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VIA ELECTRONIC FILING

PUC Filing Center
Public Utility Commission of Oregon
PO Box 2148
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**Re: PacifiCorp's Direct Testimony on Reconsideration
Docket UE 170 (RECON)**

Enclosed for filing is an original and five copies of PacifiCorp's Direct Testimony on Reconsideration in the above-referenced proceeding. A copy of this filing was served on all parties to this proceeding as indicated on the attached certificate of service.

Very truly yours,

A handwritten signature in black ink, appearing to be "Katherine A. McDowell", written over a horizontal line.

Katherine A. McDowell

KAM:knp
Enclosures
cc: Service List

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

UE 170 (RECON)

DIRECT TESTIMONY ON RECONSIDERATION

February 2006

UE 170 (RECON)
PPL Exhibit 1702
Witness: Doug Larson

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

Direct Testimony of Doug Larson on Reconsideration

Policy

February 2006

1 **Q. Are you the same Doug Larson who testified as the policy witness in this**
2 **proceeding?**

3 A. Yes.

4 **Q. What are the purposes of your testimony on reconsideration?**

5 A. I will give an overview of the Company's position in this reconsideration proceeding
6 and introduce the Company's witnesses on reconsideration. I will also address three
7 substantive matters: (1) the relationship of this reconsideration proceeding to the
8 general rate case PacifiCorp plans to file in Oregon in the near future; (2) why the
9 impending acquisition of PacifiCorp by MidAmerican Energy Holdings Company
10 (MEHC) is a known and measurable change which eliminates the basis for the tax
11 adjustment; and (3) the importance of the Company's request for deferred accounting,
12 docketed as UM 1229, in terms of granting PacifiCorp complete and meaningful
13 relief on reconsideration.

14 **Overview of PacifiCorp's Reconsideration Case**

15 **Q. Please explain PacifiCorp's position on reconsideration.**

16 A. In granting reconsideration of Order 05-1050 ("the Rate Order"), the Commission
17 indicated that it would review three issues: the applicability of SB 408 to this case,
18 the proper application of SB 408 in this case, and whether a SB 408 adjustment in this
19 case would result in rates that fall below the "fair, just and reasonable" standard
20 contained in ORS 756.040.

21 The Company's position is that SB 408 is inapplicable to this case for a whole
22 host of reasons, not the least of which is that SB 408 expressly applies only to post-
23 2006 tax collected and paid and the Rate Order resulted in rates effective in 2005.

1 Even if SB 408 does apply, there are a number of known and measurable changes for
2 2006 that eliminate or dramatically reduce the size of the adjustment. Finally,
3 PacifiCorp's current rate levels in Oregon do not have headroom to meet the fair, just
4 and reasonable standard if these rates are reduced based upon consolidated tax issues.
5 This was made clear by the recent downgrade in PacifiCorp's credit rating linked
6 directly to the Rate Order.

7 Larry Martin, PacifiCorp's Senior Tax Director, addresses the inapplicability
8 of SB 408 to this case. My testimony demonstrates that even if SB 408 is applicable,
9 a tax adjustment based upon continued PHI/ScottishPower ownership cannot be
10 sustained under ratemaking conventions requiring adjustments for known and
11 measurable changes and normalization of temporary circumstances within the test
12 period. Alternatively, Mr. Martin addresses the proper calculation of a SB 408
13 adjustment that assumes continued PHI/ScottishPower ownership, pointing out
14 significant updates to and errors and omissions in the Commission's calculation of the
15 tax adjustment in the Rate Order.

16 Finally, Bruce Williams, PacifiCorp's Treasurer, demonstrates how a
17 consolidated tax adjustment in this case results in rates that fall below the fair, just
18 and reasonable threshold, and submits evidence of the financial harm PacifiCorp has
19 suffered due to the Rate Order.

20 **Relationship of Reconsideration Proceedings and 2006 Oregon General Rate Case**

21 **Q. Does PacifiCorp intend to file a general rate case in Oregon in 2006?**

22 A. Yes. Consistent with national trends, PacifiCorp's costs continue to rise. Investment
23 pressures directly related to serving customers continue to mount, and as Mr.

Williams demonstrates in his testimony, PacifiCorp's earnings and financial ratios remain well below industry averages. PacifiCorp intends to file a general rate case in Oregon in early 2006.

Q. How does the Company intend to treat its tax expense in that filing?

A. The Company intends to seek the full amount of its tax expense, essentially reversing the tax adjustment in the Rate Order. Assuming the reconsideration proceedings result in the Commission eliminating its UE 170 tax adjustment, the effect in the new rate case would be an increase in the authorized revenues reflected and a decrease in the rate increase requested.

Q. Will that filing moot this reconsideration proceeding?

A. No, for several reasons. First, the effective date for rates resulting from a new rate case would be 10 months from the date of filing. This reconsideration proceeding is scheduled to be completed in June, resulting in a potential restoration of PacifiCorp's full tax expense much earlier in the year. Second, the Company has filed for deferred accounting to recover its full tax expense assuming that the Commission grants reconsideration. Resolution of the deferred accounting request is therefore contingent upon resolution of the reconsideration motion. Third, the test years in the two cases are different. UE 170 is based upon a 2006 calendar year test year (CY06) and the new rate case will be based upon a 2007 calendar year test year.

Impact of MEHC Acquisition of PacifiCorp

Q. Is the Commission required to consider known and measurable changes to PacifiCorp's corporate structure and tax expense in 2006 before making a tax adjustment?

1 A. Yes. Regulatory conventions require the Commission to set rates at a level that will
2 be representative of costs and revenues in the future test period, in this case CY06.
3 Thus, the Commission must consider PacifiCorp's known and measurable changes
4 for its corporate structure and tax expenses in 2006. The Commission must also
5 normalize out circumstances that exist for only a short period in the test year and are
6 not expected to recur.

