

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application)
of Rocky Mountain Power for) Docket No.
Authority to Increase Its Retail) 07-035-93
Electric Utility Service Rates)
in Utah and for Approval of Its)
Proposed Electric Service)
Schedules and Electric Service)
Regulations, Consisting of a)
General Rate Increase of)
Approximately \$161.2 Million Per)
Year, and for Approval of a New)
Large Load Surcharge.)

TRANSCRIPT OF HEARING PROCEEDINGS

TAKEN AT: Public Service Commission
160 East 300 South, Room 403
Salt Lake City, Utah

DATE: May 20, 2008

TIME: 9:05 a.m.

REPORTED BY: Kelly L. Wilburn, CSR, RPR

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4 Ric Campbell
5 Ron Allen

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20 were prefiled and are part of the PSC record
21 and filed at the Commission.)

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1 MAY 20, 2008 9:05 A.M.

2 P R O C E E D I N G S

3 COMMISSIONER BOYER: This is the time and
4 place duly noticed for the Rate of Return portion of
5 the case hearing in the Docket No. 0703593, in the
6 matter of the application of Rocky Mountain Power for
7 authority to increase its retail electric utility
8 service rates in Utah, and for approval of it's
9 proposed electric service schedule and electric
10 service regulations, consisting of a general rate
11 increase of approximately 161.2 million per year, and
12 for approval of a new large load surcharge.

13 And we know that that -- the amount of the
14 request has now been reduced because of the test year
15 change. You've all received -- hopefully have all
16 received a letter we issued last week to explain how
17 we wish to proceed.

18 We're trying to, trying to manage our
19 schedule as best we can with two simultaneous rate
20 cases, another one threatened, three resource cases, a
21 transmission line, and then the regular daily workload
22 that we have.

23 And our expectation is that we will complete
24 the Rate of Return portion of the Rocky Mountain case
25 today. We'll do the same with Questar tomorrow.

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1 We've -- I don't know how you want to call the two
2 categories of witnesses. In my own mind I'm calling
3 them "technical" witnesses and "policy" witnesses.

4 But we thought we would hear the technical
5 witnesses first, and then the policy or opinion
6 witnesses later in the day. I thought we would begin
7 by putting all of the written prefiled testimony on
8 record now. That would give everyone an opportunity
9 to make any corrections they need to make, objections
10 to the admissibility of the, the testimony.

11 We'll rule on the motion to strike Mr. Ball's
12 testimony also at the outset. And I guess is there
13 any confusion about which witnesses we consider to be
14 which category? In this case essentially Mr. Walje
15 and Mr. Ball will be heard later in the day is our
16 expectation, anyway. We're calling them the policy
17 witnesses or opinion witnesses.

18 The order of witnesses will be we'll let the
19 Company go first. Put on a witness. There will be
20 cross examination and then redirect. Go to the next
21 witness, and so on. Then we'll go to the Company
22 (sic.) Following the Company witness, the committee.
23 And then Mr. Ball and Mr. Walje will be heard this
24 afternoon.

25 MS. SCHMID: Pardon me. Would the Division

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1 go after the Company?

2 COMMISSIONER BOYER: Yes.

3 MS. SCHMID: Okay, thank you.

4 COMMISSIONER BOYER: They're supposed to go
5 first, Ms. Schmid. It's their case.

6 MS. SCHMID: Certainly.

7 COMMISSIONER BOYER: If you're going -- if
8 your witnesses are going to give summaries we would
9 hope that those summaries would be very brief. We
10 state this in every hearing, but we have read all the
11 testimony.

12 I myself stayed up into the wee hours
13 rereading the testimony last night. And I know my two
14 colleagues have written it -- have read it as well and
15 understand it more clearly even than I do. So we
16 don't need a lot in the way of summery; we know what
17 the testimony is.

18 The purpose of this hearing is to have an
19 opportunity to cross examination witnesses under the
20 hot lights. And we think that that's gonna be the
21 most fruitful and the best use of time today.

22 As always, we discourage trying to prove your
23 case through cross examination. It's largely in
24 effectual, and a huge waste of time for everyone else
25 as you try to do that.

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1 We don't anticipate issuing an order -- a
2 separate order on Rate of Return, but rather we'll
3 issue an order in the case in chief later in the
4 summer as we go forward. Have I missed anything or
5 are there any questions about what I've said so far?

6 No? Well, okay. We don't know if this
7 format is going to work, but we're hoping that it
8 does. Our anticipation is that we can go through the
9 technical witnesses this morning, and perhaps into the
10 early afternoon. And then have an opportunity to hear
11 from the policy witnesses. We would hope to conclude
12 the hearing by 5:00, if possible.

13 We'll take regular breaks to give our
14 reporter a rest and us an opportunity to regroup and
15 rethink. Okay. With that, then, let's take
16 appearances first. And we'll begin with the Company.

17 MS. McDOWELL: Katherine McDowell from the
18 law firm of McDowell & Rackner here on behalf of Rocky
19 Mountain Power.

20 MR. MOENCH: Mark Moench, general counsel for
21 Rocky Mountain Power, on behalf of Rocky Mountain
22 Power.

23 COMMISSIONER BOYER: Welcome. And welcome
24 Ms. McDowell. Is this the first time you've testified
25 in our -- or rather participated in a hearing in Utah?

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1 Ms. McDowell: Yes it is, Commissioner, and
2 I'm honored to be here.

3 COMMISSIONER BOYER: Thank you, we're glad to
4 have you.

5 Ms. Schmid?

6 MS. SCHMID: Patricia E. Schmid from the
7 Attorney General's Office representing the Division of
8 Public Utilities.

9 MR. PROCTOR: Paul Proctor on behalf of the
10 Utah Committee of Consumer Services.

11 COMMISSIONER BOYER: Very well. Mr. Reeder?

12 MR. REEDER: Good morning. I'm Robert
13 Reeder, on behalf of a group of industrial customers
14 whose names appear and are identified as the UIEC.

15 I would note that I would ask to be excused
16 from this hearing at the conclusion of my appearance.
17 I have no witnesses. And to facilitate your
18 expedition -- expeditiously disposing of this matter,
19 I'll waive cross examination.

20 COMMISSIONER BOYER: Very well Mr. Reeder,
21 thank you. You may well be back in my will.

22 Mr. Dodge?

23 MR. DODGE: Gary Dodge on behalf of the UAE
24 Intervention Group.

25 MR. BALL: Roger Ball, on my own behalf.

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1 COMMISSIONER BOYER: Okay, thank you
2 Mr. Ball. With that why don't we -- let's try to get
3 the prefiled written testimony into the record at this
4 point, and then we'll begin with the witnesses.

5 Ms. McDowell?

6 Ms. McDowell: Yes, Commissioner. So would
7 it be helpful to just read through what the testimony
8 is and what the exhibits are?

9 COMMISSIONER BOYER: That would be very
10 helpful.

11 Ms. McDowell: Okay. We have the witness
12 Mr. Williams. We have his direct testimony. And that
13 direct testimony is accompanied by 14 witnesses -- or
14 excuse me.

15 COMMISSIONER BOYER: Exhibits?

16 Ms. McDowell: Fourteen exhibits, BNW-1
17 through 14. Then we have Mr. Williams' supplemental
18 direct testimony which is accompanied by two exhibits,
19 BNW-1-S and BNW-2-S. Then Mr. Williams has rebuttal
20 testimony. No exhibits with that testimony.

21 COMMISSIONER BOYER: Very well.

22 Ms. McDowell: So shall I proceed to
23 Mr. Hadaway and Mr. Walje as well?

24 COMMISSIONER BOYER: Why don't we go one by
25 one. Let's get Mr. Williams' testimony into the

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1 record if it's admissible.

2 Ms. McDowell: Very good. So we would offer
3 Mr. Williams' testimony.

4 COMMISSIONER BOYER: Are there any objections
5 to Mr. Williams' testimony?

6 MS. SCHMID: None.

7 MR. PROCTOR: No objection.

8 COMMISSIONER BOYER: Okay. Mr. Williams'
9 direct testimony, his supplemental testimony, both
10 with exhibits, and his rebuttal testimony are admitted
11 into evidence.

12 Ms. McDowell: Thank you, Commissioner.
13 Would you like me to proceed?

14 COMMISSIONER BOYER: Please, if you would.

15 Ms. McDowell: Our next witness this morning
16 will be Dr. Hadaway. He has prepared direct
17 testimony, which is accompanied by Exhibits SCH-1
18 through SCH-7. Mr. Hadaway has also prepared rebuttal
19 testimony, and that testimony is accompanied by
20 Rebuttal Exhibits SCH-1-R through SCH-8-R. We would
21 offer Mr. Hadaway's testimony and exhibits.

22 COMMISSIONER BOYER: Are there objections
23 on -- to Mr. Had -- Dr. Hadaway's testimony?

24 MS. SCHMID: None.

25 COMMISSIONER BOYER: None? Okay, then the --

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1 both the direct and rebuttal testimony of Mr. --
2 Dr. Hadaway, together with exhibits, are admitted into
3 evidence.

4 Ms. McDowell: And Commissioner, our final
5 witness will be Mr. Rich Walje. Mr. Walje submitted
6 specific testimony for this phase of the proceedings
7 but also has aspects of his direct and rebuttal
8 testimony from the Revenue Requirement proceedings
9 which are relevant to the Rate of Return testimony.

10 So we could go ahead and offer those for the
11 limited purpose of their applicability to this
12 hearing, and then go ahead and offer the specific
13 rebuttal for Rate of Return if that would be
14 acceptable.

15 COMMISSIONER BOYER: Let's do that.

16 Ms. McDowell: So in that case we have the
17 direct policy testimony of Rich Walje. We have his
18 rebuttal testimony in the Rate of Return hearing. And
19 then we have his rebuttal testimony in the Revenue
20 Requirement phase. And that's accompanied by two
21 exhibits, ARW-1-R and ARW-2-R. We would offer
22 Mr. Walje's testimony.

23 COMMISSIONER BOYER: Are there objections to
24 Mr. Walje's testimony?

25 MS. SCHMID: None.

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1 MR. PROCTOR: None.

2 COMMISSIONER BOYER: Very well. Mr. Walje's
3 direct policy testimony, his rebuttal testimony, and
4 the Rate of Return portion of this proceeding and his
5 rebuttal testimony in the Revenue Requirement, with
6 the two exhibits, are admitted into evidence.

7 Ms. McDowell: Thank you, Commissioner.
8 That's all of the testimony that we -- prefiled
9 testimony we intend to offer today.

10 COMMISSIONER BOYER: Thank you, Ms. McDowell.

11 Ms. Schmid?

12 MS. SCHMID: Good morning. The Division
13 would like to offer DPU Exhibit No. 2.0. And there's
14 also a confidential version of that testimony. And
15 DPU Exhibits No. 2.1 through 2.16. This is the
16 prefiled direct Rate of Return exhibit -- testimony of
17 Charles E. Peterson and the associated exhibits.

18 COMMISSIONER BOYER: Very well. Are there
19 objections to Mr. Peterson's testimony, prefiled
20 written testimony?

21 MS. SCHMID: We also have a surrebuttal. I
22 didn't know if you wanted to do them together or
23 separate.

24 COMMISSIONER BOYER: Please.

25 MS. SCHMID: Okay. We'd also like to offer

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1 DPU Exhibit No. 2.0-SR which is the prefiled
2 surrebuttal Rate of Return testimony of Charles
3 Peterson.

4 COMMISSIONER BOYER: Okay. I ask the
5 question again, are there objections to Mr. Peterson's
6 testimony, prefiled? Very well. The testimony of
7 Mr. Peterson, together with exhibits, are admitted.

8 Mr. Proctor?

9 MR. PROCTOR: Thank you, Mr. Chairman. The,
10 the Committee has previously filed with the Commission
11 two sets of testimony by Daniel J. Lawton, both direct
12 and surrebuttal. The direct has been marked as
13 CCS-3-D, and it consists of 31 pages.

14 In addition, there are ten exhibits marked
15 CCS-3.1 through and including 3.10. In addition,
16 there is testimony -- surrebuttal testimony marked
17 CCS-3-SR, consisting of seven pages. And three
18 exhibits that have been marked 3.1-SR through and
19 including 3.3.

20 Upon Mr. Lawton being sworn appropriately, of
21 course, and with three corrections that need to be
22 made -- two to the direct, two to the surrebuttal --
23 they're not consequential but nevertheless need to be
24 made --

25 COMMISSIONER BOYER: Would you like to take

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1 care of that at this moment? We could swear
2 Mr. Lawton.

3 MR. PROCTOR: If I could, yes.

4 COMMISSIONER BOYER: We could swear
5 Mr. Lawton.

6 MR. PROCTOR: Would you, please?

7 (Mr. Lawton was duly sworn.)

8 DANIEL LAWTON,
9 called as a witness, having been duly sworn,
10 was examined and testified as follows:

11 DIRECT EXAMINATION

12 BY MR. PROCTOR:

13 Q. Mr. Lawton, if I could ask you just very
14 quickly, are there changes that you wish to make to
15 your direct testimony, in particular page 2, lines 45
16 and 46?

17 A. Yes. On page 2 of my direct testimony at the
18 end of line 44, the 985 percent -- 9.85 percent should
19 be 9.65 percent. Then if you go down to line 46, at
20 the start of the first sentence, the 9.65 percent
21 should be 9.85 percent. For some reason those two
22 numbers were inverted. With that change, the
23 testimony is correct.

24 Q. Is there a change that you would like to make
25 to Exhibit 3.7 to your direct testimony?

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1 A. Yes. Exhibit 3 -- CCS-3.7, if I can -- no.
2 I think that was my direct, wasn't it?

3 Q. Yeah, in your direct testimony.

4 A. Yeah. Exhibit CCS-3.7, I incorrectly
5 misspelled the name of the Company, and I wanted to
6 correct the name. The word "Mountain," there's a "u"
7 missing.

8 Q. And finally Mr. Lawton to your surrebuttal,
9 Exhibit 3.3-SR, is there a change that needs to be
10 made on page 2 of this three-page document?

11 A. Yes. On page 2 in the upper right-hand
12 corner of the Exhibit CCS-3.3 should be SR, not R,
13 signifying this is surrebuttal testimony.

14 Q. Mr. Lawton, if I were to ask you the
15 questions today that have -- you have responded to in
16 your prefiled written testimony would your answers
17 remain the same?

18 A. Yes they would, sir.

19 MR. PROCTOR: With that, Mr. Chairman, the
20 Committee would offer into evidence the direct and
21 surrebuttal testimony of Daniel Lawton as we have
22 earlier identified it.

23 COMMISSIONER BOYER: Thank you, Mr. Proctor.
24 Are there any objections to the admission of the
25 prefiled testimony of Mr. Lawton?

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1 MS. SCHMID: None.

2 Ms. McDowell: No.

3 COMMISSIONER BOYER: Seeing none, then the
4 prefiled testimony of Mr. Lawton together with
5 exhibits, and as corrected today, are admitted into
6 evidence.

7 And that does raise the question that with --
8 were there corrections to any of the written testimony
9 previously submitted into evidence?

10 Ms. McDowell: No.

11 COMMISSIONER BOYER: Thank you.

12 MS. SCHMID: And sorry Mr. Chairman, the
13 Division has one question with respect to an exhibit,
14 but we will check on that. It may have gone in with
15 zeroes instead of numbers. But we will check.

16 COMMISSIONER BOYER: Very well. If you would
17 check and let us know that.

18 Let's see. Mr. Dodge, you have no witnesses
19 but you're gonna participate today?

20 MR. DODGE: Yes, in a limited role.

21 COMMISSIONER BOYER: And Mr. Ball, there has
22 been a motion to strike your testimony. You've
23 responded to that. I suppose we should let
24 Ms. McDowell have an opportunity to argue that, and
25 then you to respond. And we'll rule here from the

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1 bench before we proceed.

2 Ms. McDowell?

3 Ms. McDowell: Thank you, Commissioner. The
4 motion basically tried to set out in advance of the
5 hearing our concerns about this testimony before it
6 was offered so that all parties had advance notice of
7 our concerns about the relevance of this testimony to
8 this hearing.

9 It's our view that the testimony essentially
10 reargues points that were handled and resolved in the
11 test year hearing. We have enough issues to address
12 here without going back and rearguing those issues.
13 So it was our opinion that this testimony was
14 irrelevant to the issues that are before the
15 Commission today, and should not be received.

16 COMMISSIONER BOYER: Thank you, Ms. McDowell.

17 Mr. Ball, response?

18 MR. BALL: Responding to Ms. McDowell's
19 remarks here, I really don't think the -- those
20 issue -- the issues that I've raised in my Rate of
21 Return testimony were addressed in the test year
22 hearing. Certainly they were raised.

23 I did testify regarding the financial impact
24 of a projected test year back then, but the Commission
25 really didn't rule on that. And so it's entirely

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1 appropriate that they should consider it now. Perhaps
2 more appropriate.

3 But I would point out that by bringing it
4 forward during the test year proceeding I gave
5 everybody plenty of opportunity to understand what my
6 position was. And I find it, I find it interesting
7 that no party, including the Company, filed any
8 contravening testimony. Thank you Chairman.

9 COMMISSIONER BOYER: Does anyone else wish to
10 speak to the motion to strike, and then we'll give
11 Ms. McDowell the last word? No? Ms. McDowell,
12 anything further?

13 Ms. McDowell: No, thank you.

14 (Pause.)

15 COMMISSIONER BOYER: All right. We share
16 some of the concerns of the Company regarding
17 relevance and materiality, whether it's probative and
18 so on and so forth, but we're going to admit
19 Mr. Ball's testimony. We'll give it appropriate
20 weight during our deliberate process.

21 Do you wish to submit your written prefiled
22 testimony into evidence, Mr. Ball?

23 MR. BALL: Thank you Chairman.

24 (Pause.)

25 MR. BALL: First of all, Chairman, I have one

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1 correction to make. Would remind everyone that I've
2 already been sworn in this proceeding. The correction
3 is to the cover sheet of my rebuttal testimony. I'm
4 grateful to PacifiCorp for pointing out that I had
5 shown in the middle of the page the wrong date.

6 I show the 31st of March, 2008. It should be
7 corrected, please, to the 28th of April, 2008. Which
8 is the same date shown in the footer of each page and
9 in the service certificate. That's the only
10 correction of which I am aware.

11 And I'd like to offer my Rate of Return
12 direct testimony, marked as Exhibit RJB-3.0, Rate of
13 Return rebuttal testimony marked as RJB Exhibit 5.0,
14 and Rate of Return surrebuttal testimony marked as RJB
15 Exhibit 6.0 and ask that it be admitted into evidence,
16 please.

17 COMMISSIONER BOYER: Okay. I think we've
18 already argued the admissibility issues. So then the
19 Rate of Return direct testimony of Mr. Ball, his
20 rebuttal testimony, and surrebuttal testimony will be
21 admitted into the -- into evidence in this proceeding.

22 MR. BALL: Thank you.

23 COMMISSIONER BOYER: Okay. I think that
24 brings us to the case in chief now. And we'll proceed
25 with alacrity, won't we? And we'll turn the time over

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1 to Ms. McDowell for your first witness.

2 MS. MCDOWELL: Thank you, Commissioner. We
3 call Bruce Williams.

4 COMMISSIONER BOYER: Mr. Williams, have you
5 been sworn in this proceeding?

6 THE WITNESS: No, I have not.

7 (Mr. Williams was duly sworn.)

8 COMMISSIONER BOYER: Thank you. Please be
9 seated.

10 BRUCE WILLIAMS,
11 called as a witness, having been duly sworn,
12 was examined and testified as follows:

13 DIRECT EXAMINATION

14 BY MS. MCDOWELL:

15 Q. Mr. Williams, can you state your full name
16 and spell it for the record?

17 A. Bruce Williams. B-r-u-c-e, W-i-l-l-i-a-m-s.

18 Q. How are you employed, Mr. Williams?

19 A. I am the vice president and treasurer of
20 PacifiCorp.

21 Q. In that capacity have you prepared testimony
22 and exhibits for this proceeding?

23 A. Yes, I have.

24 Q. And have those exhibits -- excuse me,
25 testimony and exhibits been previously filed and

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1 offered and admitted in this proceeding?

2 A. Yes, they have been.

3 Q. Have you prepared a summary of your prefiled
4 testimony?

5 A. Yes, I have.

6 Q. Mindful of Commissioner Boyer's admonition to
7 make summaries brief, can you please provide that
8 summary of your testimony now?

9 A. Yes, I will.

10 And I also did hear your comments about being
11 brief and I'll try my best to comply with those.

12 COMMISSIONER BOYER: I'd like to characterize
13 it as a suggestion, but admonition has a nice ring to
14 it as well. Thank you, Mr. Williams.

15 MS. McDOWELL: I'm gonna err on the side of
16 deference this morning.

17 COMMISSIONER BOYER: Thank you.

18 THE WITNESS: Well, first of all good
19 morning. Thank you for the opportunity to be here
20 with you again. There are three main parts to my
21 testimony. The first concerns the Company's capital
22 structure. Cost of debt and preferred are the other
23 two pieces.

24 Dr. Hadaway will testify concerning the cost
25 of common equity, which is a final component necessary

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1 to determine the overall cost of capital for Rocky
2 Mountain Power. In my updated testimony, as directed
3 by the Commission in its order concerning the test
4 period, the Company utilized the 12 months ending
5 December 31, 2008, as the test period to determine the
6 capital structure and cost of capital in this matter.

7 My testimony demonstrates that the Company's
8 capital structure will be 49.2 percent debt, .4
9 percent preferred stock, and 50.4 percent common
10 equity. No party in this case has raised objections
11 or proposed a different capital structure.

