERNIGAN: No questions.

MR. DODGE: No questions.

THE HEARING OFFICER: Redirect?

MR. MONSON: No questions.

THE HEARING OFFICER: Thank you.

EXAMINATION

BY-THE HEARING OFFICER:

Q. I have a couple of questions, Mr. Williams. At page 14 of your direct testimony, you describe the recent common stock dividend and the plans for future dividend payments. And I just wanted your sense--I'm going to let you turn there. I wanted your sense of how much these dividend payments have affected the common equity component of the capital structure.

A. Well, excuse me. They've certainly had an impact on it. And the impact of the dividend payment is to reduce the common equity component. So, I can't quantify it exactly, but it's--
you know, the common equity level we're talking about in this case is 51.43. And I'm going to just kind of estimate. Without the impact of the dividends, I would think the common equity component would be 54, 55 percent. You know, these are the dividends during the test period through June of 2015. So, it's served to lower the common equity component and then the revenue requirements in this case.

Q. And just your ballpark estimate would be 2 or 300 basis points or something like that.

A. I think so, I mean, subject to check. Trying to be helpful, but I don't have the exact number.

Q. Thank you. Then, a question or two about the S&P adjustments for purchase power--

A. Yeah.

Q. --agreements and other items that you discuss on page 19. The PPAs account for about 229 million of $843 million in adjustments. And I just would like any general information about the other--

A. Sure.

Q. --components of the adjustment, if you have them--

A. Okay. I would say there's probably three or four big other items. I think the biggest other one is the underfunded pension and health care benefits. When S&P and other analysts look at our financial statements, they see the present value of the liabilities of the pension plan-- excuse me--and the post-retirement--the health care plan, and they compare those liabilities to the assets that are in the trust to fund those. And I think when S&P did that, it was underfunded by several hundred million dollars, primarily in the post-retirement health care trust. The pension is pretty well funded now.

The other items that are in there accrue interest, which isn't yet payable. And that would be interest on our long-term debt and other securities. That's about 100 million dollars. There's also an adjustment for operating leases. These are not leases that show up as debt on the balance sheet, but just more normal operating leases.

The other significant adjustment they make is for asset retirement obligations, which would be essentially decommissioning and restoring plant sites at the end of a plant's life. And that was, I think, in the order of 60 or 80 million dollars--60 to 80 million dollars. So, those are kind of the bigger items that they make adjustments for.

And the different agencies will do similar or different adjustments. They're all a little bit unique in how they do that, but they generally kind of follow the same thought process. They might have different treatment of PPAs or pensions or things like that, but it's the general same theory.

Q. So--excuse me--Moody's, for example, do they make similar adjustments for similar categories of interest obligations?

A. They do for certain of them. Now, Moody's is not as rigid on their PPA adjustments. I think Moody's has the view that if you're recovering the PPAs in rates, customer rates, they will not make the adjustment. Moody's does make the adjustments, though, for the pensions, the post- retirement welfare plans, the leases, and I believe the AROs--asset retirement obligations, as well. So, there's some consistency between them. There's not a perfect overlap, but there are some similarities on those items.

Q. Forgive me if you mentioned this in your previous answer, but can you roughly quantify the unfunded pension liability component?

A. The pension is pretty well funded. I don't think that's a significant amount. It's mostly the health care liability and--

Q. Thank you.

A. It's the order of magnitude of several hundred million dollars.

THE HEARING OFFICER: Those are all my questions. Any additional redirect?

MR. MONSON: I do have a question based on those questions.

REDIRECT EXAMINATION

BY-MR.MONSON:

Q. Mr. Williams, are you aware of whether the adjustments that are made to PacifiCorp's balance sheet by the rating agencies--how they compare in size or, I guess, percentage or scope with those of other electric utilities?

A. I haven't done a detailed or, I guess, a wide comparison of other utilities. I have looked at a few kind of western utilities. And, typically, in my experience, PacifiCorp had more adjustments because of the PPAs than the other utilities do. So, based on my, you know, selection and the analysis of those companies, PacifiCorp typically had more adjustments than other utilities.

MR. MONSON: That's all.

THE HEARING OFFICER: Thank you. You're excused.

THE WITNESS: Thank you.

MR. MONSON: Okay. We call as our next witness, Dr. Samuel Hadaway.

THE HEARING OFFICER: Please raise your right hand, Dr. Hadaway. Do you solemnly swear that the testimony you are about to give will be the truth, the whole truth, and nothing but the truth?

THE WITNESS: I do.

THE HEARING OFFICER: Thank you. Please be seated.

SAMUEL C. HADAWAY, being first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY-MR.MONSON:

Q. Could you please state your full name for the record, Dr. Hadaway?

A. Samuel C. Hadaway.

Q. And by whom are you employed?

A. I'm employed by Financo, Incorporated, in Austin, Texas.

Q. Okay. And did you prepare direct testimony that was filed in this case in January consisting of the testimony and six exhibits?

A. Yes, I did.

Q. Do you have any corrections you wish to make to that testimony?

A. No, sir.

Q. And did you prepare rebuttal testimony filed in--in this month, May of this year, which also had six exhibits?

A. Yes.

Q. Do you have any corrections you wish to make to that testimony?

A. No.

Q. So, if I were to ask up the questions set forth in those testimonies today, would your answers then be the same as they're set forth?

A. Yes.

MR. MONSON: We would offer Dr. Hadaway's direct and rebuttal testimony with his exhibits.

THE HEARING OFFICER: Any objections?

MS. SCHMID: None.

THE HEARING OFFICER: They're received in evidence.

BY MR. MONSON:

Q. Dr. Hadaway, do you have a summary of your testimony prepared?

A. Yes. I have a brief summary.

Q. Could you please present that to the Commission?

A. Yes. Thank you.

Mr. Chairman, Commissioners, thank you for the opportunity to be here today. My testimony addresses the return on equity, or ROE, as we call it. And my direct and rebuttal testimony support an ROE of 10.0 percent. The 10 percent ROE for Rocky Mountain Power is appropriate for several reasons. Most important, the interest rate environment has changed significantly since 2012, when the Company's existing 9.8 percent ROE was negotiated with the parties and approved by the Commission.

Additionally, the Commission has more recently found an ROE of 9.85 percent for Questar, even though Questar has acknowledged to have a lower risk profile than Rocky Mountain Power. While it is true that interest rates have dropped back somewhat since the beginning of 2014, they remain 50 basis points higher than they were in 2012 when the prior case was considered and finally decided.

The much lower ROEs recommended by the other parties are based on technical models that I believe are out of sync with current market conditions. Back in the 2012 case, interest rates on the 30-year Treasury bond had been pushed down by government--by the government's monetary policies to the lowest levels that ever have existed on that bond.

In July of 2012, the average rate on the 30-year Treasury was only 2.59 percent. At that time, I testified that risk premium estimates of ROE, based on those artificially low bond yields, did not make sense. On the other hand, in the 2012 case, the DCF models were producing ROEs at 10 percent and slightly above.

While interest rates have increased and risk premium estimates are now in the 10 percent range and higher, the DCF models are producing ROEs below 9 1/2 percent. It is my testimony in this case that it is the DCF's model that is now out of sync. It is simply not logical for long-term interest rates to go up substantially and at the same time quantitative DCF model results to go down just as substantially.

The other parties' low ROE estimates are caused by their overreliance on the DCF and other technical models. Had the other witnesses relied less on their low DCF estimates, some of their risk premium estimates support ROEs at 10 percent and higher. For example, Mr. Peterson's Ibbotson/Morningstar risk premium model produces an ROE of 10.08 percent. In fairness, he produces other risk premium estimates that are lower than that, but the Ibbotson data that you have used and other commissions have used show slightly over 10 percent.

Similarly, Mr. Lawton's traditional risk premium model produces an ROE of 9.75 to 10.01 percent. Likewise, Mr. Gorman's risk premium result, based on projected Treasury bond rates in his own testimony, is 10.24 percent. Had Mr. Gorman further adjusted his risk premium results for the tendency of risk premiums to expand when interest rates are low, his numbers would have been 10 1/2 percent or higher. I demonstrate that in my rebuttal testimony.

These data show that there is a sound support for an ROE well above the other parties' recommendations. Their continuing reliance on the DCF model, even though that model is now out of sync with market conditions, is the cause for their low ROE estimates. A more balanced approach, less tied to the technical models and further consideration for economic conditions that are improving and interest rates that, while they have declined somewhat in the past few months, are still higher than they were in 2012, it clearly supports the Company's requested 10 percent.

Thank you. I'll be glad to try to answer any questions you may have.

MR. MONSON: So, Dr. Hadaway's available for cross.

THE HEARING OFFICER: Ms. Schmid.

CROSS-EXAMINATION

BY-MS.SCHMID:

Q. Here we go. Good morning, Dr. Hadaway.

A. Good morning, Ms. Schmid.

Q. In general, is the economy better today than it was in 2009?

A. Yes.

Q. In your testimony, did you say any specific things about the 2013 economy?

A. I believe that I did. I don't remember exactly, but I usually do.

Q. And if we turn to your testimony, we see that what you said is--sorry--on line 101 is that the U.S. economy is finally on what appears to be a sustainably improving track. Does that--

A. I'm with you.

Q. And, also, later down there, you say that although unemployment remains a concern, most economists now expect the government's monetary policy to become less accommodative over the coming year. Is that right?
A. Yes.
Q. And is that still your view?
A. Absolutely.
Q. Would you say that the financial markets are in less turmoil now than they were in 2013-- sorry--2009?
A. Yes.
Q. I have an exhibit that I would like to present. And if we could label this as DPU Cross Exhibit 1. It is a two-sided exhibit. And the title is "Financial Market Stress Falls to its Lowest Level in Over Seven Years." You could take just a quick look at that while I continue to hand these out.
Have you had a chance to quickly take a look at this?
A. I'm just getting to the back part.
Q. Okay.
A. Yes, I have.
Q. I will represent that this was downloaded from the stlouisfed.org website on May 22 and is a true and correct copy of what this was.
Sorry. It was on the 27th. And the date of the

article is the 22d. I downloaded on the 27th.

Will you look at the top of the page where it says, "Financial Market Stress Falls to its Lowest Level in Over Seven Years"? And, then, there is a graph below that. Is that correct?

A. That's right.

Q. Do you agree with the St. Louis Fed's conclusion that the financial market stress is at its lowest level in seven years?

A. With the caveat we have to look at those other two graphs that are down below there.

Q. Okay.

A. You notice they're based on the level of the stock market, the S&P 500, and various other kinds of interest rates. So, it depends on how you define "stress." But certainly the graph speaks for itself in terms of the stock market has come back up to record high levels, interest rates have been low, those kinds of things. If that's the indication of stress that they're talking about here, then those are certainly true facts.

Q. Thank you. And the St. Louis Fed is one organization that you relied upon for some of your numbers. Is that correct?

A. For the data, yes.

MS. SCHMID: I'd like to move for the admission of DPU Cross Exhibit 1.

THE HEARING OFFICER: Any objection? Any

objection?

MR. MONSON: No objection.

MR. COLEMAN: No objection.

THE HEARING OFFICER: It's received.

BY MS. SCHMID:

Q. In your direct, you talk about significant increases in long-term interest rates from June 19, 2013, forward. Does that sound familiar? That would be at your direct pages 5 and 6.

A. Yes. I'm sorry. I was looking at page 8 where the table is. That's the easiest place to see how they've changed.

Q. I'll reference Table 8, then, too. So, you still believe that there will be significant increases.

A. The next table that we come to is a forward curve, so-called Bloomberg curves. And, yes, they still indicate that the interest rates will go up, not from where they were in December or November of 2013, but from where they are now.

Q. The Federal government has had what it's called a quantitative easing program for quite some time. Have the Feds announced that they will change what they are doing under that program, and if so, when?

A. Yes. They started back earlier in--they announced in June of 2013. And, then, they delayed the so-called tapering of their asset purchases, that they have now had at least four announcements of where they have reduced those purchases and have said they can plan to stop those purchases altogether by the end of 2014.

Q. Has the Federal government also announced an intention to raise its interest rates right away in conjunction with its changes to the quantitative easing program?

A. Well, not the short-term interest rates. They're tying that more to the level of unemployment and--with the new chairman, Ms. Yellen, the look at the unemployment rate has become more of a focus maybe than the inflation rate. And, so, they're saying the short-term rates may be a while out before they reduce--increase those, but they have acknowledged that they're going to do that. But the quantitative easing program is more the long-term Treasury bond rates that we talk about in the cost of equity.

Q. In conjunction with that, I'd like to pass out something that I'd like to label as DPU Cross Exhibit 2. And it also is a two-sided exhibit. And the top is entitled "Board of Governors of the Federal Reserve System."

Have you had a chance to take just a quick look at this?

A. Yes. I've read it before.

Q. Is it correct that this press release, dated April 30, 2014, says that economic conditions--and I'll read the whole sentence--"The Committee currently anticipates that, even after employment and inflation are [at] near mandate consistent levels, economic conditions may, for some time, warrant keeping the Federal"--"the target Federal funds rate below levels the Committee views as normal in the long run."

A. Yes. Again, that's the short-term rate.

Q. And, next, I'd like to talk just a little bit about ROE trends.

THE HEARING OFFICER: Are you finished--

MS. SCHMID: Yes.

THE HEARING OFFICER: --are you finished with the Cross Exhibit 2?

MS. SCHMID: Thank you. I would request that it be admitted.

THE HEARING OFFICER: And just for the record, the copy that I have really has nothing of substance on the back. There's just a header. Is that true?

MS. SCHMID: That is correct. The only thing of substance on the back page is that it says the last update was April 30, 2014.

THE HEARING OFFICER: All right.

MS. SCHMID: May that be admitted?

THE HEARING OFFICER: Any objection?

MR. MONSON: (Moves head from side to side.)

THE HEARING OFFICER: It's received.

BY MS. SCHMID:

Q. Next, I'd like to talk just a little bit about ROE trends. In your testimony, you--and in your testimony today, you say that the regulated ROE returns are in the 10 percent range and higher. Did I hear that correctly?

A. No. I think in my summary I said that the risk premium models indicate that. I have an exhibit that shows in my rebuttal testimony--it's Exhibit SCH2-R that shows exactly what the trends and the allowed rates of return would be.

Q. And I have something I'd like you to take just a quick look at here. And I'd like this marked as DPU Cross Exhibit 3, please. It is a multi-paged document. And on the first page, left-hand margin, it says, "Rate Case History, Past Rate Cases." And, then, there's a list of companies with their ROEs and other financial--other statistics of financial interest listed across a table of each sheet.

Have you had a chance just to take a brief look at this?

A. Yes. I've seen this before, too.

Q. That makes my job easier. Thank you.

When we turn to the last page, which talks about the year 2012, and it's the last page of a three-page exhibit, single-sided--for 2012, the average to date was 10.17. Is that correct? Return on equity, 10.17.

A. Yes. I was just looking at the dates. They're upside down and go from January at the bottom up to December. But that's--yes, the full year for 2012, the average for all cases was 10.17.

Q. Are you familiar with what Virginia rider decisions are?

A. Yes.

Q. Could you give just a brief two or three-sentence explanation of how a--of what they are and how perhaps they affect return on equity?

A. Right. And I exclude those in my Exhibit 2-R just for the purpose of what you're asking. But in Virginia, they have had commission orders that--for the past several years on preapproved power plant construction situations that they have adders. And they have riders and rates that automatically adjust the ROE upward, I think by maybe as much as 100 or 150 basis points. So, RRA and I and most regulatory economists take those cases out of the averages when we're talking about that. In fact, in my Exhibit 2-R, I certainly do that. I must say that we also take out the distribution-only companies, which is not done in this exhibit.

Q. So, on the 2012 page, the return on equity that I would like to focus on is 10-point--is that 05?

A. I believe it's 06. 10.06. That's the one where those power plant cases are taken out from Virginia.

Q. Thank you. Then, if we turn to the middle sheet of our three-page exhibit, we see that that is for 2013. Is that correct?

A. That's right.

Q. And what does it say that the average for 2013 is without the Virginia rider decisions?

A. 9.84. And again, Ms. Schmid, that does include the T&D-only cases that are about 40 basis--

THE REPORTER: Sorry. It includes the what cases?

THE WITNESS: T&D, transmission and distribution-only cases. They are about 40 basis points lower than the average.

BY MS. SCHMID:

Q. And I'll get to that in just a minute. On the first page, it talks about the average ROE 2014 to date. Is that correct?

A. That's right.

Q. And the average there is 9.62. Is that correct?

A. That's right.

Q. In your exhibits, you have an exhibit that contains--no. I'll leave that there.

Moving on to some more cost of equity issues, if we can look at your testimony--and what I've done is, I've had excerpts from your testimony copied. But before actually we do that, I'd like to request the admission of DPU Cross Exhibit 3.

THE HEARING OFFICER: Any objections?

MR. MONSON: (Moves head from side to side.)

THE HEARING OFFICER: Any objections? They're received.