7 **Q. Are there material known and measurable changes to PacifiCorp's corporate**
8 **structure and tax expense in 2006?**

9 A. Yes. ScottishPower's sale of PacifiCorp to MEHC is now on track to close early in
10 2006. All federal agencies, FERC, Department of Justice and NRC, and two states,
11 Utah and Wyoming, have approved the transaction. By February 28, 2006, the end of
12 the suspension period in UM 1209, PacifiCorp hopes to receive an Oregon order
13 approving the transaction based upon an unopposed Stipulation among all major
14 parties to the case which was filed in December. PacifiCorp expects approval orders
15 from the remaining states in the same timeframe.

16 Well before resolution of these reconsideration proceedings, PacifiCorp
17 expects its ownership structure to change and it will no longer contribute any income
18 to the PHI affiliated group. This change completely eliminates the evidentiary basis
19 for the consolidated tax adjustment made in this case.

20 **Q. Should the Commission normalize PacifiCorp's 2006 tax expense by eliminating**
21 **the ScottishPower-related consolidated tax adjustment?**

1 A. Yes. The adjustment is based upon circumstances that will exist for only a few
2 months in 2006 and will not recur. The consolidated tax adjustment cannot be
3 sustained as a legitimate adjustment to costs in the CY06 test year.

4 **Importance of Company's Deferred Accounting Application**

5 **Q. Has the Company filed an application for deferred accounting in conjunction**
6 **with these reconsideration proceedings?**

7 A. Yes. This application was docketed as UM 1229.

8 **Q. Why did the Company file this application?**

9 A. Because of the rule against retroactive ratemaking, the Company needs the
10 Commission to approve its request for deferred accounting if it is to ultimately
11 recover its lost revenues associated with the tax adjustment. Otherwise, even if the
12 Commission vacated or modified the tax adjustment in the case, PacifiCorp's relief
13 would be on a prospective basis only and it would not be made whole for its lost
14 revenues.

15 **Q. Why is full recovery through the deferred accounting application a good**
16 **outcome from a policy perspective if the Commission vacates or reduces the tax**
17 **adjustment?**

18 A. The suspension period in this case made rates effective in early October 2005. In
19 granting reconsideration, the Commission acknowledged that it needed additional
20 proceedings to fully understand the application and operation of SB 408 in this case.
21 Thus, through the reconsideration process, the Commission has effectively extended
22 the suspension date indefinitely on the tax issue. While PacifiCorp agrees that
23 additional proceedings are necessary to resolve the SB 408 issues in this case, they

1 should not come at the expense of revenues to which PacifiCorp was otherwise
2 entitled in October 2005. These revenues are material, amounting to approximately
3 \$500,000 per week.

4 **Q. Are there other fairness issues that weigh in favor of granting the deferred**
5 **accounting application if the Commission vacates or modifies the tax**
6 **adjustment?**

7 A. Yes. By its terms, SB 408 is applicable only to taxes collected and paid after 2006.
8 The Commission implemented the tax adjustment in 2005. The theory that
9 PacifiCorp can eventually recoup any under recovery in tax revenues through the
10 automatic adjustment clause is simply inapplicable to the 2005 under recovery period.
11 The theory provides little comfort for the early months of 2006, as well, given the
12 consensus that the automatic adjustment clause will not begin to operate until after
13 the 2007 tax report. The effect of a denial of deferred accounting on the basis that
14 PacifiCorp can theoretically recoup these amounts in the automatic adjustment clause
15 results in an uncompensated delay in recovery of actual tax expenses of nearly two
16 years.

17 As Mr. Williams discusses, the Rate Order has caused the Company
18 significant harm in the financial community, including a ratings downgrade and
19 degradation of financial ratios. An order in this proceeding reconsidering the tax
20 adjustment and allowing PacifiCorp a deferral to recover lost revenues associated
21 with that adjustment is necessary to restore investor confidence in the Company.

22 **Q. Does this conclude your testimony?**

23 A. Yes, it does.

UE 170 (RECON)
PPL Exhibit 1303
Witness: Larry O. Martin

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

Direct Testimony of Larry O. Martin on Reconsideration

Tax

February 2006

1 **Q. Are you the same Larry Martin who previously filed rebuttal testimony and**
2 **sursurrebuttal testimony in this proceeding?**

3 A. Yes.

4 **Q. What are the purposes of your testimony?**

5 A. My previous testimony explained why a consolidated tax adjustment based upon
6 PHI's interest deduction was unfounded and inappropriate in this case. My testimony
7 in these reconsideration proceedings demonstrates why this remains true,
8 notwithstanding the enactment of Senate Bill 408 ("SB 408") in the last days of this
9 case. The consolidated tax adjustment is not mandated by SB 408, nor even
10 consistent with key provisions of that legislation.

11 My reconsideration testimony also addresses how the Commission should
12 apply SB 408 or "its principles" in this case if it concludes that the law applies,
13 notwithstanding PacifiCorp's arguments to the contrary. As an alternative to the
14 testimony of Mr. Larson showing that the expected change in PacifiCorp ownership
15 eliminates the basis for the tax adjustment made in Order 05-1050 (the "Rate Order"),
16 I analyze the tax adjustment assuming continued ScottishPower/PHI ownership. I
17 demonstrate that the Commission's disallowance of \$26.63 million did not take into
18 account known and measurable changes for calendar year 2006 (CY06) and was
19 inaccurately calculated. I show that the original adjustment made by the
20 Commission, when calculated with an appropriate allocation factor and using actual
21 CY06 interest rates and offsets for tax liability associated with the interest, would be
22 approximately \$1.6 million on an Oregon-allocated basis, which is approximately
23 \$2.6 million on a grossed-up basis.

Inapplicability of SB 408

Q. Does SB 408 apply to this rate case?

A. No. SB 408 creates an automatic adjustment clause (AAC) to true-up taxes collected in rates after January 1, 2006 to actual taxes paid to units of government. It does not purport to address the calculation of tax expense in base rates, and does not apply to UE 170, a case that resulted in rates effective in 2005. The premise of SB 408, which is that an AAC is the means by which actual taxes and taxes in rates are trued-up, is inconsistent with a Commission decision forecasting such a “truing up” adjustment in base rates.