12 My testimony further describes how the cost
13 of debt is determined, including the cost of
14 700 million of new long-term debt which is to be
15 issued during the test period. This is a significant
16 amount of new debt for the Company. And it's
17 necessary to fund the investments that we're making in
18 new generation, transmission, environmental resources,
19 and local distribution facilities.

20 It's important that the cost of this debt be
21 determined appropriately, as the Company will be a
22 regular ongoing issuer of long-term debt going
23 forward. The cost of this debt is really composed of
24 two pieces:

25 The first is the underlying treasury bond

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1 rate. Then in addition to that treasury bond rate
2 there is the credit spread or premium that investors
3 require because of the greater risk of the Company
4 compared to U.S. Treasury securities.

5 This is the same method that the Company has
6 utilized previously here in Utah and in the other
7 states that regulate Rocky Mountain Power or Pacific
8 Power. My testimony demonstrates that the cost of
9 debt is 6.30 percent for the test period.

10 My testimony also describes a methodology for
11 determining the cost of preferred stock, and that cost
12 is 5.41 percent. Again, this methodology is also
13 consistent with past practices of this Commission and
14 the other states that regulate Rocky Mountain Power or
15 Pacific Power.

16 Again, no parties have raised any objections
17 to the cost of preferred stock or proposed an
18 alternative. You will hear later from Dr. Hadaway as
19 to the cost of common equity and why it is
20 10.75 percent. This capital structure and the costs
21 then produce a weighted average cost of capital of
22 8.54 percent for Rocky Mountain Power.

23 My rebuttal testimony responds to several
24 issues raised by Mr. Lawton and Mr. Peterson. Most
25 significantly we disagree about one item, and that is

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1 the cost of the new debt to be issued during the test
2 period.

3 Mr. Lawton and Mr. Peterson propose a
4 reduction in the cost of this new debt, citing a
5 general decline in yields or interest rates on U.S.
6 Treasury bonds since my direct testimony was prepared.
7 However, they admit a corresponding and offsetting
8 increase in the credit spreads that investors
9 currently require for corporate bonds, including those
10 of the Company.

11 They are correct that treasury bonds have
12 declined. But importantly, the credit spreads
13 required of Single-A rated public utility companies
14 like Rocky Mountain Power has widened significantly,
15 resulting in borrowing costs that are higher than when
16 the direct testimony was prepared.

17 My rebuttal testimony demonstrates that the
18 6.30 percent continues to be appropriate overall cost
19 of debt. Finally I'd like to comment on the
20 surrebuttal testimony of Mr. Lawton and Mr. Peterson.
21 Both gentlemen have expressed concerns that
22 Dr. Hadaway and I have made contradictory statements
23 concerning interest rates. I'd like to be clear that
24 this is not the case.

25 Dr. Hadaway and I have correctly utilized

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1 rates that are appropriate for different borrowers at
2 different periods in time. Dr. Hadaway will further
3 elaborate on his interest rate selections during his
4 testimony.

5 Finally in closing I'd like to say the
6 Company's provided clear testimony as to the capital
7 structure during the test period and the cost of
8 capital. There's really only one important item of
9 disagreement, and that's the cost of this new debt
10 that will be issued.

11 On that point, Rocky Mountain Power has
12 demonstrated the costs in the direct testimony are the
13 most appropriate. That concludes my opening
14 statement.

15 COMMISSIONER BOYER: Thank you Mr. Williams.

16 Ms. Schmid, cross examination?

17 MS. SCHMID: Thank you. Very few questions.

18 CROSS EXAMINATION

19 BY MS. SCHMID:

20 Q. Mr. Williams, is it correct that the Company,
21 in approximately November of 2008, plans to issue
22 about a \$700 million debt issuance?

23 A. I'd say that's approximately correct, though
24 the time could move. But that's the size we have
25 targeted, yes.

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1 Q. Has the Company hedged the future interest
2 rate for this?

3 A. No, we have not.

4 MS. SCHMID: Thank you, that's all.

5 COMMISSIONER BOYER: You are parsimonious
6 today, Ms. Schmid, thank you.

7 Mr. Proctor, cross examination for
8 Mr. Williams?

9 MR. PROCTOR: Could I just have one moment?

10 COMMISSIONER BOYER: Surely.

11 (Pause.)

12 CROSS EXAMINATION

13 BY MR. PROCTOR:

14 Q. Mr. Williams, prior to coming here today did
15 you review Dr. Hadaway's surrebuttal -- or excuse me,
16 rebuttal testimony, and in particular that part where
17 he describes the cost of new debt for companies such
18 as PacifiCorp?

19 A. I believe so. But if you could refer to a
20 specific section, that would be helpful.

21 Q. It would be Table 1, page 5, of his rebuttal
22 testimony.

23 A. I'm sorry, could you repeat that?

24 Q. Table 1, page 5, to Dr. Hadaway's rebuttal
25 testimony. Long-term interest rate trends. Do you

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1 see that?

2 A. Well, I think I'm looking at the same thing
3 you are, but I'm not certain. Do you have --

4 Q. Well, what -- doesn't that table reflect that
5 as of March 2008 the Single-A utility long-term
6 interest rate was 6.21 percent?

7 A. I think you are looking at the column that's
8 labelled monthly average for March 2008?

9 Q. Yes.

10 A. That 6.2? And yes, that is correct.

11 Q. Okay. And that is different than the all-in
12 cost that you describe on page 2 of your rebuttal
13 testimony, is it not?

14 A. It's different because they're different
15 points in time. This is March. My testimony is
16 looking at costs in December.

17 Q. December of 2007?

18 A. No, December 2008.

19 Q. Thank you, sir.

20 COMMISSIONER BOYER: Is that all,
21 Mr. Proctor?

22 MR. PROCTOR: That's all.

23 COMMISSIONER BOYER: Okay, very well.

24 Mr. Dodge?

25 MR. DODGE: No questions.

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1 COMMISSIONER BOYER: No questions?

2 Mr. Ball?

3 MR. BALL: No, thank you.

4 COMMISSIONER BOYER: Ms. McDowell, anything
5 further?

6 MS. McDOWELL: No, your Honor.

7 COMMISSIONER BOYER: Thank you Mr. Williams,
8 you may be excused. Or step down, anyway.

9 I guess that brings to us Dr. Hadaway?

10 MS. McDOWELL: That's correct.

11 (Dr. Hadaway was duly sworn.)

12 COMMISSIONER BOYER: Thank you. You may be
13 seated.

14 SAMUEL C. HADAWAY,
15 called as a witness, having been duly sworn,
16 was examined and testified as follows:

17 EXAMINATION

18 BY MS. McDOWELL:

19 Q. Good morning Dr. Hadaway.

20 A. Good morning.

21 Q. Can you please state your full name and spell
22 it for the record?

23 A. My name is Samuel C. Hadaway. S-a-m-u-e-l,
24 middle initial C. Hadaway, H-a-d-a-w-a-y.

25 Q. Mr. Hadaway, how are you employed?

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1 A. I'm a principal and co-owner in a financial
2 consulting firm, Financo, Inc., of Austin, Texas.

3 Q. And in that capacity have you been employed
4 by the Company to prepare expert testimony in this
5 proceeding?

6 A. Yes.

7 Q. Have you prepared direct and rebuttal
8 testimony in this proceeding that has been offered and
9 admitted already?

10 A. Yes.

11 Q. Dr. Hadaway, have you prepared a summary of
12 your direct and rebuttal testimony?

13 A. Yes, I have.

14 Q. Can you please provide that summary?

15 A. Yes, thank you. Good morning, Mr. Chairman,
16 Commissioners, thank you for being here again.

17 COMMISSIONER BOYER: Welcome Dr. Hadaway.

18 THE WITNESS: My testimony covers the
19 Company's requested Rate of Return on equity. As
20 Mr. Williams just covered with you, he uses the cost
21 of debt, preferred stock, and capital structure, along
22 with my estimate of ROE, to calculate the overall Rate
23 of Return, which is then applied to the rate base.

24 Rate of Return, as you well know, is often
25 controversial, for at least two very important

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1 reasons: One, the dollars are large. When one
2 applies the Rate of Return to the rate base, the
3 amount of money involved is a lot. But ROE is also
4 controversial because it's quite subjective.

5 There's no book or other publication to tell
6 us what ROE is. For this reason, economists usually
7 rely on two categories of information to estimate ROE:
8 They rely on financial models, and they rely on
9 financial market data.

10 While there is not a data source that tells
11 us what ROE is, such things as interest rates, rates
12 of return allowed by other regulators, and other
13 economic data are often used. With respect to
14 financial models there's several different categories,
15 but most regulators use the discounted cash flow
16 model, or DCF model. And many use some form of risk
17 premium analysis, at least as a check of
18 reasonableness.

19 In my direct and rebuttal testimony I present
20 results from three forms of the DCF model, as well as
21 various risk premium methods. My updated DCF results,
22 with data through March of 2008, are summarized in my
23 rebuttal testimony in Exhibit SCH-R-7.

24 Those results from the DCF model indicate a
25 range of 10.4 percent to 11.3 percent. If we might --

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1 and I am going recall the Chairman's admonition. If
2 we might, I think we would expedite things if we
3 looked at that exhibit very briefly.

4 It's exhibit -- it's under the tab Exhibit
5 SCH-R-7 -- or 7-R. That exhibit consists of 5 pages.
6 But I'd like to just start with the first page, which
7 is a summary of the results from the three DCF models.
8 There should be a tab that says Exhibit RMP-SCH-7-R.

9 COMMISSIONER BOYER: Seven-R?

10 THE WITNESS: Yes, sir.

11 COMMISSIONER BOYER: That's my problem. I'm
12 now with you, Mr. Hadaway.

13 THE WITNESS: Okay. If you look at that
14 first page of 7-R there are four columns. The first
15 column is just the name of the companies, the
16 comparable companies that we used in our estimation
17 process. The other three columns show the results
18 from, from the various versions of the DCF model.

19 In the DCF model, as you know, ROE is just
20 the sum of the expected yield -- the dividend yield --
21 that investors, expect plus the growth rate that they
22 expect. In, in the first column of numbers there,
23 this is strictly the traditional constant growth DCF
24 model.

25 And in that model I used only analyst

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1 estimates of earnings growth to estimate the growth
2 rate. Later we're gonna talk about gross domestic
3 product and some other ways of doing that. But that
4 first column is about as traditional as you can get in
5 terms of the DCF model. The range from that model is
6 10.4 to 10.8 percent, as you see down there in the
7 average median at the bottom.

8 If you want to flip over to the second page.
9 This sort of makes how the DCF model work -- works
10 pretty clear. Again, it's just the dividend yield
11 plus the growth rate. And if you look in column 3 you
12 see that the dividend yield that we use is next year's
13 projected dividend from column 2, divided by the
14 recent price in column 1.

15 Down at the bottom of column 3 you see that
16 the average median is 4.7 to 4.8 percent, about. So
17 that's the first part of the constant growth DCF
18 model. If you look over in columns 4 through 7,
19 that's where I calculate the growth rate that's used
20 in that first model.

21 Columns 4, 5, and 6 are simply surveys done
22 by Zack's, Reuters, and Thompson financial, where they
23 ask security analysts on Wall Street and elsewhere
24 what they project the earnings growth rate to be for
25 these companies for the next five years.

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1 These are traditionally used by Rate of
2 Return analysts. I've criticized them in some cases
3 because they're quite volatile. Sometimes they change
4 more than the constant growth DCF model would -- you
5 would expect for them to. But that's what they are.

6 We averaged those together in column 7. And
7 then you see, you see that over in column 8 we add
8 together 7 and 3, and that's where you get the DCF
9 range of 10.4 to 10.8. That's the first model, and
10 that's the one that people typically argue about.

11 If we flip back to the first page, the
12 summary page, I'll very briefly talk about the other
13 two models. The column of numbers in the middle is
14 the same in terms of form as the constant growth DCF
15 model, but in that I use a growth rate based on the
16 overall growth in the U.S. economy as proxied by the
17 nominal gross domestic product growth rate.

18 In my direct testimony and rebuttal I provide
19 forecasts of what that GDP growth rate is. That
20 number has been updated in my rebuttal and it is
21 6.5 percent. In this version of the model the
22 analysts' growth rates at the present time are just a
23 little bit lower than 6.5 percent. So you can see
24 that the GDP model produces numbers of 11.2 to
25 11.3 percent.

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1 That's not my final recommendation. My final
2 recommendation is 10.75. But that's the most
3 aggressive of the three models. The third model, in
4 the far right-hand column of the summary page, is sort
5 of a compromise.

6 It uses dividends from Value Line for the
7 first five years, and then it switches to the
8 long-term GDP growth rate in years five out to the
9 future. This is a model that has been used,
10 particularly in the state of Oregon it is the one that
11 is required to be used.

12 It is not -- I don't want to say that they
13 use the DCF growth rate as the growth rate in it, but
14 it's the form of the model that they use. And many
15 commissions use two-stage models. You can see that
16 because it is a combination of dividends and other
17 growth rates, it's sort of in between the other two.

18 At any rate, based on all these three models,
19 the DCF range is 10.4 to 11.3, quantitatively from all
20 of those. My final recommendation, as I said, is
21 10.75 percent. I also update my risk premium analysis
22 in Exhibit SCH-8-R.

23 In that analysis I used, at the time, a
24 forecasted Single-A utility interest rate. And that
25 interest rate in Exhibit 8-R is 6.36 percent. That

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1 results in a risk premium estimate of ROE of
2 10.73 percent.

3 However, you've read the surrebuttal
4 testimony and other testimony and know that there is
5 controversy about interest rate forecasts in this
6 case. So I have also rerun that model with just the
7 current interest rate.

8 I'll show you an update to my Table 1 in a
9 few minutes. But through April the Single-A interest
10 rate is 6.29 percent. About the same -- last one that
11 was discussed earlier here for March, but it's up just
12 a little bit in April.

13 For the month of April it was 6.29 percent.
14 I looked on Moody's website yesterday, it was
15 6.27 percent as of Friday. So that rate has been
16 pretty constant the last 30 days or so in that 6 1/4,
17 6.3 range.

18 The three of us who estimated ROE used
19 various models. We used all -- all of us used the DCF
20 model. And based on that model alone, if it was just
21 DCF, our ROE estimates are not as far apart as our ROE
22 recommendations are.

23 For example, Mr. Peterson recommends a
24 10.1 percent ROE, but his DCF analysis based on his
25 earnings growth rates indicates an ROE range of 10.37

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1 to 10.69. That's on page 26 of his direct testimony.

2 Mr. Lawton recommends an ROE of only
3 9.85 percent, but his primary DCF analysis based on
4 his actual DCF work, not his critiques of mine,
5 produces about a 10 percent ROE.

6 While I continue to disagree with the other
7 witnesses' growth rate inputs, if this Commission
8 relies strictly on the DCF model, even with their
9 growth rates, that model indicates ROEs between 10 and
10 10.7 percent.

11 If some weight is also given to my slightly
12 higher long-term growth rates, the range is between
13 10 1/2 and 11 percent. In addition to the DCF models,
14 we all also offered various risk premium results.

15 As I indicated in my rebuttal, I disagree
16 with Mr. Peterson's CAPM results because under current
17 market condition the CAPM, using the government bond
18 interest rate and historical market risk premiums,
19 cannot reflect the current market turmoil or the
20 higher current corporate interest rates that companies
21 like Rocky Mountain Power are having to pay.

22 I've been criticized by the other parties
23 because I used CAPM in my direct testimony. And that
24 result was 9.8 percent to 10.6 percent when I prepared
25 my direct testimony. But I have excluded the updated

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1 results from the CAPM in my rebuttal testimony. I
2 didn't include the CAPM in my rebuttal because
3 government policy has pushed down government interest
4 rates to artificially low levels.

5 The short-term Treasury Bill rate that's
6 sometimes used -- and that I used in one version of
7 the CAPM -- dropped to as low as 1 percent a few weeks
8 back. It's about 1.8 percent now.

9 Other government interest rates, because of
10 the "Flight to Safety" as it's called -- that is,
11 investors being afraid of the market turmoil and
12 moving their money into Treasury bonds -- has also
13 pushed down even the long-term Treasury bond rate.

14 I did rerun CAPM, doing it the same way I did
15 in my direct testimony, and the result was about
16 8 percent to 9.5 percent ROE. Those results indicate
17 declining capital costs when, in fact, corporate costs
18 have gone up. For that reason I rely on the updated
19 DCF and corporate bond risk premium methods, and not
20 the CAPM, to support my final 10.75 percent ROE
21 recommendation.

22 I also disagree with Mr. Lawton's risk
23 premium analysis because he uses a base interest rate
24 in that analysis of only 5 1/2 percent. That number
25 is simply wrong. Current Single-A utility interest

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1 rates, as I've said, are about 6.3 percent. They
2 haven't been as low as 5.5 percent since 2005.
3 Mr. Lawton and the other parties here agreed to a
4 settlement at 10 1/4 percent ROE. Interest rates have
5 gone up almost a hundred basis points since then.

6 To make sure that everything is clear about
7 these interest rate issues I've prepared an update of
8 the Table 1 interest rate data that appeared in my
9 direct and rebuttal testimony. Table 1 lists the
10 average Single-A utility interest rates for each
11 month, along with government bond interest rates for
12 each month, January 2005 through April 2008.

13 Now, I believe we have copies of that updated
14 table. It's exactly the same as in my two pieces of
15 testimony, with just one more month added to it.

16 (Pause.)

17 THE WITNESS: I hope that this exhibit will
18 help to clarify some of the confusion about
19 difficulties in interest rate forecasts, about where
20 government bond rates have gone, but also make quite
21 clear where corporate borrowing costs and corporate
22 capital costs have gone.

23 As I also said a few minutes ago, I looked in
24 Moody's website yesterday. And the number for
25 April -- I'm sorry. The number for May the 16th,

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1 Friday's interest rate, the Single-A interest rate was
2 6.27 percent.

3 Last week it went up as high as 6.32 percent.
4 It fluctuates a few basis points each day. But there
5 is no material change that has occurred since this
6 exhibit -- since the data was available for this
7 exhibit.

8 The first column of numbers in Table 1 shows,
9 about as clearly as possible, that utility interest
10 rates have not declined to but in fact increased
11 almost a full percentage point since their lows in
12 2005. I hope that the Commission will not be
13 distracted by Mr. Peterson, and particularly
14 Mr. Lawton's discussion of interest rate forecasts and
15 government rate policies.

16 Table 1 also shows government interest rates
17 that have occurred, but in the right hand two columns
18 the much wider interest rate spreads that utilities
19 like Rocky Mountain Power and other corporations have
20 had to pay.

21 Those spreads have almost doubled from the
22 levels that existed you can see back early, if you
23 look in the last two columns of the exhibit. The
24 spread is simply the Single-A interest rate in the
25 20 year column, minus the 20 year Treasury bond rate.

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1 And the last column is the Single-A utility rate minus
2 the 10 year utility rate.

3 The market turmoil that has occurred has
4 caused corporate interest rates to go up. These facts
5 show that Mr. Peterson and Mr. Lawton are simply
6 incorrect in their statements that rates have
7 declined.

8 In this context, their estimates of ROE are
9 too low. They do not reflect the increased borrowing
10 costs that Rocky Mountain is required to pay. The
11 Company's requested an ROE of 10.75 is the most
12 reasonable reflection of these costs.

13 Thank you for your attention. I'll be happy
14 to answer any questions.

15 COMMISSIONER BOYER: Thank you, Dr. Hadaway.

16 Ms. McDowell: Commissioner Boyer, if I
17 might, can I ask a couple of questions to lay the
18 foundation for this exhibit?

19 COMMISSIONER BOYER: Please, if you would.

20 Ms. McDowell: Thank you.

21 Q. (By Ms. McDowell) Dr. Hadaway, have you
22 previously provided versions of Table 1 in your direct
23 and rebuttal testimony?

24 A. Yes.

25 Q. What is the change that you have made to

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1 Updated Table 1 for purposes of this morning's
2 hearing?

3 A. The data on this table are published in
4 what's called Moody's Bond Record. Moody's has been
5 bought by Emergent, so sometimes it's called Emergent
6 Bond Record now as well. But these come out each
7 month, with the average of the daily interest rates.

8 So all that I've done is add the month of
9 April to these dates. For the data in the 20 year and
10 10 year Treasury bond columns I looked on the Federal
11 Reserve website, that economists like me typically
12 use. They're the official interest rates that are
13 published on the Federal Reserve website.

14 Q. All right Dr. Hadaway. I think you were --
15 you indicated that the data through March of '08 had
16 been provided in your rebuttal testimony?

17 A. Yes, that's right.

18 Q. So the only addition is the last line on the
19 table?

20 A. That's right.

21 Ms. McDowell: We would offer Updated
22 Table 1. And I'm not sure what the next exhibit in
23 sequence is.

24 COMMISSIONER BOYER: Nor am I.

25 Ms. McDowell: So who might be able to inform

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1 us of that?

2 COMMISSIONER BOYER: According to my records
3 the last exhibit is SCH-8R.

4 Ms. McDowell: So would it be appropriate to
5 make this hearing Exhibit No. 1-ROR-1? Is that per
6 your numbering purposes?

7 COMMISSIONER BOYER: Whatever your -- it just
8 needs to be identified separate from the other
9 exhibits.

10 Ms. McDowell: Okay. So if we do Exhibit
11 RMP-1(RoR), that's how we would mark this exhibit.
12 And we would offer it now into the record.

13 COMMISSIONER BOYER: Any objections to
14 Updated Table 1, referred to as Exhibit RMP-1-(RoR)?

15 MS. SCHMID: None.

16 MR. PROCTOR: No objections, thank you.

17 COMMISSIONER BOYER: Seeing none, it will be
18 admitted into evidence. Thank you.

19 Ms. McDowell: Thank you. And I just had one
20 point of clarification for Dr. Hadaway.

21 Q. (By Ms. McDowell) I believe you misspoke,
22 Dr. Hadaway, when you indicated that the agreement on
23 ROE in 2005 was 10.25. Did you mean to say 10.5?