BY MS. SCHMID:

Q. What I'm passing out now I'd like to pre-mark for identification as DPU Cross Exhibit 4. And what this is, is it is several excerpts from Dr. Hadaway's testimony in Utah over the years. And it starts with excerpts of your testimony from 2013. Is that right?

A. You missed me.

Q. Oh, my apologies.

A. Thank you. That's all right.

Q. And I will represent that these are true and accurate copies of your testimonies, but you may wish to use the printed testimonies in your book. They should be exactly the same.

So, in this case, in your direct, is it true that you recommended an ROE of 10 percent?

A. Yes. That's right.

Q. And when I look at something that is not in here--when I look at Table 5 in your direct at pages 28 and 29, which model produces the highest result out of the models that you have listed there?

A. On page 29, Table 4?

Q. Yes.

A. The equity risk premium ROE model.

Q. And that is a 10.1 percent. Is that correct?

A. Yes.

Q. And if we looked at your indicated DCF range in your direct, it's 9.1 to 9.7.

A. That's right.

Q. You also say some things in your direct that I would like to discuss. If we turn to your direct at lines 438, which are not in our packet either. I apologize.

And, so, that's on about page 20 of your direct and continues on to page 21. Is that correct?

A. I'm sorry. I may have missed the first part of your question.

Q. Okay. I'm just trying to get you to a certain place in your testimony right now.

A. I'm on page 20 right now.

Q. Perfect. Do you state that a combination of DCF and the basic risk premiums method usually provide the most reliable approach?

A. Well, that's the bottom part of that sentence, but the line immediately before it says in periods of reasonable capital market equilibrium that that's been the case.

Q. And, then, do you also say that the combination and base risk premium methods usually provide--should be discounted because of the low ROE results? More or less. Paraphrasing.

A. I'm sorry, Ms. Schmid. Could you tell me the lines you're looking at?

Q. I'm looking at 447 through 449. So, you want to discount the low ROE estimates from both the risk premium and the DCF model. Is that correct?

A. And, again, I say because of government's monetary policy in the previous line to that. That's explaining why I think they're not as reliable right now as they've been in the past.

Q. Then, when we switch to your rebuttal, what is your recommended range of your risk premium results?

A. The updated risk premium?

Q. Uh-huh (affirmative).

A. Is 9.7 to 9.8.

Q. But your recommendation is at 10.

A. Yes. That's what I explained in my rebuttal, my risk premium--in my original testimony, the other parties' risk premium results in their own testimony show returns well above 10 percent, as I explained that in my summary a few minutes ago.

Q. Now, turning to your testimony in the Docket 11-035-200 case. And the excerpts from this testimony are in your packet--

THE HEARING OFFICER: So, we're looking--

MS. SCHMID: --the excerpts I'm going to

reference.

THE HEARING OFFICER: --we're looking at Cross-Examination Exhibit 4.

MS. SCHMID: Yes. Or actually, why don't we make it--can we make this Cross Exhibit 5, just for reference?

THE HEARING OFFICER: And what would be 4, then?

MS. SCHMID: No. This would be--4 would be the 2013 packet, which we don't have. So, this would be 4. This would be 4. And that's the 2012 excerpts.

BY MS. SCHMID:

Q. Okay. If we look at your table on page 31, what type--or what methods produce the highest range, your DCF or your equity premium?

A. The DCF model did.

Q. And here you recommend the cost of equity at the highest of your DCF range. Is that correct?

A. Yes.

Q. And I'm going to read a statement. And, then, I'm going to ask you if you have comments on it. If we turn to your direct at page 31--the direct for the docket, the 11 docket, 11-035-200--

MR. COLEMAN: (Moves head up and down.)

BY MS. SCHMID:

Q. So, I'm at lines 627 through 629. And I'll just read this. And, then, I have some questions.

THE HEARING OFFICER: Ms. Schmid, just so I'm clear, so you're in the subset of DPU Cross-Examination Exhibit 4 that has the handwritten date 2/15/2012.

MS. SCHMID: Yes. And I think it might be easier if we make this one 4 and then the 10 docket 5 and the 9 docket 6, just so I can keep track.

BY MS. SCHMID:

Q. So, we're looking at what's been premarked as Cross Exhibit 4 for the DPU. And we're now looking at lines 627 through 629. And there you say--I'll paraphrase--that the requested ROE, the ROE that you recommend, which is at the top of your DCF range, is appropriate given the turmoil in the markets. Is that correct?

A. Well, the sentence is there, if everybody's at the same place here, and it speaks for itself. It says, The fair and reasonable ROE for RMP is 10.2 percent. The requested ROE at the top of my DCF range is appropriate, given the ongoing effects of U.S. and global economic turmoil and the equity market utility shares. And I explained both of those in a lot more detail earlier in this testimony.

Q. In your rebuttal, you change companies and then you have a DCF range of--sorry--you change methods, and you now have a DCF of 9.6 to 10.2.

A. No. I don't think that's right.

MR. MONSON: I'm going to object. That's very vague. I'm not sure what rebuttal we're talking about or where we are.

THE HEARING OFFICER: Ms. Schmid, I think it would be helpful if you could rephrase your question.

MS. SCHMID: I think that you're right. If we turn to the end of the packet that we've marked Cross Exhibit 4, the last two pages are from his rebuttal testimony in that docket.

THE HEARING OFFICER: Okay. So, we're still within the 2/15/2012.

MS. SCHMID: Yes. And that's the date on the--

THE HEARING OFFICER: Right.

MS. SCHMID: --front of the packet.

BY MS. SCHMID:

Q. What--

A. I'm sorry, Ms. Schmid. I'm not with you. I'm trying, but . . .

Q. Okay. So, if we take our packet that has the "2/15/2002"--

A. Okay.

Q. --we turn to the last page.

THE HEARING OFFICER: 2012, right?

MS. SCHMID: 2012. Thank you.

BY MS. SCHMID:

Q. And, then, we flip it to the front side of that last page.

A. Okay. I'm with you now.

Q. Here you continue to use the DCF analysis, which gave you the highest result, is that correct, in your recommendation, higher than the risk premium models?

A. Back in that Table 5, it did. This seems to be talking about--looking in my rebuttal update, I don't see a table for that.

10.2 was certainly the highest in the direct testimony. I don't recall, as I sit here, just what the total analysis showed in the update.

Q. I believe that you--on the last page of that exhibit, you say that the Company's initial rate of 10.2 percent remains reasonable.

A. On the left--very back, I do.

Q. So, that's using the DCF model.

Turning to our third group of--or turning to what I'll call the second group in our packet--

and we'll mark that DPU Cross Exhibit 5 for identification . . .

THE HEARING OFFICER: And which . . .

MS. SCHMID: It has--on the front, it has a date of 1--handwritten date of 1/24/2011.

THE HEARING OFFICER: So, we'll mark that DPU Cross Exhibit 5.

BY MS. SCHMID:

Q. Here you use--here you say--and I'm on page 32 and 33, which is the second page of your packet--here you say that you discount the bond yield premium results because the interest rates are artificially depressed by the government--monetary policy and continuing turbulence of the equity capital markets.

A. That's at the bottom of page 32--

Q. Yeah.

A. --where you're reading? Yes.

Q. And here you use--your highest number is a DCF range. Is that right? And--or your highest numbers are derived from your DCF models. And that range is 10.1 to 10.7.

A. They're a lot of different cases, but we didn't ask for 10.7 in that case--

Q. Right.

A. --just so we're clear on that.

Q. And here, you discounted the bond yield premium results. Is that right?

A. Yes. And go ahead with the sentence that you started to read. It says, "Because interest rates on high-quality debt are currently artificially depressed by the government's monetary policy," which I had, again, discussed in detail earlier in this testimony.

Q. If we turn to the next page, it is--it starts an excerpt on your rebuttal testimony in that docket.

A. Are you saying that these pages are from the rebuttal?

Q. Yes.

A. I'm having trouble telling that. Okay. If that's--

Q. On the bottom of the page there's a footer, which says "Rebuttal" or "Direct"?

A. Right. Mine says "Direct."

Q. Okay. Keep going. I'll give you mine.

A. I'm sorry. I had it folded. I'm with you now.

Q. Okay. Here, instead of disparaging the risk premium results, you adopted the risk premium results in contrast to what you did in your direct. Is that correct?

A. In the Docket 10-35-125?

Q. Uh-huh (affirmative).

A. So, when you say "here," you're talking about . . .

Q. It's 10-035-124.

A. Okay. And I'm sorry. You're saying that in my rebuttal testimony . . .

Q. In your rebuttal testimony, your risk-- your equity risk premium numbers were higher than your DCF numbers, is that correct, in your rebuttal?

A. Yes. Back on page 35?

Q. Uh-huh (affirmative). Yes.

A. They are at lines 723 through 726 that shows what you just said to be true, but we did not reject the DCF numbers or switch to the risk premium numbers. We stayed at the 10.5.

Q. But that's also within the range of the risk premium, right?

A. And the DCF.

Q. Okay. Also, in this section of your testimony, you state that interest forecasts for the coming year indicate significant further rate increases. Do you know what--

THE HEARING OFFICER: Could you give us a line number?

MS. SCHMID: I'll give you--yeah.

THE HEARING OFFICER: We're still in Cross Exhibit 5?

MS. SCHMID: Still in Cross Exhibit 5. Lines 733 and 734.

THE HEARING OFFICER: And that's the rebuttal.

MS. SCHMID: Of the rebuttal. Uh-huh (affirmative).

THE HEARING OFFICER: Thank you.

BY MS. SCHMID:

Q. Do you know if the expected or anticipated further interest rate increases occurred and if they were significant?

A. They did not occur. The Federal Reserve system pressed its quantitative easing policies during the period that followed this and they pushed interest rates down further.

MS. RHOADES: Hello?

THE HEARING OFFICER: Hello. Is someone on the line that needs to be recognized or has a question?

We assume not, then.

BY MS. SCHMID:

Q. And, then, turning to the last set in your packet, which is for the 2009 case, and on the front page of this packet, which I'd like to label DPU Cross Exhibit 6 for identification, there is a page from the Commission's docket index that lists the docket number and then lists some documents that were filed in this docket. Are we there?

A. I believe so.

THE HEARING OFFICER: So, this is 09-035-23.

MS. SCHMID: Yes.

THE HEARING OFFICER: And, then, just for clarification, the excerpts from Dr. Hadaway's testimony in this proceeding, those going to be used or are they no longer part of the cross-examination exhibits?

MS. SCHMID: Let's eliminate them from the cross-examination exhibits and use the testimony that we referenced in his book and in our books that was filed for reference. I apologize for having the wrong pages in the first one.

BY MS. SCHMID:

Q. Okay. In Docket No. 09-035-23, which--
did you use both the DCF model and the risk premium model

and is that depicted in your chart--
your Table No. 4 on page 35?

A. I haven't read this in a long time, but certainly both models support the requested 11 percent, yes.

Q. Your DCF model there, the "Constant Growth (Analysts' Growth)" produced the highest result of a range ending in 12?

A. Well, they're higher than the risk premium results, but we didn't even ask for the number as high as any of those numbers that you're pointing to.

Q. So, you asked for the 11 there. And here did you say that the risk premium methods and the DCF methods--I'll skip that.

You had some interesting things to say about the DCF results in this case. And if we turn to page 35 and we look at lines 748 through 753, you talk about increased market volatility and investor risk. And, then, is it true that you say that both the DCF and the risk premium models-- and I'll use my word--are useful in this analysis?

A. No. I say they're very conservative estimates.

Ms. Schmid, this case--and I'm glad you brought it up, because this shows exactly what's wrong with what's going on in the present case. We don't rely strictly on these quantitative models; this Commission never has. And it should not in the present case. Currently, DCF numbers are off the chart low. Here they were a bit on the high side. We didn't use them and the Commission didn't use them. And that's what this shows.

Q. But in the cases that we've discussed here today, hasn't the--hasn't your recommended range been within the range of your DCF and risk premium model results except for in today's case, where you're requesting a rate that is higher?

A. Absolutely not. Look at Table 4 right there on page 35 of the '09 case. The 11 percent is below any number in the DCF results up there in that box. There--only 11 percent--there's only one number down in risk premium at 10.77 that's lower than what we asked for. We don't mechanically apply these models. We always have to use judgment and review what's going on in the economy and review what's going on, not mechanically try to say here's the lowest number or the highest number we could present.

Q. Okay. I'll move on. You talked about the Questar rate case in your testimony and in your summary. And is it your opinion here today that the Questar rate--Questar Gas decision supports your recommended 10 percent ROE in this case?

A. It depends on how you look at the risk nature of the company. But you have, in your own testimony, stated that Questar is less risky than Rocky Mountain Power. And depending on what sort of a spread you would put there, then the 10.85 certainly--the 9.85 would certainly support 10.

Q. Is Questar Gas one of your proxy companies?
A. No.
Q. Why not?
A. It's a gas company.
Q. And gas companies are different than electric companies?
A. They are.
Q. In--
A. They're less risky, generally.
Q. Less risky. In the Questar case, the Commission dropped the awarded ROE by 0.5 basis points. If we--sorry--by 50 basis points. If we use that drop here, do we get to a 9.5?
A. We were never at 10.35 like Questar was, so I don't know. You subtract 50 basis points from any number you want to and come up with a different number but doesn't have anything to do with what Rocky Mountain Power's cost of equity is.
Q. But you said that gas and electric companies are different.
A. Gas companies are generally viewed as less risky.
Q. And, so, you're saying--actually, I'm not going to ask that question.
And, then, I believe that someone else probably has questions on the Washington case. Does someone else have questions--I'll let them address those. All my questions.

Thank you.

Oh, I would like to move for the admission of DPU 4, 5, and 6, however, DPU Cross Exhibits 4, 5, and 6?

THE HEARING OFFICER: Objections?

They're received.

Mr. Coleman.

CROSS-EXAMINATION

BY-MR.COLEMAN:

Q. Dr. Hadaway, good morning.

A. Good morning, Mr. Coleman.

Q. My name is Brent Coleman. I am counsel for the Office of Consumer Services. This is the first time we've had an opportunity to meet, so greetings. And I have a number of subject matters to talk to you about, hopefully relatively quickly. I don't mean to make promises perhaps I can't keep, but I'll do my best.

You do have a copy of your direct and rebuttal testimonies with you in front of you.

A. Yes.

Q. I'm going to ask you to turn--first, I'd like to turn in your direct testimony in this case to line 103.

THE HEARING OFFICER: Mr. Coleman, for your planning purposes, we're going to take a break at 10:30. We'll have a ten-minute break.

MR. COLEMAN: Okay.

THE HEARING OFFICER: Will that be adequate, given the stairs or the elevators and other issues? Okay. Thank you. Please proceed.

MR. COLEMAN: Thank you.

BY MR. COLEMAN:

Q. So, line 103 of your direct.

A. Yes. I'm there.

Q. So, just--this first part, just trying to make maybe some discussion about maybe some language corrections or clarifications, just to be clear, but what I understand.

I'm going to go ahead and read the sentence that you have from your testimony that begins on line 103. If you go ahead and correct me if I misstate, if I insert something that's not there, omit something that's there. Beginning, again, line 103, the sentence reads, "The stock market has largely recovered from its losses during the financial crisis and consumer confidence is improving." Did I read that correctly?

A. Yes.

Q. And this testimony was submitted to the Commission early January of this year, I presume, probably prepared by you sometime during December of 2013 and drafted--for drafting purposes.

A. That's about right.

Q. Would you agree with me that since the preparation and presentation of your testimony, that multiple stock indices have closed at near or at record highs?

A. Some of them have.

Q. Would you agree with me that just this week the S&P 500 closed at a record high?

A. It came down yesterday, but, yes, the two days before it was at a record high.

Q. Two days ago, it was at a record high. And would you agree with me that the S&P closing of two days ago was the 12th record-high closing of this calendar year?

A. I read that in the paper this morning, yes.

Q. I assume you would agree that's correct.

A. That's correct.

Q. So, would you--in the beginning of your testimony, you had no corrections. Would you still continue to characterize those record-high and near-record-high closings as largely recovered or would you consider the stock market to be fully recovered and stronger?

A. The S&P, which is broadest market--
well, it's not the broadest, but it's probably the most representative of the overall market, has certainly fully recovered and then some. But some of the small cap stocks and others that were pushed down more have not quite recovered. So, that's all I had in mind by "large."

Q. The Dow Jones Industrial has also closed at--

A. But those are even larger companies, only 30 of the very largest. And all I meant by "largely," there--simply, that there are some segments of the small cap and some tech areas that simply haven't recovered from where they went down.

Q. Then just below there, begins--I guess-- well, the very next sentence, line 104 through 106 and again, some of these subject matters may overlap with Ms. Schmid, but I guess I might need a slightly different point. So, I apologize for perhaps sounding a bit redundant. Line--I'll go ahead and read again. Correct me if I misstate. "Although unemployment remains a concern, most economists now expect the government's monetary policies to become less accommodative over the coming year." Did I get that correct?