Q. If the Commission has the discretion to apply SB 408 to this case, should it exercise that discretion?

A. No. By its terms, SB 408 applies only to taxes collected in rates and taxes paid after January 1, 2006. Information on 2006 taxes collected and paid will not be available until 2007. For this reason, parties to the SB 408 rulemaking, AR 499, all agreed that the SB 408 tax reports filed in 2005 and 2006—which contain pre-2006 data—“are for the sole purpose of determining whether there is a trigger for the automatic adjustment clause, not to support a rate change.” *See* Department of Justice letter to AR 499 participants (October 7, 2005). The parties also agreed that “even if the Commission may use forecast data for the automatic adjustment clause, it should, as a matter of policy, use only historic data.” *Id.*

The result of this consensus interpretation is that SB 408 tax adjustments will not occur until after the 2007 tax report, more than two years after the Commission’s consolidated tax adjustment in this case, because an earlier implementation could

1 violate the terms of the bill and/or good regulatory policy. All parties to the
2 rulemaking also concur that, as a policy matter, SB 408 automatic adjustments should
3 be made in a backward-looking manner based upon post-2006 historical data, not the
4 forward-looking approach used in this case.

5 **Q. Was the Commission's reliance on SB 408 faulty and incomplete?**

6 A. Yes. The tax adjustment looked only at one aspect of PacifiCorp's consolidated taxes
7 and was not based upon a determination that PHI's tax benefits were "properly
8 attributed" to PacifiCorp. Indeed, because the Commission has yet to define how
9 consolidated taxes are to be attributed to the regulated utility, it is impossible for the
10 Commission to establish whether the attribution of some part of PHI's interest
11 deduction to PacifiCorp is proper under SB 408.

12 Further, in calculating an adjustment under SB 408, the Commission must
13 compare taxes paid to taxes authorized to be collected in rates. In this comparison,
14 the Commission must add back to the taxes paid calculation certain tax elements,
15 including deferred taxes, tax settlement payments and charitable contributions. The
16 consolidated tax adjustment made in this case considered none of these matters,
17 including settlement payments to units of government in FY05 (for years other than
18 FY05), which totaled in excess of \$70 million, deferred taxes of \$44 million related to
19 PacifiCorp and charitable contributions of \$435,000.

20 **Proper Calculation of the Commission's SB 408 Adjustment Assuming Continued**

21 **PHI/ScottishPower Ownership**

22 **Q. Please explain your statement that the disallowance was based on an inaccurate**
23 **calculation.**

1 A. In the Rate Order, the Commission calculated the adjustment by apportioning to
2 PacifiCorp a percentage of the fiscal year 2005 (FY05) PacifiCorp Holdings, Inc.
3 (“PHI”) interest deduction based on PacifiCorp’s contribution of “gross profits” to the
4 PHI affiliated group. This calculation resulted in an allocation of 91.5% of the PHI
5 interest deduction to PacifiCorp. As the Commission notes in the Rate Order,
6 however, taxes are based upon net taxable income, not gross profits. Gross profits,
7 which exclude expenses and deductions, are not a recognized method to apportion
8 consolidated taxes. As I stated in my sur-surrebuttal testimony, and as intimated by
9 the Commission in its order, relative taxable income is a rational apportionment
10 factor; gross profits are not.

11 **Q. Are there any provisions of SB 408 that support use of a gross profits attribution**
12 **methodology?**

13 A. No.

14 **Q. Has any party to AR 499 suggested that consolidated taxes be attributed to**
15 **PacifiCorp using a gross profits methodology?**

16 A. No. All suggested approaches to allocation of consolidated taxes assume the use of
17 relative taxable income or relative tax liability as the basis for the attribution
18 calculation.

19 **Q. What was PacifiCorp’s contribution to the PHI group’s taxable income in**
20 **FY05?**

21 A. Based upon PacifiCorp’s FY05 federal tax return, which was filed on December 15,
22 2005, PacifiCorp contributed 50% of PHI’s group taxable income in FY05.

23 **Q. Was this relative taxable income percentage available earlier?**

1 A. No. I had previously estimated this percentage, but the final numbers from
2 PacifiCorp's FY05 federal tax return were not available at the time of my earlier
3 testimony in this case.

4 **Q. Is PacifiCorp's contribution to the PHI group's taxable income expected to**
5 **increase in CY06?**

6 A. No. It is expected to decrease based upon projected revenue increases for
7 nonregulated affiliates within the PHI consolidated group, potential corporate
8 restructuring and the sale of PacifiCorp to MidAmerican Energy Holdings Company
9 ("MEHC").

10 **Q. The Commission's Rate Order indicates that the PHI interest deduction is a**
11 **"constant" that SB 408 requires the Commission to pass on to customers. Is this**
12 **true?**

13 A. No. Over the past several years, the interest deduction has decreased significantly. In
14 2006, it is expected to decrease even further and then disappear upon closing of
15 MEHC's purchase of PacifiCorp.

16 **Q. Which known and measurable changes in CY06 should be reflected in any**
17 **consolidated tax adjustment based upon PHI's interest deduction?**

18 A. First, the Commission's Rate Order should account for a change in the PHI debt
19 structure, which occurred on September 22, 2005, and which will decrease PHI's
20 interest deduction in the test year. This change decreased the level of interest that
21 PHI will pay in CY06 to \$136 million, which is significantly less than the
22 \$160 million assumed by the Commission in the calculation of the disallowance. The

1 current debt is \$2.731 billion at 4.97688% interest. The interest rate is effective for
2 90 days from the end of December 2005.

3 Second, the Rate Order also failed to consider the offsetting effect of
4 ScottishPower's tax payments in CY06. The Rate Order concluded that the PHI
5 interest deduction would decrease the CY06 tax liability of PacifiCorp's corporate
6 family by 37.95%. This is not true. In fact, the PHI interest deduction will decrease
7 the CY06 tax liability of PacifiCorp's corporate family by only 7.95%. As a result of
8 the passage of the UK Finance Act of 2005, ScottishPower now pays taxes at a rate of
9 30% on the PHI interest payments. Thus, ScottishPower will pay taxes at a rate of
10 30% in CY06 on any PHI interest payments it receives.