24 A. Yes. The later one was 10.25, sorry.

25 Q. Thank you, Dr. Hadaway.

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1 Ms. McDowell: With that, I have nothing
2 further. And witness is available for cross
3 examination.

4 COMMISSIONER BOYER: Very well. Let's turn
5 to Ms. Schmid.

6 CROSS EXAMINATION

7 BY MS. SCHMID:

8 Q. Good morning, Dr. Hadaway. How are you?

9 A. Good morning, Ms. Schmid. Thank you.

10 Q. Dr. Hadaway, if we turn to the exhibit you
11 referenced a little earlier, which is in your rebuttal
12 testimony marked as SCH-7-R, the first page?

13 A. I have that.

14 Q. If we look at your column entitled "Constant
15 Growth DCF Model Analyst Growth Rates," we see numbers
16 most generally in the 10, 11, or 9 percent range; is
17 that correct? And I'll eliminate the decimal points,
18 after the decimal points.

19 A. Yes, that's right.

20 Q. But we do see one 16.8 reference; is that
21 correct?

22 A. Yes, for PPL Corporation.

23 Q. If we delete the PPL Corporation at 16.8, as
24 it is much higher than the others, would you accept
25 subject to check that the group average is

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1 10.2 percent?

2 A. I'll accept that subject to check.

3 Q. Thank you. Dr. Hadaway -- it's always
4 frightening when a lawyer tries to ask economic
5 questions, but here I go. What is a rate of return?

6 A. It's the expected rate that equity investors
7 wish to receive on their equity investment.

8 Q. And what is a market, please?

9 A. A market is a place where securities, in this
10 case, are traded.

11 Q. So it's true that a rate of return is not
12 necessarily the same thing as a market; is that
13 correct?

14 A. It's certainly not the same as a market, but
15 the estimate of the rate of return is derived from
16 market data.

17 Q. Okay. Did you read the Commission's 2002
18 Questar Gas order, insofar as it addressed rate of
19 return and a weighted dividends earnings formula in
20 preparation for this case?

21 A. I did not. I have discussed it with
22 Counsel -- and I don't know if it's the 2002 case, but
23 I have discussed Questar cases with Counsel about that
24 issue.

25 Q. Okay. Are you familiar that the Commission

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1 did a 75/25 equation in that case?

2 A. It's my understanding that that was the low
3 end of the Commission's range. And that they used
4 earnings only as the upper end of the DCF range.

5 Q. Okay. Are you familiar with the recent Rocky
6 Mountain Power rate case in Wyoming, which is Docket
7 No. 20000-277-ER-07?

8 A. I am. I was a witness in that case.

9 Q. Thank you. Are you also familiar with the
10 recent Rocky Mountain Power rate case in Idaho, Docket
11 PAC-E-07-05?

12 A. Yes. I was also a witness in that case.

13 Q. Thank you. Didn't you originally recommend a
14 10.75 rate for each of those cases?

15 A. I did.

16 Q. And then didn't you say, at least in Wyoming
17 and I believe in Idaho as well, that a 10.25 wasn't --
18 rate was in a range of reasonableness?

19 A. We didn't have a hearing and I didn't say
20 anything in Idaho, but I did testify about the
21 settlement in Wyoming. I don't remember the exact
22 words. But in the context of the settlement I
23 certainly would agree with that.

24 Q. Okay. And so the decision in Wyoming was a
25 result of a settlement, but the decision in Idaho was

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1 a result of litigation?

2 A. No, they were both settlements.

3 Q. They were both settlements? Okay. Isn't
4 10.25 much closer to the 10.1 that the Division is
5 recommending here than 10.25 is to 10.75?

6 A. Mathematically, perhaps so.

7 Q. Um --

8 A. Interest rates have gone up since those
9 settlements that you asked me about.

10 Q. Is it true that you were involved, on behalf
11 of the Public Service Commission of New Mexico, in a
12 gas case, Docket No. 06-00210-UT, and an electric
13 case, Docket No. 07-00077-UT, before the New Mexico
14 Public Regulation Commission?

15 A. Yes. I testified for the company there, not,
16 not for the Commission.

17 Q. And isn't it true that you used a GDP
18 component in your calculations there?

19 A. I did.

20 Q. And isn't it true that the New Mexico Public
21 Regulation Commission rejected the use of GDP in that
22 case?

23 A. That Commission has done a lot of things.
24 Company stock price has fallen in half since the
25 decisions that were made there. But they did indeed

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1 impose, to my knowledge, the most hash decision in a
2 gas case that's been made in the country.

3 Q. Isn't it true, however, that they did reject
4 your use of the GDP?

5 A. Actually they didn't, Ms. Schmid. The
6 examiner did. And then the Commission came back and,
7 in their modifications to the proposal for decision,
8 said that they did include some consideration of it in
9 one of the averages.

10 Q. When I look at that -- let's see.

11 MS. SCHMID: One moment, please.

12 (Pause.)

13 Q. (By Ms. Schmid) Okay. And isn't it true
14 that if we delete the GDP component from your
15 calculations here, then your rate is not very far from
16 Mr. Peterson and Mr. Lawton?

17 A. Yes. That's why I talked about that first
18 column of my exhibit. That one and retail --
19 re -- that one uses only analyst growth rates. The
20 10.4 to 10.8 percent.

21 MS. SCHMID: Thank you very much. Those are
22 all my questions.

23 THE WITNESS: Thank you.

24 COMMISSIONER BOYER: Thank you, Ms. Schmid.

25 Mr. Proctor, questions for Dr. Hadaway?

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1 MR. PROCTOR: Yes.

2 CROSS EXAMINATION

3 BY MR. PROCTOR:

4 Q. Dr. Hadaway, in your direct testimony I
5 understand that you did, in fact, use the CAPM model
6 to estimate a rate of return; is that correct?

7 A. Yes, I did.

8 Q. And what was the outcome of your analysis
9 using that model in your direct?

10 A. I gave that in my summary. Let me look here
11 just for a second. At that time government interest
12 rates indicated, let's see, 9.8 to 10.6 percent.

13 Q. Now, in your surrebuttal you abandoned that
14 model. And I don't mean to misstate, so you can
15 correct me. But it's because of the turmoil that you
16 saw in the markets that had occurred since the time
17 you prepared that testimony until the time you filed
18 your surrebuttal. Is that a fair statement?

19 A. It's a little more than that. It's the
20 inconsistency between rising corporate borrowing costs
21 and government policies that have pushed down the
22 federal funds rate to a low of 2 percent, the
23 short-term Treasury Bill rate to 1 percent.

24 Q. Okay.

25 A. Which the one year Treasury also went down to

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1 1 percent. It happens that those indexes are what
2 banks borrow overnight for on the federal funds rate.
3 And the one year Treasury Bill rate is the basis for
4 the adjustable rate mortgage that many, many people
5 have.

6 So to avoid upward movements in that mortgage
7 rate, the government has had a policy of driving down
8 particularly the one year Treasury Bill rate. Those
9 rates figure directly into the CAPM. And I explained
10 why I didn't think it was appropriate to use them now
11 to estimate the corporate cost of capital.

12 Q. Did you ever use the term "market turmoil" in
13 your surrebuttal test -- or your rebuttal testimony?

14 A. I'm sure that I did, yes.

15 Q. Yes. In fact, on page 6 is the first time it
16 appears, market turmoil, along with your Flight to
17 Safety reference; is that correct?

18 A. Yes.

19 Q. So in fact weren't you referencing -- in
20 abandoning your CAPM model weren't you referencing the
21 same economic conditions and uncertainty that this
22 Commission referenced when it determined that 2008 was
23 in fact the test period to be utilized in this case?

24 A. I'm not sure I understand where you're going,
25 Mr. Proctor.

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1 Q. It's not a matter of where I'm going, sir.
2 It's a question that I've asked you, and I would like
3 an answer to the question.

4 A. I don't know what the Commission referenced.

5 Q. Didn't they use similar terms to "economic
6 uncertainty"?

7 A. I don't know.

8 Q. Have you read that order?

9 A. No.

10 MR. PROCTOR: Thank you very much. No more
11 questions.

12 COMMISSIONER BOYER: Thank you, Mr. Proctor.
13 Mr. Dodge?

14 MR. DODGE: No questions.

15 COMMISSIONER BOYER: No questions?

16 Mr. Ball?

17 MR. BALL: Nothing, thank you.

18 COMMISSIONER BOYER: Very well. Redirect,
19 Ms. McDowell -- oh, we might have questions ourselves.
20 Commissioner Allen?

21 COMMISSIONER ALLEN: Thank you, Mr. Chairman.

22 In your testimony you've indicated,
23 Dr. Hadaway, that you used GDP. And I'm just assuming
24 that gross domestic product helps you get a handle on
25 whether we have an expanding or contracting economy as

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1 you do your model; is that correct?

2 THE WITNESS: Yes, sir that's right.

3 COMMISSIONER ALLEN: In the process of doing
4 that do you ever take into account regional
5 differences in the potentials of --

6 THE WITNESS: I don't. And the reason why is
7 because the capital markets really are nation wide,
8 and even really global now.

9 Once in a while, when there's certain issues
10 like the Western energy crisis, you know, major, major
11 things like that, then certainly economists take that
12 into account. But in a routine circumstance, where
13 we're just looking at national markets and what the
14 costs are, then we don't do that.

15 COMMISSIONER ALLEN: Do you think that even
16 if you were, do you think it would be material --
17 we've see some spreads now recently, I'm just
18 wondering what you think about the materiality if you
19 did do that.

20 THE WITNESS: Well they would be much higher,
21 obviously, but I haven't tried to incorporate that.

22 COMMISSIONER ALLEN: Thank you.

23 COMMISSIONER BOYER: Commissioner Campbell?

24 COMMISSIONER CAMPBELL: Just out of
25 curiosity, are you aware of what's going on with PPL

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1 that is causing analysts to estimate such a high
2 growth rate?

3 THE WITNESS: They have had a restructuring
4 of that entire company, and I don't know exactly what
5 it is that's happened. Sometimes in these data you'll
6 see a company that has probably gone through a low
7 point and is expected to make a tremendous recovery.
8 That will cause a higher number like that. But I
9 don't know about PPL.

10 COMMISSIONER BOYER: Dr. Hadaway, I just have
11 a couple of questions relating to your Exhibit
12 SCH-7-R. In the first column you list a number of
13 comparable companies, 14 of them to be exact. How did
14 you go about selecting those? What kind of variables
15 do you look at?

16 THE WITNESS: That's very important. We
17 start with the company -- the subject company's bond
18 rate. PacifiCorp and Rocky Mountain Power are rated
19 Single-A minus. So we require that at least one of
20 the bond rating agencies rate companies at least
21 Single-A to be included in our group.

22 We also then -- a lot of companies have such
23 diversification efforts going on that it causes their
24 data to be influenced by things other than regulation.
25 So we require that at least 70 percent of the revenues

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1 be from regulated activities.

2 We also look and require that they haven't
3 cut their dividends in the past two years, because the
4 dividend is so important in the DCF model. And we
5 make sure that they're not currently engaged in merger
6 activities, because there's been so much of that.

7 Between the direct and rebuttal testimony,
8 for example, Energy East has become subject of a
9 merger. And so it has been removed from the group.
10 The group, as you can see here, is 14 companies, and
11 it was previously 15.

12 But those are the most general kinds of
13 screens. There are others. In my long experience in
14 this business I've found that economists are
15 criticized more for picking and choosing if they get
16 too careful about the companies that they pick, so we
17 have stuck with a very broad base like this.

18 I think 15 companies, 14 companies is okay as
19 a sample size. If it gets too much smaller than that,
20 then sometimes one has to try to look at other
21 factors. But here I think we're okay with this
22 sample.

23 COMMISSIONER BOYER: Do -- does capital
24 structure play any role in this?

25 THE WITNESS: It does not, except indirectly,

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1 as it certainly affects the bond rating. You're not
2 gonna find a Single-A rated company that's got 70
3 percent debt or something like that.

4 COMMISSIONER BOYER: And on this list
5 Ms. Schmid pointed out PPL, and Commissioner Campbell,
6 would you consider that to be an outlier?

7 THE WITNESS: Yes.

8 COMMISSIONER BOYER: Just because of
9 various -- okay.

10 Commissioner Allen has one additional
11 question.

12 COMMISSIONER ALLEN: Thank you, Mr. Chairman.

13 I almost forgot to ask -- it's kind of
14 related to my previous question -- when you talk about
15 the inputs to your analysis and where that comes from.
16 I'm just curious, when you look at company --
17 comparable companies, I think the Value Line analysis
18 is where you looking at that.

19 I'm curious, is that pretty much strictly a
20 financial analysis? Or does that include other
21 factors, such as similar companies, whether they're
22 fully regulated, partially deregulated?

23 THE WITNESS: We do use the screen that says
24 they have to be -- 70 percent of the revenues have to
25 come from regulated activities. So that, that helps

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1 to at least mitigate -- it doesn't entirely eliminate
2 the effect -- but it helps to mitigate the
3 non-regulated activities.

4 COMMISSIONER ALLEN: Thank you.

5 COMMISSIONER BOYER: Back to you,
6 Ms. McDowell. Anything further for Dr. Hadaway?

7 Ms. McDowell: Thank you, Commissioner Boyer.

8 REDIRECT EXAMINATION

9 BY MS. McDOWELL:

10 Q. I have a couple of questions for you,
11 Dr. Hadaway. The first pertains to Ms. Schmid's
12 questions about the settlements in Wyoming and Idaho
13 and the ROE numbers that came out of those
14 settlements.

15 Dr. Hadaway, were those settlements all-issue
16 settlements?

17 A. As far as I know, they were, yes.

18 Q. They were not ROE-only settlements?

19 A. No, absolutely not.

20 Q. So you were testifying as to the
21 reasonableness of ROE in the context of an overall
22 revenue requirements settlement?

23 A. There was no testimony in Idaho. That
24 settlement was accepted. There was testimony in
25 Wyoming. And I was asked, because there was concern,

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1 that the Commission might reduce the ROE or change it
2 somehow. I presented this same data to say why that
3 that was the minimum ROE that I thought the company
4 should settle for.

5 Q. Dr. Hadaway, you were asked about your
6 testimony in New Mexico, and the New Mexico
7 Commission's reactions to your GDP proposal. Have you
8 presented that proposal to other State Commissions?

9 A. Yes, I have.

10 Q. And has it been received by other State
11 Commissions and approved?

12 A. Yes. There, there have only been about three
13 cases in my long history where the Company's requested
14 ROE was accepted. Once in Wyoming. And most recently
15 in Missouri, where the Missouri Commission looked
16 directly at the GDP growth rate. They looked at the
17 other witnesses' analyses.

18 I had recommended an 11 1/4 percent based
19 R0 -- or 11 percent based ROE, and they accepted it.
20 They added 25 basis points to that for a construction
21 program as well.

22 But the FERC has used GDP growth in their gas
23 pipeline cases for a long, long time. Other
24 commissions -- I testified recently in Massachusetts,
25 where I was criticized for using GDP in a

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1 distribution-only case out there.

2 Fully litigated. That Commission found that
3 GDP did not reflect the ROE as far as they were
4 concerned. They requested 10.75. And they granted,
5 after full litigation and delivery on the case,
6 10 1/4.

7 So, you know, those are sort of the
8 directions that things are going. The problem with
9 the analyst growth rates by themselves is that they
10 have been as low as 3 1/2 percent. And now they're
11 back up, they are as high as 6 1/2 percent. At least
12 equal to the GDP growth rate that I used.

13 But the constant growth DCF model is not
14 supposed to bounce around like that. And that's why I
15 think the FERC and others have started to use GDP as
16 least as part of what they're doing.

17 MS. McDOWELL: That's all I have,
18 Commissioner.

19 MS. SCHMID: Chairman? If I might.

20 COMMISSIONER BOYER: Yes, you may.

21 MS. SCHMID: I have very, very limited
22 recross. Limited to the subjects on redirect.

23 COMMISSIONER BOYER: That's slightly unusual,
24 but you -- for Dr. Hadaway?

25 MS. SCHMID: Yes.

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1 COMMISSIONER BOYER: All right, let's hear
2 them.

3 MS. SCHMID: Okay.

4 REXCROSS EXAMINATION

5 BY MS. SCHMID:

6 Q. Dr. Hadaway, would it surprise you that the
7 Wyoming Commission's order at paragraph 97
8 characterized your testimony and position as:

9 "Dr. Hadaway also addressed the
10 stipulation, stating that although the
11 agreed upon ROE of 10.25 percent was
12 50 basis points lower than his
13 recommended ROE, he believed the
14 stipulated 10.25 was within a range of
15 reasonableness.

16 "Dr. Hadaway recommended the
17 stipulation as it relates to the agreed
18 upon ROE at 10.25 be accepted by the
19 Commission, transcript pages 346-347."

20 A. I think you read it right.

21 Q. Okay. Would you also accept that the New
22 Mexico final electric order -- the final Commission
23 order in the docket number referenced earlier
24 beginning with 07 states that --

25 MS. McDOWELL: You know, I'm gonna object to

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1 this, because I didn't ask about New Mexico. I
2 asked -- I accepted New Mexico and asked about other
3 commissions.

4 COMMISSIONER BOYER: I think that goes beyond
5 the scope of direct, thank you.

6 MS. SCHMID: Okay. My apologies.

7 COMMISSIONER BOYER: And I think you
8 already -- that other question was already asked and
9 answered, Dr. Hadaway. Very well. Thank you,
10 Dr. Hadaway. Thank you for being here. You may step
11 down.

12 THE WITNESS: Thank you, Mr. Chairman.

13 COMMISSIONER BOYER: I think that brings us
14 to the next policy witness, which will be Mr. Peterson
15 of the Division of Public Utilities.

16 Let's check with our reporter and see how
17 you're doing.

18 THE COURT REPORTER: I'm fine.

19 COMMISSIONER BOYLE: Are you okay? All
20 right.

21 Our intention will be to go to till about
22 10:30, take a short break so that our reporter can
23 rest, and then we'll reconvene in 10 or 15 minutes.

24 Ms. Schmid?

25 MS. SCHMID: Thank you.

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1 COMMISSIONER BOYER: Have you been -- you
2 have not?

3 THE WITNESS: I have not been.

4 (Mr. Peterson was duly sworn.)

5 COMMISSIONER BOYER: Thank you, Mr. Peterson.
6 Please be seated.

7 CHARLES E. PETERSON,
8 called as a witness, having been duly sworn,
9 was examined and testified as follows:

10 DIRECT EXAMINATION

11 BY MS. SCHMID:

12 Q. Good morning Mr. Peterson.

13 A. Hello.

14 Q. Could you please state your name and business
15 address for the record?

16 A. My name is Charles E. Peterson. My business
17 address is here in this building.

18 Q. And --

19 A. I don't know the -- Heber Wells Building,
20 Salt Lake City, Utah.

21 Q. And by whom are you employed, and in what
22 capacity?

23 A. The Division of Public Utilities. And I am a
24 technical consultant within the Division.

25 Q. And are you the same Charles E. Peterson that

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1 filed DPU Exhibit No. 2.0, in both confidential and
2 non-confidential forms, as your direct, with
3 associated exhibits, and DPU Exhibit No. 2.R --
4 2.0-SR?

5 A. Yes.

6 Q. And isn't it true that we do need to check on
7 one exhibit just to make sure that one of the columns
8 was transmitted properly, and we'll get back to the
9 Commission on that?

10 A. Yes.

11 Q. Do you have a brief summary of your testimony
12 that you would like to give today?

13 A. Yes. I hope it will be brief enough.

14 Q. Thank you. Please proceed.

15 A. In my direct testimony I asserted a midpoint
16 cost of equity of 10.1 percent. That is surrounded by
17 what I consider to be a reasonable range of
18 approximately 8.65 to 10.45 percent.

19 In arriving at this conclusion I considered a
20 number of options in the Discounted Cash Flow, or DCF
21 model, and the Capital Asset Pricing Model, usually
22 referred to as CAPM. I also developed a Risk Premium
23 Model based upon Value Line financial strength
24 ratings, which I used as a check on the other models.

25 In developing the DCF models I applied

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1 earnings-only growth rates, dividend-only growth
2 rates, and the 75/25 percent weighted average of
3 forecast earnings and dividend growth rates that the
4 Commission used in its order in the 2002 Questar Gas
5 general rate case.

6 I support this weighting as a reasonable
7 compromise between the arguments for earnings-only
8 growth rates and dividend growth rates, or sometimes
9 there are other growth rates that are offered to be
10 included in the DCF model.

11 The single-stage or one-step DCF model ranged
12 from 8.63 to 10.69 percent. I also estimated
13 two-stage DCF models that gave a range from
14 9.76 percent to 10.32 percent. I also compiled
15 estimates based upon 10 year historical growth rates.

16 These growth -- these historical growth rates
17 typically gave very low results after some
18 adjustments, 7 percent range, but before adjustments
19 as low as 4 percent. I considered these to be
20 unreasonably low.

21 I've applied several variations of the CAPM,
22 including a version similar to the CAPM model that
23 PacifiCorp witness Dr. Hadaway originally used and
24 later abandoned. Except I -- that I did update the
25 risk free rates to the time period that I prepared my

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1 direct testimony.

2 Dr. Hadaway talked about using Treasury Bill
3 rates or short-term Treasury rates. I have included
4 in my models the Treasury rates, but do not recommend
5 their application in this case. I rely on 20 year
6 Treasury bond rates in developing the CAPM model as
7 the risk free rate.