A. Yes.

Q. And, then, you have a--line 143, beginning there, I'll continue to read again--correct me if I'm wrong--"This slightly changed stance from the FOMC has led investors"--"to investors' expectations for less accommodative monetary policy, which in turn have led to significant increases in long-term interest rates." Did I read that correctly?

A. Yes.

Q. And, then, you have a similar reference on line 156 of your testimony--direct testimony in this case. And it reads, "As noted above in its June 19, 2013, press release, the FOMC indicated that improving economic conditions might lead to tapering off of its stimulus programs." Did I read that correctly?

A. Yes.

Q. And in conjunction with that testimony, you have a block quote--begins on page 5, line 107--or 109 of your direct testimony--spills over to page 6. And that is from the FOMC press release of June 19, 2013--

A. Right.

Q. --right? And you represent that that is the source for your concern of the less accommodative monetary policies presented by the Fed.

A. Well, there was also a press release in-- then-Chairman Bernanke did a video presentation. It was a whole lot of things that went on that same meeting of the FOMC. But this is what their official release was that they put on the Fed's website, a portion of it.

Q. Since the presentation of this testimony and the quotation of this June 19 press release, the Fed has announced the continuation of those highly accommodative policies, correct?

A. Right. And in the piece that Ms. Schmid put up here--I believe it's one of her exhibits--that's from the most recent meeting, in April of this year. And if you look at them, they say the same thing. There are slight tweaks to the words here and there.

Q. Sure. Correct. And, actually, you cite in a footnote on page 6 that the concern that you outline from the June press release didn't actually come to pass. In your footnote 1 on page 6, you cite the October 2013 notes. And your testimony, the footnote reads, "While the FOMC, as of its most recent meeting October 29-October 30, 2013, has not reduced its Treasury bond or mortgage-backed securities purchases."

And, then, the statement goes on, "Statements following each meeting have continued to indicate likely tapering of accommodative monetary policy as economic and particularly labor markets' conditions improve over the coming year." That's the footnote.

A. That's the footnote at that time, but they certainly have--as showed in the more recent FOMC announcement, they certainly have started the tapering. They've reduced their bond purchases by about half. And it continued to say they're going, by the end of the year, to have entirely eliminated those bond purchases.

Q. But when you presented this testimony, you cited the June comments, the footnote indicates that you understood that those--that the reduction of those accommodative policies hadn't actually occurred when you provided--

A. Not by November--

Q. --when you drafted the testimony.

A. --when we were preparing this testimony, they hadn't, but they have now. And that's discussed in the rebuttal testimony.

Q. So, let me turn your attention back to Ms. Schmid's DPU 4 Cross Exhibit--Cross Exam Exhibit No. 2. Do you have that with you?

A. I have . . .

Q. Let's see. In the text, it appears to be the third paragraph from the bottom, the Paragraph 1 being the paragraph that reads, "Voting for FOMC monetary policy." So, if you go up to the paragraph that begins "To support continuing progress," do you have that one?

A. Yes.

Q. So, the last--I'm going to go ahead and read the last sentence of that paragraph. Again, correct me if I misstate. The press release reads, "The committee continues to anticipate, based on its assessment of these factors, that it likely will be appropriate to maintain the current target range for the Federal funds rate for a considerable time after the asset purchase program ends, especially if projected inflation continues to run below the committee's 2 percent longer run goal and provided that longer-term inflation expectations remain well anchored." Did I read that correctly?

A. You read that correctly, but the relevant paragraph is a bit above that.

Q. Well, that--

A. The one you're asking me about--excuse me--the one you're asking me about is what I explained to Ms. Schmid and also said, I believe, in one of the other questions is about short-term interest rates. Up at the paragraph that begins with "The committee judges there is sufficient underlying strength in the broader economy," they explain that they have done what they've done with their asset purchase program and that they intend over the year to complete that program and cease that effect on long-term interest rates. So, you're talking about two different things.

Q. But the larger accommodative monetary policies will continue for a considerable amount of time.

A. The short-term interest rate policy of maintaining the Federal funds rate, which is an overnight rate that banks pay to borrow reserves, is intended to stay low until they're satisfied that unemployment has--is at a low enough level.

Q. Did you provide testimony to the Washington Utilities and Transportation Commission in Docket UE-130043?

A. I'll accept that docket number, yes, in PacifiCorp's most recent case there.

Q. January of 2013.

A. That sounds about right.

MR. COLEMAN: If I may.

THE HEARING OFFICER: Please.

BY MR. COLEMAN:

Q. I have an excerpt of testimony from your direct. And I have a full copy, if you'd like to confirm it's accurate. In the interest of resources, I just tried to have a couple. And for purposes of identification, if we could mark this as OCS Cross No. 1.

Do you recognize this testimony?

A. Yes.

Q. And this was, in fact, the testimony that you provided to the Washington commission in January of 2013.

A. Yes.

Q. If you would turn to the part of your exhibit that contains pages 5 and 6--now I've got to find my notes. Apologies.

THE HEARING OFFICER: Good time for a break?

MR. COLEMAN: Sure. Perfect.

THE HEARING OFFICER: We'll be in recess until 20 minutes to 11:00.

Off the record.

(Recess taken, 10:28-10:42 a.m.)

THE HEARING OFFICER: On the record.

Mr. Coleman.

MR. COLEMAN: Thank you.

BY MR. COLEMAN:

Q. So, Dr. Hadaway, we are looking at the excerpt of your testimony from the Washington docket UE-130043. And if you could turn to the page that's identified as page No. 5 in OCS Cross Exhibit No. 1, I'd like to read the answer that you give at the bottom of page 5 that spills over to the top of page 6. Again, I'll go ahead and read. And correct me if I misstate anything.

Your testimony in this--in the Washington docket reads, "Growth for the U.S. economy is improving but is expected to remain slow in the near term. While most economists expect the growth rate to be positive, unemployment is also expected to remain stubbornly high near the 8 percent range. Forecasts for 2013 and beyond indicate continuing recovery, with new job creation a fundamental concern. Based on these conditions, the Fed has announced its intention to keep interest rates at their current historically low levels." Did I read that correctly?

A. Yes.

Q. So, to the Washington commission, you testified of the Fed's intention to keep interest rates low, correct?

A. At the time, that's what they said.

Q. And is that the same testimony that you present to the Utah commission here today, that your concern is that in Utah, your testimony is that they're phasing out the accommodative policy, that it doesn't exist any longer?

A. It doesn't. There's a footnote after the piece of the Washington testimony explaining exactly what I said again with the Fed's press release at the time. Time has passed and the policy has changed.

Q. Would you turn to your surrebuttal testimony. And at this point in time, I'm not going to move for the admission of OCS Cross Exhibit No. 1, because I have some intention to return to it, so I want to make sure that it's complete before I move its admission. Just to make sure that you're aware, I'm not forgetting to do that.

In your rebuttal testimony, Table 2, June 13, which was the date of this--of the Fed policy statement that you quoted, your--you represent that the single-A utility long-term interest rate was 4.53 percent, correct?

A. I say that, yes.

Q. And, then, giving a little bit of time to respond to the concern that you believe exists in the Fed policy statement, July, 4.68 percent, correct?

A. Yeah.

Q. And, then, the most recent number that you have is April of 2014 of 4.41 percent. So, that's a decrease.

A. A small one, yes.

Q. Decreasing trend. And, then, from your testimony, the date of your--

A. I'm sorry. Not a decreasing trend, sir.

Q. Okay. A decrease.

A. Yes.

Q. Okay. So, if we go to the time of your direct testimony, December of 2013 in this table, you have 4.81

percent compared to the April of 2014 of 4.41 percent. So, that's also a decrease.

A. I'm sorry.

Q. 4.41 of--in April of '14 is lower than 4.81 in December of 2013.

A. Yes. And as I acknowledged in my summary, interest rates have come down since the beginning of the year.

Q. And, then, you would agree, then, that there is a decreasing trend from two thousand--
from December of 2013 through April of 2014, the move is consistently downward in that--

A. Since December--

Q. Okay.

A. --but a trend depends on when you start. And as I explained relative to 2014, we're still 50 basis points higher than we were back at that time.

Q. Relative to your direct testimony, we're down 40 basis points.

A. Relative to December of 2013, yes.

Q. Then, looking at the 30-year Treasury rate, the same time frames--let's go with July of 2013--it is 3.61 percent in your chart and it reduces down to 3.52 in April of 2014, correct?

A. We've switched now from June to July? Because it's higher than it was in June that you asked me about before, but--

Q. No. Yeah, July of 2013 is 3.61, correct?

A. Okay. I see that, yes.

Q. And, then, April of '14 is 3.52, correct?

A. Yeah.

Q. Correct?

A. I agree.

Q. And do you know what the close was yesterday?

A. About 3.3.

MR. COLEMAN: May I approach?

THE HEARING OFFICER: Yes.

BY MR. COLEMAN:

Q. I'm going to go ahead and hand to you my tablet device, which is connected to the building's wireless. It's at money.cnn.com/data/markets. If you could just look right here (indicating), 30-year Treasury previous yield was close of yesterday.

MR. MONSON: I want a tablet.

MR. COLEMAN: I'll be happy to--

THE WITNESS: 3.3. It's 3.29.

BY MR. COLEMAN:

Q. 3.29.

MR. MONSON: I'm just kidding. I do want a tablet, but I don't expect you to give me one.

BY MR. COLEMAN:

Q. So, today's rate--or yesterday's rate at 3.29 is a further reduction from the number you have of April '14 of 3.52.

A. That's right, but it's still higher than 2012.

Q. Further in your rebuttal testimony, on line 245--actually, my apologies. Your direct testimony. Trying to keep my papers straight. Direct testimony, line 257.

A. Okay. I have that.

Q. And, then, we will spill over a little bit to the next page. Your testimony reads, "Over the past five years, average allowed ROEs have ranged between 9.9 percent and 10.6 percent." Did I read that correctly?

A. Yes.

Q. And, then, you have a Table 3 that, in a different manner--I want to say graphically, but I don't think that's the correct term--represents that same piece--bit of information, correct. You have the authorized equity returns for vertically integrated electric utilities from 2009 and up to the then-present time of third quarter of 2013. Presents the same information, 10.6 to 9.9 range.

A. Yes. That's right.

Q. So, it does range between those, but in your Table 3, there's additional information that you can read from it and that would be that there is, in fact, a downward trend, that the 10.6 is 2009, which is followed by a full- year average of 10.38 in 2010; 10.35 in 2011; 10.10 in 2012; and the then-current number in 2013 of 9.90. That's a downward trend.

A. That is a downward trend.

Q. So, then, if we turn to your rebuttal testimony--goes a little bit further. The 2009 drops off due to simply the scale, I suppose, of the table.

THE HEARING OFFICER: Can you give us a page number, please?

MR. COLEMAN: That is page 7 of the rebuttal testimony, Table 1.

THE HEARING OFFICER: Thank you.

BY MR. COLEMAN:

Q. So, to kind of flip back and forth between these two, your--the 2009 full-year average was 10.63, and that falls off in this rebuttal table, the then-current number in your direct of the 2003 [sic] full-year average was 9.90. The full year turned out to be 9.93. And, then, the first quarter of 2014, your table indicates 9.86. So, that would be a further decrease in trend. That's another lower number moving from 10.63 through the spectrum to 9.86.

A. It depends on how you look at those quarterly numbers, obviously.

Q. Well--

A. Some people have said that 2013, when rates popped up in third quarter a bit was sort of the bottom of the trend. The difference between 9.9 or 9.93 and 9.86 is certainly not a trend. So, it's a very small difference. Most people believe that allowed ROEs--

THE REPORTER: I'm sorry. I missed a word. "Most people believe" . . .

THE WITNESS: --that allowed rates of return for integrated electric companies have bottomed out.

BY MR. COLEMAN:

Q. Okay. But if you plotted on a graph the numbers 10.63, 10.38, 10.25, 10.10, 9.93, and 9.86, that would be a line moving from left to right that slopes downward.

A. Slopes downward, but the bottom end of it sort of flattens out. That's all I'm saying.

Q. With a downward slope. It may or may not have an asymptote, but the slope is downward.

A. Yes.

Q. Now, staying in your rebuttal testimony, line 245, page 13 . . .

A. Okay. I'm there.

Q. Okay. Again, I'll go ahead and read. Correct me if I misstate. Your testimony reads, "The market cost of equity is not lower today than it was in 2012 or during the past two years while interest rates were forced by government intervention to historically low levels." Did I read that correctly?

A. Yes.

Q. And Ms. Schmid talked to you before, but you did, in fact, provide testimony to this Commission on behalf of the Company in Docket 11-035-200, correct?

A. Yes.

MR. COLEMAN: I would ask the Commission to take administrative notice of Dr. Hadaway's testimony in that docket 11-035-200.

THE HEARING OFFICER: Any objections?

BY MR. COLEMAN:

Q. Do you recall the cost--your cost of equity recommendation in that docket?

THE HEARING OFFICER: Mr. Coleman, let me just reflect--your request is granted.

MR. COLEMAN: Thank you.

THE WITNESS: I'm afraid I get all the cases mixed up.

BY MR. COLEMAN:

Q. Okay.

A. But I think it was 10.2, if that's where you're going.

Q. I believe it was. And your recommendation today is 10.0 percent.

A. Correct.

Q. And, so, 10.0 is less than 10.2, correct?

A. Yes.

Q. So, your opinion is that the cost of equity is lower today, based upon your recommendation, than it was in your recommendation in the Docket 11-035-200.

A. It depends on the time periods. Obviously, that docket number has an "11" in front of it, not "12." And my opinion is that--my statement in the testimony that you read is that the cost of equity has not gone down since 2012. It's certainly was trending downward, as you correctly pointed out, during the 2011 time frame. In 2012, it trended down a little bit more. In 2013, the first three quarters it actually went up a little bit. So, it's a little bit in the eye of the beholder, but you're using 2011 data to ask me about something I said about 2012.

Q. That was your testimony about what the rates were going to be during that rate-affected period, correct?

A. I'm not sure what you're saying.

Q. The testimony that you provided in that docket was reflected--reflective of a test period, a forward-looking test period, correct?

A. I don't know. It may have been.

Q. You don't know whether or not the Company uses a forward-looking test period.

A. I know it does in this case. I don't know if it did back then or not.

Q. So, your concern is that the docket has an "11" and we're talking about 2012, and therefore, you think that those are--have a disconnect.

A. Well, you read a sentence from line 245 on page 13 of my current rebuttal testimony that says that I don't believe the cost of equity has declined since 2012. And, then, you started asking me about some testimony that has a docket number that begins with "11" and was prepared on data even before that. So, the two--I'm just saying they're a little bit inconsistent.

Q. Do you know the date of your direct testimony in Docket 11-035-200?

A. No.

Q. Would you agree with me, subject to check, that that was February 15, 2012?

A. Probably was.

Q. Did you provide rebuttal testimony in that docket?

A. Case settled, but I believe I did.

Q. Do you know the date that you provided that rebuttal testimony?

A. No.

Q. Would you agree with me, subject to check, that it was June 27, 2012?

A. Okay.

Q. Do you recall your recommendation in that rebuttal testimony?

A. I think we stayed with the 10.2.

Q. So, subject to check, on June 26--excuse me--June 27, 2012, you recommended an appropriate ROE of 10.2 in the year of 2012 was your testimony.

A. During that time period, interest rates were trending down because of the quantitative easing program. And I explained in that testimony that I thought that was an artificial reduction to the cost of interest rates and that that shouldn't be used to push the ROE down further. The Company and the other parties ultimately settled for 9.8. I believe it was in September of 2012, the Commission approved the 9.8. So, through that time period, interest rates did indeed trend down. And now they have trended up from there. And that's really--we just have to be careful about the time period so we don't get a mismatch.

Q. Your testimony is that the cost of equity has not gone down from 2012, but your recommendation has gone down from 2012.

A. But my recommendation has not gone down from the 9.8 to which the parties agreed.

Q. Your recommendation in 2012-- your testimony was 10.2.

A. Yes.

Q. And your recommendation today is 10.0.

A. That's right.

Q. And 10.0 is less than 10.2.

A. It is.

Q. We can go back to--if I could go back to your rebuttal testimony in this case, to Table 1. And, again, the piece of testimony that I'm--we're trying to focus on at this point in time is your testimony that the market cost of equity is not lower today than it was in 2012. If we look at Table 1, the annual average was 10.10, correct?

A. Yes.

Q. And, then, the annual average of authorized equity returns for vertically integrated electric utilities in 2013 was 9.93, correct?

A. That's right.

Q. Which is less than 10.10.

A. That's right.

Q. And for the first quarter of 2014, you represent the number was 9.86, correct?

A. Yes.

Q. Which is also less than 10.10.

A. Yes.

Q. And according to your chart, there are 32 commissions that have issued authorized equity--that have authorized equity returns for vertically integrated electric utilities, the majority of which are less than 10.10.

MR. MONSON: Objection. Misstates the testimony.