11 **Q. Why should the Commission consider ScottishPower's tax payments?**

12 A. ScottishPower's tax payments are actual tax payments made to units of government
13 on the PHI interest, which must be considered under SB 408 or "its principles."
14 Furthermore, ScottishPower is PHI's only shareholder and therefore PacifiCorp's
15 ultimate shareholder. The notion that underlies the disallowance—*i.e.*, that PHI or
16 the PHI group receives an economic windfall benefit from the PHI tax deduction
17 which should be returned to customers—is unfounded. Not only does PHI suffer a
18 burden that creates the deduction (it makes the interest payment), ScottishPower pays
19 tax on the income it receives from PHI. Thus, the alleged economic benefit to the
20 PHI group of the interest deduction cannot be more than the difference between the
21 PHI tax savings and the ScottishPower tax burden. There is no sound legal or policy
22 basis under SB 408 or otherwise to impute a larger tax benefit than actually exists and
23 then allocate a portion of that phantom tax benefit to customers.

1 **Q. You state that the Commission's adjustment, when calculated with a correct**
2 **allocation factor and considering known and measurable changes in the CY06**
3 **test year, should be \$2.6 million on an Oregon-allocated and grossed-up basis.**

4 **How exactly did you calculate this figure?**

5 A. The figure is derived as follows: ((PHI interest deduction * combined U.S. effective
6 tax rate) – (PHI interest payment * UK tax rate)) * Percentage of PHI group taxable
7 income from PacifiCorp * Oregon allocation factor on an SNP basis * tax gross-up
8 factor = adjustment to revenue requirement. In numeric form, the calculation is as
9 follows: $((\$136m * 37.95\%) - (\$136m * 30\%)) * 50.3095\% * 28.8723\% = 1.570m *$
10 $1.657 = \$2.602$ million.

11 The calculation demonstrates that there are a number of issues with the
12 Commission's tax adjustment, each of which materially reduce the amount of the
13 adjustment, and taken together, result in a decrease of the adjustment to 10% of its
14 original amount.

15 **Q. Does this conclude your direct testimony on reconsideration?**

16 A. Yes, it does.

UE 170 (RECON)
PPL Exhibit 317
Witness: Bruce Williams

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

Direct Testimony of Bruce Williams on Reconsideration

February 2006

1 **Q. Are you the same Bruce Williams who previously filed direct, rebuttal and sur-**
2 **surrebuttal testimony in this proceeding?**

3 A. Yes.

4 **Q. What are the purposes of your direct testimony on reconsideration?**

5 A. My testimony demonstrates that the Commission's disallowance of \$26.63 million,
6 on an Oregon-allocated and grossed-up basis, in Order No. 05-1050 ("the Rate
7 Order") will result in a significantly negative impact on the return on equity the
8 Company would have any reasonable expectation of earning. These results
9 demonstrate that the Commission's tax adjustment in this case leads to rates which
10 fall below the "fair, just and reasonable" rate standard required by SB 408. Further, I
11 will explain the risk of a downgrade in the Company's credit rating as a result of the
12 Rate Order, a risk that was recently realized when Fitch Ratings lowered PacifiCorp's
13 credit rating from "A-" to "BBB+", citing the "unfavorable final order" in UE 170.

14 **Q. What is the source of the "fair, just and reasonable" rate standard you**
15 **reference?**

16 A. ORS 756.040 requires the Commission to set rates that are "fair, just and reasonable."
17 The Attorney General's legal opinion on SB 408 interpreted the "fair, just and
18 reasonable" standard as a cap on utilities' exposure to rate reductions under SB 408.
19 (Letter to Lee Beyer from Attorney General Hardy Myers at 16 (December 27,
20 2005)). The Commission's order on reconsideration directed review of whether the
21 Order's tax adjustment results in rates that violate the "fair, just and reasonable"
22 standard in ORS 756.040.

1 **Q. Is this a different interpretation of the “fair, just and reasonable” standard than**
2 **that set forth in the Commission’s Rate Order?**

3 A. Yes. In its Rate Order, the Commission construed SB 408’s reference to the “fair,
4 just and reasonable” standard as mandating immediate implementation of SB 408 or
5 “its principles” in PacifiCorp’s base rates. In contrast, the Attorney General’s
6 Opinion makes clear that the “fair, just and reasonable” standard is one that protects
7 utilities against rate reductions under SB 408. The standard, in other words, is a
8 shield for utilities, not a sword to justify premature or overbroad implementation of
9 SB 408.

10 **Q. Have you considered the impact the Rate Order will have on PacifiCorp’s**
11 **financial position?**

12 A. Yes. The impact on PacifiCorp is significantly negative for several reasons. First,
13 the Company will have no reasonable opportunity to earn the authorized 10% return
14 on equity that was stipulated to and approved in the Order. Based on Oregon
15 normalized results of operations for the test period of 12 months ending
16 December 31, 2006, the Company’s projected return on equity will be 8.4%; that is,
17 160 basis points lower than the approved 10%, based on the \$16.07 million tax
18 expense adjustment. That disparity is due to the fact that in arriving at the tax
19 adjustment, the Commission essentially assumed that the Company will not have that
20 tax expense, which as explained by Larry Martin in his Direct Testimony on
21 Reconsideration, is erroneous. The Company’s actual results for calendar year 2006
22 will not have the benefit of the \$16.07 million interest deduction assumed by the
23 Commission.

1 **Q. Please explain these results in the context of PacifiCorp's overall financial**
2 **position.**

3 A. The Company has chronically under earned over the past several years as it has faced
4 increased costs related to power costs, pensions, benefits, insurance and other external
5 cost drivers, while its investment needs to serve load and maintain system reliability
6 have also grown. For instance, PacifiCorp's semi-annual report for the year ended
7 March 31, 2005 showed its unadjusted Oregon return on equity to be 7.07%, and its
8 adjusted return on equity to be 6.895%. The Commission's Rate Order ensures that
9 this ultimately unsustainable pattern of under earning could continue under the rates
10 in effect pursuant to the Rate Order, as the authorized return on equity is now
11 effectively 8.4%.