8 Twenty -- the CAPM model ranged from about
9 8.6 percent to a little over 9.9 percent. My risk
10 free -- or my Risk Premium Model ranged from 8.8 to
11 10.3 percent. In these ranges I've concluded that
12 10.1 percent is a reasonable point estimate.

13 As testified earlier, we have no -- the
14 Division has and I have no problems with the capping
15 structure recommended by the Company, nor the cost of
16 preferred stock. There is an issue about using the
17 forecast forward interest rate curve for the
18 \$700 million debt offering that the company
19 anticipates making toward the end of the year.

20 The Company is late -- lately discussing that
21 interest rates have gone -- or that the long-term
22 interest rates have gone down and the credit spread
23 has widened between corporate debt and the government
24 bond interest rates.

25 While this may be true, Dr. Hadaway also

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1 mentioned in his rebuttal testimony that these credit
2 spreads are narrowing. And I would expect them to
3 continue to narrow back to a more typical range.
4 Therefore, at this point in time I'm still standing by
5 my 2 percentage point -- or 2 basis point, rather --
6 there's a big difference -- 2 basis point reduction in
7 the cost of debt for long-term debt.

8 Dr. Hadaway did a pretty good job of
9 discussing some of our differences. I do not agree
10 with his GDP growth rate. And certainly if it -- if
11 GDP growth is appropriate, it should be a
12 forward-looking GDP growth rate. And not one based
13 upon the historical averages that Mr. -- or excuse me,
14 Dr. Hadaway testified to.

15 There are forecasts of long-term GDP growth
16 rate. I highlighted two of the sources of government
17 estimates in my testimony, both of which conclude that
18 a growth -- a long-term GDP growth rate of around
19 4 1/2 percent is currently expected. And I explained
20 why I believe that is reasonable, given current
21 economic conditions worldwide.

22 Well, to make this quicker, I just would
23 conclude by saying that, despite the criticisms
24 offered by the Company's witnesses, I stand by my
25 original direct testimony. And suggest a recommended

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1 point estimate of 10.1 percent for the return on
2 equity portion, and an overall cost of capital of
3 8.2 percent. Thank you, that concludes my summary.

4 COMMISSIONER BOYER: Any questions for
5 Mr. Peterson?

6 MS. SCHMID: No. Mr. Peterson is now
7 available for cross examination.

8 COMMISSIONER BOYER: All right. Let's start
9 with Ms. McDowell, with the Company, and then with
10 Mr. Proctor, and around the room. Are you -- do you
11 anticipate lots of questions for Mr. Peterson?

12 MS. McDOWELL: More than seven minutes. So I
13 don't know if --

14 COMMISSIONER BOYER: All right, let's --

15 MS. McDOWELL: I'm happy to commence, but I'm
16 also happy to --

17 COMMISSIONER BOYER: No, let's -- rather than
18 interrupt your cross examination let's take a
19 13 minute break. And we'll come back here about 25 to
20 the hour.

21 (A recess was taken from 10:23 to 10:38 a.m.)

22 COMMISSIONER BOYER: Ms. Schmid would like to
23 introduce a corrected exhibit to Mr. Peterson's
24 testimony at this time, and she's distributing it at
25 this moment.

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1 Q. (By Ms. Schmid) Mr. Peterson, do you have
2 before you a document entitled DPU Exhibit 7 --
3 2.7(a)?

4 A. Yes.

5 Q. Is this the same as the previous exhibit,
6 except that the column there that had zeroes has been
7 corrected and it now has numbers?

8 A. Yes.

9 Q. The -- do you recall which column that was
10 that had the zeroes?

11 A. It was the projected three to five year EPS
12 growth.

13 Q. Thank you.

14 MS. SCHMID: The division would like to move
15 and request that this page be substituted for the
16 deficient previous DPU Exhibit 2.7(a.) And the
17 Division believes also that the electronic copy
18 contained -- submitted to the Commission contained the
19 same defect of zeroes.

20 COMMISSIONER BOYER: Any objection to the
21 admission of this corrected exhibit?

22 MS. McDOWELL: No.

23 COMMISSIONER BOYER: Very well. It is
24 admitted into evidence. Thank you Ms. Schmid.

25 Ms. McDowell, you may proceed with your cross

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1 examination of Mr. Peterson.

2 MS. McDOWELL: Thank you, Commissioner Boyer.

3 CROSS EXAMINATION

4 BY MS. McDOWELL:

5 Q. Good morning Mr. Peterson.

6 A. Hello.

7 Q. So, I was struck by one comment you made in
8 your summary, and I wanted to begin with that. You
9 indicated that in Mr. Hadaway's rebuttal testimony he
10 indicated that spreads are starting to narrow?

11 A. Yes.

12 Q. Can you please direct me to the point in
13 Mr. Hadaway's testimony that your comment is based on?

14 A. I hope I can. Yes, it's on page 4. The
15 broader context is lines 80 through 88. Starting with
16 line 83: "Corporate interest rate spreads" -- no,
17 wait a minute. That's the wrong one.

18 Q. In fact, that reference states that corporate
19 interest spreads are currently the highest level seen
20 in many years.

21 A. Right.

22 Q. Do you see that?

23 A. That's, that's correct. I went to that one
24 because that was part of my surrebuttal testimony, so.

25 Q. Well, we could go through the pages where he

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1 talks about spreads, if that would be helpful.

2 A. Um.

3 Q. Page 1, lines 11 through 12, is the first
4 reference.

5 A. Well, I will either find it because I've
6 highlighted it, or I will not be able to find it.

7 Q. Well, let's go back to the beginning of the
8 testimony, page 1.

9 A. Okay.

10 Q. Lines 11 and 12. Do you see that
11 testimony --

12 A. Yes.

13 Q. -- there pertaining to spreads? And now
14 there that testimony says that your recommendation and
15 Mr. Lawton's are not consistent with much wider
16 interest rate spreads. Do you see that?

17 A. I see that, yes.

18 Q. So that's, that's certainly not the reference
19 to narrowing spreads?

20 A. No.

21 Q. How about page 2, lines 35 and 36? That's a
22 similar reference, isn't it --

23 A. Yes.

24 Q. -- to widening spreads?

25 (Pause.)

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1 THE WITNESS: Well, I have to confess that I
2 have not been able to find where I got that notion
3 from. I with -- I apologize. I withdraw the comment.

4 Q. (By Ms. McDowell) Thank you Mr. Peterson.
5 Can you please turn to page 10 of your surrebuttal?
6 Do you have that?

7 A. Yes.

8 Q. I'd like to basically direct your attention
9 to the far -- that Q&A that begins on line 175. Do
10 you have that?

11 A. Yes.

12 Q. And there you testify that the turmoil in the
13 credit markets is not significant to cost of equity
14 for utilities. Is that a fair summary?

15 A. It hasn't been -- it has not significantly
16 affected stock prices.

17 Q. But it -- cost of capital is certainly more
18 than just stock prices, wouldn't you agree?

19 A. Well, depending on which model you use. It
20 can be more. But that -- but stock prices are the
21 basis for cost of equity in every model that I'm aware
22 of. And stock prices have shown very -- especially
23 utility stock prices have shown very little reaction
24 to the --

25 Q. So --

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1 A. -- to the credit prices.

2 Q. So Mr. Peterson, do you agree that the
3 turmoil in the credit markets would impact utilities
4 if they could not access financing at market rates?

5 A. Well, as a broad statement, if they couldn't
6 access financing then I guess I would have to agree
7 with that. But there's no evidence that they are not
8 able to access financing.

9 Q. So in that Q&A at the bottom of the page
10 there you reference the Questar Gas general rate case,
11 correct?

12 A. Yes.

13 Q. And you've filed testimony in that case as
14 well?

15 A. Yes.

16 Q. I'm going to hand you a cross examination
17 exhibit which I'll mark as RMP Cross Examination
18 Exhibit 1.

19 MS. McDOWELL: That was a direct exhibit.
20 This is our first cross examination exhibit, so I
21 began the sequence again.

22 MR. BALL: Beg your pardon. Trying to be
23 helpful.

24 MS. McDOWELL: Thank you.

25 Q. (By Ms. McDowell) So Mr. Peterson, do you

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1 recognize this as portions of your testimony in the
2 concurrent Questar general rate case?

3 A. Yes, appears to be.

4 Q. Can you please turn to page 9 of that
5 testimony?

6 A. Yes.

7 Q. Now, in that testimony it appears that market
8 turmoil, according to your testimony, resulted in a
9 rate of 7.20 for Questar's March 2008 debt offering;
10 is that correct?

11 A. Yes. That's my understanding from Questar.

12 Q. And then on page 10, top of page 10, you
13 testified that that rate was reasonable, given -- and
14 this is lines 202 to 203 -- the current difficulties
15 in the credit market. Do you see that?

16 A. Yes.

17 Q. Now, this testimony was filed on March 31st,
18 wasn't it?

19 A. Yes.

20 Q. And on that same date you filed testimony in
21 this case, correct?

22 A. Yes.

23 Q. Now, can you turn to page 6 of your direct
24 testimony?

25 A. In this same exhibit?

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1 Q. No, that would be in Rocky Mountain's case.
2 Your direct testimony in this case, page 6, lines 132
3 to 133.

4 A. Okay.

5 Q. Now, in this case you propose lowering the
6 cost of debt to -- and this begins on line 132 -- to
7 reflect the current environment. Do you see that?

8 A. Yes.

9 Q. Now, don't you agree that the current
10 environment, informed by the recent experience that
11 Questar Gas has had in the market, suggests that
12 interest rates could actually be much higher than the
13 published average rates?

14 A. For Questar that's possibly correct, given
15 the, what I understand about the Questar case. We're
16 talking about PacifiCorp.

17 Q. Now, both Questar and PacifiCorp have the
18 same debt ratings, don't they?

19 A. Yes.

20 Q. Can you turn to your direct testimony at
21 page 4?

22 A. In, in this case?

23 Q. Yes. And I'm --

24 A. Okay.

25 Q. -- just to avoid confusion, I won't be

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1 referring again to that cross examination exhibit in
2 the Questar case.

3 A. Okay.

4 Q. So any further references to your testimony
5 are to your testimony in this case.

6 A. Okay, thank you. Page 4 you said?

7 Q. Yes, page 4. And I believe the line
8 reference is line -- well it's basically lines 1 --
9 lines 75 to 77. And there you're testifying about the
10 CAPM model, or the C-A-P-M model? How do you prefer
11 to reference this? I want to make sure I'm.

12 A. CAP-M is fine. However you want to.

13 Q. Okay, all right.

14 A. I understand C-A-P-M too.

15 Q. Now, there you note that the Commission has
16 "Expressed justified skepticism about the CAPM model."
17 Do you see that?

18 A. Yes.

19 Q. Now, notwithstanding this precedent, your
20 testimony asks the commission to consider the CAPM in
21 this case, correct?

22 A. Yes.

23 Q. But your testimony does not present evidence
24 directed at the concerns and issues the Commission has
25 previously found with the CAPM, does it?

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1 A. I believe it does, in fact, discuss those
2 various issues. At least some of them.

3 Q. Well now, in the Questar case that you cited
4 before I believe the Commission had concerns about the
5 statistical validity of the beta estimate. Do you
6 remember that?

7 A. I believe that was in the context of, of I
8 think the Questar's home witness bringing a concern
9 about statistical validity. But --

10 Q. But you haven't addressed that issue?

11 A. I haven't, I haven't addressed that -- well,
12 in a sense I have too, but I'm not sure what the
13 statistical validity problem was exactly in that
14 matter.

15 Q. Can you turn to page 20 of your testimony?
16 Again, your direct testimony.

17 A. Yes.

18 Q. Here, lines 447 through 448? So you
19 acknowledge, don't you, that the implementation of the
20 CAPM model has created controversy and consternation;
21 is that correct?

22 A. Which line are you reading from?

23 Q. Page 20, lines 447 to 448. Bottom of the
24 page. Are you with me?

25 A. Well, I don't see where "consternation" is

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1 mention there.

2 Q. "Practical implementation of the model
3 has resulted in much controversy and
4 consternation."

5 A. I guess I have a different line numbering.

6 Q. So page 20, DPU Exhibit 2.0, lines 447 to
7 448?

8 MS. SCHMID: May I approach the witness? I
9 believe that opposing counsel and I have the same
10 pages and lines. And I could give --

11 MS. McDOWELL: Yeah, let's just make sure
12 we're literally all on the same page.

13 THE WITNESS: The copy that I have is -- does
14 not refer to what you're saying on lines 447 and 448
15 on page 20. They relate to my Risk Premium Model.
16 I'm not sure why there would be a difference, but --
17 okay.

18 MS. SCHMID: Occa -- if I may note.
19 Occasionally when pages are printed from an online
20 reference, page number -- line numbers occasionally
21 change.

22 THE WITNESS: Okay. I, I see it. It's
23 actually, on the copy I had what you are referencing
24 is 422 on page 19. But in any case.

25 Q. (By Ms. McDowell) So you certainly

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1 acknowledge concerns about application of the model?

2 A. There has been much controversy, yes.

3 Q. So, now can you turn to page 31 of your
4 testimony, lines 680 through 681?

5 A. Okay, which, which line numbers?

6 Q. Basically I'm gonna ask you about your
7 results -- the testimony on your results from CAPM.
8 It's the Q beginning on 679. It goes to 687, but I
9 specifically was gonna ask you about the testimony at
10 the beginning of that, of that Q. Are you with me
11 there?

12 A. Yes, I believe so.

13 Q. Okay, great. Now, in your application of the
14 CAPM you rejected the results using T-bills because
15 they were, I think your words were "unreasonably low"?

16 A. Yes.

17 Q. Is that correct? And then going down to
18 lines 685 to 686. It appears that you also threw out
19 the lower half of your CAPM results because they were
20 outside the reasonable range; is that correct?

21 A. Yes.

22 Q. So it's fair to say that the difference
23 between you and Mr. Hadaway in this case is that you
24 threw out some of your CAPM results and Dr. Hadaway
25 just simply ceased using the model; is that correct?

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1 Dr. Hadaway's Exhibit 1, his Updated Table 1? It's
2 actually RMP Exhibit 1(RoR.) It's the Updated
3 Table 1.

4 A. I don't believe I have -- the one that was
5 handed out today?

6 Q. That's correct.

7 A. I don't have a copy of that.

8 Q. Well, we'll get you a copy. Now, I think you
9 had just identified the date of the Commission order
10 approving the '06 stipulation as December '06; is that
11 correct?

12 A. Yes.

13 Q. Can you tell me, what was the Single-A
14 corporate rate in December '06, according to Table 1?

15 A. Five point eight one percent.

16 Q. Now, looking down to the bottom of the table,
17 the current rate for April '08 is 6.29 percent,
18 correct?

19 A. That's what it shows, yes.

20 Q. So the current rate is approximately 48 basis
21 points higher than the rate at the time of the
22 approval of the stipulation in the 2006 case; is that
23 correct?

24 A. As of April average, yes.

25 Q. Now, the stipulation in that case approved a

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1 10.25 percent ROE, correct?

2 A. Yes.

3 Q. Now, if you subtract 10.25 -- or excuse me.
4 If you subtract the 5.81 interest rate you identified
5 from the 10.25 ROE you just discussed, that would
6 produce a 4.4 percent difference, wouldn't it?

7 A. Approximately.

8 MR. PROCTOR: Excuse me Mr. Chairman, I --
9 this is not my witness and so I'm very uncomfortable
10 objecting. But I think in the interest of my own
11 client, who was a party to the stipulation, I think I
12 have to.

13 I don't believe that I'm misspeaking when I
14 say that referencing that it was a settlement and the
15 outcome is one thing. But I believe there are bars in
16 the stipulation to citing to the foundations -- the
17 information upon which a settlement was based in a
18 subsequent proceeding as substantive evidence on the
19 merits of a party's position taken later.

20 Such a thing would also be contrary to this
21 Commission's own authority, as determined by the
22 Supreme Court of Utah, with respect to the extent to
23 which one rate case is res judicata, or collaterally
24 estops in evidence is a subsequent one.

25 Again, this is not my witness. And if I'm

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1 out of place, please tell me, and I will withdraw this
2 objection. But I believe we're getting into an
3 objectionable area with this line of questions.

4 COMMISSIONER BOYER: Ms. McDowell?

5 MS. McDOWELL: Well, I -- that was the last
6 question I was gonna ask specifically about the
7 stipulation, so. And I was not going to ask any
8 questions about the foundation for the stipulation or
9 Mr. Peterson's opinion about the stipulation. I was
10 simply asking about the interest rates at the time of
11 the stipulation.

12 COMMISSIONER BOYER: All right. Well, I
13 think Mr. Proctor is right as to the specific terms or
14 the negotiation of the terms of the settlement. But
15 at this point your question relates to a portion of
16 the order which does reflect a 10.25 percent return on
17 equity, so we'll let Mr. Peterson answer that
18 question.

19 MS. McDOWELL: I was actually careful to only
20 use the face page, because I didn't want to violate
21 anybody's sensibilities around the settlement. Thank
22 you.

23 Q. (By Ms. McDowell) So can you turn to
24 Dr. Hadaway's Exhibit 8-R, please? This is his -- the
25 last exhibit in his rebuttal testimony.

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1 A. Yes.

2 Q. So this is Dr. Hadaway's risk premium
3 analysis, correct?

4 A. Yes.

5 Q. Now, what risk premium does Dr. Hadaway
6 identify on Exhibit 8-R?

7 A. It appears he identifies 4.37 percent.

8 Q. So that number is close to the 4.4 percent
9 number we just identified with respect to the 2006
10 stipulation, correct?

11 A. Yes.

12 Q. Now, Dr. Hadaway produces a number of 10.73
13 in his risk premium analysis. Do you see that?

14 A. Yes.

15 Q. Now, would you accept, subject to check, that
16 if you add the 4.4 percent number we just identified
17 to the current 6.29 percent rate in Table 1, it would
18 produce the same number, 10.73 percent?

19 A. Well, it would produce 10.69 percent, I
20 think.

21 Q. Close?

22 A. All right.

23 Q. Can you turn to your direct at page 14,
24 please?

25 A. I believe I have it.

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1 Q. Now, there you, on lines 310 through 313 in
2 the question, make a reference to the 2002 Questar Gas
3 case. Do you see that?

4 A. Yes.

5 Q. Now it's true, isn't it, that that case
6 accepted a weighted average of earnings and dividends
7 for purposes of setting the bottom of the range; isn't
8 that correct?

9 A. I don't recall that.

10 Q. And it also accepted a 100 percent earnings
11 growth as the other end of the range, the high end of
12 the range. Are you familiar with that part of the
13 order?

14 A. I don't specifically recall that, no.

15 Q. Now, I'd like to turn to your exhibits on
16 your Discounted Cash Flow analysis. And that
17 includes, I think, your corrected Exhibit 2.7. I
18 believe those exhibits, your summary exhibit is
19 DPU 2.5?

20 A. Yes. Did you want to look at 2.5?

21 Q. I do. I just need to get it and --

22 A. Okay.

23 Q. -- keep my papers organized. So just for a
24 point of clarification, these -- the summary of model
25 results includes ten-year historical growth rates. Do

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1 you see that?

2 A. Yes.

3 Q. Now, in your testimony you stated that they
4 do not warrant consideration in the final estimate of
5 cost of equity; is that correct?

6 A. That's correct.

7 Q. So we just want to focus on the top two lines
8 of your summary, correct? Not the, the third line
9 under each column, correct?

10 A. Yes.

11 Q. Now, if, if the weighted average were to set
12 the bottom of the range and the EPS growth rate were
13 to set the top of the range, it would produce a range
14 from 10.03 to 10.69; is that correct?

15 A. Yes, looking at the individual calculations.

16 Q. And that produces a midpoint approximately of
17 10.36; does that sound right?

18 A. Approximately.

19 Q. Now, you use two different estimates, one
20 based on spot prices and one based on one month
21 prices; is that correct?

22 A. Yes.

23 Q. And your spot prices were derived from
24 Exhibit 2.7(a); is that right?

25 A. Yes.

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1 Q. That's the exhibit you corrected today?

2 A. Yes.

3 Q. Now, the exhibit that we have has all zeroes
4 in the EPS growth column. And that's the change
5 you've corrected; is that right?

6 A. Well, yes.

7 Q. Did -- I just want to verify. Did that
8 correction change any of the other data points on this
9 exhibit?

10 A. I don't believe it should have. I believe I
11 tried to check those before, but I don't believe
12 there's any further changes.

13 Q. Well, I guess it does -- you know, just
14 looking at it and doing this on the fly -- it does
15 change all of the results, because if you have a zero
16 column for earnings the input of zero is going to skew
17 the results, correct?

18 A. On, on that schedule. If you look back on
19 Exhibit 2.5, the correct numbers were there.

20 Q. So those correct numbers, just so the record
21 is clear, in your corrected 2.7(a) your range is
22 10.69 -- 10.13 to 10.169; is that correct?

23 A. Well, excluding the dividend only, that would
24 be correct.

25 Q. Well, the Commission has never acknowledged

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1 just a dividend only result, have they?

2 A. Not to my knowledge.

3 Q. Okay. So then can you turn to your next
4 page, which is where you derive your one month prices?

5 A. Okay.

6 Q. So that's Exhibit 7 -- DPU Exhibit 2.7(b); is
7 that -- does that sound right?

8 A. Yes.

9 Q. Okay. I'm gonna hand you one more cross
10 examination exhibit. And in your --

11 MS. McDOWELL: Commissioner Boyer, while
12 Mr. Moench is distributing those is it good practice
13 to accept all the -- to offer the cross exhibits at
14 the end of the cross examination, or shall I offer
15 them as I go?