BY MR. COLEMAN:

Q. I believe the table indicates in 2013 the number of cases is indicated as 30 and the number of cases that lead to the 9.86 in 2014 is 2. And, so, I believe the table indicates that 32 commissions--there have been 32 cases that result--well, let me--okay. Let me restate it. Thirty cases that averaged to 9.93, correct?

A. That's right.

Q. And two cases that averaged to 9.86.

A. Yes.

Q. But it's your opinion, then, with your testimony that the market cost of equity is not lower today than it was in 2012, that the majority of those 32 commissions got it wrong.

A. That's quite a bit an overstatement on your part. The--in September, when this case--the prior case was settled in 2012, the quarterly average was 9.9. That's when the prior case--the parties settled for 9.8 here. All I'm saying in the testimony that you read a while ago is that the cost of equity has not gone down since that 9.9 was set--9.8. Excuse me.

Q. Your testimony reads, "The market cost of equity is not lower today than it was in 2012."

A. And the discussion there is about the case that was settled in 2012, in September, approved by the Commission. And that's all--my testimony may not be very artfully worded, but that's all I was saying there.

Q. If you could turn to page 13 of your rebuttal testimony. And the majority of page 13 of your rebuttal testimony, including the sentence that we've been talking about, is in response a question that reads, "What are your responses to Mr. Peterson's DCF growth rate selections?" I don't see anywhere in that answer a discussion of specifically the settled case in two thousand--the case that was settled and approved by the Commission in September 2012.

A. Mr. Coleman, on that particular page, it's not there, but if you go back earlier in the testimony, I explain that the Commission reviewed the Division and the Office testimony in the Questar case and said that the numbers that you had in those cases were too low to support that Company's operations properly and that your current recommendations are even lower. That's what all of this is leading from into a statement that since the 9.8 was settled in the 2012 case, the cost of equity has not gone down. And I don't believe it has. In fact, I think it's gone up.

Q. Okay. I would submit that your testimony doesn't say that, but--

A. Well, we have a disagreement. But, I mean, you have to look at the whole piece.

Q. I think your testimony--

A. And you can select pieces out of it like this and try to--you know, sort of like 2012 versus 2011. We have to look at the whole thing to be fair about it.

Q. I believe I read your--I read the sentence in total.

But your testimony is saying that--is that the market cost of equity is not lower than it was--
not lower today than it was in 2012. And the 2012 average that you represent in Table 1, annual average, is 1.10. And there are 30 decisions that average to a number that's lower than 1.10, which was the 2012 average--annual average, and two decisions that averaged to 9.86. And, so, you believe that the majority of those 32 decisions should have been higher than what they resulted.

MR. MONSON: I'm going to object. I think it's been asked and answered. I think it's argumentative. And I think it also misrepresents the testimony again. And I'll tell you why I think it misrepresents the testimony so that we don't have to waste a lot of time. You keep saying "majority." It's an average, so there's no majority involved.

THE HEARING OFFICER: Dr. Hadaway, would you answer the question, please?

THE WITNESS: Yes. I'll try.

THE HEARING OFFICER: It's cross-examination and we've been over the ground a great deal, but I think it's appropriate to allow--

THE WITNESS: My point, and I wasn't even trying to be argumentative about this, but yes, you read one sentence correctly. And so far today you've asked me to confirm that you've read half a dozen more sentences correctly. But if you go back and read the testimony that leads up to that sentence, you can start on page 1 where I explain what's happened since 2012. And if I didn't state that artfully on that one page where I was rebutting Mr. Peterson, then maybe I should have written it better. But what you're saying is not what the testimony reflects is the problem I'm having. So, I disagree with you.

BY MR. COLEMAN:

Q. You would agree with me, though, that capital costs are composed of debt costs and equity costs.

A. Yes.

Q. And you would agree that, based upon Mr. Williams' testimony prior--previously today, that the debt cost component of that formula has decreased for the Company.

A. That's the embedded cost of debt, yes.

Q. So, there's a decrease in the debt cost.

A. In the embedded cost of debt. There have been increases and decreases in the marginal interest rate--the current market interest rate, which is how we go about trying to set the equity rate of return. So, they're two different things.

Q. The Company's cost of debt decreased with their current--with their most recent bond issue from their expected--

A. Yes. That's what he said.

Q. And your recommendation today of 10.0 is less than your recommendation in 2012 of 10.2.

A. That's right.

Q. So, the equity component of that has decreased at least 20 basis points, in your opinion.

A. Not an equity return that the Company was authorized. They were authorized 9.8.

Q. But your opinion about--your recommendation is lower today for the equity cost component of the capital cost than it was in the prior case.

A. The recommendation is lower, but my opinion of the cost of equity is it has gone up since the 9.8 percent was established.

Q. In your direct testimony, line 188, it reads, "Interest rates are expected to rise further during the coming year," correct?

A. That's right.

Q. And your Table 2 indicates that the expected 30-year Treasury for the close of 2014 was 4.1 percent, correct?

A. Yes.

Q. And we just looked. It's significantly lower than that yesterday at close.

A. Yes, it certainly is.

Q. And, then, if we look at your rebuttal testimony, Table 2--we've already talked about the downward slope from the time of the presentation of your direct to presentation of your rebuttal testimony, correct? We did talk about that. Yes?

A. That interest rates have gone down since? Yes, of course.

Q. So, when you claim in your rebuttal testimony on line 20 that interest rates have stabilized, that might be a conservative characterization of the events from December to the present.

A. Mr. Coleman, you're right about that. And I changed that word in editing this testimony, at least in one other place, and I think two, to say "dropped." So, it's in this same testimony that I said interest rates have dropped.

Q. Line 245 of your rebuttal testimony--go back to this again--we're going to go ahead a little bit further from where we've read before. So, we've read 245 through 247, first half of 247 a couple times. I'll go ahead and finish the next sentence. And, again, the concern here is whether market costs of equity are lower.

Line 247 continues to read, "Until that intervention has ceased and reasonable equilibrium has returned between debt and equity markets, DCF estimates of COE, regardless of the growth rate inputs, will remain unreliable." Correct? Did I read that correctly?

A. Yes.

Q. So, your concern in that section of 245 through 249 is the government intervention keeping interest rates at a historically low level and the resulting lack of equilibrium in the equity markets?

A. We're going to get into it again, Mr. Coleman. That one sentence is a summary of things that I've explained previously in the other parts of the testimony. And it is true that the tapering of long-term asset purchases of the Federal Reserve system will continue on through December. And what we've seen is that as this process is started and interest rates did move up back in parts of 2013, the cost of equity indicated by the DCF model actually continued to go down.

And my explanation here is that that indicates there's something wrong with that model when you have interest rates go up 50 to 100 basis points and your cost of equity models are saying that the cost of equity has dropped by 50 basis points or more, you need to rethink whether that model is in sync with what's happening. And that's all that I'm explaining here. In that one sentence that you read, there's--you know, there's not all that explanation, but that's what I said previously in the testimony.

Q. Okay. So, just--in line 143 of your rebuttal testimony--again, I want to make sure--
perhaps I just don't understand--it reads, "The Fed has held interest rates at record low levels in an effort to stimulate the economy. While the Fed has announced or begun efforts to taper its accommodative monetary policies, the effects continue to restrain interest rates and boost stock prices."

So, am I correct in understanding that one of your concerns about the market--the current market pressures is that--is the intervention and the imposition of Federal accommodative monetary policies. Is that correct?

A. I'm not sure I understood your question.

Q. You outline a number of concerns that you have with the current market and the reasons that you believe that the discounted cash flow model, for example, doesn't provide reliable results. And one of those pressures is the government's accommodative monetary policies, correct?

A. Yes. That's right.

Q. And the resultant, in your opinion, artificially low interest rates.

A. Which then result in artificially low dividend yields, because utility stock prices have been pushed up by people seeking income. Again, I explained all of this in great detail--

Q. Sure.

A. --in my direct testimony.

Q. Okay. And, then, with respect to some of the equity risk premium analyses, in your--
excuse me--in your rebuttal, line 272, you state, "The government's intervention in the debt markets has produced artificially low interest rates. And in this environment, COE models that are affected by those rates cannot produce market-based estimates of the cost of equity for the CAPM and most other risk premium models, the effect is direct with low

COE estimates tracking the low interest rates." Correct?

A. That's right.

Q. So, we look--in your--again, I apologize for flipping back and forth--but in your direct testimony, Table 4 of your direct testimony, which is just a summary of your cost of equity estimates--
it's on page 29, the risk premium analysis that you employ is not the CAPM, correct?

A. That's right.

Q. And not the arbitrage pricing theory.

A. No.

Q. But rather a forecasted utility debt yield plus equity risk premium.

A. Right. It's exactly the same model that your witness Mr. Lawton uses.

Q. Did you provide testimony to this Commission in Docket 10-035-124?

A. If that's one of those dockets that we discussed earlier, yes, I did.

Q. I can't recall if it's a docket that Ms. Schmid referenced, but I'm going to go ahead and hand you what I'm going to mark as OCS Cross No. 2.

THE HEARING OFFICER: For the record, I believe DPU Cross Exhibit 5--

MR. COLEMAN: Okay.

THE HEARING OFFICER: --refers to Docket 10-035-124.

MR. COLEMAN: Thank you. You might have a slightly different excerpt, so . . .

BY MR. COLEMAN:

Q. Does that testimony look familiar?

A. Yes.

Q. If you'll turn to the page that has the footer page 31--so, the second page of the handout I just gave to you--

A. Yes. I'm there.

Q. --I'm going to begin reading at line 655. And at this point, I probably--I need to apologize. I changed the font in these Word documents to a font that uses a little bit less toner. And, so, the line numbers may not match the exhibit that was presented by the Division. So, as I reference the line numbers, those line numbers will be--most likely will be specific to OCS Cross No. 2.

THE HEARING OFFICER: Thank you.

BY MR. COLEMAN:

Q. Your testimony, beginning on line 655 of OCS Cross No. 2 reads, "I conclude that an ROE of 10.5 percent is reasonable for setting rates. This ROE is well within my DCF range. Under current market conditions, I discount the bond yield plus risk premium results because interest rates on high-quality debt are currently artificially depressed by government monetary policy and the continuing turbulence of the equity capital markets." Did I read that correctly?

A. Yes.

Q. So, in your testimony in this docket, when the government monetary policy artificially depresses interest rates and results in turbulence in the equity capital markets, the bond yield plus risk premium result is the only one that can see through the noise, but when those same existing conditions existed in--at the time you filed this testimony in Docket 10-35-124, the--not only did you fully discount the bond yield plus risk premium results, but you also relied upon the DCF to provide your recommendation.

A. Mr. Coleman, again, I'm sorry, but in the middle of part of your predicate--and I'm not sure I even remember exactly what you said, but what you said was not correct. These are not exactly the same conditions that existed back then. The Fed's quantitative easing policies were starting to be in full bore. Now, the quantitative easing policies are half removed and will be ended by the end of this year, according to their recent statements. So, it's very difficult to agree. And I can't sit here and say yes or no to questions where you put things like that into the predicate of the question. I'm sorry.

Q. Okay. Your testimony read--I read your testimony correctly.

A. Yes.

Q. One last exhibit. You provided testimony to this Commission--rebuttal testimony to this Commission in Docket 11-035-200. Do you remember doing that?

A. Yes.

Q. I'm going to go ahead and hand you an excerpt from that testimony.

MR. COLEMAN: And I would like to have this marked as OCS Cross Exhibit No. 3.

THE HEARING OFFICER: For the record, I marked the extract from 10-035-124 as OCS Cross Exhibit 2.

MR. COLEMAN: Correct. Yes. Thank you.

BY MR. COLEMAN:

Q. Does this testimony look familiar?

A. Yes.

Q. I'll have you turn to the second page of the exhibit, which was, after I changed the font, page 18 of your rebuttal testimony in that docket. And beginning on line 354 of OCS Cross No. 3, your testimony reads, "If an analyst were to recommend an ROE that was outside the range of all models, he or she would clearly be required to provide some reasonable justification for doing so." Correct? Did I read that correctly?

A. Yes.

Q. And your recommendation today is 10.0 percent--

A. That's right.

Q. --correct?

And did any of the models that you ran for your rebuttal testimony include 10.0 percent in their results?

A. Yes. Mr. Lawton's did. Mr. Gorman's did. One of Mr. Peterson's did. And as I explained--you said here at the end of this sentence that you need to explain why would make a recommendation out of that range. I did explain that. And that was in my rebuttal testimony.

Q. That other people's models that you modified set those.

A. Yes. And I said that in my summary earlier this morning.

Q. So, the reason--just so I understand--the reasonable support that you provide is that when you modified models run by Mr. Lawton, Mr. Peterson, and Mr. Gorman, they came up with more than 10 percent.

A. I did not modify them. They're in Mr. Lawton's testimony. Take a look. His risk premium range is 9.75 to 10 percent.

Q. So, you rely upon his testimony and not yours.

A. I'm explaining to you that there are other numbers out there that widen the range. I didn't change the way I run my models. I simply updated them with the numbers. And I explained why interest rates have dropped back since the beginning of the year. They may go up more by the end of the year. But there are clearly models in this record that support not just 9.8 as the top end of my risk premium range, but 10 percent and more. And I did not modify those models to get there.

I did, in my rebuttal of Mr. Gorman, go ahead and show that we have a disagreement about the inverse relationship between interest rates and risk premiums--it's an ongoing disagreement this Commission has had to endure for a long time--and that his risk premium model, one of them, would have produced 10 1/2 percent. So, in my rebuttal testimony, I continued to support 10. And I provided all of that information about what all of the models showed.

Q. So, you feel like you met your--

THE REPORTER: You met your what?

BY MR. COLEMAN:

Q. You feel like you met your own established threshold for providing a recommendation outside of the models that you ran.

A. Well, the last line of the sentence that you read correctly said it would clearly be required to provide a reasonable justification for doing so. And that's what I'm providing.

Q. And you believe you met that threshold.

A. I believe I did.

Q. And you were asked earlier by the Division about whether Questar was a comparable company, and the answer was no, in your analysis.

A. I did not use them in my comparable group, I believe, is what she asked me.

Q. And was there any Questar data presented--incorporated in any analysis--any of the analytical models that you ran that you presented in your testimony?

A. In this case?

Q. In this case.

A. No.

Q. You testified recently in the Entergy Arkansas case, did you not?

A. Yes.

Q. And do you recall your recommendation in that case?

A. That was sort of a funny case. The commission--the company's president said that he selected an ROE of 10.4 as the request in that case based on three witnesses' data. And my analytical models were lower. So, while I said in that testimony that I understood his reasoning and agreed with it, I did not recommend the 10.4.

Q. What did you recommend?

A. I don't remember in rebuttal what the numbers were, but I wasn't asked to say this is what the number would be without any of the other considerations that the president of the company discussed.

Q. Okay. Do you recall what the commission ordered in that case?

A. It's under review, even as we sit here. But they went below their staff to a number of 10.3 percent, which I think was the lowest ROE for an integrated electric company other than one unusual, some people say, penalty case in Hawaii. So, it was arguably the lowest ROE set during 2013.

Q. Would that be 9.3 as opposed to--

A. 9.3, yes.

Q. So, that's a data point that's actually included in your analysis in this--in your rebuttal testimony today.

A. Yes. I included it.

Q. Because that's part of the fourth-quarter results that lead to the 2013 annual average for authorized equity returns for vertically integrated electric companies.

A. That's right.

Q. That's a relevant data point.

A. I don't think it's relevant, because it's under reconsideration and hopefully it's going to be raised, so it's not such an outlier.

Q. You included it in your analysis.

A. RRA included it in their analysis. And if it is changed on reconsideration, they'll go back and make a correction to it.

Q. It makes up part of the number that you include in

Table 1 in your rebuttal for--
A. Yes, no question about it. We didn't exclude it. We used it, because it was reported by RRA.
Q. And when you provided your direct testimony in this case of 10.0 as the appropriate ROE for Rocky Mountain Power, do you know what the then-existing approved Questar rate was approved by this Commission?
A. 10.35.
Q. And, so, you felt it was appropriate to recommend a number lower than the existing Questar rate.
A. I didn't know what it was when I wrote the direct testimony.
Q. Okay. And your recommendation in Docket 11-035-200 was 10.2, in your direct testimony.
A. Third time, yes.
Q. And your rebuttal testimony stayed at 10.2.
A. Yes.
Q. And do you know the then-existing approved Questar rate approved by this Commission when you made those recommendations?
A. When I made my rebuttal recommendations?
Q. When you made both your rebuttal and your direct testimony recommendations in Docket 11-35-200, do you know the then-approved Questar ROE rate?
A. I do now, because I've read the Commission's

order. I did not know that when I prepared my direct testimony. I did know it when I prepared my rebuttal testimony.

Q. So, today, you're aware that you have made three recommendations to this Commission for an appropriate ROE for Rocky Mountain Power that were lower than the then-existing Questar rate approved by this Commission.

A. The 10.35?

Q. Yes.

A. Numerically, that's true, but I never thought about it until you brought it up.

MR. COLEMAN: I have no further questions.

THE HEARING OFFICER: Captain Jernigan.