12 **Q. How do these returns compare to utility averages?**

13 A. These returns are far below the US industry average of 11.3% for the 12 months
14 ending September 30, 2005. Based on Regulatory Research Associates, Inc.'s
15 January 2, 2006 ranking of industry equity returns, PacifiCorp's Oregon earned return
16 on equity of 6.895% places it 45th out of 48 utilities listed with measurable returns.
17 Exhibit PPL/318. Instead of aggressively addressing this situation by increasing
18 PacifiCorp's rates to "fair, just and reasonable" levels, the Rate Order has lowered
19 earnings and returns even further by setting rates with an effective authorized return
20 on equity of 8.4%.

21 **Q. Does the reduction in tax expense and earnings suggest the possibility of future**
22 **downward adjustments in tax expense and earnings?**

1 A. Yes. The tax expense disallowance may have an additional adverse impact on the
2 Company's risk profile as a result of the under earning it causes. With less earnings,
3 the Company will have less income tax expense, leading to further downward
4 pressure on rates. Further rate reductions in turn will increase the Company's risk.

5 **Q. What is the likely impact of the reduced return on equity?**

6 A. A return on equity of 8.4% is not commensurate with returns on investment in other
7 enterprises having corresponding risk. Normally, a return on equity should be
8 sufficient to assure confidence in the financial integrity of a utility so as to allow the
9 utility to attract capital. In a case, such as here, where the effective return on equity is
10 set too low, the utility is diminished in its capacity as an investment. If the utility, as
11 a result, receives less investment support from its parent company, it may have to take
12 on additional debt, which results in higher costs of borrowing and could lead to
13 higher utility rates.

14 **Q. Is a reduced return on equity the only impact of the tax expense disallowance?**

15 A. No. In addition to the impact on return on equity, the disallowance also negatively
16 impacts key financial ratios underlying PacifiCorp's credit rating. Without the
17 disallowance, PacifiCorp's ratios were already sufficiently borderline between its
18 current "A-" credit rating by Standard & Poor's ("S&P") and a "BBB" rating that it
19 has been necessary to rely upon the benefit from ScottishPower ownership in order to
20 avoid a downgrade. As the table below illustrates, however, the negative change in
21 those ratios heightens the risk of an S&P downgrade as PacifiCorp moves further
22 down the scale of "BBB" ratios. The table below compares the key financial ratios
23 that result from the Rate Order to the S&P benchmarks.

| | | Oregon | | | |
|--|--------------------|------------|---------------|-------------------|------------|
| | S&P Guideline for | Normalized | Pass/Fail 'A' | S&P Guideline | Indicative |
| | A Rating Category* | Result** | Guideline? | For BBB Category* | Rating |
| | FFO/ 4.5x – 3.8x | 3.6x | Fail | 3.8x - 2.8x | high BBB |
| | Interest | | | | |
| | FFO/ 30% – 22% | 17% | Fail | 22% - 15% | low BBB |
| | Total Debt | | | | |
| | Debt/ 42% – 50% | 56% | Fail | 50% - 60% | mid BBB |
| | Capitalization | | | | |

*for Business Position 5 (i.e. PacifiCorp)

**includes S&P adjustments for imputed debt

What this comparison shows is that based on the metrics used by S&P in establishing credit rating for a company such as PacifiCorp, a mid-“BBB” to weak-“BBB” rating would likely be given. In its most recent ratings report dated January 30, 2006, S&P reaffirmed its position that “PacifiCorp’s standalone financial metrics are weak for its current “A-” CCR.” Exhibit PPL/319 at 1.

Q. Please explain the risks of weak credit metrics such as these.

A. It is important to note that being just barely within the S&P guidelines’ ranges is not a preferred position, since it does not leave the Company acceptable “headroom” in the event of unusual and significant occurrences, such as the power cost upswing of 2000-2001. It is best to be positioned such that anomalous events do not cause a change in credit rating due to the metrics moving outside the guidelines. Inadequate headroom exposes customers to increased risk of the adverse consequences of a credit rating downgrade.

Q. How do PacifiCorp’s financial ratios compare to the ratios of other utilities?

A. A review of PacifiCorp’s financial ratios for the last five years compared to industry average and to the reference group its uses for cost of capital purposes demonstrates

1 that PacifiCorp has significantly under performed in every year relative to both
2 comparators. Exhibit PPL/320. Even prior to the tax adjustment in this case, these
3 results raise serious questions about whether the ORS 756.040 standard was being
4 met in Oregon because PacifiCorp's returns are simply not comparable to others with
5 similar risk. The Rate Order widens the negative gap between PacifiCorp's financial
6 performance and that of other utilities.

7 **Q. What are the consequences of a credit rating downgrade?**

8 A. There are two primary impacts, both negative: higher cost of debt for the Company,
9 and reduced access to borrowed capital, at a time when PacifiCorp will need to invest
10 approximately one billion dollars per year for the next several years. The significant
11 impact for the Company's customers would be higher rates due to the higher cost of
12 capital, but there are additional impacts as well, such as reduced access to long-term
13 markets for power purchases and sales, increased PPA debt imputation to credit ratios
14 (debt imputation is calculated using the Company's current cost of debt) and more
15 onerous collateral requirements related to such transactions. Those more onerous
16 collateral requirements, which are potentially very substantial, can in turn put
17 constraints on the Company's ability to make investments in facilities for customers.
18 The costs of these impacts, especially in light of wholesale power market cost
19 increases, could far exceed the amount of the tax adjustment.

20 **Q. Has PacifiCorp's credit rating been lowered in response to the tax adjustment in**
21 **the Rate Order?**

22 A. Yes. On January 31, 2006, Fitch Ratings lowered PacifiCorp's credit rating on senior
23 unsecured debt to "BBB+" from "A-", noting "the unfavorable final order issued in

1 September 2005 by the Oregon commission in PPW's general rate case." According
2 to the ratings announcement, "the Oregon Public Utilities Commission's September
3 2005 order incorporating recently enacted tax legislation (Senate Bill 408) in PPW's
4 Oregon GRC is a serious matter for concern in Fitch's view." Fitch also noted that
5 the outcome of these reconsideration proceedings, as well as the permanent rules on
6 SB 408 "will affect PPW's future earnings and cash flows." Exhibit PPL/321 at 1-2.