16 COMMISSIONER BOYER: It's really your
17 preference.

18 MS. McDOWELL: Okay.

19 COMMISSIONER BOYER: I was going to remind
20 you at the end of your cross examination if you
21 haven't done so.

22 MS. McDOWELL: All right. Well, I have at
23 this point I think we're on Cross Examination
24 Exhibit RMP-3.

25 Q. (By Ms. McDowell) So Mr. Peterson, I've

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1 handed you an exhibit which works off of your
2 Exhibit 2.7(b.) And before we go through that I just
3 want to talk with you a little bit about what
4 Exhibit 7. -- 2.7(b) purports to show.

5 So you use, it's basically a similar
6 spreadsheet to your 2.7(a), but instead of using spot
7 prices this has monthly prices; is that correct?

8 A. Yes.

9 Q. Now, it appears from your testimony that
10 you're -- you emphasize your weighted results more
11 than your earnings only results. Is that a fair
12 summary?

13 A. I considered both of them in the, in the
14 final analysis. So I, I would say that I considered
15 both of them.

16 Q. Okay. So the weighted growth numbers are
17 from the third column from the right on
18 Exhibit 2.7(b); is that correct?

19 A. Yes.

20 Q. And can you tell me what the calculation is
21 that you used to derive the estimated weighted growth
22 numbers, EPS growth numbers, and dividend growth
23 numbers? I guess first of all, was it the same
24 calculation for all three?

25 A. It should be, yes, the same formula. Do you

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1 want me to go ahead and explain now, or?

2 Q. Please.

3 A. On the estimated cost of equity using
4 weighted growth, first of all the weighted growth
5 figure was calculated, which is the next column to the
6 left, which says 75.25 weighted growth. I took
7 25 percent of the 3 to 5 year EPS growth rate, and
8 25 percent of the projected 3 to 5 year dividend
9 growth rate, to arrive in the -- for Alliant Energy,
10 for example, of 6.12 percent.

11 The current dividend yield was increased by
12 that growth rate to get an adjusted dividend yield
13 figure, which is not shown explicitly here. And then
14 that would -- and then to that was added the
15 6.12 percent.

16 Q. So now, you do a, a basic calculation of
17 dividend and growth rates to get your final numbers;
18 is that correct?

19 A. Yes.

20 Q. So you would basically multiply your dividend
21 yield times one plus your projected growth rate plus
22 your growth rate. Is that a fair calculation?

23 A. Actually, I'm -- I'm thinking that I probably
24 actually used the, just the dividend growth of
25 5. -- in the -- for Alliant Energy it would be 3.96

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1 percent increase by 5.5 percent. And that would be
2 the adjusted dividend. And then I added to that the
3 weighted average growth.

4 Q. So are you saying you did a different
5 calculation for your weighted growth estimates than
6 for your EPS growth estimates?

7 A. I believe that's -- subject to
8 double-checking, I believe that's the case.

9 Q. And would you accept that, subject to check,
10 that if you use that cal -- that same calculation that
11 you used for calculating your EPS growth and dividend
12 growth columns with your weighted growth columns, your
13 weighted growth numbers are understated?

14 A. Would you rephrase -- repeat that, please? I
15 couldn't quite follow you.

16 Q. Well, let's start with the assumption that
17 you're using the same calculation for all three
18 results. For all three estimates.

19 A. Okay.

20 Q. The same DCF calculation. And would you
21 accept, subject to check, that if you apply that same
22 calculation that you used for EPS growth and dividend
23 growth to your weighted growth, that the numbers you
24 have on Exhibit 2.7 are all incorrect?

25 A. Well, that presumes that the same -- that the

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1 EPS growth and dividend growth columns are correct,
2 so.

3 Q. It's your exhibit.

4 MS. SCHMID: Objection to the form of the
5 question. It seems quite circular.

6 THE WITNESS: Um, well, if there's a
7 calculation error somewhere in it that I haven't been
8 able to discuss, then certainly something is mistaken.

9 Q. (By Ms. McDowell) Well, just assume, subject
10 to check, that that's the result. I've handed you
11 what's been marked as RMP Exhibit 3. Do you see that?

12 A. Yes.

13 Q. And there the column we've been discussing is
14 boxed in and demonstrates the application of your
15 formula in a consistent manner to all three columns.
16 Do you see that?

17 A. Well, I'll accept your representation that
18 it's consistent, but --

19 Q. Subject to check?

20 A. Subject to check. But I see what you're
21 talking about.

22 Q. And the effect of applying that consistent
23 calculation throughout would be to raise the weighted
24 growth average from 10.03 to 10.10. Do you see that?

25 A. Yes.

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1 Q. So then going back to your summary page.
2 Basically that would revise the range we previously
3 talked about from 10.03 to 10.69 to now 10.10 to
4 10.69; is that correct?

5 A. Assuming everything else is correct, then
6 that would be -- would flow through, yes.

7 Q. And that, in turn, would produce a revised
8 midpoint of approximately 10.40. Does that sound
9 correct?

10 A. Ten point four oh relative to what? I'm
11 sorry.

12 Q. Between the bottom of the range,
13 10.10 percent, and the top of the range,
14 10.69 percent.

15 A. Yes, approximately 10.4.

16 MS. McDOWELL: That's all I have, thank you.
17 And before I stop I'd like to offer the Cross Exhibits
18 1 through -- RMP 1 through 3.

19 COMMISSIONER BOYER: Any objection to the
20 admission of the Cross Examination Exhibits 1 through
21 3?

22 MS. SCHMID: None.

23 MR. PROCTOR: None.

24 COMMISSIONER BOYER: Seeing none, they are
25 admitted into evidence. Thank you. Let's move now to

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1 Mr. Proctor.

2 MR. PROCTOR: Thank you Mr. Chairman.

3 CROSS EXAMINATION

4 BY MR. PROCTOR:

5 Q. Mr. Peterson, would you turn to page 15 of
6 your surrebuttal, please.

7 A. Page 15?

8 Q. Page 15, yes. Do you have it?

9 A. I believe so, yes.

10 Q. Line 280 -- actually 279, at the end of the
11 line, begins the sentence:

12 "Dr. Hadaway, by contrast, uses a
13 forecast long-term government rate of 5
14 percent."

15 Do you see that?

16 A. Yes.

17 Q. Do you know whether or not Dr. Hadaway was
18 using an estimated 2008 or an estimated 2009 long-term
19 government interest rate?

20 A. Well, without looking at, I -- looking at it,
21 I'm not sure.

22 Q. Would the place that you would look be
23 Dr. Hadaway's Exhibit 2-R? Do you have that?

24 A. I have 2-R. That's where he gets his
25 estimate from, yes.

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1 Q. Now, on the left-hand column it has an E 2008
2 for 30 year bonds. That's in the lower part of the
3 page. Do you see that?

4 A. Yes.

5 Q. And what is that estimate for 30 year bond
6 rates for 2008?

7 A. Four point three.

8 Q. And to the right of that is the estimate for
9 2009; is that correct?

10 A. Yes.

11 Q. And that is 5.0?

12 A. Yes.

13 Q. So from that would you conclude that
14 Dr. Hadaway was using a 2009 estimate when he
15 calculated the borrowing cost of 6.36 percent?

16 A. Yes.

17 Q. Now, if you were to apply the same 1. -- or
18 136 basis points addition to the estimated 2008
19 number, what then would be the interest rate?

20 A. It would be approximately 6.66.

21 Q. Six six?

22 A. Or 5.66 rather, sorry.

23 Q. Okay. Now, as you went on in that top
24 paragraph on page 15 you discussed the fact that
25 interest yields -- or excuse me, that corporate

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1 interest rate spreads were converging. Do you see
2 that?

3 A. Yes.

4 Q. And at the very beginning of your testimony
5 in your summary you did mention that in your judgment
6 Dr. Hadaway had acknowledged that spreads were
7 narrowing. And you subsequently withdrew that
8 reference to Dr. Hadaway.

9 But is this the particular part where you
10 drew your conclusion that indeed, under the
11 circumstances, that spread was in fact narrowing?

12 A. Well, that -- the difference between
13 forecasted -- the actual reference is the current and
14 forecasted Single-A utility interest rates are
15 converging.

16 Q. In the last sentence beginning on page 289
17 you make a statement with respect to rate spreads and
18 a correction to them; do you see that?

19 A. Yes.

20 Q. Is that the basis for your reference that,
21 indeed, the rate spreads would be narrowing?

22 MS. McDOWELL: I'm gonna object to this line
23 of questioning. It doesn't sound like cross
24 examination to me. It sounds like friendly cross.
25 And I heard your directions at the beginning of this

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1 hearing, which were that you wanted to see cross
2 examination conducted as cross examination.

3 MR. PROCTOR: I being my best to be
4 unfriendly.

5 COMMISSIONER BOYER: Well, I believe it's in
6 the context of Mr. Peterson's testimony regarding
7 Mr. Lawton's testimony, so I'd like to hear it.

8 Q. (By Mr. Proctor) Is, is those -- are those
9 calculations from the basis upon your conclusion -- or
10 for your conclusion that rate spreads are narrowing?

11 A. Well, the -- yes. That we have a very high
12 rate spread right at the moment, as highlighted by
13 Dr. Hadaway. I do not necessarily believe that that
14 rate spread is going to persist. We have several
15 months for things to change before the company
16 contemplates issuing debt.

17 Q. And that would be the latter part of this
18 year?

19 A. Yes.

20 Q. On that same Exhibit 2-R from Dr. Hadaway, on
21 the -- on that exhibit there is a fourth quarter
22 estimate for 2008 long-term corporate -- or excuse me,
23 long-term Treasury bonds?

24 A. One moment, I've lost my place. Okay. Where
25 are you looking, sir?

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1 Q. Again, it's Hadaway Exhibit 2-R.

2 A. Yes.

3 Q. And on the right-hand side there's a
4 per-quarter estimate 2008, 30 year bond rate?

5 A. Yes.

6 Q. So what is the estimate from Dr. Hadaway's
7 exhibit for the fourth quarter of 2008?

8 A. Four point four percent.

9 Q. Thank you, Mr. Peterson. Thank you.

10 MR. PROCTOR: I have no further questions.

11 COMMISSIONER BOYER: Thank you, Mr. Proctor.

12 Mr. Dodge?

13 MR. DODGE: No questions, thank you.

14 COMMISSIONER BOYER: Mr. Ball, have you
15 questions of Mr. Peterson?

16 MR. BALL: Yes. Just a little bit, please,
17 Chairman.

18 CROSS EXAMINATION

19 BY MR. BALL:

20 Q. Morning Mr. Peterson.

21 A. Hello.

22 Q. I'd like to refer you back to Rocky Mountain
23 Power's Cross Exhibit 2 Rate of Return, the cover
24 sheet from The Commission's Report and Order in Docket
25 06-035-21 issued on December 1, 2006. Do you have

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1 that in front of you?

2 A. Yes.

3 Q. Do you happen to recall, Mr. Peterson, when
4 the stipulation referred to in the synopsis of the
5 order was filed and when PacifiCorp petitioned the
6 Commission to approve it?

7 A. Offhand, I don't remember the specific date.

8 Q. Subject to your check would you accept that
9 it was filed and the motion filed on the 26th of July,
10 2006?

11 A. That would sound consistent with when we were
12 having settlement discussions, so that isn't --
13 wouldn't surprise me.

14 Q. Referring now to PacifiCorp's exhibit -- or
15 rather Rocky Mountain Power's Exhibit 1 Rate of
16 Return, the Updated Table 1, Long-Term Interest Rate
17 Trends?

18 A. I have it.

19 Q. Looking at the December '06 line, the
20 5.81 percent in the Single-A utility rates. On the
21 26th of July, 2006, would anybody have known about
22 that 5.81 percent?

23 A. No.

24 Q. What do you -- what rate do you suppose they
25 would have had as the most recent available rate when

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1 that stipulation was being drafted, just before it was
2 filed?

3 A. The June or July rates.

4 Q. So 6.42 or 6.4?

5 A. Yes.

6 Q. So running through the same calculation that
7 Ms. McDowell took you through. If you take 6.4 away
8 from 10.25 would you agree, subject to check, that the
9 answer is 3.85?

10 A. Sounds approximately correct.

11 Q. If you then add 3.85 to the 6.29 percent for
12 April '08 would you agree, again subject to check,
13 that the answer is 10.14?

14 A. Again, that sounds approximately correct.

15 MR. BALL: Thank you very much, Mr. Peterson.

16 Thank you, Chairman. I'm done.

17 COMMISSIONER BOYER: Ms. Schmid?

18 MS. SCHMID: Yes.

19 COMMISSIONER BOYER: Let's see if the
20 Commissioners have questions of Mr. Peterson and then
21 we'll let do you your redirect. Commissioner Allen?

22 COMMISSIONER ALLEN: Thank you, Mr. Chair. I
23 just have a couple of questions following on the
24 length, excuse me, backing up and looking at the
25 inputs on our assumptions. As we do the analysis I'm

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1 curious, on your list of comparable companies for your
2 cash flow models, did you just use strictly financial
3 information?

4 Did you try to come up with a list that was
5 more specifically applicable to our company in other
6 areas? How did you, how did you develop your comps?

7 THE WITNESS: Well, in general I started off
8 similarly to Dr. Hadaway. And we do have overlap, to
9 some extent, between our comparables. However, as I
10 was looking at it I discovered that there were items
11 that caused me concern that are of a non-financial
12 nature.

13 For example PPL, that we previously were
14 discussing, has a substantial investment in utilities
15 in the United Kingdom, which are subject to different
16 forms of regulation or -- than we have in this -- than
17 is typical in this country, from what I understand.

18 And I thought that was a significant
19 difference from what PacifiCorp, as it exists today,
20 is like. It does not hold foreign assets to a -- to
21 any noticeable degree. I also compared -- or one of
22 the things I was interested in was whether the
23 company, the proxy company had thermal generation.
24 Had its own generation. Which PacifiCorp has
25 substantial amounts of.

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1 And I discovered that several of
2 Dr. Hadaway's companies are strictly distribution
3 companies. They do not have their own generation but
4 purchase most, if not all of it. And so I eliminated
5 those on the basis of lack of similarity to PacifiCorp
6 in terms of generation.

7 And if you were to look at my Exhibit 2.4 you
8 will see some notes on those companies that
9 Dr. Hadaway used that I elected not to use. So
10 those -- I don't know. Does that give you some answer
11 to your question, or?

12 COMMISSIONER ALLEN: That helps, I guess. If
13 I were to just add to that I would just ask how you --
14 if you feel comfortable that your, your inputs reflect
15 fully-integrated fully-regulated company in terms
16 of -- like you mentioned one of the possible outliers
17 there.

18 But are you comfortable with the model in
19 terms of how it reflects, and did you, did you
20 consider that? When you were creating these inputs
21 did you consider the differences in our -- the company
22 before us versus those on the sheet? That's what I'm
23 really interested in.

24 THE WITNESS: Well that, of course, is the
25 goal. You're trying to find comparable companies or

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1 proxy companies that are as close to the subject
2 company as you reasonably can find. And I think an
3 additional item that differs somewhat between me and
4 Dr. Hadaway is Dr. Hadaway apparently only looked at
5 electric utility revenues.

6 I also looked at the relative earnings of the
7 electric utilities to the holding -- the parent
8 holding company. And again referencing PPL
9 Corporation as an example, only 16 percent of the
10 income to the parent corporation comes from domestic
11 electric utilities.

12 So I was looking for the companies that, at
13 least to the extent possible, maximized both revenues
14 and income to the parent companies. It's the nature
15 of things right now that there are relatively few pure
16 electric companies that are publicly traded. So you
17 do the best you can.

18 And Dr. Hadaway had different criterias than
19 I did, apparently, which gave different results. And
20 I've compared the companies that I included with the
21 ones I -- that Dr. Hadaway had that I did not include,
22 again on page 2.4.

23 Both of us used bond ratings as a, as an
24 initial screening, I guess you could say. We wanted
25 to have bond ratings that were at least close to

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1 PacifiCorp's A-minus rating. I also had a size
2 factor. I didn't want companies to be a whole lot
3 larger than PacifiCorp, or very tiny.

4 Again, thinking that there's, there's going
5 to be a size issue at some point of companies too
6 small to be comparable. And specifically I used the
7 plus or minus 5 times revenues or 5 times net plan as
8 a size factor.

9 COMMISSIONER ALLEN: Great, thank you.

10 COMMISSIONER BOYER: Commissioner Campbell,
11 please.

12 COMMISSIONER CAMPBELL: Mr. Peterson, if you
13 would turn to Exhibit 2.3 of your direct testimony?
14 I'm just gonna ask you a question or two about capital
15 structure.

16 THE WITNESS: Okay.

17 COMMISSIONER CAMPBELL: You made the
18 statement that you have no problem with the capital
19 structure proposed by the company. Could you
20 elaborate on that, please? Based on what, what your
21 comparable group of companies shows.

22 THE WITNESS: Yes. The comparable group of
23 companies taken as a whole have an equity capital
24 structure on average two or three percentage points
25 below PacifiCorp's. There are also companies that

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1 have similar equity capital structures.

2 In particular I considered that DPL Energy
3 and American Electric Power. Although they, they had
4 comparable bond ratings, they had noticeably lower
5 equity capital structure than the other companies. So
6 when I took those out, then there was a capital
7 structure from 2007 that I considered to be fairly
8 similar, as an average of the others, to the
9 50.8 percent that PacifiCorp is -- currently has.

10 The other aspect of this is that the capital
11 structure at PacifiCorp, while it's fluctuated around
12 from year to year, even from quarter to quarter, it
13 has held fairly constant in the approximate 50 to
14 51 percent range. Which is what we were looking at in
15 previous rate -- what we, meaning the Division, was
16 looking at in previous rate cases and also during the
17 acquisition.

18 As I concluded in my testimony, I believe,
19 the slightly higher than average capital structure, in
20 my view, is justified in the -- because -- in part
21 because PacifiCorp is engaged in a fairly large
22 capital expenditure program. And the capital
23 structure here will help support its bond rating and
24 its financing.

25 So those were the thoughts that I had in

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1 evaluating capital structure.

2 COMMISSIONER CAMPBELL: And have you -- or
3 has the Division changed at all its policy as it
4 relates to actual versus hypothetical capital
5 structures?

6 THE WITNESS: I know that in past matters the
7 Division I think has advocated a hypothetical. But
8 I'm not sure of the details there.

9 COMMISSIONER CAMPBELL: Final question, and
10 it has to do with the comparison of the debt, the debt
11 that -- interest rate that Questar issued debt at
12 versus in this hearing. Are there other factors
13 besides debt ratings that affect the interest rates
14 that the companies get when they issue debt?

15 THE WITNESS: Yes. The -- referencing the
16 Questar debt issuance, they issued it in two parts.
17 One of it was actual -- one part actually was below
18 their forecasted amount that they originally filed.
19 Their forecasted cost of debt when they initially
20 filed their direct testimony.

21 The other part was the 7.2 percent figure,
22 which apparently -- well, it surprised me and it also
23 apparently surprised Questar, in a conversation I had
24 with them. Part of the problem appears to be that, in
25 the markets at the time, the size of the debt issue

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1 was a problem.

2 It was too small to find buyers for a
3 relatively small issuance. And that apparently
4 contributed to the higher than expected debt rate. So
5 as I indicated, or started to indicate in my testimony
6 being crossed by Mrs. -- Ms. McDowell, PacifiCorp
7 should not be faced with that circumstance with their
8 debt offering that's coming up. Even assuming the
9 market conditions are exactly the same as they were
10 when Questar issued its debt.

11 So that's why I believe that it's an apples
12 and orange comparison.

13 COMMISSIONER CAMPBELL: Thank you.

14 COMMISSIONER BOYER: I also have a couple of
15 questions, Mr. Peterson, on the, the capital
16 structure. And I appreciate your clarification here
17 in response to Commissioner Campbell.

18 At what level would red flags be raised if,
19 for example, equity to cap -- equity to debt increased
20 to 52, or 55, or 60, or 80? Any rules of thumb, or
21 how would you determine whether or not that was
22 problematic.

23 THE WITNESS: I think that if, if the -- it
24 would start to become clearly problematic if the
25 rate -- the equity percentage started to be at or even

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1 above the high end of the range of the comparable
2 companies.

3 On my schedule 2.3 that you have a high of
4 Alliant Energy of around 65 percent, I think that
5 would be a red flag if they came in there. You have a
6 couple of others that are in the 50 to 54 percent
7 range, which is where PacifiCorp sits. Actually
8 closer to the 50 percent, 51.

9 Then you have a couple that are -- well, at
10 least one that's just slightly under 50 percent. So
11 PacifiCorp is clearly in the upper half of, of these
12 comparable companies. But at this point they're not
13 really far out in that sense. If that makes any
14 sense.

15 COMMISSIONER BOYER: Yes, thank you. Does
16 capital structure, in your opinion, have anything to
17 do with allocating or balancing costs for risk sharing
18 between customers and shareholders?

19 THE WITNESS: It can. Again, it, it's I
20 suppose a policy decision as much as anything else.
21 But clearly a -- the higher the equity capital
22 structure, the, the higher the overall cost of capital
23 would be. Which would increase rates to ratepayers.

24 And the opposite would be true if you had a
25 low capital equity capital structure, then

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1 theoretically at least you have lower cost of capital.
2 But there of course would be offsetting considerations
3 in both instances.

4 COMMISSIONER BOYER: Moving now to selection
5 of comparables. You heard my question to Dr. Hadaway
6 about what variables -- he called them screens -- but
7 what variables he used in selecting comparable
8 companies. You've given us some testimony on that as
9 well.

10 Would it be useful at all to evaluate other
11 kinds of variables? For example, the regulatory
12 environment in which those companies operate. For
13 example, do they -- do those compan -- do those
14 regulatory environments permit weather normalization?

15 Or other kinds of things, like weather
16 patterns, or age of facilities, age of generation, age
17 of transmission, whether or not there's a fuel pass
18 through, those kinds of things. Would that be useful
19 in selecting comparables?