CAPTAIN JERNIGAN: No questions.

MR. DODGE: No questions.

MR. COLEMAN: Oh, my apologies. At this point in time, I do need to go back and move for admission of OCS Cross Exhibits 1, 2, and 3 into the record.

THE HEARING OFFICER: Any objections?

They're received.

Redirect, Mr. Monson?

MR. MONSON: Thank you.

REDIRECT EXAMINATION

BY-MR.MONSON:

Q. Dr. Hadaway, you were asked some questions based on DPU Cross 3 that is the SNL report of various rates of return awarded in three years. And you wanted to explain why you didn't think the average just excluding the Virginia cases was accurate or reliable. Could you now--go ahead and explain that?

A. Yes. If we might look at my rebuttal Exhibit SCH2-R, I think we can make this very clear. We talked about these numbers at various places during the cross-examination. It's--in my opinion, sometimes confusing if we just take the RRA data and look at it, because a lot of cases a lot of different things, and you've heard the cross about whether it's 30 or 32 or whatever cases.

So, what we try to do is to parse out these cases, so we are looking at ROEs allowed for companies just like the subject company. Rocky Mountain Power is a vertically integrated company. They have generation, so forth. There are other companies in Virginia that have rate cases that only involve power plants where they have special adders. So, in this exhibit, we exclude those, and so does RRA when they discuss the average allowed rate of return.

But we also show on this exhibit the delivery-only cases, because when I've testified in the delivery-only cases, I've been asked many, many times, Aren't these companies operationally less risky? Rating agencies say that they are. And we have to agree they are.

If you look at this exhibit and you look at the delivery-only companies and then we compare it--that's in the second row of data--and you compare those to the average for the vertically integrated companies, which go right along the bottom, on average there's a 40-basis-point-lower ROE allowed for the T&D companies. Not everybody agrees that that's right, but that's what's reflected. Rating agencies say that operationally T&D companies are less risky than integrated companies. And the arguments go from there.

But the point is, the number that's been mentioned in more than one place here includes those T&D companies in the average, so it makes the trend looks like it's going down more than it is. The purpose of this exhibit is to provide the data that you've used to parse that out and decide for yourself what the right comparison is. And I didn't think that I got that clearly--that point clearly made back there in the cross-examination.

Q. Thank you. And, then, one other--well, a couple more questions. And I don't want to belabor this issue, because we spent a lot of time on it this morning. And maybe, if you think it's clear, Dr. Hadaway, don't--let me know. But you've been asked a lot of questions about a supposed change of position where you used to rely on the DCF model in one case and now you rely on the risk premium model more, because you think it's more indicative. I think you've testified in cross that in response to questions that there's been a change in circumstances. Can you just briefly explain what that is again so that the record's clear?

A. Well, really, there are at least two things there. One, certainly the market's revolving. We're moving from a very serious financial crisis out to hopefully a better situation. The first quarter of this year, though, cold weather and other things caused the gross domestic product not to grow. In fact, a corrected version now says it went down slightly. So, all these things contributed to sort of the hiccup in this--what's happening with interest rates.

The other thing about all of these cases is, though, I don't believe many times--I've read your orders or the orders of this Commission--that you've relied strictly on this is the only kind of model to use. In most commissions where I testify, they don't do that. So, that's what I was trying to explain.

And fortunately, the Division, all the way back to the 2009 case, where I didn't say the DCF model was wrong, but I recommended an ROE that was 100 to 150 basis points lower than the DCF results, because I looked at the other things that were going on at the time.

And, so, this idea that I've always recommended the top end of the range or the top end model is simply not correct if you consider the cases that Ms. Schmid put out there before you. In the last two cases, it is true. I've discounted the DCF model in this case. And I discounted the risk premium model in the prior case when the full force of the quantitative easing policies was in place. So, I appreciate the opportunity to make it clear that it's not just models.

I don't think Mr. Peterson or anyone else should go down to a very low range and offer to reduce this company's ROE when, in fact, interest rates, even with the reduction that have occurred since the beginning of the year, are still higher than they were back when that 9.8 was set. And that's been my whole point on this. But it is simply not true in the broader context of things that I've always picked the ROE from the highest model, as Mr. Peterson attempted to say in his testimony, in surrebuttal testimony, and as I believe Ms. Schmid intended to say in cross-examination. But I appreciate the opportunity to explain that.

MR. MONSON: That's all I have.

THE HEARING OFFICER: Commissioner LeVar.

EXAMINATION

BY-COMMISSIONER LeVAR:

Q. Thank you. I'll apologize to the extent that this might be somewhat repetitive, but there has been a lot of--there was a lot of discussion during cross-examination about the 20-basis-point difference between your recommendation of 2012 and your recommendation today. What would you say are the two or three most significant drivers of that difference?

A. Back when we did the analysis for the other case, the DCF results were higher. They were like--I don't remember exactly--they're in some of these exhibits, but they were above 10.2. And, so, we selected something out of that range at 10.2 back at that time, because that's what those models were saying. And we rejected or at least discounted the risk premium results, because that's when the Fed was really laying in on the quantitative easing, pushing down interest rates. So, that's why they turned out to be different.

Now we have sort of just the reverse. The Fed is reducing its policy. And the DCF model, because the stock market has gone up, dividend yields have been pushed down, analysts--Value Line and others say they believe utility stocks may be overpriced. And, therefore, analysts have reduced their growth rates, so when you put those yield plus growth numbers together in a DCF model, today you get lower ROE estimates than you got two years ago, substantially lower, even though interest rates have gone up from that time. So, the model is just out of sync. It will catch up whenever we all get back kind of to an equilibrium situation. The model is fine. People are going to continue to use it, but it's out of sync right now.

COMMISSIONER LeVAR: Thank you.

EXAMINATION

BY-THE HEARING OFFICER:

Q. I have a couple of questions, too. And my question's going to be somewhat like Mr. Monson's to you. And I suppose it also relates to your characterization of a model being out of sync. I'm trying to understand what quantitatively allows you or any analyst to make that judgment. I'm going to set aside the results of this model, because they're out of sync.

So, the way I'd like to frame this for you is if we look at the period of time and the proceeding--the Commission proceeding where you favored the results of the DCF models and discounted the results of risk premium models, in relation to your position in this proceeding, where the--your preferences are reversed, rather than, if you can, using the term "turmoil in the markets," what are the quantitative--what are the input changes that are driving those--that reversal in position of the results of those models?

A. If I get too much into the textbook mode here, just tell me that's not what you want to hear. But if I may, if we can go back to the 2009 case that Ms. Schmid finally asked me about, we didn't use the DCF results there, because utility stock prices, right along with everything else, had been really hammered and pushed down. By March of 2009, the S&P had fallen by 50 percent and utilities had fallen by twice that much.

But I looked at the model results then, and those low prices were caused by just an extraordinary event that had occurred. And, so, the dividend yields at that time were way up and produced ROEs from the DCF model in the 11 and even 12 percent range. So, our requested ROE was not based on that model, because of the unusual circumstances.

What's happened now, and when I was answering Commissioner LeVar's question, this is what I was trying to say, is utility stock prices, right along with the rest of the market, have been pushed up now, because investors, for whatever reason, are extremely optimistic. I can't read the tea leaves any better than anyone else. But many people, analysts, particularly Value Line, where we get our data, seem to think that we're probably overpriced. Twelve times we've hit all-times high in the S&P, as I was asked about earlier.

And in that environment, the analysts that look at utilities have reduced their expected growth rates in earnings for utilities, even though the economy is improving. Analysts' growth rates have come down. Well, in my experience, that happens when analysts are just not optimistic about the industry. They don't want to be making recommendations that stock prices are okay or maybe going to go up. And the way analysts who follow utilities are able to communicate that is they reduce their projected growth rates. And that's what we've seen.

Well, gee, the second term in the DCF model comes from those growth rates in some of my models and in all of some of the other models. So, that's gone down. That's one quantitative factor.

Dividend yields have gone down to below 4 percent for many utilities now, which is historically low, because of this run-up in stock prices. The argument that markets are efficient and that simply reflects a reduction in the cost of equity are beyond where most textbooks go now. There are events that occur that say that the market goes to extremes. And that's what I'm trying to explain.

The current dividend yields are understated because they've been pushed down because investors don't have any other choices. And the growth rates have been pushed down because analysts are not optimistic. But it's a matter of opinion about what that all really means.

To me, the test is, did the DCF sort of track the rest of the market as reflected by long-term interest rates. And, no, it hasn't. It's actually gone in exactly the opposite direction for interest rates. So, quantitatively, that's why I think it's appropriate now to place weight on the risk premium but not on the low, low DCF results.

THE HEARING OFFICER: Thank you. Any questions based on ours?

MR. COLEMAN: No.

THE HEARING OFFICER: Thank you, Dr. Hadaway. You're excused.

THE WITNESS: Thank you.

THE HEARING OFFICER: Anything further, Mr. Monson--

MR. MONSON: No.

THE HEARING OFFICER: --from the Applicant?

MR. MONSON: No. That's it. Thanks.

THE HEARING OFFICER: Ms. Schmid.

MS. SCHMID: Thank you. The Division would like to call Mr. Charles Peterson as its witness. Could Mr. Peterson please be sworn?

THE HEARING OFFICER: Do you solemnly swear that the testimony you are about to give shall be the truth, the whole truth, and nothing but the truth?

THE WITNESS: Yes.

THE HEARING OFFICER: Thank you. Please be seated, Mr. Peterson.

CHARLES E. PETERSON, being first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY-MS.SCHMID:

Q. Mr. Petersen, could you please state your full name, employer, and business address for the record?

A. Yes. My name is Charles E. Peterson, spelled S-O-N. And I'm a technical consultant for the Division of Public Utilities. And I'm employed in this building, which is the Heber Wells Building, on the fourth floor, 160 East South--300 South in Salt Lake City.

Q. On behalf of the Division, have you participated in this docket?

A. Yes.

Q. Did you prepare and cause to be filed what we have listed here as DPU Exhibit No. 1.10COC through DPU Exhibit No. 1.15COC, and those pertain to your direct testimony, and then DPU Exhibit No. 1.0SR and 1.1SR, which pertain to your surrebuttal testimony?

A. Yes.

Q. Do you have any substantive changes--

A. No.

Q. --to your answers?

The Division would like to move for the admission of DPU Exhibits 1.10COC through 1.15COC and 1.0SR and 1.1SR at this time.

THE HEARING OFFICER: Any objections?

They're received.

BY MS. SCHMID:

Q. Do you have a summary you would like to give today?

A. Yes. Do you want me to proceed, then?

Q. Please proceed. One--before I do the summary, would like to make a correction to Dr. Hadaway's statement. I'm sure it was inadvertent, but I only, in my testimony, represented that the last two rate cases were--his recommended ROE was at the top of his range. I recognize that in previous cases he had a much more nuanced approach.

Good morning. It's still morning. PacifiCorp, doing business as Rocky Mountain Power, has filed a general rate case in which it is requesting a return on equity of 10.0 percent, which is 0.2 percent, or 20 basis points higher than its currently authorized allowed rate of return of 9.8 percent.

Just to flesh out some value--or the value of that to the Commission: Each 10 basis points results in an approximate change in the Company's revenue requirement in Utah of $5 million or so. So, the 20-basis-point increase the Company is requesting is roughly $10 million, the increase the Company's requesting in this case.

None of the witnesses that you have heard or will hear today has demonstrated or even claimed to have demonstrated that actual investors in actual markets expect to receive a number as high as 10 percent or return on equity for investments similar to PacifiCorp. The witnesses for the Office, for the Federal Executive Agencies, and I all believe that the authorized ROE today should be below 9.5 percent.

Arguably, the Company expert, Dr. Hadaway, who you just heard, in his rebuttal testimony, estimates that the range up to about 9.8 percent is appropriate. And he has--as you've just heard, he admits that he has to reach outside of his own calculations to continue to recommend a 10 percent ROE for the--for his client.

My point estimate is 9.25 percent, but I suggested that if the Commission wishes to invoke the principle of gradualism in this case that it may be appropriate to award an ROE for the upper end of a reasonable range, which I suggest is about 9 1/2 percent.

There is general agreement among the parties for this case that regarding cost of debt and capital structure, the Company's request to set forth in Mr. Williams' testimony should be accepted. And as Mr. Williams mentioned this morning, I've raised an issue that the Company's relatively high capital structure with respect to equity may no longer be justifiable. And I was encouraged that Mr. Williams today said that the Company intends, as circumstances allow, to continue to reduce that equity percentage.

In sum, I recommend a cost of equity figure of 9.25 percent based upon the capital structure set forth in Mr. Williams'--and based upon the capital structure set forth in Mr. Williams' testimony--rebuttal testimony, specifically, and overall weighted average cost of capital of 7.28 percent.

This concludes my comments.

MS. SCHMID: Mr. Peterson is now available for cross-examination questions and questions from the Commission.

THE HEARING OFFICER: Mr. Coleman.

MR. COLEMAN: I have no questions for Mr.

Peterson. Thank you.

THE HEARING OFFICER: Captain Jernigan.

CAPTAIN JERNIGAN: No questions. Thank you.

THE HEARING OFFICER: Mr. Monson.

MR. MONSON: I have a few questions.

CROSS-EXAMINATION

BY-MR.MONSON:

Q. Mr. Peterson, good morning.

A. Hello.

Q. In your summary that you just gave, you said that none of the witnesses are telling the Commission that investors expect to receive a rate of return on utility stocks for a utility like PacifiCorp of 10 percent. Did I understand that correctly?

A. Market conditions right now do not reflect or support that--the 10 percent. And I believe all witnesses outside of Dr. Hadaway would agree with that. And even Dr. Hadaway just testified, as I understood his testimony, that he has to reach outside of his own calculations. He calls them technical calculations now--in order to continue to support the 10 percent figure.

Q. Even in one of your risk premium analyses, you got a result higher than 10 percent, didn't you?

A. I did, but I do not consider that to be reliable at all in this case.

Q. And so did Mr. Lawton and Mr. Gorman.

A. They'll have to answer for themselves.
Q. You didn't read their testimony.
A. I read their testimony, but their conclusions do not support a 10-percent figure.
Q. But they have risk premium results that were higher than 10 percent, didn't they?
A. They showed the numbers, but they obviously gave very little weight to them.
Q. Right. And, so, when you say that--first of all, I wanted to clarify: You aren't saying that Dr. Hadaway doesn't say that investors would expect a return of 10 percent, are you?
A. Would you repeat the question?
Q. Yeah.
A. It was a little bit different than I . . .
Q. I'm sorry.
A. Go ahead.
Q. When you said that none of the witnesses have told the Commission that investors expect a return of 10 percent, I assume you weren't including Dr. Hadaway in that statement?
A. I was including Dr. Hadaway in that statement. Dr. Hadaway just testified that the market conditions right now do not support what he thinks is a reasonable estimate of 10 percent. His own indicators do not support 10 percent. His rebuttal testimony indicators, none of them go above 9.8.
Q. I'm sorry. Were you--

A. Go ahead. No, go ahead.

Q. So, you're basing that statement solely on the results of the models that you ran as rebuttal testimony, is that right, or--with regard to Dr. Hadaway?

A. Well, yes. The models that you run are supposed to give indications of what investors are expecting in the marketplace. That is the intent of the models. Dr. Hadaway seems to reject those models entirely and picks and chooses a few isolated numbers that I and other witnesses have decided to put in our testimony as support for continuing the ten-point--or the continuing advocacy of 10.0 percent.

Q. Okay. But isn't, by definition, his recommendation of a 10 percent ROE an indication that he believes that's what investors expect from--
if there were a common stock at PacifiCorp, which there isn't, but--

A. I don't believe he said that. I may be wrong. I'd have to review the transcript, but I do not think he said that investors today are investing or buying and selling in the market with an expectation of receiving 10 percent or more.

Q. Okay. Well, let me just ask you a couple other things. How many CAPM studies did you do, and how many results did you get in your analysis?

A. Well, I run several models with different assumptions, different beta assumptions and risk-free rates that are based on different periods of time, averages of different periods of time. I would have to add up the exact number, but there are several.

Q. So, I think on one of your exhibits you show five results, but did you run more than that? Do you know?

A. If my exhibits show five, we could go and count them. And that would be how many I ran.

Q. Okay. But you didn't use all those in your range of a reasonable ROE, did you?

A. No.

Q. Why not?

A. I believe that the lower numbers were outside of a reasonable range that I wanted to offer the Commission.

Q. So, just as Commissioner Clark asked Dr. Hadaway as an expert witness, you do exclude the results of some models when you think that they aren't reasonable.

A. Yes. And also exclude them when they're on the high range.

Q. Right. And, in fact, you did that with the risk premium analyses you did, because one of those was over 10 percent, but you didn't include 10 percent in the high end of your range.

A. That's correct.

Q. But you did include a CAPM result of 8.65 percent, right?

A. Yes. I believe that was the highest CAPM result. And I included that at the low end of my reasonable range.

Q. But you also considered risk premium results that were below 8.65 percent, didn't you? They're on your chart.

A. They may be on my chart, but the reasonable range, if they're below the 8.65, then I would have put, basically, no weight on them in the final consideration.