7 **Q. Have you received other indications that the Rate Order will negatively impact**
8 **the Company's credit rating?**

9 A. Yes. Following issuance of the Order, S&P published a note on October 7, 2005,
10 regarding the Rate Order's tax disallowance, stating that "the ruling is adverse for
11 credit quality." Exhibit PPL/322 at 1. The note warned that in the future there could
12 be an adverse ratings action due to the disallowance. Whether an adverse ratings
13 action occurs will be dependent on a number of factors, including the provisions of
14 the permanent rules to be adopted for implementation of SB 408. S&P reiterated this
15 point in its most recent credit report, noting that "the ultimate outcome of the
16 permanent rules related to Oregon Senate Bill 408, passed in the fall of 2005, may
17 have implications for PacifiCorp's earnings and cash flow." Exhibit PPL/319 at 1.

18 **Q. Have other institutions expressed concern regarding the impact of the Rate**
19 **Order?**

20 A. Yes. Consistent with the concern reflected in the Fitch downgrade and the S&P
21 notes, representatives of Barclay's Bank, JP Morgan and BNP Paribas, all of whom
22 have substantial financial commitments to PacifiCorp, have expressed concerns to me
23 not only about the magnitude of the dollar impact from the disallowance, but also its

1 very nature, in that it flows to ratepayers the tax benefits of non-regulated affiliates.
2 That is, such an adjustment will tend to increase the risk profile of the Company in
3 that the performance of nonregulated affiliates may now impact the Company's rate
4 of return.

5 **Q. Have other institutions commented negatively on Oregon's regulatory**
6 **environment as a result of SB 408 and the Rate Order?**

7 A. Yes. Regulatory Research Associates, Inc. in its recent State Regulatory Evaluation
8 report, dated January 6, 2006, stated "we are lowering our rating of Oregon regulation
9 to Average/2 from Average/1 due to the potential negative ramifications of Senate
10 Bill 408, enacted in September 2005, that requires the flow through of consolidated
11 tax savings to ratepayers." Exhibit PPL/323 at 1.

12 **Q. What should the Commission do to ensure that PacifiCorp's rates are fair, just**
13 **and reasonable?**

14 A. The Commission should vacate the Rate Order's tax adjustment on the basis that it
15 produces rates that fall below the standard required by ORS 756.040 and allow a
16 deferred account to permit the Company to recover its associated lost revenues.

17 **Q. Does this conclude your testimony?**

18 A. Yes, it does.

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

Exhibit Accompanying Direct Testimony of Bruce Williams on Reconsideration

February 2006



UTILITY FOCUS



Regulatory Research Associates, Inc. -- 30 Montgomery Street -- Jersey City, New Jersey 07302 -- (201) 433-5507 -- FAX: (201) 433-6138

INDUSTRY STUDY

January 3, 2006

ELECTRIC UTILITY QUALITY MEASURES: Rankings and Trends Calendar Years 2000-2004 and 12 Months Ended September 30, 2005

This report is intended to enable the reader to assess the underlying financial quality of the electric utility industry and to provide an understanding of the status of the industry's financial quality in comparison with historical measures. We have calculated several quality measures for the 12 months ended September 30, 2005, for each of 53 "parent" electric utility companies, and have presented most of the data with comparable calculations for calendar-years 2000 through 2004. Table I, on pages 2 and 3, lists the actual current financial statement data from which most of the updated ratios were calculated. In addition, we have isolated the utility-specific financial data into a separate section for 96 electric operating companies only (Table XII, on pages 18 to 21). To help the reader assess the relative qualitative position of any specific company, we rank the 53 companies for each measurement (for the 12 months ended September 30, 2005) in order of highest-to-lowest quality. These current rankings are consolidated into Table II, on pages 4 through 6. By using the alphabetical and ranked tables as cross-references, the relative position of an individual company can easily be identified. There are 11 different quality measures listed in this report, and, in total, they utilize data from the companies' key financial documents--the income statement, the statement of cash flow, and the balance sheet. Below is an index of the tables in which the specific quality measurements are found, and the numbered pages on which each table is located. This report is published quarterly.

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(Text continued on page 16.)