20 THE WITNESS: Well, it could be useful.
21 The -- to look at other things. Whether they're
22 deregulated or, or not would be a useful criteria.

23 The problem is, you start -- if you start to
24 become too restrictive on what you're going to accept,
25 then quickly you run the risk of only ending up with a

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1 very few comparable companies. Or maybe even none at
2 all if you make it too stringent as to what sort of
3 hurdle a company has to cross in order to become a
4 proxy company.

5 And usually I consider having eight or ten
6 proxy companies as kind of a minimum number, so.

7 COMMISSIONER BOYER: Assuming that you have a
8 cross-section of --

9 THE WITNESS: Assuming you have --

10 COMMISSIONER BOYER: -- different kinds of
11 variables.

12 THE WITNESS: Right.

13 COMMISSIONER BOYER: If you have a large
14 enough sample.

15 THE WITNESS: I think the sam -- you're
16 right. You could look -- ideally you would have a
17 collection of companies that were identical to
18 PacifiCorp, if such a thing were possible. But since
19 that isn't possible, you have to make some selection.

20 COMMISSIONER BOYER: It doesn't appear, at
21 least from my reading of the prefiled written
22 testimony, that anyone did that sort of analysis.
23 Maybe they did it offline or something, but it wasn't
24 expressed in the testimony in this case.

25 THE WITNESS: In my instance I do remember

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1 looking at issues of whether a company was in a
2 deregulated state or not. But that was the only other
3 issue that I -- or the only other criterion that I
4 looked at as a possible screen.

5 But as you can see from Exhibit 2.4, I
6 haven't detailed that out. So in the end I did not
7 elect to use it as a significant screening tool.

8 COMMISSIONER BOYER: Thank you, Mr. Peterson.
9 Regarding rate spread, you've heard Dr. Hadaway
10 testify that the spread seems to be increasing. And
11 he's provided some exhibits that seem to demonstrate
12 that.

13 You've testified that you think that that
14 increase is gonna diminish, or that the spread is
15 going to narrow. What are the variables causing this?
16 Is it the Fed tinkering with interest rates that
17 control inflation? What do you think?

18 THE WITNESS: Well, there's a lot of things.
19 First of all, the Federal Reserve actions are only
20 directly effective on short-term interest rates. And
21 what we're really looking at, in my opinion should be
22 looking at, are the longer-term interest rates. The
23 20, 30 year Treasury bonds and similarly-maturing
24 corporate bonds.

25 Those are certainly less directly affected by

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1 and influenced by Federal Reserve tinkering, although
2 I wouldn't say that they have -- that there's no
3 influence on them. Now they're -- the problems that
4 affect longer-term rates are perceptions of long-term
5 inflation and credit quality would be the primary
6 things that would drive those.

7 And we have been in an environment lately
8 where there are concerns of higher inflation, although
9 they haven't specifically manifest themselves in the
10 broad index. So, at least not to an extreme degree.

11 COMMISSIONER BOYER: Okay. Thank you,
12 Mr. Peterson.

13 Ms. Schmid, have you any further questions of
14 Mr. Peterson?

15 MS. SCHMID: Very limited.

16 COMMISSIONER BOYER: Okay.

17 REDIRECT EXAMINATION

18 BY MS. SCHMID:

19 Q. Mr. Peterson, Rocky Mountain Power asked you
20 questions about CAPM. Was CAPM the only mechanism
21 that you presented to the Commission for its
22 consideration in your evidence concerning ROE?

23 A. No.

24 Q. Did you offer any sort of qualification or
25 caveat on CAPM to the Commission in your testimony?

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1 A. I presented I think a fairly lengthy
2 discussion of issues surrounding the Capital Asset
3 Pricing Model for the Commission's consideration.
4 There are a lot of -- there are a number of issues. I
5 think they can be reasonably resolved. Which I've
6 attempted to point directions where those could be
7 resolved.

8 My primary concern about using the CAPM is
9 that analysts or rate of return experts should use the
10 commonly used models. And CAPM is certainly a
11 commonly used model. The Commission needs to
12 understand that there are difficulties with it.

13 There's also difficulties with the DCF model
14 that can be raised. Dr. Hadaway, for example,
15 complains that -- or has complained that analysts
16 forecasts fluctuate around. Which is true. And there
17 is, in fact, no one universally accepted long-term
18 growth rate that someone can come up with for a DCF
19 model, just as an example.

20 These are all tools that we all have to
21 judiciously look at and apply. So I just offer that
22 the Commission should at least consider a judicious
23 application of CAPM as one of the tools the analysts
24 use.

25 MS. SCHMID: Thank you.

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1 COMMISSIONER BOYER: Thank you, Mr. Peterson.

2 You may step down.

3 Mr. Proctor, do you think there would be any
4 possibility of getting Mr. Lawton's summary in before
5 we break for lunch?

6 MR. PROCTOR: Absolutely.

7 COMMISSIONER BOYER: Okay, let's hear it.

8 THE WITNESS: I've already been sworn,
9 Mr. Chairman. May I take the seat?

10 COMMISSIONER BOYER: Thank you, Mr. Lawton,
11 please be seated.

12 THE WITNESS: Thank you.

13 DANIEL J. LAWTON,

14 called as a witness, having been duly sworn,
15 was examined and testified as follows:

16 FURTHER DIRECT EXAMINATION

17 BY MR. PROCTOR:

18 Q. For the record, sir, could you state your
19 name and business address and on whose behalf you are
20 appearing here today?

21 A. Yes, sir. My name is Daniel J. Lawton.
22 D-a-n-i-e-l, middle initial J., L-a-w-t-o-n. My
23 business address is 816 Congress Avenue, Suite 1120,
24 Austin, Texas. And I'm appearing today on behalf of
25 the CCS, or Committee.

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1 Q. Mr. Lawton, what is your profession?

2 A. I am an economist. And I've been providing
3 cost of capital in all sorts of regulatory consulting
4 since the early 1980s. I'm also an attorney. And I
5 advise and represent municipalities throughout Texas
6 in regulatory proceedings such as this as their
7 counsel.

8 Q. Mr. Lawton, your testimony, direct and
9 surrebuttal, has already been admitted. Do you have a
10 summary of your testimony in this matter?

11 A. Yes, I do. And, and in keeping with the
12 Chairman's admonition, I will be short. And the lunch
13 hour coming about as well. Certainly you
14 Commissioners have been asking questions and have read
15 all the testimony. That's clear, clear from your
16 questions.

17 And I'm not gonna go through the details.
18 I've laid it out in the testimony. And I invite you
19 to ask me questions about my testimony when that time
20 comes. But I provided you an analysis. And I've
21 tried to provide you a backup document for all my
22 analyses and numbers.

23 It's not just Mr. Lawton coming in saying,
24 Here's the number, or here's the way to go. I tried
25 to provide you a source reference. But basically the

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1 case right now has been down to three issues presented
2 to the Commission:

3 What's the overall rate of return we have to
4 grant this company, or should grant this company, for
5 its invested capital? And you're gonna decide
6 invested capital, I understand, later in these
7 proceedings.

8 And the Company's requested 8.54. I've
9 recommended 8.07 percent. And I think Mr. Peterson's
10 recommended a slightly different number than mine, but
11 they're relatively close.

12 Another issue is, what is the cost of debt
13 associated with the debt issue the company has to
14 issue or projects to issue in December of 2008? As we
15 all know, they've been building plant. They're gonna
16 issue a debt issue, a pro forma issue, for the end of
17 the projected test year that this Commission recently
18 decided.

19 The Company -- Mr. Williams was here on the
20 stand for us this morning -- recommended 6.52 percent.
21 I'm recommending that the cost of that debt ought to
22 be around 6.07 percent.

23 The third and final issue that, that you're
24 facing is what cost of equity should you include in
25 the overall cost of capital. The Company's at 10.75.

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1 My testimony recommends 9.85 percent. Now, I think
2 you can look at these issues and, and decide them.
3 And my testimony tries to address that, both in direct
4 and surrebuttal.

5 There's not much difference between the
6 approach that Dr. Hadaway took in this case and the
7 approach I took. We use the same models all the time.
8 And what I did is I updated Dr. Hadaway's models. His
9 data was outdated, that's clear. I think he's
10 admitted that on the stand, in terms of he had to
11 update interest rates because of the interest rate
12 changes and so forth.

13 But Dr. Hadaway also uses forecasted data.
14 Forecasted data well beyond the end of the test year.
15 And I invite you to, in your deliberations, to examine
16 Dr. Hadaway's forecast sheet. And I talk about it.
17 And I think it's at his -- his exhibit is Rebuttal
18 Exhibit SCH-2-R. It's a one-page sheet.

19 And I talk quite a bit about it in those
20 forecasts in my testimony, and I won't elaborate on
21 that again here. But I would point out, this
22 Commission has given all the analysts in this case
23 some guidance.

24 That guidance from your test year decision
25 where you, in fact, stated that the -- it may be

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1 because of the economic problems and turmoil -- I
2 think it was caused -- talked about this morning --
3 that more frequent rate cases may be necessary.

4 And you shortened the test year and didn't go
5 out to the '09 period. Well, the company has heeded
6 that, that statement. And it's my understanding
7 they've announced they're gonna file another case here
8 shortly.

9 Well, that tells me that we should stay in
10 the '08 time period, not stray too far beyond that.
11 And that's what I've done in my testimony. It also
12 tells me that if you're going to err -- and there's,
13 you know, different opinions. You see it all the
14 time.

15 Err on the side of the consumer in this case,
16 for the following reason: Any error that is
17 corrected, if there is one -- an underestimate, an
18 overestimate -- can quickly be corrected in a rate
19 case that's filing -- being filed soon.

20 The last major difference between me and
21 Dr. Hadaway has to do with growth rates. And you
22 heard about the GDP growth rate and that sort of
23 stuff. And I actually use the GDP growth rate in this
24 case. But I don't recommend that you use
25 Dr. Hadaway's 6.6 or 6.5 percent growth as an expected

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1 growth for -- that investors are expecting in the
2 future.

3 Instead, his own documents show that if you
4 rely upon a 20 year GDP growth rate, gross domestic
5 product growth rate, you'll be at 5.5 percent.
6 Dr. Hadaway used to use a 20 year forecast. Only in
7 recent years has he switched to employing -- and if he
8 stuck to what he was doing before, he would have a
9 5.5 percent growth rate.

10 Only in recent years has he changed to using
11 a GDP growth rate that's based upon averaging 10
12 years, then averaging 20 years, then averaging 30
13 years, 40 years, 50 years, and 60 years, and dividing
14 all those averages by 6 and coming up with a number.

15 He claims that the -- he's trying to
16 weight -- give more weight to more recent times.
17 Well, if you want to use and give more weight to
18 recent times you would use a 10 year or 20 year
19 forecast, which comes out 5.5 percent.

20 So his analysis has no mathematical basis, no
21 financial basis, it just kind of ups the number. Now
22 when, when I take all these things into consideration
23 and I run Dr. Hadaway's models it comes out
24 9.85 percent.

25 Well, how -- and I know there's been some

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1 confusion here in terms of the conflicts and the
2 testimony given orally and passed in, in the direct as
3 well as the sur -- the rebuttal. How does Dr. Hadaway
4 change it? How does he still end up at 10.75?

5 Well, if you look closely at his testimony
6 you'll see that he picks and chooses the models he's
7 going to use. The first thing he did this morning was
8 to present you a table in his testimony and said
9 there's the constant growth DCF. I used analyst
10 estimates.

11 Well, when he filed direct testimony he said
12 that model comes out 9.9 percent. It's under
13 10 percent, I'm gonna discard that. He didn't even
14 present that to you as a possible choice. In rebuttal
15 he comes along, the number's up, you can use that now.

16 I don't believe you should pick and choose.
17 You should be consistent. If the numbers fall low,
18 they fall low. If they go high, they go high. You
19 ought not pick and choose based upon an end result.
20 And that's what I think Dr. Hadaway has done in this
21 case. I pointed that out in my testimony.

22 And I believe that it's data snooping, and
23 you ought not do that. And with that, I complete my
24 summary statement.

25 COMMISSIONER BOYER: Thank you, Mr. Lawton.

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1 I didn't know that one could be both an attorney and
2 an economist. I thought they were mutually exclusive.

3 THE WITNESS: I have a right side of the
4 brain for the economist part.

5 COMMISSIONER BOYER: Right side, left?

6 THE WITNESS: Left side, yes.

7 COMMISSIONER BOYER: Okay. That's exactly
8 what I was thinking.

9 All right. We'll commence with cross
10 examination, then, after the lunch break. And I fully
11 anticipate that we'll be able to hear the policy
12 witnesses. So, Ms. McDowell, you probably want to get
13 Mr. Walje over here. And hopefully Mr. Ball can be
14 with us. We'll recess now until 1:30. Thank you.

15 (A luncheon recess was taken
16 from 12:00 to 1:32 p.m.)

17 COMMISSIONER BOYER: Okay, we're back on the
18 record. As I reminded my colleagues, hard as this is
19 at least we're not handling child custody cases in
20 Texas today.

21 Well, let's see if we can stay apace. We've
22 heard Mr. Lawton's summary, so we'll proceed now to
23 cross examination. I think we'll start with the
24 Company. And then, let's see, go to Ms. Schmid. And
25 then around the room, as we have in the past.

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1 The time is yours, Ms. McDowell.

2 MS. McDOWELL: Thank you, Commissioner Boyer.

3 Make sure my mic is on. There we go.

4 CROSS EXAMINATION

5 BY MS. McDOWELL:

6 Q. Good afternoon, Mr. Lawton.

7 A. Good afternoon, Ms. McDowell.

8 Q. So in your summary you indicated that you had
9 updated Mr. -- or excuse me, Dr. Hadaway's analysis;
10 is that correct?

11 A. That's what I said. Yes, that is correct.

12 Q. And you were specifically talking about his
13 DCF analysis, I think; is that right?

14 A. No, that's not correct.

15 Q. So you were talking about all of the analyses
16 he did?

17 A. That is correct.

18 THE COURT REPORTER: Is your microphone on,
19 sir?

20 THE WITNESS: I'm rarely accused of talking
21 too softly, but I'll go up a notch.

22 Q. (By Ms. McDowell) And I think in your
23 summary you said when you updated Dr. Hadaway's
24 analysis it produced an ROE of 9.85; is that correct?

25 A. Yes. It supported a result of -- actually it

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1 was less than 9.85. And by averaging it with an
2 independent alternative DCF, it came out 9.85.
3 Dr. Hadaway's analysis I believe came out 9.75, so.

4 Q. Can you turn to page -- or excuse me, it's I
5 think schedule 3.3-SR. It's your Exhibit 3 to your
6 surrebuttal testimony.

7 A. 3.3-SR. Which page, ma'am?

8 Q. Page 1.

9 A. I'm there.

10 Q. And is this the table where you do go ahead
11 and update Dr. Hadaway's analysis?

12 A. No. When I was talking in my summary I was
13 talking about my direct testimony, where I updated
14 Dr. Hadaway's analyses for current data. And I did my
15 own other alternative DCF independent analysis.
16 That's what I was talking to the Commissioners about
17 in my summary.

18 In my surrebuttal I was responding to
19 Dr. Hadaway's claimed update and showing that it still
20 comes out well below the 10.75.

21 Q. Well let's, let's go through that. So --

22 A. Sure.

23 Q. This is an update to Dr. Hadaway's. It's
24 titled: "Update Hadaway Constant Growth." Do you see
25 that?

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1 A. Yes. It says: "Rebuttal Update Hadaway
2 Constant Growth."

3 Q. All right. So let's start with your update
4 to Hadaway's Traditional DCF ROE. Do you see that
5 Column E?

6 A. Yes.

7 Q. And that result is 10.17 percent. Do you see
8 that?

9 A. I see that.

10 Q. And then if you go over to Column G. And
11 that's a second update to a DCF result; is that
12 correct?

13 A. That is correct.

14 Q. And that result is 10.22, do you see that?

15 A. I see that.

16 Q. So the updates to the DCF analysis show a
17 range between 10.17 and 10.22, correct?

18 A. No, that's incorrect.

19 Q. These are the two updates to the DCF
20 analysis -- the single-stage DCF analysis you have on
21 this page, correct?

22 A. Correct. You rephrased your question to
23 single-stage DCF analysis --

24 Q. I see.

25 A. -- rather than the more global DCF analysis

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1 your first question asked me.

2 Q. I see. Thank you for that. So that -- so
3 that would be the next two columns over, H and I; is
4 that correct?

5 A. That would be Column H only.

6 Q. And then Column I is an average of all of
7 those results?

8 A. Column I is an average of all three of
9 Dr. Hadaway's analyses employing the DCF model.

10 Q. And that update gets you to 10.14 percent,
11 correct?

12 A. That is correct.

13 Q. So it's certainly higher than the 9.85
14 percent you suggested in your summary?

15 A. The premise of your question is the 9.85 is
16 premised only on DCF. As you'll recall in your first
17 question in your cross examination, did I also include
18 capital as a pricing model. And I said yes. And so
19 when you go to the next columns you'll see how we get
20 to 9.85.

21 Q. Okay. And we'll do that, but first let's go
22 to Column L, which is your risk premium update. Do
23 you see that?

24 A. Yes.

25 Q. And that's a 10.3 percent number, correct?

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1 A. Yes.

2 Q. Okay. So then back to your CAPM column. And
3 that's column, it's Column I and K; is that right?

4 A. Yes.

5 Q. And so those numbers are 8 percent to 9.3
6 percent, correct?

7 A. Right. These are Dr. Hadaway's models
8 employing updated data.

9 Q. And Dr. Hadaway didn't use these models in
10 his rebuttal because the rates had gone so low,
11 correct?

12 A. Right. That's what I said in my opening
13 statement. That, that Dr. Hadaway saw the numbers
14 were low and he discarded or abandoned the model.

15 Q. And, in fact, the numbers were low because
16 they're premised on a 1.4 percent Treasury rate,
17 correct?

18 A. No, not correct. The numbers are low because
19 the inputs to the model result in a lower number than
20 you had prior because the interest rates have
21 declined.

22 Q. Well, can you turn to page 3 of Exhibit 3.3?

23 A. I'm there.

24 Q. And there you indicate that you used a
25 1.42 percent rate for your CAPM model?

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1 A. Yes, I used the same method. Also, so, so
2 we're clear, one input was 1.42. The other input was
3 the 84.33 percent beta you see above it. And the
4 other input was the 7.6 percent long-term risk
5 premium. All based on Dr. Hadaway's analyses.

6 So it's one of more -- it's just not the only
7 input.

8 Q. So now, did you hear Mr. Peterson's testimony
9 this morning where he indicated that he refused to use
10 CAPM results between 8 and 9.1 percent because they
11 were just unreasonably low?

12 A. I, I heard what he said. He -- in the
13 context, as I recall, I don't think -- I think the way
14 you asked your question of Mr. Peterson, as I
15 understood his response he wouldn't use it as a final
16 recommendation. I don't recall him saying he wouldn't
17 use it as part of the overall analysis in terms of
18 ranges and evaluating it.

19 Q. So can you tell me, if you threw out the CAPM
20 results -- mindful of the fact that this Commission
21 has never used CAPM -- and simply averaged the updates
22 for the other columns on Dr. Hadaway's -- your update
23 to Dr. Hadaway's analysis on Exhibit 3.3, what would
24 that average be?

25 MR. PROCTOR: Mr. Chairman, excuse me,

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1 objection. The question's argumentative insofar as
2 suggesting that this Commission has never used that
3 particular model. And secondly, it's without
4 foundation.

5 MS. McDOWELL: I'll rephrase.

6 COMMISSIONER BOYER: Please do.

7 Q. (By Ms. McDowell) Can you please average
8 Column E, Column G, Column H, and L, and give me that
9 result?

10 A. And L?

11 Q. Yeah. So it's traditional DCF ROE, GDP
12 growth ROE, two-stage DCF, and risk premium.

13 A. Okay. It's a meaningless result, but I'll
14 give it to you. I'll do the math. I mean, nobody
15 would do this.

16 (Pause.)

17 THE WITNESS: Ten point one seven seven.

18 Q. (By Ms. McDowell) And the range there is
19 what, 10.02 to 10.13; is that correct? Ten point
20 three oh -- 10.02 to 10.30, correct?

21 A. Your question had so many numbers in it,
22 could you start over for me?

23 Q. I'm saying that number is based on a range of
24 10.02, which is Column H, to Column L, which is 10.30.

25 A. Yes, those are the highs and the lows of the

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1 exercise.

2 Q. Okay, thank you. What was the Single-A
3 utility bond yield that you employed in your analysis?

4 A. Which analysis are you speaking of?

5 Q. Well, let's go to page 14 of your direct
6 testimony.

7 A. Do you have a line number, ma'am?

8 Q. Lines 3 -- line 321.

9 A. It says in my testimony 5.5 percent. And
10 that would be the Single-A rate.

11 Q. So can you turn to your exhibit --
12 Surrebuttal Exhibit 3.1?

13 A. I'm there.

14 Q. And that exhibit is entitled: "Long-Term
15 Interest Rate Trends." Do you see that?

16 A. Yes.

17 Q. This chart includes data back to 1993,
18 correct?

19 A. That's correct.

20 Q. Now, there is no yield on this chart as low
21 as your proposed 5.5 percent Single-A rate, is there?

22 A. There is no annual yield as low as
23 5.5 percent from 1993 forward, that is correct. But
24 as you know, I calculated the 5.5 percent using
25 Dr. Hadaway's model and method. And it's supported by

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1 his own rebuttal testimony. His own forecast.