Q. You acknowledge in your testimony that PacifiCorp has a lower--a higher risk profile than Questar Gas. Is that right?

A. I would generally believe that Questar Gas is a less risky company than PacifiCorp, yes.

Q. Are you aware that just this week that Barclays has issued a downgrade of all electric sector stocks--I mean bonds--I'm sorry. Have you heard that news?

A. Barclays?

Q. Barclays.

A. I haven't heard that.

Q. Okay. Assuming for a minute that's correct, would that further indicate that electrics are more risky than they were a short time ago?

A. Well, in view of--I guess in the opinion-- in the published opinion of Barclays, their published opinion I guess is lower or they're more risky. I'm making assumptions about what Barclays says. When we're talking about whether they're risky or not riskier, that they were--the companies in the industry is what it is. And, of course, at discrete periods of time, various analysts and rating agencies will publish their opinions about them, but . . .

Q. You refer in your testimony to the Questar Gas rate case order, the recent rate case order in which the Commission found a 9.85 percent ROE just and reasonable. Is that right?

A. That I referenced it or--

Q. That you referenced it.

A. I did reference it, yes. I'm aware of that decision.

Q. That's what I'm getting to. So, you're aware of that decision.

And are you aware, also, that the Commission historically, over the past several years, has typically found a higher ROE for Rocky Mountain Power, for PacifiCorp, than it has for Questar Gas?

A. That it typically has? There's been very few litigated cases involving both companies at the same time. The most recent was the 2007 case that were--cases that were just about one on top of the other. So, I don't know what the--

Q. Do you remember the results in that case--those cases?

A. Not offhand, I don't. But based upon the discussion that we just had, if you litigate PacifiCorp and Questar Gas at the same time with presumably the same models, then Questar Gas should have a lower ROE than PacifiCorp, if that's what you're getting at. That would be my general expectation in recent years. As it came out--as it's come out earlier today, Questar Gas, in fact, has had a higher ROE than PacifiCorp.

Q. During the past some years while they had the 10.35 and PacifiCorp agreed to the 9.8, is that what you're referring to?

A. Yes, specifically.

Q. Okay. You, in your testimony, try to explain this 9.85 result as a step in gradualism. Is that correct?

A. Since the Division does not understand fully the Commission's decision, that's an interpretation--that's one interpretation that the Commission did not move further in its ROE determination.

Q. And you'd agree with me that there's no mention of gradualism in that decision in connection with the ROE decision.

A. I would agree the word does not appear.

Q. And there's no indication, using other words, that that's why the Commission did what it did. Is that correct?

A. I--yes, that's correct.

MR. MONSON: And I've got a copy of some excerpts from the order. Maybe it's more efficient if I pass it out, so may I do that?

THE HEARING OFFICER: Yes.

MR. MONSON: Thank you.

MS. SCHMID: And while he's doing that, there was a question raised as to whether or not I requested admission of DPU Exhibits 1 through 1.5--1 through 1.15. And if I did not, I would like to move for the admission of those.

THE HEARING OFFICER: They've been received, I believe, but--

MS. SCHMID: Just in case.

THE HEARING OFFICER: They are received.

MS. SCHMID: Thank you.

THE HEARING OFFICER: Mr. Monson, before you continue, do you have a sense of sort of how long we're going to--

MR. MONSON: This is about it.

THE HEARING OFFICER: Okay. All right. Then, we'll--

MR. MONSON: Couple more minutes.

THE HEARING OFFICER: --we'll keep going.

BY MR. MONSON:

Q. Mr. Peterson, this is the order that we've been talking about, right?

A. Yes.

Q. And, in fact, the Commission did explain at least why it rejected the Division's recommendation and the Office's recommendation on the bottom of page 33 and the top of page

34. Isn't that correct?

A. There is one sentence that gives some explanation.

Q. And that sentence reads, "While we decline to grant Questar's request to maintain a 10.35 percent return on equity, we also find the evidence of record shows a 9.25 or 9.45 return on equity is too low to support properly Questar's operations." Is that what the Commission said?

A. You read it correctly.

Q. Okay. And in that case, the Division's recommended ROE was actually 20 basis points higher--20 basis points higher than your recommended ROE in this case. Is that correct?

A. That's correct.

MR. MONSON: That's all I have.

THE HEARING OFFICER: Redirect, Ms. Schmid?

MS. SCHMID: Just one.

REDIRECT EXAMINATION

BY-MS.SCHMID:

Q. Do you believe that the Questar Gas decision we've discussed mandates or strongly supports an ROE of 10.0 for Rocky Mountain Power now?

A. I do not.

MS. SCHMID: Thank you.

THE HEARING OFFICER: Commissioner LeVar.

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EXAMINATION

BY-COMMISSIONER LeVAR:

Q. First one's a minor one. Do you have your testimony in front of you?

A. Yes.

Q. On page 17 of your direct, on Table 4, you have a--it's authorized return of equity by State for PacifiCorp. You have a "Not Applicable" listed in California. Could you explain that to me?

A. Well, I actually intended that to mean not available.

Q. Oh, not available. Okay.

A. Maybe this is more than you want to know. We tried calling the California commission to find out what the authorized rate of return was. Ad nobody seemed to know. So, rather than--this was getting late in the preparation of this testimony. So, rather than trying to track it down through PacifiCorp, we just left it like that.

Q. Okay. Thank you. That answers that question. And one other question: I suppose I'll take the prerogative to take administrative notice of your recommendation in the 2012 rate case where your recommended ROE was 5 basis points higher than what you are recommending in this case.

A. Yes.

Q. What would you describe as the two or three most significant drivers behind that change in your recommendation?

A. Well, of course, stock prices fluctuate and analysts forecasts also fluctuate, but the 5-basis-point difference is primarily due to higher--
that stock prices are a little bit higher for electric utilities has forced down--or the result is the dividend yields are reduced, even though dividends have increased a little bit. Since that time, stock prices have increased even more for an electric utility. So, that's the main driver. The market reflects a little bit higher stock price and lower dividend yields.

COMMISSIONER LeVAR: Thank you.

THE WITNESS: Okay.

EXAMINATION

BY-THE HEARING OFFICER:

Q. I have a question or two, Mr. Peterson. On the subject of gradualism, rate stability, and the starting points for proceedings like this one being the existing authorized return on equity, you reference all of those concepts. Are those appropriate considerations, in your mind, as the Commission reviews the recommendations of the experts that testify before it?

A. Yes. I think it's important. The Questar Gas case, the various analysts and witnesses in that case were developing their analyses from a little bit different market situation last summer than I was doing the spring. So, there have been changes in the market situations from that time period, which at least partially explains why my ROE is lower than the Division's recommendation in the Questar case.

And, you know, with respect to the principle of gradualism, I think that's the valid regulatory principle and that has been in effect for a long time. And I've cited, in my testimony, references where that has been specifically invoked by commissions in dealing with rates of return. It's--in years past when you've seen, for example, dramatic shifts in the market, it's appropriate for commissions to not make a knee-jerk reaction and just match the market gyrations, but we haven't been in a dramatic shift lately.

So, I would disagree with Dr. Hadaway's continuing characterizations of the market being in turmoil. If he means that they're always fluctuating and there's always stuff going on, I guess that's true, but they are relatively stable. And I would say that they're in equilibrium, but maybe I have a different definition of "equilibrium" from his.

But, yes, I--to make a short answer, yes, I think that those are all factors to consider when the Commission deliberates it's decision in this case.

THE HEARING OFFICER: That concludes my questioning.

MS. SCHMID: (Moves head from side to side.)

MR. MONSON: Could I ask one more question, based on . . .

THE HEARING OFFICER: Do you have an objection to that, Ms. Schmid?

MS. SCHMID: I do not.

THE HEARING OFFICER: Mr. Monson, go ahead.

THE WITNESS: I thought you might.

RECROSS-EXAMINATION

BY-MR.MONSON:

Q. It's just on this--I haven't focused on this California thing. I'm sorry. But would you accept, subject to check, that the authorized ROE in California is over 10 percent, subject to check?

A. I would accept that.

MR. MONSON: Thank you.

THE HEARING OFFICER: Any . . .

Thank you, Mr. Peterson. You're excused.

Off the record.

(A discussion was held off the record.)

THE HEARING OFFICER: On the record. We'll be in recess until 1:30.

(Luncheon recess taken, 12:14-1:30 p.m.)

THE HEARING OFFICER: Okay. We'll be on the record.

Mr. Coleman, you have--you may call your witness.

MR. COLEMAN: Thank you. The Office would call Daniel Lawton and ask him to be sworn.

THE HEARING OFFICER: Please raise your right hand. Do you solemnly swear that the testimony you are about to give shall be the truth, the whole truth, and nothing but the truth?

THE WITNESS: Yes, I do.

THE HEARING OFFICER: Please be seated.

THE WITNESS: Thank you.

MS. RHOADES: Hi. It's Meshach Rhoades from Greenberg, Traurig calling back in.

THE HEARING OFFICER: Thank you. We are just starting. Your timing's perfect.

MS. RHOADES: Fantastic.

THE HEARING OFFICER: We have Mr. Lawton on the stand.

MS. RHOADES: Okay. Thank you. I'm going to put it on mute, then.

DANIEL J. LAWTON, being first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY-MR.COLEMAN:

Q. Thank you.

Mr. Lawton, would you state your name and business address for the record?

A. Sure. My name is Daniel J. Lawton, L-A-W-T-O-N. And my business address is 12600 Hill Country Boulevard, Suite

275, Austin, Texas 78738.

Q. Did you prepare direct testimony identified as OCS-1D Lawton submitted to the Commission on April 17, 2014, in this docket?

A. I did.

Q. And along with that, did that testimony also encompass Exhibits OCS 1.1D through Exhibit OCS 1.11D?

A. It does. And they were both--all prepared by me or under my direct supervision.

Q. Did you also prepare surrebuttal testimony in this case identified as OCS-1SR Lawton filed with the Commission on May 22, 2014?

A. Yes, I did.

Q. Do you have any changes or corrections to any of that testimony or any of those exhibits that you'd like to make at this time?

A. None that I'm aware of at this time.

Q. So, if I asked you the questions contained in both your direct testimony and your surrebuttal testimony today, your answers would be the same as contained therein.

A. Yes, sir.

MR. COLEMAN: At this time, I would move for the admission of Mr. Lawton's direct testimony, the related exhibits, OCS 1.1D through OCS 1.11D, as well as Mr. Lawton's surrebuttal May 22, 2014, into the record.

THE HEARING OFFICER: Objections?

MS. SCHMID: None.

THE HEARING OFFICER: They're received.

BY MR. COLEMAN:

Q. Thank you.

Mr. Lawton, do you have a brief summary of your testimony and position in this case to present?

A. I do.

Q. Please proceed.

A. Thank you.

And good afternoon, Commissioners. I changed my summary already from the morning, but we're moving along and it's nice to be back again.

Basically, the issues in this case--and I've outlined in my direct and surrebuttal testimony--is that on behalf of the Office, I am recommending a 9.2 percent cost of equity for Rocky Mountain Power. The end result is a 7.26 percent overall return to be earned on invested capital.

There is no dispute in my testimony between me and Dr. Hadaway or Mr. Williams with regard to capital structure. I agree and--with the capital structure Mr. Williams recommended in his rebuttal testimony. And I would urge the Commission to adopt the updated capital structure, as well as cost rates for debt and preferred.

Our basic disagreement is the one big issue that you've heard about quite a bit this morning, is the cost of equity. The models I employ are the same or similar models that Dr. Hadaway employs. The comparable groups of companies are quite similar. There's no major differences there.

The end result is, do we rely upon the DCF--discounted cash flow--risk premium or capital asset pricing models? I've outlined in my testimony what those results produce--what those models produce and to give you a range of results. The basic models, not only in my analysis but in Dr. Hadaway's updated analysis, none of the models support a return on equity in excess of 10 percent. Moreover, they don't support a return on equity in excess of your currently authorized 9.8 percent.

What I would ask that you look at and I tried to outline throughout my direct testimony and throughout my surrebuttal testimony are the following facts: Commissions, like this regulatory body that have to make these kinds of decisions all the time like you recently made and are making again with regard to return on equity--commissions around the country, regulatory authorities are authorizing lower and lower equity returns. That's in the data of Dr. Hadaway's testimony, as well as mine. That data is a fact.

Interest rates have been declining since the end of last year, continue to decline. If you want to look at interest rate declines, Treasury rates and all interest rates have declined since the '80s, I mean. But recent declines are even more pronounced given what--the level they're at as of December 2013.

In terms of the Federal Reserve, I think there's some confusion--the documents or exhibits and the testimony. The Federal Reserve policy is to be accommodative. Yes, tapering has ceased, or in terms of it's being scaled down, it's gone from $85 billion of asset purchases down to 45 million [sic], but remember this plan has been in place for a long period of time and a lot of asset purchases have taken place. A lot of liquidity has been put into the market. So--and the end result is, the interest rates you see declining, as well as the Federal Reserve statements on this matter.

So, I think interest rates are continuing to fall. They're at very low levels. And nothing in the evidence in this record supports the return on equity that the Company's requesting. Rather, a lower return, I believe, should be authorized.

And that's all I have. Thank you.

MR. COLEMAN: At this point in time, I would make Mr. Lawton available for cross-examination from the parties or from the Commission.

THE HEARING OFFICER: Any questions?

MS. SCHMID: No questions.

CAPTAIN JERNIGAN: No questions.

THE HEARING OFFICER: Mr. Monson.

MR. MONSON: I have just a few questions.

THE WITNESS: Good afternoon, Mr. Monson. Good to see you.

CROSS-EXAMINATION

BY-MR.MONSON:

Q. Good afternoon. How are you?

A. Good.

Q. Okay. First of all, on this interest rate question that you brought up in your summary--

A. Sure.

Q. --you would agree, however, that interest rates are lower--were lower--I'm sorry--
during Rocky Mountain Power's last case than they are currently on long term.

A. Do you have a specific--

Q. Yeah. Do you have a chart in your--

A. I do. If you would look at my Schedule DJL3--I mean OCS3. Excuse me. I--in other cases, I call them DJL. OCS 1-3D.

Q. Okay. So, if you look at the interest rates for 30-year Treasuries in the fall of 2012, what do you get? Let's see. Say September.

A. In September, you're seeing about 2.88 percent.

Q. Okay. And, then, what do you get currently?

A. About--today it's 3.28 percent.

Q. Okay.

A. Two basis points difference.

Q. And that would essentially hold the same for any of these 20-year treasuries or corporate bonds, not the same ratio, but the same--they would have been lower in September of 2012 than they are today.

A. Right.

Q. Okay.

A. Because the numbers in September or that period in 2012 is the lowest historical number ever for these securities. So, any measure against it is obviously going to be higher.

Q. All right. And that was the time just before the Commission decided the last case and the parties negotiated the settlement in that case, right?

A. That was the time period that--I think the Commission order came out September 2012 period, somewhere around there or the settlement was agreed to.

Q. Okay. And, then, on the issue--I think you may have clarified this in your summary, but this issue about the Fed's policy.

A. Yes.

Q. I mean, you agree that they have--they are tapering the amount that they're buying of the longer-term bonds.

A. Yes. They've tapered that in four different installments down to roughly 45 billion per month.

Q. Right. And at least their announced plan is they're going to taper it further. They may change that, but right now their announced plan is they're going to taper it down to zero by the end of the year, right?

A. Their announced plan is there's no specific schedule of when the tapering will be completed. It could be adjusted by facts and circumstances.

Q. Okay.

A. The expectation of the markets out there and other analysts are that it would be completed by the end of the year, but I think Chairman Yellen of the Federal Reserve has said there is no specific hard-and-fast dead day.

Q. So, when you say in your--let's see--in your direct testimony when you say on line 1033--

A. Excuse me. One-oh what?

Q. 1033.

A. Give me a moment.

Q. On page 40.

A. I'm there.

Q. When you say that Dr. Hadaway is quite incorrect, the OMC has not announced plans to change the course of accommodative monetary policies, you're referring there to the Federal fund rate, I assume.

A. No. I'm referring to the tools in the toolbox of the

Federal Reserve and the statements by the Federal Reserve that the Federal Reserve's policy on monetary policy will continue to be accommodative. And that's set forth in my Exhibit OCS 2 in my testimony.

Q. Okay. So, you don't include, I guess, within that, then, the fact that they are tapering their purchases of long term bonds.

A. No. I think you're incorrect. You seem to be under the misperception that because we lower the amount of asset purchases, we're changing the course of accommodative policy. That's not the case at all. And as you can see from my Exhibit 2, is why I included it here, the language of the Federal Reserve is: Our policy will continue to be accommodative, both the short-term and long-term rates. Remember, there's a housing problem in this country and they're trying to get that market going.

Q. So, the fact they've gone from 85 billion down to 45 billion, in your mind, doesn't reflect a change in approach they're taking toward monetary policy.

