BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

IN THE MATTER OF THE APPLICATION OF PACIFICORP FOR APPROVAL OF ITS PROPOSED ELECTRIC RATE SCHEDULES & ELECTRIC SERVICE REGULATIONS	Docket No. 03-2035-02 REPLACEMENT PAGES OF DANIEL J. ROSBOROUGH

OCTOBER 2003

I describe the Company's proposal to recover in base rates the $69 million in test period medical, dental and other benefit coverage costs and explain the major reasons for the increase in those costs. Finally, I describe the actions the Company is taking to control those costs.

Pension Expense

Defined Benefit Pension Plan Expense

Q. How is the Company's pension expense determined?

A. The expense for the plan is determined annually by an independent actuary, Hewitt Associates, as prescribed by the Financial Accounting Standards Board through its accounting standard governing the calculation of pension expense (SFAS 87). Under SFAS 87, the pension expense amount is calculated by the actuary based upon the actual demographics of the participants in the plan, the expected benefits to be paid, assumed terminations and retirements, assumed pay raises, current interest rates for valuing the plan's liabilities and an assumption for the expected long-term rate of return on plan assets. Pension expense is calculated by the actuary on a calendar year basis but SFAS 87 permits this calculation to be used by companies utilizing a different fiscal year, such as PacifiCorp, provided the fiscal year end is no more than three months divergent from the calendar year. To the extent that actual investment returns and other plan experience differ from the assumptions, these differences are amortized into future expense once they exceed a certain threshold.

Q. What is the plan's current funding status?

A. The plan is currently underfunded. This situation exists for two primary reasons:

The Trustees of the PacifiCorp/IBEW Local 57 Retirement Trust Fund now manage these assets. There are four Trustees from PacifiCorp management and four from Local 57 IBEW leadership. The Trust employs professional actuarial consultants, administrators, an attorney, an auditor and investment managers. PacifiCorp provides funding to the plan based upon a collectively bargained agreement that recognizes seven percent (7%) of regular pay as pension eligible compensation. Pension eligible compensation is calculated at the end of each pay period and funds are transferred to the Trust per the terms of the bargained agreement.

Q. What ratemaking treatment is PacifiCorp proposing for the IBEW 57 pension expense?

A. PacifiCorp proposes to recover the $5.0 million contribution as an in-period test year expense.

Q. Is the IBEW 57 Pension expense a recurring expense?

A. Yes, the required expense for the plan is determined on an annual basis by the plans actuarial consultant under the same accounting standards identified above. The terms of the agreement with IBEW 57 require that the Company provide a contribution based on covered employees' regular pay.

Medical, Dental and Other Benefit Coverage Costs

Q. **What level of medical, dental and other benefit costs are included in the Company's revenue requirement in this case?**

The Company has recorded an increase from $55 million in 2000 to $69 million during the test period for medical, dental and other benefit costs that it incurred during the test period.

Q. **Please explain the reasons for the increase in these costs.**

A. The increase in medical coverage costs is the primary reason for the increase in these costs. PacifiCorp's health plans, like most every other health plan in the United States, have been experiencing significant increases in medical inflation. The primary drivers behind the increases are:

- Lesser degree of effectiveness of managed care plans. It is widely believed that after several years of successful negotiations with providers to minimize annual cost increases, the "market" has now turned and providers are being more successful at negotiating increases with managed care networks;
- Government mandates and continued cost shifting by government plans to the private sector;
- An aging population;
- The cost of prescription drugs, compounded by very effective direct consumer marketing;
- Increased prevalence of chronic and high cost treatment; and
- Development and expansion of new medical technology.

I describe the Company's proposal to recover in base rates the ~~$62 million~~ $69 million in test period medical, dental and other benefit coverage costs and explain the major reasons for the increase in those costs. Finally, I describe the actions the Company is taking to control those costs.

Pension Expense

Defined Benefit Pension Plan Expense

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A. The expense for the plan is determined annually by an independent actuary, Hewitt Associates, as prescribed by the Financial Accounting Standards Board through its accounting standard governing the calculation of pension expense (SFAS 87). Under SFAS 87, the pension expense amount is calculated by the actuary based upon the actual demographics of the participants in the plan, the expected benefits to be paid, assumed terminations and retirements, assumed pay raises, current interest rates for valuing the plan's liabilities and an assumption for the expected long-term rate of return on plan assets. Pension expense is calculated by the actuary on a calendar year basis but SFAS 87 permits this calculation to be used by companies utilizing a different fiscal year, such as PacifiCorp, provided the fiscal year end is no more than three months divergent from the calendar year. To the extent that actual investment returns and other plan experience differ from the assumptions, these differences are amortized into future expense once they exceed a certain threshold.

Q. What is the plan's current funding status?

A. The plan is currently underfunded. This situation exists for two primary reasons:

The Trustees of the PacifiCorp/IBEW Local 57 Retirement Trust Fund now manage these assets. There are four Trustees from PacifiCorp management and four from Local 57 IBEW leadership. The Trust employs professional actuarial consultants, administrators, an attorney, an auditor and investment managers. PacifiCorp provides funding to the plan based upon a collectively bargained agreement that recognizes seven percent (7%) of regular pay as pension eligible compensation. Pension eligible compensation is calculated at the end of each pay period and funds are transferred to the Trust per the terms of the bargained agreement.

Q. What ratemaking treatment is PacifiCorp proposing for the IBEW 57 pension expense?

A. PacifiCorp proposes to recover the $5.0 million contribution as an in-period test year expense.

Q. Is the IBEW 57 Pension expense a recurring expense?

A. Yes, the required expense for the plan is determined on an annual basis by the plans actuarial consultant under the same accounting standards identified above. The terms of the agreement with IBEW 57 require that the Company provide a contribution based on covered employees' regular pay. ~~The Company expects to update the expense levels for the next contribution as part of its October 15, 2003 filing.~~

Medical, Dental and Other Benefit Coverage Costs

Q. What level of medical, dental and other benefit costs are included in the Company's revenue requirement in this case?

A. The Company has recorded an increase from $55 million in 2000 to ~~$61 million~~ $69 million during the test period for medical, dental and other benefit costs that it incurred during the test period. ~~The Company also anticipates that this will increase to $70 million and has included this information in its filing. This reflects a total increase of $15 million in those costs since 2000.~~

Q. Please explain the reasons for the increase in these costs.

A. The increase in medical coverage costs is the primary reason for the increase in these costs. PacifiCorp's health plans, like most every other health plan in the United States, have been experiencing significant increases in medical inflation. The primary drivers behind the increases are:

- Lesser degree of effectiveness of managed care plans. It is widely believed that after several years of successful negotiations with providers to minimize annual cost increases, the "market" has now turned and providers are being more successful at negotiating increases with managed care networks;
- Government mandates and continued cost shifting by government plans to the private sector;
- An aging population;
- The cost of prescription drugs, compounded by very effective direct consumer marketing;
- Increased prevalence of chronic and high cost treatment; and