2 Q. Can you turn to Exhibit 3.10 of your
3 testimony?

4 A. We're back on direct?

5 Q. On your direct, sir.

6 A. Sure. Is that the last one?

7 Q. It is.

8 A. Okay, I'm there.

9 Q. It's your update to -- or your correction to
10 Dr. Hadaway's risk premium analysis.

11 A. I'm there.

12 Q. So in this correction you employed that same
13 5.5 percent rate we were just talking about?

14 A. Yes. The one that Dr. Hadaway's analysis and
15 data support.

16 Q. Mr. Lawton, were you here when Dr. Hadaway
17 testified this morning that the most recent Single-A
18 utility rate published is 6 -- for a monthly average
19 is 6.29 percent?

20 A. If you're asking was I here when he said the
21 most recent one?

22 Q. Yes.

23 A. Yes. As of April.

24 Q. That's right. And do you dispute that rate?

25 A. No.

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1 Q. So can you take a look at your Exhibit 3.10?

2 A. I'm there.

3 Q. And instead of using the number 5.50 for the
4 Single-A rate use the number 6.30, the most recent
5 Single-A rate.

6 A. Give me a moment.

7 Q. Thank you.

8 A. For some reason the 6.30 doesn't sound right.
9 And I just don't have that exhibit. I think it's one
10 of your --

11 Q. Six point two nine?

12 A. Oh, 6 -- okay.

13 Q. I rounded up. Please use 6.29, if you're
14 more comfortable doing that analysis.

15 A. Either one.

16 Q. But the point is, can you use the most recent
17 rate in lieu of the -- or instead of the 5.5 percent?

18 A. Sure, you can do 6.3. Do you want me to do
19 the calculation?

20 Q. Just tell me the result -- yes, if you would
21 do the calculation and then tell me what that would
22 produce.

23 A. Okay.

24 (Pause.)

25 THE WITNESS: I'm ready. Ten point seven two

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1 would be the number. But of course nobody would do
2 this.

3 Q. (By Ms. McDowell) So that number, you had
4 some concerns that you expressed in your summary about
5 the use of forecast data, didn't you?

6 A. Yes, I did.

7 Q. And that number that you just quoted, 10.73,
8 does not rely on forecast data, does it?

9 A. No, it doesn't.

10 Q. That's the most current data available?

11 A. That's the most current spot month we have
12 available. And that is the reason you wouldn't use
13 it.

14 MS. McDOWELL: That's all I have.

15 COMMISSIONER BOYER: Thank you, Ms. McDowell.

16 Let's turn to Ms. Schmid. Cross examination
17 of Mr. Lawton?

18 MS. SCHMID: The Division has no questions
19 for Mr. Lawton.

20 COMMISSIONER BOYER: Very well. Let's move
21 to Mr. Dodge.

22 MR. DODGE: No questions.

23 COMMISSIONER BOYER: Mr. Ball?

24 MR. BALL: No thank you, Chairman.

25 COMMISSIONER BOYER: Okay. Let's turn to the

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1 commissioners. Commissioner Allen?

2 COMMISSIONER ALLEN: Thank you.

3 Mr. Lawton, I'll just give you the same
4 opportunity if you want to address the nature of the
5 questions that I had about finding comparable
6 companies.

7 THE WITNESS: Yes.

8 COMMISSIONER ALLEN: How difficult and
9 challenging it may be for our own situation. And also
10 if you have any distinctions to add in terms of how
11 you might have used some of these in your models.

12 THE WITNESS: Sure. In this case I employed
13 Dr. Hadaway's comparable companies. And he used a
14 screen or -- I think we've been using the word
15 "screen." And he used a screen of revenues, had to
16 have certain revenue -- level of revenues. Had to be
17 followed by Value Line. And had to have I think 65 or
18 70 percent of its revenues from regulatory operations
19 and things like that.

20 And those screens, what they do is we used to
21 have so many more electric utilities to pick from but
22 through -- over the years these mergers and
23 acquisitions we see out there have resulted in a
24 smaller and smaller group.

25 Now, these screens will give you a smaller

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1 group. And what you're trying to do is get a
2 comparable set of companies with similar financial and
3 business risks that -- as your target company, in this
4 case Rocky Mountain Power.

5 Now, as you add more screens or more criteria
6 to your selection process, you are gonna limit it.
7 And as you limit it, you get fewer and fewer
8 companies. And my background in economics and
9 statistics tells me the more I get out there in terms
10 of comparable companies, the more those aberrations
11 get ironed out.

12 For example, you talked about a growth rate
13 of 16 percent for PPL earlier in your questioning.
14 And by having 15 companies versus 5, a 16 percent
15 growth rate, that kind of aberration will be limited.
16 So that's why you want a -- first, a bigger group.
17 But second and most important in this case and I and
18 Dr. Hadaway used the one group.

19 Mr. Peterson from, from the staff used, used
20 a different group, with a different set of criteria.
21 Yet if you look at the results of Mr. Peterson and his
22 group, he came up with 10.1 percent. And I used
23 Dr. Hadaway's group, using his selection criteria. I
24 came up with just about the same results of
25 Mr. Peterson.

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1 And so we have two different groups selected
2 in this case, in this very case, albeit Mr. Peterson
3 and I go at it and approach it a little differently
4 than Dr. Hadaway, but we came up with basically the
5 same result with different comparable groups.

6 I think that's something that should give the
7 Commission some comfort that we're, we're capturing
8 what the cost of capital is for this company.

9 COMMISSIONER ALLEN: Thank you.

10 COMMISSIONER BOYER: Commissioner Campbell?

11 COMMISSIONER CAMPBELL: I only have one
12 question. It deals with your selection of 20 years
13 as -- for your GDP growth estimate. And I guess my
14 question is why 20 versus 40? Take the averaging
15 aside that you're critical of.

16 THE WITNESS: Sure.

17 COMMISSIONER CAMPBELL: Does 20 years
18 adequately capture the business cycle? Explain 20
19 versus 30 or 40.

20 THE WITNESS: No, I understand absolutely
21 your concern. And probably today 10 would -- might
22 even be better. Because what you want to find out is,
23 is the history of GDP growth -- and we can go back
24 from 1947, the starting point, and I'll get to your
25 20 year in a moment.

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1 Is, is what happened in those years
2 representative of what we can expect to happen in the
3 future, when these rates are gonna be in effect?
4 Well, if we think back to the '40's, probably not.
5 Now 20 years, I'm going back to 1988 from -- 1987,
6 '86.

7 From that time period, the end of the '80's
8 through the '90's, is that gonna be more
9 representative? Is that gonna be representative of
10 hopefully lower inflation and lower interest rates
11 than we had in the early '80's and other times before
12 that?

13 And I think 20 years, and possibly even 10 --
14 and it makes no difference in this case, the numbers
15 are the same -- is probably more representative of the
16 growth situation or the things we'll see in the
17 economy that will likely cause growth.

18 And I think you could expect the 5.5 percent
19 as more reasonable. In addition, the second check on
20 that is if you look at analyst growth I think you're
21 more in line with 5.5 percent. So it makes sense in
22 two ways. Sorry.

23 COMMISSIONER CAMPBELL: Would you comment on
24 the idea that a 10 year -- a 10 year time period would
25 perhaps not capture a business cycle? Or --

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1 THE WITNESS: Well --

2 COMMISSIONER CAMPBELL: -- or multitude
3 business cycles that would factor into the growth
4 rate.

5 THE WITNESS: A 10 year time period may, in
6 fact, not capture a multitude of business cycles that
7 would contribute to, to growth. But the 10 years
8 we're looking at here?

9 I don't see where, where the past 10 years
10 would be anything real different to expect -- or the
11 past 20 years is what I ultimately selected -- than
12 what we could expect for the short run future. I
13 think that's a good projection base. Thank you,
14 Commissioner.

15 COMMISSIONER BOYER: Mr. Lawton, just a
16 couple of questions. You did not, as I recall, object
17 to the capital structure proposed by the company?

18 THE WITNESS: No, I did not. I accepted
19 their capitalization.

20 COMMISSIONER BOYER: How do you arrive at
21 that opinion?

22 THE WITNESS: Sure. If you look at, I think
23 it's my first exhibit in my direct testimony. I
24 compare the capitalization levels, the equity levels
25 of the comparable companies to that of Rocky Mountain

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1 Power.

2 And they're pretty much in sync. The
3 50 percent level. I think the comparable group might
4 have been at 49 percent on average. A little less.
5 But that equity level, when you do that comparison
6 you're looking at financial risk is what you're
7 looking at. Because obviously utilities could issue a
8 lot more debt, because it's cheaper for consumers.

9 But if you start getting up there at very
10 high debt levels, well, you could run into problems.
11 A, borrowing, B, servicing that debt. And what I see
12 in regulatory commissions around the country and when
13 you read these decisions, this is a very reasonable
14 capitalization level.

15 And it's -- you're gonna balance consumer
16 interest and the company shareholder interest against
17 each other. And I don't see anything out of line in
18 this capitalization level.

19 COMMISSIONER BOYER: Thank you. Now, both
20 Dr. Hadaway and Mr. Peterson testified about a rate
21 spread.

22 THE WITNESS: Sure.

23 COMMISSIONER BOYER: With Dr. Hadaway
24 predicting an increase in the spread. Mr. Peterson
25 predicting a narrowing in the future. Do you have an

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1 opinion on that?

2 THE WITNESS: Yes. And I outlined it in my
3 surrebuttal testimony -- I get confused, and I
4 apologize. Surrebuttal testimony. Where I pointed
5 out in my first exhibit there and the second exhibit,
6 I think I pointed to the years 2002 and 2003.

7 And I noted that, boy, the rate spreads back
8 then were pretty big. Looking at annual rate spreads.
9 And I said, What was the Federal Reserve doing then?
10 And I provided the Federal Reserve changes to the
11 discount rate.

12 For that -- well, I do it historically, but
13 for that time period we see the Federal Reserve being
14 very active in its monetary policy, lowering that
15 discount rate spreads group. Now, what do we have
16 today? We have a time when we all know the Federal
17 Reserve has been pretty active.

18 I mean, going in on a Sunday and cutting the
19 discount rate 75 basis points on a Sunday, that's
20 rare. And certainly the amount of times they've cut
21 the discount rate is comparable to that time period.
22 So what is happening is you'll see the government
23 rates responding more quickly.

24 Obviously they control direct -- more
25 directly the short-term government rates. And -- but

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1 the, the 2002 experience tells us, yeah, the spreads
2 were big. Corporate rates were higher. The spreads
3 were bigger. But corporate debt was declining all
4 that time, albeit more slowly than the, than the
5 government bonds.

6 And that's the kind of the same thing we see
7 today. And the last check on Dr. Hadaway's statement
8 that this Commission can make to see if it's
9 reasonable, give it a reasonable test, is we all
10 agree -- and Dr. Hadaway said a number of times --
11 economy's in turmoil.

12 We all know we have problems around the
13 country. Some parts of the country are worse off than
14 others. But how do we come out of economic turmoil or
15 recession? Do we tell Corporate America to create
16 jobs by investing, and raise the cost of money?
17 They're not gonna do that.

18 The monetary policy is to lower corporate
19 borrowing. Lower it and give the -- incentivize them
20 to invest more, to get more jobs, to get the economy
21 rolling forward again.

22 But Dr. Hadaway's approach, if we're going to
23 have higher interest rates we're not gonna tell
24 Corporate America, We want you to invest but we're
25 gonna charge you a lot more for it. That just doesn't

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1 make sense. And that's not what the Federal Reserve
2 is trying to do, as we see every day.

3 COMMISSIONER BOYER: Thank you, Mr. Lawton.
4 So my question about tinkering wasn't too far afield,
5 was it?

6 Mr. Proctor, anything further?

7 MR. PROCTOR: Just two questions.

8 REDIRECT EXAMINATION

9 BY MR. PROCTOR:

10 Q. Mr. Lawton, the first I have for you pertains
11 to the Company's examination pertaining to 3.3-SR,
12 page 1 of 3.

13 A. I'm almost there.

14 Q. Okay.

15 A. I'm there.

16 Q. The Company's counsel asked you to perform an
17 average calculation utilizing Columns E, G, H, and L,
18 I believe?

19 A. Yes, sir.

20 Q. And also I, pardon me. And you performed
21 that calculation. I believe the result was 10.177.
22 You also stated that one wouldn't perform that
23 calculation. Why would one not perform it?

24 A. Well, just as far as your question goes, I
25 was not included in that calculation.

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1 Q. Oh, okay. I'm sorry.

2 A. The Column I. I was, but the Column I
3 wasn't.

4 Q. Oh, okay.

5 A. But why wouldn't I perform, perform that
6 calculation? Well, that's just doing the same
7 tinkering that we, we say Dr. Hadaway should not do.
8 And that is selecting your results and saying, Hey,
9 these numbers are low. And throwing them out and
10 hoping for, for a best-result scenario.

11 That's not good. When you're -- you come up
12 and you do these analyses you take the high with the
13 low. You stay consistent. And that's the best advice
14 you can give to any regulatory commission. And, and I
15 think that's tinkering by taking it out. It's silly.

16 Q. Now, with respect to in your direct
17 testimony, Exhibit 3.10, again Ms. McDowell asked you
18 to perform a calculation utilizing a spot month amount
19 for the corporate Single-A utility bond rate. Why
20 would one not use that spot month?

21 A. Sure. Again, basically because it's a spot
22 month. And that is a snapshot. A moment in time.
23 And as you can see the other months they, they move
24 quickly and, and they move sometimes considerably from
25 month to month.

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1 The, the other thing -- and even
2 Dr. Hadaway's analysis rather than using a spot month,
3 when he used historical data, would use a three month
4 average. You don't use those spot months. So that
5 would be more reasonable.

6 MR. PROCTOR: Thank you, Mr. Lawton.

7 COMMISSIONER BOYER: Okay Mr. Lawton, thank
8 you. You may step down.

9 THE WITNESS: Thank you, Commissioners. And
10 I appreciate you inviting me out here. It's my first
11 trip to Utah and I'm enjoying it.

12 COMMISSIONER BOYER: Pleasure having you. We
13 even ordered up some good weather for you.

14 I think we'll move on to the policy
15 witnesses. And what I've determined to do is to hear
16 from Mr. Ball first, inasmuch as --if we do run out of
17 time, it doesn't look like we will run out of time --
18 but if we were to have, Mr. Walje could be available
19 in June. Mr. Ball could not because of his travel
20 schedule. So we will proceed to Mr. Ball. Do you
21 have a brief summary, Mr. Ball?

22 MR. BALL: Yes. Yes Chairman, thank you.
23 Sorry, you took me just a little by surprise here
24 by --

25 COMMISSIONER BOYER: Do you need a moment to

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1 collect your thoughts? We could take a short break.

2 MR. BALL: No, there's no need for that. But
3 it will just take me a moment or two to assemble. I
4 was doing something else when you broke that happy
5 news to me. Okay, here we go then.

6 COMMISSIONER BOYER: Mr. Ball, why don't you
7 sit up here at the stand and then everyone can have a
8 good vantage point.

9 MR. BALL: Okay. That might just take a
10 little longer, then. If you want to take a break, go
11 ahead.

12 COMMISSIONER BOYER: I guess while we're
13 waiting for Mr. Ball to, to make the move over to the
14 witness stand I'm hoping that you're making
15 arrangements to get Mr. Walje here.

16 MS. McDOWELL: We are.

17 COMMISSIONER BOYER: Fantastic, thank you.
18 And there he is. Were your ears ringing, Mr. Walje?
19 We were just speaking of you.

20 MS. McDOWELL: Commissioner Boyer, is it, is
21 it all right to excuse the Company's witnesses who
22 have already testified?

23 COMMISSIONER BOYER: It is indeed. Yeah,
24 thank you very much --

25 MS. McDOWELL: Thank you. I just wanted to

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1 make sure that nobody else had any other questions.

2 COMMISSIONER BOYER: Yes. Thank you very
3 much to all of them. Both of them, I guess.

4 Mr. Ball you have been sworn in this case,
5 have you not?

6 MR. BALL: Yes, sir. Okay, I think I'm ready
7 if everybody else is.

8 COMMISSIONER BOYER: Okay. You may proceed,
9 Mr. Ball.

10 MR. BALL: Thank you. First of all let me
11 say I am Roger J. Ball. My address is 1375 Vintry,
12 V-i-n-t-r-y, Lane, Salt Lake City, Utah 84121. I'm
13 appearing here today on my own behalf as a residential
14 ratepayer of PacifiCorp, which does business in Utah
15 as Rocky Mountain Power.

16 There is no other supplier of electricity to
17 whom I can turn, because Rocky Mountain Power has a
18 monopoly where I live. To the extent that there are
19 other similarly-situated Rocky Mountain Power
20 ratepayers, their interest in these proceedings may
21 align with my own.

22 I am the same Roger J. Ball who filed rate of
23 return direct testimony marked as RJB Exhibit 3,
24 consisting of 15 pages, including a certificate -- a
25 service certificate on the 31st of March 2008. I also

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1 filed rate of return rebuttal testimony marked RJB
2 Exhibit 5, consisting of 6 pages, including a service
3 certificate on the 28th of April.

4 And a rate -- and rate of return surrebuttal
5 testimony marked RJB Exhibit 6, consisting of 6 -- of
6 4 pages, including a service certificate on the 12th
7 of March -- 12th of May, 2008.

8 I'd like to say that if I were asked same
9 questions today that are in my prefiled written
10 direct, rebuttal, and surrebuttal testimony my answers
11 would remain the same.

12 By way of summary of my testimony, there are
13 essentially three points. The Commission last heard
14 return on equity litigated in Docket 99-03-510 when
15 PacifiCorp sought 11 1/4 percent.

16 Eight years ago this coming Saturday the
17 Commission ordered 11 percent and increased rates by
18 \$17 million. A little over 25 percent of PacifiCorp's
19 requested 67 million. In the next case, 01-03-501,
20 PacifiCorp received \$41 million, about 29 percent of
21 the 141 million it requested.

22 Net power costs have been hotly contested but
23 some 100 issues, including return on equity, were
24 settled. Then came Senate Bill 61 in 2003, one
25 provision of which encouraged settlement.

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1 Three subsequent cases in a row were settled
2 with black box stipulations, as a result of which the
3 company received 52 percent, 46 percent, and 58
4 percent. An average of 54 percent of its requests, or
5 about twice as large a share as before Senate Bill 61.

6 In the two most recent of those cases
7 PacifiCorp moved the Commission to approve agreements,
8 including stay out provisions, or periods during which
9 the company would make no further rate increase
10 applications.

11 The sole owner of PacifiCorp during the early
12 years of the period I'm talking about, Scottish Power,
13 clearly didn't require returns conforming with the
14 theoretical underpinnings of the Company's witnesses.
15 Berkshire Hathaway and its subsidiary, MidAmerican
16 Energy Holdings Company, clearly didn't when it
17 invested all that was needed to buy PacifiCorp, and
18 didn't when the last case was settled.

19 Rocky Mountain Power's plea of poverty in
20 paragraph 10 of its application that, "In recent years
21 it has consistently under earned the return on equity
22 established by the Commission," makes my point.

23 Not only does PacifiCorp routinely, as it has
24 over many years, asked for about twice as much as the
25 rate increase it is willing to accept in a settlement

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1 agreement and about four times as much as it has
2 received in fully-litigated cases, but it has
3 repeatedly, four times in a row now, agreed to those
4 lower-than-requested increases over the past seven
5 years.

6 Any poverty is self-imposed. But the lesson
7 for this Commission is that PacifiCorp's corporate
8 owners over those years simply don't require rates of
9 return on their equity at the levels Dr. Hadaway
10 claims.

11 Second point: This will be the first
12 PacifiCorp rate case since the passage of Senate Bill
13 61 in which the Commission has adopted a fully
14 forecasted test year.

15 Senate Bill 61 also amended Title 54, Chapter
16 4, Section 4, Subsection 3 of the Utah Code
17 eliminating the option for the Commission to use an
18 entirely historic test year, and strongly encouraging
19 the use of a future test period. However, it was
20 silent on the question of the consequent shift of
21 financial risk from stockholders to ratepayers, such
22 as me, leaving the Commission to figure out how to
23 handle that.

24 PacifiCorp Exhibit Rocky Mountain --
25 RMP-SRM-1-5 -- sorry, 1 -S -- can't read my own

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1 writing -- values the shift at \$27,583,763. And my
2 second point is that nowhere did the legislature say
3 that it intended, in passing Senate Bill 61, to give a
4 utility a windfall.

5 So the Commission should offset any rate
6 change resulting from this proceeding by deducting
7 that approximately \$27 1/2 million figure from the
8 result so that ratepayers' interests are balanced with
9 stockholders' and the resulting rates can be just and
10 reasonable.

11 My argument is if the Commission doesn't do
12 that, the resulting rates won't be just and
13 reasonable. The Commission will, in fact, be granting
14 PacifiCorp a windfall.

15 Third point: In my testimony I address
16 PacifiCorp's approach to risk. It's 1990 strategy to
17 take its Utah utility revenues and invest them outside
18 the United States. Not just outside Utah, but outside
19 the United States. And how it has subjected
20 ratepayers like me to the risks of rapidly increasing
21 power costs by failing to build and acquire adequate
22 reasonable cost generation and long-term contracts.

23 PacifiCorp shouldn't be rewarded with a
24 higher return on equity because it's building now. It
25 wouldn't need all this construction now if it had done

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1 what it should have done through the 1990's and the
2 early part of this decade.

3 The Commission should balance the interests
4 of ratepayers with the interests of stockholders by
5 taking account of the fact of the risks that the
6 company has willfully exposed Utah ratepayers,
7 including myself, to. And should be looking, if
8 anything, to reduce the rate of return, not increase
9 it. Thank you, sir.

10 COMMISSIONER BOYER: Thank you, Mr. Ball.
11 Mr. Ball's now available for cross examination. Let's
12 begin with the Company, then we'll move to the
13 Division, the Committee, and Mr. Dodge.