A. No, not at all. It's a change in the tools--in the mix of tools they're using.

Q. Okay.

A. We've got to keep in mind that the Fed, through the policy of quantitative easing, was making asset purchases of $85 billion a month for quite a few months. Those asset purchases have been made. That hasn't changed. That liquidity's still out there. That doesn't mean that the Federal Reserve planned to have $85 billion a month for five years or ten years. It looked at the facts on the ground and determined that they could scale back to about 45 million [sic] as the new number.

Q. Okay. All right. Let me just ask you one other thing.

A. Sure.

Q. You were the Office's witness in the Questar Gas case, right?

A. I was indeed.

Q. And you recommended a ROE in that case of 9.25, right?

A. I did.

Q. The Commission ordered 9.85.

A. I believe that's correct.

Q. So, you were 60 basis points lower than when the Commission found to be the appropriate authorized ROE.

A. That's correct.

Q. Okay. And in this case, you're recommending a 9.2, but that's based, at least in part, on a 20-basis-point adjustment for capital structure. Is that right?

A. For capital structure, or to be clear, financial risk differences.

Q. Right. And, so, other than that, you would have--would you have been recommending 9.4?

A. Absent another adjustment, yes.

MR. MONSON: Okay. That's all my questions.

THE HEARING OFFICER: Thank you.

Redirect?

MR. COLEMAN: I have no redirect questions. Thank you.

COMMISSIONER LeVAR: I have one.

THE WITNESS: Good afternoon.

EXAMINATION

BY-COMMISSIONER LeVAR:

Q. Mr. Lawton, did--in your opinion in your experience, did you find anything anomalous about this year's modeling results?

A. Anomalous? No. The modeling results obviously--the yields have been affected. We all know that. But to say that--and by modeling, I'm referring to the discounted cash flow. And by the expected growth rates, the levels that they're at compared to other years, I don't see anything anomalous there. But I do agree with Dr. Hadaway to the extent that the yields have decreased because utility prices have increased in recent years. But overall, anomalous results that they cannot be used, the answer would be "No."

COMMISSIONER LeVAR: I don't have anything else.

THE HEARING OFFICER: A couple of follow-up questions.

THE WITNESS: Yes, Commissioner. I'm sorry. I didn't mean . . .

EXAMINATION

BY-THE HEARING OFFICER:

Q. That's all right. So, does that mean that you--the current utility stock prices are sustainable, in your view?

A. I think that there are some sectors of the market right now that may be subject to the decreases or market correction. I don't know that--
and I don't believe that the utility sector is going to be subject to such a correction until interest rates change substantially. And, so, if--the short answer to your question, if you're referring only to utility stock prices--

Q. Right.

A. --the answer is "Yes" on the accommodative course of the Federal government, which they plan to have for some time.

THE HEARING OFFICER: Thank you.

Any questions based on ours?

MR. COLEMAN: I have no additional questions.

THE HEARING OFFICER: Thank you.

THE WITNESS: Thank you, Commissioners, again.

Thank you for having me.

THE HEARING OFFICER: Thank you very much.

Captain Jernigan.

CAPTAIN JERNIGAN: Yes. The FEA would like to call Mr. Gorman to the stand, please.

THE HEARING OFFICER: Thank you.

Do you solemnly swear that the testimony you are about to give will be the truth, the whole truth, and nothing but the truth?

THE WITNESS: I do.

THE HEARING OFFICER: Thank you, Mr. Gorman. Please be seated.

Captain.

MICHAEL GORMAN, being first duly sworn, was examined and testified as follows:

DIRECT EXAMINATION

BY-CAPTAIN JERNIGAN:

Q. Can you please state your full name and your employer, please?

A. My name is Michael Gorman. I'm employed by Brubaker & Associates, Chesterfield, Missouri.

Q. And did you prepare and file direct testimony and surrebuttal along with exhibits for both of those that have already been filed?

A. Yes.

Q. And do you have any changes or corrections you would like to make to either of those?

A. I do. Some of these changes were made on an errata filed earlier. And some of the changes were found by Dr. Hadaway. And I agree that some corrections were needed in my surrebuttal testimony.

On page 2, on line 25, the number 7.74 percent should be struck. The number 7.41 percent should be inserted.

THE HEARING OFFICER: Is that in the surrebuttal?

THE WITNESS: In the direct testimony.

THE HEARING OFFICER: In the direct.

THE WITNESS: Thank you. That was part of the errata filed earlier.

On page 12, footnote No. 8 should be changed to footnote No. 5.

On page 37, on line 737, the number 6.3 percent should be changed to 6.2 percent. That same page and on that same line within the parenthetical, the number 6.9 percent should be changed to 6.6 percent.

On my Exhibit FEA MPG5, the column titled "2012" should be corrected to "2013." That would be under both dividend per share, earnings per share, and payout per share --or payout ratio. Excuse me.

And on my Exhibit FEA MPG17, page 1, on line 12 under the column reference, line 1 should be changed to line 4 and Column 1 should be changed to Column 2.

That completes my corrections.

THE HEARING OFFICER: Would you mind restating those last ones? I just got to the right page.

THE WITNESS: I apologize. On my Exhibit MPG17--

THE HEARING OFFICER: Right.

THE WITNESS: --page 1, on line 12, under the column reference, the line that's--it states page 3, comma, line 1, it should read line 4.

And it states Column 1. It should be Column 2. Col. 2 rather than Col. 1.

THE HEARING OFFICER: Thank you.

THE WITNESS: Those complete my corrections.

BY CAPTAIN JERNIGAN:

Q. With those changes, if I ask you the same questions here today, would your answers be the same?

A. Yes.

CAPTAIN JERNIGAN: Move for admission of Mr. Gorman's . . .

THE HEARING OFFICER: Objections?

MS. SCHMID: None.

THE HEARING OFFICER: They are received.

BY CAPTAIN JERNIGAN:

Q. Would you like to give a brief summary of your testimony, please?

A. Yes. Thank you.

Good afternoon, Commissioners. In my testimony, I comment on the Company's proposed overall rate of return. In my recommendations, I propose that the Commission adopt a return on equity of 9.4 percent.

In arriving at my recommended return on equity, I conducted three versions of the discounted cash flow analysis, a risk premium study, and a capital asset pricing study.

In performing the discounted cash flow analysis, I performed three versions of that study. The three versions include a constant growth model reflecting analyst projected growth, a sustainable constant growth model reflecting the internal growth characteristics of the companies included in a proxy group, and a multistage growth DCF model, which reflect a long-term transition from current short-term growth outlooks reflecting the analyst three to five-year growth projections trending out to a long-term sustainable growth rate outlook as reflected by what I believe to be the maximum sustainable long-term growth rate for a utility company.

I also looked at the relative fundamental factors underlying DCF components for each of the companies in my proxy group. And I find that the DCF model now produces fundamentally sound return on equity estimates. I did that in response to Dr. Hadaway where I showed that the valuation metrics for utility stocks are reasonably consistent with long-term historical valuation metrics. Those include price/earnings ratios and price-to-cash-flow ratios.

In my sustainable growth rate DCF analysis, I developed a growth rate reflecting the internal earnings growth potential of utility stocks. And that included looking at whether or not the utility can afford their dividend and whether or not the utility can retain enough earnings in order to grow their earnings over time. Those analyses indicate to me that the fundamentals of the DCF model, at this time, are producing reliable results.

I--in my risk premium analysis, I also reflected some uncertainty and risk in long-term interest rate markets. Those uncertainties are created by the current Federal Reserve policies and the ultimate impact of what long-term interest rates will be once quantitative easing is terminated.

There is some uncertainty in the interest rate markets. And I tried to capture that uncertainty by recognizing risk in the equity markets, which indicated to me an above-average equity risk premium was appropriate in supporting my recommended return on equity in this case.

My capital asset pricing model, I used the forecasted Treasury bond yield, which was significantly higher than current observable Treasury bond yields, which I felt was appropriate, given the uncertain outlook for interest rates in the current environment.

Based on that analysis, I believe that my 9.4 percent return on equity is reasonable in consideration of the full analysis that I conducted to measure the current market cost of equity for PacifiCorp, or Rocky Mountain Power.

That concludes my summary.

THE HEARING OFFICER: Thank you.

CAPTAIN JERNIGAN: Now I submit Mr. Gorman for examination, please.

THE HEARING OFFICER: Questions?

MS. SCHMID: No questions.

MR. COLEMAN: I have none from the Office. Thank you.

THE HEARING OFFICER: Mr. Monson.

MR. MONSON: Thank you.

CROSS-EXAMINATION

BY-MR.MONSON:

Q. Good afternoon.

A. Good afternoon.

Q. You did an analysis in your testimony that was intended to show that if the Commission adopts your recommended ROE of 9.4 percent that the--that it won't negatively impact the financial integrity of the Company. Is that right?

A. Yes.

Q. And you did this by comparing the results for the Company under certain ratios considered by rating agencies in determining the bond ratings, but using your recommended ROE of 9.4 versus the current authorized ROE of 9.8. Is that right?

A. No. I measured with the financial metrics under the cost of service in this case using a 9.4 percent return on equity.

Q. Okay. Thank you for that clarification.

And in his rebuttal testimony, Mr. Williams noted that you had done that but didn't use the current S&P metrics. Is that right?

A. That is his testimony. And he is correct. S&P did modify their metrics in November of last year. And I used the metric formula which had been in effect since around 2008. But it was revised in November of last year. So, that is correct.

Q. So, you redid the analysis in your surrebuttal testimony. Is that right?

A. I compared the benchmarks to the benchmarks in the new methodology, yes.

Q. Okay. Can you turn to page 2 of your Exhibit 1-SR? Have you got that?

A. Page 2?

Q. Page 2, yeah.

A. Yes, I'm there.

Q. Okay. And this is where you're getting your pretax rate of return that you're going to use in the analysis, correct?

A. Yes.

Q. Okay. And I notice in your first--in column 1, the one that's numbered 1, you end up with a weighting of over 100 percent--100.17 percent. Is that right?

A. Yes.

Q. That would be an error, right? You can't have more than 100 percent, can you?

A. Yeah. There does appear to be a calculation error on that schedule, yes.

Q. And, so, this--the number you used, 10.36 percent on that same row 4 would be an error somewhat. Is that correct?

A. I would have to review it, but it looks like there may be an error on that schedule, yes.

Q. So, then, if we take that 10.36 back to page 1 of the same exhibit, that's used in your analysis for all these numbers. Is that correct?

A. It is.

Q. So, those would also be an error if that's an error.

A. Error--a correction would be necessary, yes.

Q. Okay. Another issue related to this analysis was a discussion about off-balance-sheet debt. And you made a--you did accept an adjustment that's shown on page 4 of this exhibit of 271 million, as I recall. Is that right?

A. Yes.

Q. Just a little nitpick point, but on line 2 of that exhibit, you got total Utah May 2013 rate base. Would that be total company instead of total Utah?

A. Which line are you looking at?

Q. Line 2, page 4 of Exhibit MPG1-SR.

A. Page 2?

Q. Page 4.

A. I'm sorry. Yes. On line 2, that should be total company.

Q. Okay. Now--but, anyway, the result of this is you have--you've made adjustments to the off-balance-sheet debt on line 6 of 271 million, effectively, right?

A. Yes.

Q. And you remember--I think you understand that Mr. Williams made an adjustment of about five hundred and some-odd million?

A. Yes.

Q. Okay. So, do you understand what the difference is between his adjustment and yours, what's included in his and what's--and not included in yours?

A. Well, the difference is based on total PacifiCorp investment characteristics versus the financial obligations that are part of the retail cost of service in Utah. And there's also differences in the way Standard & Poor's treats some of the financial obligations of the Company versus the regulatory treatment of those financial obligations. Specifically, one of the largest differences deals with pension and other post-retirement health benefits for the Company.

I believe Mr. Williams testified this morning about their health benefit obligation being underfunded. S&P recognizes that as a financial obligation. And that financial obligation is picked up in the cost of service in this case in a way that is different than the way S&P treats it. So, if I recognized it in my financial metrics the same way S&P was treating it, it would be double-counted in the cost of service methodology here.

So, the difference between what Mr. Williams is proposing to do with that particular off-balance-sheet debt obligation is different than the way I'm proposing to treat it here, because, again, the way pension benefits and OPEB benefits for regulatory purpose treatment is different than the way S&P recognizes them in their financial obligation development.

Another issue deals with curve interest expense. And, again, that's different in the way S&P treats it versus the way interest expense is recognized in cost of service. By cost--all the interest expense that is the obligation of Utah customers is reflected in a rate of return--

THE REPORTER: Sorry. Could you just slow down just a little bit? ". . . obligation of Utah customers is reflected in a" . . .

THE WITNESS: --in the rate of return on rate base and possibly in some CWIP interest obligations. So, again, there's a difference in the regulatory treatment and the S&P treatment.

I tried to take just S&P's general framework and modify it in a way that produces meaningful metrics, recognizing the regulatory treatment of some of those financial obligations.

So, I haven't replicated S&P's treatment, but I've been pretty true to the treatment, recognizing the distinction--distinctive differences in pension and some interest obligations of the Company.

BY MR. MONSON:

Q. So, now, I take it that you're not saying, then, that you have compared the metrics that S&P uses with the current metrics to determine if there would be a deterioration in credit rating or in--even in credit worthiness. You've done something different than that. Is that right?

A. No. I've--my--again, the methodology-- the regulatory process includes pension obligations and it includes OPEB obligations. So, those are in the cost of service formula being covered by the cash flows of the Company. So, I believe that I have captured that in my methodology in a way that is comparable to what S&P does. But to also make S&P's adjustment on top of the regulatory treatment, I believe would have double-counted those financial options.

Q. But you'd agree with me that when S&P does their analysis, they do include those obligations.

A. And I have, also. I've just included them in a way that is consistent with the regulatory framework. To do what you're suggesting, I would need to move the cash flows out of cost of service, put them in the funds from operation, and then recognize them as additional cash flow to meet additional financial obligations. I believe that process would have been very difficult and likely would not have produced meaningfully different results.

Q. And you also mention that you have tried to take a Utah ratio and apply that to these numbers so that you're just looking at a Utah cost of service effect of the change in ROE. Is that right?

A. It is, because I'm trying to answer the question: Is my proposed return on equity appropriate for setting prices for Utah customers?

Q. Right.

A. Does it reflect fair compensation to the investments made in Utah? Does it support financial metrics that are consistent with investment-grade credit quality for providing service to Utah customers? That's what I'm attempting to measure with my metrics.

Q. So, when S&P makes its ratings and looks at these metrics, it doesn't look at just Utah, does it?

A. It does not. It looks at total company.

Q. And when investors buy the bonds of the Company, they don't just buy the Utah--bonds on the Utah operations, they buy them on the entire company.

A. Correct. Yes.

Q. So, if you're trying to compare the difference between the cost of service, which I guess I misstated as 10 percent ROE and you're 9.4 percent and you're trying to do it to compare what S&P's ratings would be to show whether they cause financial impairment, you wouldn't take the Utah portion, would you? Because S&P doesn't take the Utah portion.

A. Well, S&P isn't concerned about just and reasonable rates to retail customers. That's the objective of what we're examining in this case. So, in ensuring rates are just and reasonable, the rate of return has to be fair compensation and has to provide adequate financial metrics to support investment-grade bond ratings for the capital invested in Utah. That's the subject of this proceeding. S&P doesn't have the same subject in their review. But this--my subject is to look at whether or not the rate of return and cost of service elements, the retail service for Utah meets the Hope and Bluefield standards.

So, my objective--the questions I'm asking myself are different than the questions S&P is asking itself, because S&P doesn't ask whether or not rates are just and reasonable; I do.

Q. Okay. But S&P's is one of the entities that determines the bond rating of the Company. Isn't that right?

A. It's true. But it's also true that rates in Utah could be adequate to support strong investment-grade credit, but other elements of the Company may not. So, if you don't distinguish between Utah operations and other parts of the Company, then Utah customers could be asked to pay excessive rates to compensate for other parts of the Company that aren't covering their financial obligations. And I don't think that would be consistent with setting just and reasonable rates.

Q. You performed a risk premium analysis in your testimony, is that correct--

A. It is.

Q. --in your analysis?

And your risk premium analysis does differ from Dr. Hadaway's in certain respects. Is that right?

A. One significant respect, yes, but otherwise, it's fairly similar.

Q. Okay. I mean, you use 1986 to 2013. He used 1980 through 2013, for example. Is that right?

A. Time periods slightly different, yes.

Q. And you also used different--you used a different bond than he uses, but, of course, you compare your risk premium to that bond versus what he compares to his bond. Is that right?

A. It's very similar, yes.

Q. Okay. So, the big difference, though, is this inverse relationship, right?

A. Yes.

Q. And do you not agree there is an inverse relationship?

A. I believe that if you look at authorized returns on equity and compare them to contemporary bond yields, you'll see the equity risk premium for authorized return expanding when bond yields decrease. But the academic literature doesn't support that as the only factor that explains what an appropriate equity risk premium is.