Table VIII

RETURN on AVERAGE COMMON EQUITY

| Company | 12 mos. | | | | | | 5-Yr. Avg. 2000- 2004 | RANKING of RETURN on COMMON EQUITY | | | | |
|----------------|---------|------|------|------|------|------|--------------------------------|------------------------------------|----------------|-----------------------|----------------|------|
| | 9/05 | 2004 | 2003 | 2002 | 2001 | 2000 | | 12 Months:9/30/05 | | 5-Year Avg: 2000-2004 | | |
| | % | % | % | % | % | % | | Rank | % | | % | |
| ALLEG ENERGY | 10.5 | n.m. | n.m. | n.a. | 20.0 | 18.3 | n.m. | 1 | EXELON | 20.0 | PPL CORP | 25.3 |
| ALLETE | 1.7 | n.m. | 11.1 | 12.0 | 14.6 | 14.5 | 13.0 | 2 | SEMPRA ENERGY | 18.2 | EXELON | 20.8 |
| ALLIANT | 11.0 | 8.5 | 7.6 | 6.4 | 10.3 | 8.4 | 8.2 | 3 | PPL CORP | 18.1 | SEMPRA ENERGY | 19.3 |
| AMEREN CORP | 10.9 | 10.1 | 11.4 | 12.2 | 14.5 | 15.0 | 12.6 | 4 | AVISTA | 16.2 | DPL INC | 18.6 |
| AMER EL PWR | 13.1 | 11.2 | 12.4 | 12.5 | 13.4 | 10.4 | 12.0 | 5 | WPS RESOURCES | 15.7 | PS ENT GROUP | 15.9 |
| AVISTA | 16.2 | 4.7 | 6.7 | 4.5 | 9.4 | 14.6 | 8.0 | 6 | EDISON INTL | 15.5 | PG&E CORP | 15.8 |
| CENTERPOINT | n.m. | n.m. | n.m. | n.m. | 16.2 | 15.9 | n.m. | 7 | SOUTHERN CO | 15.1 | DUKE ENERGY | 15.6 |
| CH ENERGY | 8.4 | 8.7 | 9.1 | 8.3 | 10.4 | 10.5 | 9.4 | 8 | CLECO CORP | 15.0 | GREAT PLAINS | 15.6 |
| CINERGY | 11.2 | 11.4 | 12.6 | 14.1 | 15.3 | 14.8 | 13.7 | 9 | DOMIN RESOU | 14.9 | TXU | 15.5 |
| CLECO CORP | 15.0 | 12.1 | 11.3 | 12.8 | 14.3 | 14.5 | 13.0 | 10 | TECO ENERGY | 14.1 | SOUTHERN CO | 14.5 |
| CMS ENERGY | 9.2 | 8.5 | n.m. | n.a. | 8.3 | 12.4 | 9.8 | 11 | DUQUESNE LT | 13.6 | EDISON INTL | 14.1 |
| CON EDISON | 9.9 | 11.0 | 10.1 | 11.5 | 12.2 | 12.7 | 11.5 | 12 | PS ENT GROUP | 13.3 | DOMIN RESOU | 13.8 |
| CONSTELLATION | 11.3 | 12.6 | 11.9 | 10.7 | 11.7 | 11.9 | 11.8 | 13 | NSTAR | 13.2 | CINERGY | 13.7 |
| DOMIN RESOU | 14.9 | 14.0 | 13.9 | 14.9 | 13.9 | 12.3 | 13.8 | 14 | AMER EL PWR | 13.1 | DUQUESNE LT | 13.3 |
| DPL INC | 10.0 | 22.1 | 18.3 | 10.3 | 24.5 | 17.6 | 18.6 | 15 | FPL GROUP | 12.3 | NSTAR | 13.3 |
| DTE ENERGY | 10.1 | 7.8 | 11.1 | 13.7 | 11.6 | 12.3 | 11.3 | 16 | OGE ENERGY | 12.1 | FPL GROUP | 13.1 |
| DUKE ENERGY | 8.1 | 8.6 | 8.0 | 11.3 | 17.6 | 32.5 | 15.6 | 17 | SCANA CORP | 11.7 | ALLETE | 13.0 |
| DUQUESNE LT | 13.6 | 15.8 | 16.6 | 15.7 | 7.9 | 10.7 | 13.3 | 18 | VECTREN | 11.5 | CLECO CORP | 13.0 |
| EDISON INTL | 15.5 | 10.9 | 15.8 | 17.1 | 14.9 | 11.7 | 14.1 | 19 | WISC ENERGY | 11.4 | TECO ENERGY | 12.9 |
| ENERGY EAST | 8.8 | 9.2 | 8.2 | 10.5 | 13.4 | 14.9 | 11.2 | 20 | CONSTELLATION | 11.3 | AMEREN CORP | 12.6 |
| ENTERGY | 11.0 | 10.0 | 11.6 | 11.0 | 9.8 | 10.1 | 10.5 | 21 | CINERGY | 11.2 | WPS RESOURCES | 12.6 |
| EXELON | 20.0 | 20.5 | 21.0 | 19.5 | 18.6 | 24.5 | 20.8 | 22 | ALLIANT | 11.0 | PROG ENERGY | 12.4 |
| FIRSTENERGY | 10.1 | 10.3 | 7.5 | 11.9 | 12.1 | 13.0 | 11.0 | 23 | ENTERGY | 11.0 | VECTREN | 12.2 |
| FPL GROUP | 12.3 | 12.2 | 13.0 | 13.4 | 13.6 | 13.5 | 13.1 | 24 | AMEREN CORP | 10.9 | OGE ENERGY | 12.2 |
| GREAT PLAINS | n.m. | 16.9 | 15.4 | 17.0 | 11.6 | 17.0 | 15.6 | 25 | PG&E CORP | 10.9 | KEYSPAN CORP | 12.1 |
| HAWAII ELEC | 9.5 | 9.3 | 11.1 | 11.9 | 12.4 | 9.7 | 10.9 | 26 | PINNACLE WST | 10.7 | AMER EL PWR | 12.0 |
| IDACORP | 8.5 | 8.2 | 5.3 | 7.0 | 14.8 | 16.7 | 10.4 | 27 | ALLEG ENERGY | 10.5 | CONSTELLATION | 11.8 |
| KEYSPAN CORP | 10.5 | 11.7 | 12.1 | 13.2 | 12.1 | 11.7 | 12.1 | 28 | KEYSPAN CORP | 10.5 | SCANA CORP | 11.6 |
| NISOURCE | 7.8 | 9.4 | 9.8 | 12.0 | 7.7 | 13.6 | 10.5 | 29 | FIRSTENERGY | 10.1 | CON EDISON | 11.5 |
| NO'EAST UT | 6.1 | 7.7 | 7.1 | 6.4 | 8.6 | 9.9 | 7.9 | 30 | DTE ENERGY | 10.1 | PNM RESOURCES | 11.5 |
| NSTAR | 13.2 | 13.3 | 13.5 | 13.9 | 13.4 | 12.5 | 13.3 | 31 | DPL INC | 10.0 | WISC ENERGY | 11.4 |
| OGE ENERGY | 12.1 | 11.8 | 13.2 | 12.0 | 9.9 | 14.0 | 12.2 | 32 | CON EDISON | 9.9 | DTE ENERGY | 11.3 |
| PEPCO HOLDINGS | 8.0 | 8.7 | 7.1 | 10.1 | 10.8 | 9.9 | 9.3 | 33 | XCEL ENERGY | 9.9 | ENERGY EAST | 11.2 |
| PG&E CORP | 10.9 | 13.7 | 14.6 | 21.8 | n.m. | 13.1 | 15.8 | 34 | HAWAII ELEC | 9.5 | PINNACLE WST | 11.1 |
| PINNACLE WST | 10.7 | 8.5 | 8.1 | 12.1 | 13.9 | 13.2 | 11.1 | 35 | CMS ENERGY | 9.2 | XCEL ENERGY | 11.1 |
| PNM RESOURCES | n.m. | 7.9 | 7.5 | 7.0 | 17.7 | 17.2 | 11.5 | 36 | PUGET ENERGY | 9.1 | FIRSTENERGY | 11.0 |
| PPL CORP | 18.1 | 18.2 | 23.3 | 27.1 | 31.7 | 26.1 | 25.3 | 37 | PROG ENERGY | 8.9 | HAWAII ELEC | 10.9 |
| PROG ENERGY | 8.9 | 9.8 | 11.9 | 13.1 | 12.3 | 14.7 | 12.4 | 38 | ENERGY EAST | 8.8 | ENTERGY | 10.5 |
| PS ENT GROUP | 13.3 | 12.8 | 17.5 | 19.2 | 18.8 | 11.3 | 15.9 | 39 | WESTAR ENERGY | 8.8 | NISOURCE | 10.5 |
| PUGET ENERGY | 9.1 | 9.3 | 7.5 | 7.5 | 8.1 | 12.9 | 9.1 | 40 | IDACORP | 8.5 | IDACORP | 10.4 |
| SCANA CORP | 11.7 | 12.5 | 12.4 | 11.7 | 10.7 | 10.7 | 11.6 | 41 | CH ENERGY | 8.4 | UNISOURCE | 10.4 |
| SEMPRA ENERGY | 18.2 | 20.7 | 18.9 | 20.7 | 19.8 | 16.5 | 19.3 | 42 | DUKE ENERGY | 8.1 | CMS ENERGY | 9.8 |
| SIERRA PAC R | n.m. | n.m. | n.m. | n.a. | 4.9 | -2.8 | 1.1 | 43 | PEPCO HOLDINGS | 8.0 | CH ENERGY | 9.4 |
| SOUTHERN CO | 15.1 | 15.0 | 15.5 | 15.7 | 11.9 | 14.4 | 14.5 | 44 | NISOURCE | 7.8 | UIL HOLDINGS | 9.4 |
| TECO ENERGY | 14.1 | 10.2 | 7.7 | 13.2 | 16.7 | 16.6 | 12.9 | 45 | UIL HOLDINGS | 6.4 | PEPCO HOLDINGS | 9.3 |
| TXU | n.m. | 30.3 | 12.6 | 10.1 | 13.1 | 11.6 | 15.5 | 46 | NO'EAST UT | 6.1 | PUGET ENERGY | 9.1 |
| UIL HOLDINGS | 6.4 | 7.1 | 6.1 | 8.9 | 12.1 | 12.5 | 9.4 | 47 | ALLETE | 1.7 | ALLIANT | 8.2 |
| UNISOURCE | n.m. | 7.6 | 9.0 | 7.5 | 15.0 | 12.8 | 10.4 | 48 | CENTERPOINT | n.m. | AVISTA | 8.0 |
| VECTREN | 11.5 | 10.7 | 11.7 | 13.4 | 11.0 | 14.5 | 12.2 | 49 | PNM RESOURCES | n.m. | NO'EAST UT | 7.9 |
| WESTAR ENERGY | 8.8 | 10.0 | n.m. | n.a. | n.m. | 3.2 | 6.6 | 50 | UNISOURCE | n.m. | WESTAR ENERGY | 6.6 |
| WISC ENERGY | 11.4 | 11.6 | 12.0 | 12.8 | 11.8 | 8.9 | 11.4 | 51 | GREAT PLAINS | n.m. | SIERRA PAC R | 1.1 |
| WPS RESOURCES | 15.7 | 14.0 | 12.5 | 11.6 | 12.5 | 12.5 | 12.6 | 52 | TXU | n.m. | CENTERPOINT | n.m. |
| XCEL ENERGY | 9.9 | 10.0 | 10.0 | 9.1 | 13.4 | 13.1 | 11.1 | 53 | SIERRA PAC R | n.m. | ALLEG ENERGY | n.m. |
| 53-Co.Avg. | 11.3 | 11.8 | 11.7 | 12.5 | 13.4 | 13.5 | 12.6 | | | 11.3 | | 12.6 |