14 Ms. McDowell, have you questions for
15 Mr. Ball?

16 MS. McDOWELL: No, Commissioner Boyer, we do
17 not. We made our points about Mr. Ball's testimony in
18 our motion this morning.

19 COMMISSIONER BOYER: Thank you.

20 Ms. Schmid, any questions?

21 MS. SCHMID: The Division also has no
22 questions for Mr. Ball. And trusts that the
23 Commission will award it its proper weight --
24 Mr. Ball's testimony its proper weight.

25 COMMISSIONER BOYER: Mr. Proctor?

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1 MR. PROCTOR: No questions.

2 COMMISSIONER BOYER: You must have persuaded
3 them all, Mr. Ball.

4 Mr. Dodge?

5 MR. DODGE: No questions.

6 COMMISSIONER BOYER: Okay, let's go to the
7 Commission. Commissioner Allen, do you have any
8 questions of Mr. Ball? Well, neither do I. I've
9 basically read the testimony, I've heard this before.

10 So you may step down. Thank you so much for
11 participating, Mr. Ball. Do you want to say something
12 further? Go ahead.

13 THE WITNESS: Can I draw the same conclusion
14 that you did; that since the Commission has no
15 questions, I've persuaded you?

16 COMMISSIONER BOYER: You can draw that, but
17 don't bank on it you know. We haven't yet decided
18 where we're going on this case.

19 Okay. Well, we're moving right along. Let's
20 see, is our reporter okay? You have a lot of energy
21 left? Fantastic.

22 Let's proceed then with Mr. Walje, our last
23 policy witness for the day.

24 MS. McDOWELL: I hope we all get a gold star
25 when this is over.

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1 COMMISSIONER BOYER: Well, I was gonna take
2 credit for it. But you certainly do deserve all of
3 the credit, I must say.

4 Mr. Walje, have you been sworn in this
5 proceeding?

6 THE WITNESS: I have.

7 COMMISSIONER BOYER: Please take a seat. You
8 weren't here this morning, but we've asked for brief
9 summaries inasmuch as we've all read all of your
10 prefiled written testimony.

11 THE WITNESS: Okay. Two-thirds of a page is
12 all.

13 COMMISSIONER BOYER: Fantastic, thank you.

14 RICH WALJE,
15 called as a witness, having been duly sworn,
16 was examined and testified as follows:

17 DIRECT EXAMINATION

18 BY MS. McDOWELL:

19 Q. Good afternoon, Mr. Walje.

20 A. Good afternoon.

21 Q. Sir, this morning we admitted -- offered your
22 testimony, both your direct and rebuttal testimony in
23 the revenue requirement phase as it pertains to the
24 issues in this proceeding, as well as your specific
25 rebuttal in the rate of return -- in our rate of

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1 return hearing.

2 So that has been offered and admitted into
3 the record. And I think that means that it's time now
4 for you to deliver your summary of that testimony.

5 A. Okay, thank you. Thank you, Chairman Boyer,
6 Commissioner Campbell, and Commissioner Allen for
7 providing me a few brief moments to provide some
8 qualitative support for quantitative testimony you
9 heard earlier today that we believe supports our
10 request for an 8.54 percent return -- rate of return,
11 based on a 10.75 percent cost of equity and a
12 6.30 percent cost of debt.

13 One of the points I would like to make is
14 that Rocky Mountain Power/PacifiCorp is facing
15 business challenges that are much greater than the
16 typical utilities, primarily driven by our fast load
17 growth. And especially industrial loads, which
18 recently have started growing at a much higher rate
19 than they have historically, particularly in the
20 states of Wyoming and Utah.

21 This is leading us to have to make an
22 unprecedented -- unprecedented level of capital
23 investment as we respond to meeting this business --
24 this growing load. The result of this, if you refer
25 to the Standard & Poor's rating that was attached as,

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1 as an exhibit in my most recent testimony, you'll see
2 that within there they're stating that our 10 year
3 \$20 billion capital program could have a potential
4 impact on the Company's financial strength.

5 To put this in perspective, at the end of a
6 ten year period we will have nearly doubled the
7 electric plant and service required to meet our
8 customers' demand for electricity. At the same time,
9 the company is managing other challenging business
10 factors.

11 In summary, as I said, electric demand is
12 increasing dramatically. Fuel and wholesale energy
13 costs are increasing. And commodity costs are also
14 escalating. In the near and midterm there are no
15 signs that these factors are going to change
16 fundamentally as we go forward into the next few
17 years.

18 Additionally, the company is facing more
19 multi-state utility business risk, as each of our
20 states begin to chart different energy policies
21 related to how they want to respond to greenhouse
22 gases, renewable portfolio standards, and their
23 generation resources as they decide how to deal
24 primarily with climate change and environmental
25 policies.

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1 And again this is, I think, further evidence
2 that our business risk is different than it was
3 several years ago when these issues weren't at the
4 forefront. As a result of this required level of
5 investment in order to meet our obligation to serve we
6 will not, through either our net operating income or
7 depreciation expense, be able to fund this capital
8 program.

9 So we will be going to the financial markets
10 for new financing to meet our customers' energy needs.
11 And if these debt markets are competitive, the credit
12 ratings are particularly important to us as we
13 undertake this multi-billion dollar investment
14 program. And we want to be able to make sure that we
15 have access to competitively priced capital because of
16 its direct benefit to our customers.

17 So in our -- in summary, we believe our
18 request for a 10.75 percent return on equity is
19 qualitatively supported by the changes in our business
20 that have taken place reasonably. And an outcome of
21 this type will allow us to continue to provide safe
22 and reliable electric service to our customers. That
23 concludes my remarks.

24 COMMISSIONER BOYER: Thank you, Mr. Walje.

25 Is he available for cross examination at this

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1 point?

2 MR. JENSEN: Yes, Commissioner Boyer.

3 COMMISSIONER BOYER: Very well. Let's start
4 with Ms. Schmid.

5 MS. SCHMID: The Division has no questions.
6 And trusts that the Commission will treat Mr. Walje's
7 testimony appropriately and give it the proper weight.

8 COMMISSIONER BOYER: Thank you. Let's hope
9 that we do that.

10 Mr. Proctor?

11 MR. PROCTOR: I have no questions.

12 COMMISSIONER BOYER: Mr. Dodge has some
13 questions, I can tell.

14 MR. DODGE: I actually do. Just a couple.

15 CROSS EXAMINATION

16 BY MR. DODGE:

17 Q. Good afternoon, Mr. Walje.

18 A. Good afternoon, Mr. Dodge.

19 Q. In your direct and surrebuttal, I guess it
20 is, testimony you referenced -- and in your summary
21 this afternoon you referenced a multi-state risk.

22 A. Yes.

23 Q. In your mind, I mean, how should this
24 Commission take into account a multi-state risk in
25 setting an ROE? I mean, is that something that Utah

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1 ratepayers should pay more in terms of the authorized
2 ROE because of the multi-state risk?

3 A. Well, I don't -- I'm not suggesting that they
4 pay more than the authorized rate of return. I'm just
5 suggesting that because of our historical
6 relationships with our six commissions and how those
7 are changing and relating -- in relation to the
8 State's energy policy decisions, that our return on
9 equity should be at a higher level than it has been
10 set previously.

11 Q. I'm gonna hand you a document very quickly.

12 MR. DODGE: May I approach?

13 COMMISSIONER BOYER: You may, please.

14 MR. DODGE: It's actually a set of documents.
15 And unless someone wants me to do it otherwise, I'll
16 treat them as one.

17 Q. (By Mr. Dodge) Mr. Walje, I'll represent
18 that these are excerpts from a company data request.
19 And I, and I bring it up only in this multi-state
20 context. The first page of the set, do you recognize
21 this as unadjusted results of operation for the State
22 of Utah for calendar year 2007?

23 A. I do not recognize this as -- this data
24 request. I have not personally reviewed it.

25 Q. Will you accept, subject to check, that at

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1 least the first page purports to show that?

2 A. Yes, I will.

3 Q. Results of operation unadjusted for calendar
4 year '07?

5 A. I will.

6 Q. And near the bottom, on line 65, it
7 calculates a return on equity. And again, these are
8 unadjusted numbers, but they will be for the others.
9 It reflects a Utah return on equity of 10.032 percent
10 for calendar year '07, correct?

11 A. Correct.

12 Q. If you'll turn to the next few pages it has a
13 similar results of operation unadjusted calendar year
14 2007 for each of the states of Washington, Oregon,
15 Idaho, and Wyoming. And I'm not quite sure which
16 order yours are in.

17 But I guess I want to call to your attention
18 that the similar lines for Washington, for example,
19 return on equity is 2.71. For Oregon, 9.62. For
20 Idaho, 6.2. For Wyoming, 7.0.

21 I guess my question being, given those
22 results of operating for the last year, don't you
23 think it's probably other states and not Utah that's
24 dragging your overall return down?

25 A. Well, I have not prepared to defend potential

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1 rate cases of what we might do in other states,
2 Mr. Dodge.

3 COMMISSIONER BOYER: Mr. Walje, I don't think
4 your mic is on.

5 THE WITNESS: Is that better?

6 COMMISSIONER BOYER: Yes, it is.

7 THE WITNESS: I must have turned it off
8 bringing it nearer to me. I guess my comment is,
9 Mr. Dodge, that I didn't come prepared to analyze our
10 return on equity or un -- our unadjusted or adjusted
11 results in the other states.

12 My, my testimony is only offered to
13 demonstrate that the Company's facing a different
14 level of business uncertainty than it has in the
15 recent past.

16 Q. (By Mr. Dodge) Sure. And again, what I'm
17 addressing is your suggestion that because of the
18 multi-state risk, your ROE in this state should be
19 higher. And don't you agree that Utah, at least as of
20 2007, actually performed better than any of your other
21 states?

22 MS. McDOWELL: I'm gonna object to that.
23 Mr. Walje has just said he is not a witness to testify
24 on the results of operations. We have Jeff Larsen
25 here, who's quite familiar with how these are put

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1 together and what they mean. We're happy to make him
2 available to testify to that.

3 COMMISSIONER BOYER: I'm gonna sustain the
4 objection, but let Mr. Dodge rephrase the question if
5 he can.

6 Q. (By Mr. Dodge) Well, again, my effort is not
7 to ask you to address the results of operation but the
8 comparative returns that the company sees among the
9 states. And it's in response to your suggestion that
10 Utah's ROE should go higher because of the multi-state
11 risk the company faces.

12 And my -- isn't the right answer other states
13 should raise their ROE so they can get up to Utah's?

14 A. I would agree that we face multi-state
15 business risks in all states and would indicate a
16 higher return on equity.

17 MR. DODGE: Thank you. No further questions.

18 COMMISSIONER BOYER: Thank you, Mr. Dodge,
19 Mr. --

20 MR. DODGE: I would ask that these be marked
21 as UAE Cross Exhibit 1(ROE) or (RoR), whichever you
22 are naming them, and ask that it be admitted.

23 COMMISSIONER BOYER: Any objection to the
24 admission of these documents as UAE Cross Exhibit --
25 Exhibit 1?

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1 MR. PROCTOR: No objection.

2 MS. SCHMID: None.

3 COMMISSIONER BOYER: They are admitted then.

4 MS. McDOWELL: I'm sorry, we do object to
5 this. And I was just conferring with Mr. Larsen to
6 understand the basis of the objection. And that is
7 that these are -- this is a rolled-in comparison. And
8 the -- it's important to understand that this case was
9 not filed under rolled-in allocation protocols.

10 So this is an illustrative document that
11 doesn't have anything to do with how the allocation
12 methodology in this case was calculated. So that's
13 the first point and first concern.

14 The second concern we have is that the
15 questioning was done about unadjusted results. The
16 unadjusted results are, again, not a regulatory
17 review. They don't take into account regulatory
18 disallowances.

19 So we have concerns about this document
20 coming in. It's the same kind of concerns we had
21 about Mr. Walje being questioned on it. We have no
22 concerns about another witness who's qualified coming
23 in and explaining the issues that we have with this
24 document. But we don't think it's appropriate to come
25 in in this examination.

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1 MR. DODGE: Mr. Chairman, may I react?

2 COMMISSIONER BOYER: Please do, Mr. Dodge.

3 MR. DODGE: For the purpose offered it's
4 certainly appropriate. It was offered solely for the
5 illustrative -- for the comparative results among the
6 states. This was a company data response to a request
7 for comparative states returns. It's offered for that
8 simple purpose.

9 Now, if Ms. McDowell wants us to spend more
10 time this afternoon by calling Jeff Larsen to indicate
11 that's what it is, that's fine. But I think the
12 Company could stipulate, for that purpose, that's what
13 it reflects. That it's in response to a data request
14 asking for the comparative results of operation from
15 the various states.

16 MS. McDOWELL: We don't have that data
17 request here. And it would have been helpful, if that
18 is the context in which it's being provided, to have
19 the cover data request so we could review that and
20 understand in what context we did provide these
21 documents. Because the cover data request is not
22 apparent here, and it's -- I'd like to take your word
23 for it, but I --

24 MR. DODGE: Does the Company dispute that
25 this is a data request to UIEC's data request?

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1 MS. McDOWELL: Well, you know, it depends on
2 what you asked precisely what we --

3 MR. DODGE: I'll call Mr. Larsen. I guess if
4 they want to play games, we'll play games.

5 MS. McDOWELL: It's not about that. I just
6 want to be clear about what the record shows. The
7 data request could have asked for many different
8 things, and we would have provided it as responsibly
9 as we could.

10 The fact that the data request is not here
11 explaining the context in which we provided this data
12 is a concern to me. As I think it should be so the
13 Commission will to have its record clear.

14 COMMISSIONER BOYER: Mr. Proctor wants to
15 weigh in on the debate.

16 MR. PROCTOR: It seems to me, if the Company
17 is questioning the genuineness of the document, that's
18 one thing. But I believe that Mr. Walje identified it
19 as the type of document that his company produces.
20 And the number is the number.

21 I mean, I don't understand why we'd continue
22 to call -- why the Company would require this
23 Commission to call another witness to testify to what
24 Mr. Walje has already acknowledged what it is. And
25 for the limited purposes Mr. Dodge has defined, it's

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1 perfectly appropriate and perfectly admissible.

2 MS. SCHMID: Pardon me.

3 COMMISSIONER BOYER: Mr. Walje, you know, may
4 have not been the, you know, the best witness to bring
5 this in, inasmuch as he wasn't prepared on it.
6 Nonetheless, with the clarifications that Ms. McDowell
7 has made as to the fact that these are unadjusted and
8 so on and so forth, we're gonna let them in and give
9 them appropriate weight. Thank you. And that -- this
10 is UAE Cross Exhibit 1?

11 MR. DODGE: Yes.

12 COMMISSIONER BOYER: Okay. It will be
13 admitted.

14 MR. DODGE: (RoR) or ROE, however you
15 designated them. I assume to keep them straight from
16 the others.

17 COMMISSIONER BOYER: Let's call it UAE
18 Cross 1(RoR.)

19 Okay. Now that brings to us Mr. Ball. Have
20 you questions for Mr. Walje?

21 MR. BALL: No, thank you.

22 COMMISSIONER BOYER: Okay. Commissioners?
23 Commissioner Campbell?

24 COMMISSIONER CAMPBELL: The one question I
25 have is, as we've sat here in the hearing room today

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1 we typically look at ROE based on comparable
2 companies. And your testimony suggests that we look
3 at utility and then adjust that up or down, based on
4 history or based on where you were and where you are.

5 Let me ask you this. You stated a number of
6 risks and those risks. Do you believe those risks are
7 captured in bond ratings of your company?

8 THE WITNESS: Commissioner Campbell, I'm not,
9 I think, technically qualified to answer that. I've
10 not analyzed what our bond ratings are versus my
11 qualitative testimony. So I think I would have to
12 leave that to either Witness Hadaway or Williams. I
13 mean --

14 COMMISSIONER CAMPBELL: I'll stop there.

15 COMMISSIONER BOYER: Just a couple of
16 questions since you walked all the way over here,
17 Mr. Walje. How does -- how's capital structure
18 determined in your company?

19 Does an edict come down from Omaha? Do you
20 have meetings on it? Does it just evolve based on the
21 needs of the company at a particular point in time?
22 How does that happen?

23 THE WITNESS: Well, there are no edicts that
24 come down from anybody. I think the capital structure
25 evolves as we go through our business planning process

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1 and we try to determine what our level of capital
2 investment needs to be. Also what we believe our
3 operating costs are going to be.

4 Then our financial group takes a look at what
5 would be an appropriate capital structure, according
6 to what our business plan indicates. And that's an
7 intricate process.

8 COMMISSIONER BOYER: Okay, thank you.
9 Earlier this morning I asked a couple of the witnesses
10 questions about capital structure. And I asked in
11 essence whether or not there's any relationship
12 between capital structure and cost allocation, risk
13 allocation between shareholders and customers.

14 THE WITNESS: I do not recall us having any
15 of those specific types of conversation about how
16 we're, how we're assigning risk within our capital
17 structure between either our owners, the people who
18 provide us debt capital, or consumers.

19 COMMISSIONER BOYER: How do you respond to
20 Mr. Ball's suggestion that the failure to build
21 generation in the late '90's exposed customers to
22 risk, which then in turn results in a lower return?

23 THE WITNESS: Well, I guess I would answer
24 that we always try to plan our investments so they are
25 closer to just-in-time delivery for when that asset is

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1 needed, whether it be distribution, transmission, or
2 generation.

3 Because I don't think it's the right decision
4 for our customers for us to build a significant margin
5 in advance. And we would be arguing about that in a
6 rate case as well. So we do try to plan our
7 investments to be contemporaneous with when we need
8 the asset in order to serve customers.

9 COMMISSIONER BOYER: You've gone on at some
10 length to talking about risks unique to PacifiCorp and
11 this current load growth, so on. The environment in
12 which we live. Are there ways, other than increasing
13 return on equity, of addressing that kind of risk?

14 THE WITNESS: Well, some of the things that
15 Mr. Ball touched on would be a, a farther-looking test
16 period that would better align our costs with our
17 revenues.

18 Also, most of our states who are facing this
19 kind of growth or uncertainty, such as Wyoming, have
20 some form of power cost adjustment mechanism. So
21 those things would be, I think, tools that we might be
22 able to use to manage our costs a little bit
23 differently and would provide us with less business
24 risk.

25 (A recess was taken from 2:30 to 2:39 p.m.)

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1 COMMISSIONER BOYER: Okay, we're back on the
2 record. I think you had finished answering my last
3 question, Mr. Walje, or.

4 THE WITNESS: I believe so, yes.

5 COMMISSIONER BOYER: Okay, good.
6 Commissioner Campbell has one more question, or one
7 more line of questioning.

8 COMMISSIONER CAMPBELL: I'm just gonna try to
9 rephrase my question.

10 THE WITNESS: Okay.

11 COMMISSIONER CAMPBELL: And that is, you have
12 enumerated a number of business risks.

13 THE WITNESS: Yes.

14 COMMISSIONER CAMPBELL: That have increased
15 since the last time you were granted an ROE.

16 THE WITNESS: (Moves head up and down.)

17 COMMISSIONER CAMPBELL: How do you factor
18 into your analysis general credit markets, and the
19 cost of capital in global credit markets going down?

20 THE WITNESS: I think the way we try to
21 address this is through looking at a range of
22 comparable companies. Seeing what aspects that we can
23 pick out there that we think are the same and things
24 that are different.

25 I think the technical question about global

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1 prices going down is something that I'm not actually
2 equipped to, to answer specifically. Other than to
3 say that we do target a regular bond rating as we try
4 to analyze where we're headed to balance a little bit
5 of the risks associated with shareholders, and
6 customers, and debt holders.

7 But we, we do take a look at those other
8 companies and try to distinguish business risk or
9 regulatory risk that they're facing as we ask for, as
10 we ask for our rate of return.

11 COMMISSIONER CAMPBELL: So your analysis was
12 solely to point out risks that you've seen increased
13 within your company, without taking into account some
14 of these other factors?

15 THE WITNESS: That's correct. Since I've
16 worked around the company since 1972 I've seen a lot
17 of different aspects of the history. And I think
18 beyond Mr. Ball.

19 And having come -- returned to Utah four
20 years ago, the business environment is distinctly
21 different than it was when I returned. And that was
22 really the only point I was trying to make in my
23 qualitative testimony.

24 COMMISSIONER BOYER: Okay. Ms. McDowell,
25 anything further for Mr. Walje?

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1 MS. McDOWELL: No, Commissioner Boyer. Thank
2 you.

3 COMMISSIONER BOYER: Okay. As I indicated at
4 the beginning of the hearing, we won't be issuing a
5 separate order on ROE, or return. That will be part
6 of our order in the case in chief. So that will
7 conclude our hearing today.

8 And I notice we have some friends in the back
9 pew who will be here tomorrow. And take, take note of
10 how we conducted today's hearing, because we may try
11 the same thing tomorrow. In fact, probably will.

12 Mr. Walje, thank you so much, you may be
13 excused. And that will conclude this hearing.

14 (The hearing was concluded at 2:42 p.m.)

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C E R T I F I C A T E

STATE OF UTAH)
) ss.
COUNTY OF SALT LAKE)

This is to certify that the foregoing proceedings in the matter of Docket No. 07-035-93 were taken before me, KELLY L. WILBURN, a Registered Professional Reporter and Notary Public in and for the State of 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, numbered 1 through 170, 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.

WITNESS MY HAND AND OFFICIAL SEAL AT KEARNS, UTAH THIS 31st DAY OF May, 2008.

Kelly L. Wilburn, CSR, RPR
My Commission Expires:
May 16, 2009

Kelly L. Wilburn, CSR, RPR
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