Academic literature is very clear. Changes in interest rate is one factor, but the true factor that changes--changes in equity risk premiums is changes in the--the risk of an equity investment compared to the current risk of a bond investment. When equity investments get more risky, the equity risk premium expands. Conversely, when bond risks--bond investments get more risky in relationship to equity investment, the equity risk premium contracts.

So, interest rates are one factor that helps explain that, but it's not the only factor. And to assume, as Dr. Hadaway does, that it's the only factor, he significantly distorts what an appropriate risk premium is when you consider other risk factors and generally total risk factors in measuring an appropriate risk premium.

Q. So, one of the sources you cited for your statement that academic literature says that there's more factors involved is Harris and Marston, right?

A. Yes.

Q. Can you turn to page 321 of your surrebuttal testimony--line 321. Sorry.

A. I'm there.

Q. This is a quote from Harris and Marston, right?

A. Yes.

Q. Okay. And if I read it correctly, it says, "The market risk premium changes over time and appears inverse"--"and appears inverse"--"inversely related to government interest rates but is positively related to the bond yield spread."

So, they are saying that it's inversely related, aren't they?

A. They say it appears.

Q. Okay. And, then, they say--let's see. Well, so even in the source you cite, they're acknowledging that they have--that it appears there's an inverse relationship between risk premiums and interest rates.

A. Yeah. As I said, changes in interest rates are one factor, but they're not the only factor.

Q. Okay.
A. And to assume, as Dr. Hadaway does, that they're the factor allows for the mis-estimate of a fair risk premium in the current market.
Q. Okay. So, Dr. Hadaway did a regression analysis in which he plugged in, as one of his factors, interest rates and the other factor, the risk premium, right?
A. No. He plugged in interest rates and commission-authorized returns on equity--
Q. Okay. Sorry.
A. --to measure risk premiums.
Q. All right. Okay. And he ran that regression analysis. And it showed that there was a correlation, an inverse correlation, right?
A. Yes.
Q. And was it a valid regression analysis? In other words--
A. Statistically, it was valid, yes.
Q. Has statistical result that's valid that shows that there is an inverse relationship, correct?
A. Yes.
Q. So, regardless what the academic literature shows, that--those facts show that there's an inverse relationship, correct?
A. I very strongly disagree with that. Statistical

models are a method of measuring statistical correlations, but they don't explain the difference. Authorized returns on equity by regulatory commissions have decreased slower than current observable market interest rates. The market immediately changes interest rates, whereas the commission generally will reduce an authorized return on equity much more slowly than the market.

And my perception of why they do that, having been in this business for over 25 years, is the commission is very conservative in changing authorized returns on equity, because they have the responsibility to ensure that that return on equity meets the Hope and Bluefield standards. So, the concerns I've heard expressed by many regulatory commissions is whether or not the decline in capital market cost is sustainable or whether or not it's going to go back to higher levels when rates are in effect.

I've also heard commissions express concern about if the authorized return on equity is decreased too fast, is that going to cause problems with the Company's ability to refinance its embedded debt to produce the sufficient earnings in cash coverage of embedded debt obligations.

Keep in mind that a utility has contractual obligations with their embedded debt structure. So, they can't immediately refinance that embedded debt when interest rates drop. They have to wait until the terms of the bond issue allows them to refinance it. So, there can be a lag between a drop in the interest rate and a reduction in the embedded debt cost structure for the utility.

So, if the authorized return on equity was reduced too fast, you wouldn't get the earnings coverage of debt interest expense. You wouldn't have the cash coverage of debt interest expense, which we just talked about, the system with the S&P benchmarks, that would ensure that the utility's financial integrity was preserved in the rate-making process.

So, it's my experience, having been in this business for quite a while, that regulatory commissions are generally rather conservative in reducing the authorized return on equity in the face of declining capital market costs.

I believe it was referred to earlier by the Department witness as a gradualistic approach to reducing the authorized return on equity down to current market capital cost. And I agree with that perspective. That's my experience.

Q. So, do you have a copy of Dr. Hadaway's rebuttal testimony?

A. Not with me, no.

Q. I want to refer you to page 25. Let me-- I've got an extra copy.

Is it all right if I--

THE HEARING OFFICER: Yes, please.

MR. MONSON: I'm already doing it. I hope it's all right.

THE HEARING OFFICER: It's all right.

BY MR. MONSON:

Q. So, you can see on page 25 that Dr. Hadaway has a graph that compares authorized returns with--or excuse me--equity risk premiums with interest rates, right?

A. Yes.

Q. And even without running a regression analysis, it does appear that there's some inverse correlation, doesn't it?

A. Yeah. I believe it can be explained for the reasons I just went over. I think regulatory commissions adjust authorized return on equity much slower than the market will adjust, which is immediate, market-required debt cost.

Q. So, you did a risk premium result--a study, and your results varied from 9.36 to 10.24 percent, right?

A. That sounds correct, yes.

Q. Okay. If you want to--

A. Can I check that number?

Q. Yeah. If you want to look at it, it's on your direct at lines 658 and 659.

A. Sorry. You said 9.36 to 10.24.

Q. Right.

A. Yes.

Q. Okay. And if you accepted that there was some inverse relationship, Dr. Hadaway redid your numbers and found that your results would have been 10.01 to 10.5. Is that right?

A. I didn't confirm that, but that's what he found.

Q. And do you have any reason to disagree that that's what would happen if you apply his regression analysis and apply that factor?

A. I dispute the accuracy of it, but I don't dispute the mathematics.

Q. You were a witness, along with Dr. Hadaway, in a case before the Illinois Commerce Commission in 2011.

A. I was.

Q. Do you recall that?

A. Yes.

Q. It was Commonwealth Edison case.

A. Yes.

Q. Let me--may I--

THE HEARING OFFICER: Yes.

MR. MONSON: --approach the witness?

I gave you mine, I think.

THE WITNESS: I'm not giving it back.

MR. MONSON: You--

THE WITNESS: I thought that was for me.

MR. MONSON: It will speed it up if I have it.

BY MR. MONSON:

Q. And which party were you a witness for in this case?

A. The Illinois Industrial Energy Consumers.

Q. Could you turn--well, first of all, does this appear to you to be a correct copy of at least a portion of that order?

A. It does.

Q. Could you turn the page 153 of the order?

A. I'm there.

Q. Could you read the paragraph third from the bottom that starts "The Commission finds"?

A. "The Commission finds the testimony of IIEC and AG/CUB relating to ROE as unpersuasive. The evidence shows that Mr. Gorman's estimated ROE is too low because his model inputs are negatively biased and that under current market conditions, his CAPM is unreasonable. In addition, the Commission agrees with ComEd that Mr. Gorman incorrectly believes that the cost of equity for utilities have declined as much as interest rates."

Q. So, at least in the Illinois Commerce Commission's view, they felt like you used biased inputs in the models. Is that right?

A. Yes.

Q. And they also felt like that CAPM was unreasonable, given those market conditions that they observed at that point. Is that correct?

A. "His CAPM is unreasonable," yes.

Q. And, finally, they felt like you had incorrectly determined that the cost of equity had declined as much as interest rates. Is that what they said?

A. It's what they said.

Q. And that's what we're talking about in this inverse relationship, isn't it?

A. No.

Q. Same issue?

A. No.

Q. It's not the same issue.

A. The issue is whether or not there's a one-for-one relationship with reduction return on equity interest rates. I haven't asserted in this case that there is. In fact, I proposed a method of developing an equity risk premium that is above average in this case reflecting the risk of--or the uncertainty of long-term interest rates in this case. I didn't do that in the Commonwealth Edison case. But in any event, that's a different issue than what we were discussing earlier.

Q. Okay. But that gives you--when you do that, it gives you result from 9.36 to 10.24, right?

A. No, sir. I just said that's not the inverse relationship argument.

Q. I thought you said you incorporated it in your risk premium.

A. We're talking about the Illinois Commission orders?

Q. No. We're talking about this case and you saying that you did something different in this case than you did in the Illinois case.

A. Yeah. In this case, I recognized the higher risk in the long-term interest rate market. And because of that risk, I felt that the equity risk premium widened. And I recommended a higher equity risk premium in this case to reflect that long-term interest rate uncertainty.

Q. And the result of that, in this case, was that your risk premium results were 9.36 to 10.24 percent.

A. I'm sorry. That's right. Yes.

Q. That's what I meant.

A. I apologize.

MR. MONSON: Okay. Thank you. That's all I have.

THE HEARING OFFICER: Thank you. Yes.

MR. MONSON: Can we mark this an exhibit, since this isn't something you would have had ready access to? I'm sorry. So, I guess we should call it RMP Cross 1.

THE HEARING OFFICER: It'll be marked RMP Cross Exhibit 1.

MR. MONSON: And I would offer it.

THE HEARING OFFICER: Any objection?

It's received.

Any redirect, Captain Jernigan?

CAPTAIN JERNIGAN: Not at this time, no.

THE HEARING OFFICER: Questions from the Commission?

Commissioner LeVar.

EXAMINATION

BY-COMMISSIONER LeVAR:

Q. Mr. Gorman, taking administrative notice of your testimony in the Rocky Mountain Power case two years ago in this Commission--

A. Yes.

Q. --your recommendation today is 15 base points higher than your recommendation two years ago. What would you say are the most significant--two or three most significant drivers that lead to that result?

A. Well, interest rates have increased since 2012; utility stock prices have not. Again, we talked about the DCF fundamentals, or I talked about them in my summary. The DCF fundamentals are still pretty stable in this case. They're fairly stable in the last case, but probably more so now.

Utility payout ratios are 60 to 70 percent for the proxy group. That's in line with what the utility management are telling the marketplace that their target payout ratios are. That's an indication that the dividend is affordable and that they're retaining enough earnings to reinvest in the utility plant to grow rate base and grow earnings, which in turn allows for the growth in dividends.

The bond yields of utility stocks right now are still above Treasury bond yields. And, historically, that's a measure of whether or not bond yields are reflecting current market cost of equity. Utility stocks yields are above Treasury bond yields, which is probably an indication the Treasury bond yields are artificially low because of Federal Reserve interaction in the marketplace, the monetative easing--quantitative easing practices.

So, I think in this case, as well as the last case, the DCF model results are pretty stable, so I'd say the increase in the return on equity is largely due to modest increase in utility bond yields and more of a significant increase in Treasury bond yields since 2012.

COMMISSIONER LeVAR: Thank you. I don't have anything else.

THE HEARING OFFICER: Thank you.

EXAMINATION

BY-THE HEARING OFFICER:

Q. A couple of questions, Mr. Gorman. First--and this is a minor point, but I just want to make sure there isn't something going on here that I don't understand. If I look at DPU Cross Exhibit 3--I don't know if you have that in front of you, but this was the compilation of rate cases for the first quarter of 2014. And it adjusted out the Virginia rider decisions.

A. Yes. I don't have that--

Q. If you'd like this in front of you, just let me know, but my question is simply that this exhibit refers to an average of 9.62 percent. You seem to have examined, I think, the same data, and your surrebuttal, I think your conclusion is 9.57 percent. And, so, I'm just wondering: Are you referring to the same data set there, or do you know, and do you need this cross exhibit in front of you to--

A. I don't. If you look at page 2 and 3 of my testimony, I actually quoted the Regulatory Research Associates, which is the company that compiles that data and publishes it, whether you get it directly from RRI or the Edison Electric Institute. And they made the calculation that I relied upon. They stated that if you take Virginia decisions out of the first quarter of this year, the average--industry average electric return on equity is 9.57. And, again, that's in the quote starting on page 2 and continuing on page 3 and on line 38 of page 2. It's where they state what the ROE would be for first quarter of this year for electric utilities, excluding Virginia decisions.

Q. And I'll note that it looks like this--the cross exhibit that I referred to has SNL Financial, LC, as a source, so maybe that's simply the explanation: It's just two different sources of data.

A. Yeah. I can't--SNL actually owns RRA. So, I can't explain the difference. It's possible that's the difference, but I would think that if SNL was publishing it, they would have relied on their subsidiary that is in the business of tracking that information. But I can't explain the difference.

Q. My next question relates to page 12 of your direct testimony. And I just would like you to elaborate on a sentence. It's a sentence that begins on line 235. And it reads, "RMP's inflated common equity ratio indicates that the proxy group has less financial risk than RMP." And I just--
again, that's page 12--

A. Okay.

Q. --line 235.

A. It's not a complete analysis of financial risk. But one general measure of financial risk is the amount of debt that is used to finance the Company. The more debt, the more financial risk. The inverse of that is the more common equity, the less financial risk.

As shown on my Exhibit MPG2 with a 51.6 percent common equity ratio, Rocky Mountain Power's amount of debt is lower than that of the companies in my proxy group, looking at the group average numbers.

Q. So, would that mean that the proxy group has more financial risk or less financial--

A. No. This is an equity ratio. So, it's one minus the debt ratio. So, it means it has less financial risk because it has less debt, less percentage of debt supporting the total capital, using it to invest in the utility plant and equipment. So, one minus the equity ratio is the debt ratio. And with a higher equity ratio, if you take one minus it, you have a lower debt ratio.

So, it's a little confusing, because, again, a high equity ratio means lower financial risk. And conversely, a high debt ratio means greater financial risk. And the combination of debt ratio and equity ratio equals total capital.

MS. SCHMID: If I may--may I just ask one question? On line 236, should it be--indicates that RMP has less financial risk than the proxy group--

THE WITNESS: Yes.

MS. SCHMID: --rather than the way it's typed?

THE WITNESS: That's correct, yes.

MS. SCHMID: Thank you.

THE WITNESS: Thank you.

BY THE HEARING OFFICER:

Q. So, I think that's what was hanging me up a little bit, too. So, the proxy group has a higher debt ratio than RMP.

A. Correct, and a lower common equity ratio.

Q. Uh-huh (affirmative). And that would mean what with respect to financial risk for the proxy group?

A. It means the proxy group has greater financial risk--

Q. Okay.

A. --than Rocky Mountain Power.

Q. Thank you very much.

THE HEARING OFFICER: Any questions based on mine?

CAPTAIN JERNIGAN: No questions, sir.

THE HEARING OFFICER: Thank you, Mr. Gorman. You're excused.

MR. MONSON: May I have just one minute?

THE HEARING OFFICER: We'll be off the record.

(Recess taken.)

RECROSS-EXAMINATION

BY-MR.MONSON:

Q. I do have one question, if that's all right. And I don't have a copy of this page, so I'll have to come show it to you. But in Mr.--Dr. Hadaway's testimony, he has a proxy group--and by the way, you used the same proxy group he did, right?

A. Yes.

Q. And he has the--an exhibit that shows the capital structure of the proxy group. Do you recall that?

A. I'd have to go back and review his testimony.

MR. MONSON: May I give this to the witness?

THE HEARING OFFICER: Yes.

MR. COLEMAN: Where did that come from, just so I can follow along?

MR. MONSON: That's a copy of Exhibit SCH1 out of Dr. Hadaway's direct testimony.

MR. COLEMAN: Okay. Thank you.

BY MR. MONSON:

Q. And what does that show the common equity ratio is of the proxy group?

A. For calendar year 2012, it shows 50.1 percent.

Q. Okay. And, then, what's Rocky Mountain Power's equity ratio?

A. I have 51.6 in their direct case. It's closer to 51 percent now, but more recent information, as reflected on my Exhibit MPG2, is that the proxy group's common equity ratio, on average, is about 49 percent, reflecting--

THE REPORTER: I'm sorry. You're fading a little bit. Ratio average is about 49 percent?

THE WITNESS: Correct, as reported by Value Line, which is the same source, I believe, as Dr. Hadaway's.

BY MR. MONSON:

Q. So, this is just a timing--the difference in these numbers is timing, when you got your data.

A. Rocky--or PacifiCorp's common equity ratio has come down and so has the proxy group's.

MR. MONSON: That's all.

THE HEARING OFFICER: Thank you, Mr. Gorman. You're excused.

Captain Jernigan, anything further?

CAPTAIN JERNIGAN: Nothing further. Thank you.

THE HEARING OFFICER: Is there any other business for the Commission in this subphase of Phase 1? That is the cost of capital subphase. Anything further?

Then, we'll be adjourned. We'll reconvene in the revenue requirement phase of Phase 1 on June 30 at 9:00 a.m. Thank you very much for your participation today.

MS. RHOADES: Thank you, everyone, for allowing me to participate telephonically.

THE HEARING OFFICER: Thank you.

(Proceedings concluded at 2:32 p.m.)

CERTIFICATE

This is to certify that the foregoing proceedings were taken before me, SCOTT M. KNIGHT, a Registered Professional Reporter and Notary Public in and for the State of Utah, residing at South Jordan, Utah;

That the proceedings were reported by me in stenotype and thereafter caused by me to be transcribed into typewriting, and that a full, true, and correct transcription of said proceedings so taken and transcribed is set forth in the foregoing pages, inclusive.

I further certify that I am not of kin or otherwise associated with any of the parties to said cause of action, and that I am not interested in the event thereof.

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Scott M. Knight, RPR

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