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

Exhibit Accompanying Direct Testimony of Bruce Williams on Reconsideration

February 2006



CLO

Print

Summary: PacifiCorp

Primary Credit Analyst:

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Rationale

Rationale

The 'A-' corporate credit rating (CCR) on PacifiCorp reflects the consolidated credit quality of the utility's ultimate parent, Scottish Power plc (A-/Stable/A-2). PacifiCorp's ratings remain on CreditWatch with negative implications following the May 2005 announcement that the utility would be acquired by MidAmerican Energy Holdings Co. (MEHC; BBB-/Watch Positive/-) for \$9.4 billion, consisting of \$5.1 billion in equity and the assumption of net debt and preferred stock of \$4.3 billion. The acquisition will be financed at the MEHC level, predominantly with equity. While final regulatory approval in each of the states PacifiCorp serves is pending, current indications suggest that the transaction may close on or before March 31, 2006.

MEHC has committed to regulators that it will structurally separate or "ring fence" PacifiCorp from MEHC. If PacifiCorp meets Standard & Poor's ring-fencing criteria, once the sale is completed, PacifiCorp's CCR could be higher than MEHC's CCR, but it would also reflect its standalone credit quality. The CreditWatch with negative implications indicates that PacifiCorp's standalone financial metrics are weak for its current 'A-' CCR. Under the settlements negotiated, MEHC has agreed to forgo dividends from PacifiCorp if PacifiCorp's common equity ratio is below 48.25% from the closing date of the transaction through Dec. 31, 2008. Other commitments include credits of up to \$142.5 million (if adopted by all states) that will reduce retail rates through 2010 to the extent that PacifiCorp does not achieve identified cost reductions or demonstrate mitigation of certain risks to customers.

PacifiCorp's satisfactory business profile score (a '5' on a 10-point scale, with '1' being the strongest) reflects a predominantly coal-fired generation fleet that in fiscal 2005 (ended March 31) provided about 70% of retail energy requirements (power purchases constitute about 21%, with hydro and natural gas providing the remaining balance), competitive retail rates, and progress in adjudicating rate cases to ensure that rates reflect current costs, which should improve the company's return on equity (ROE), that has consistently been below authorized levels. The ultimate outcome of the permanent rules related to Oregon Senate bill 408, passed in the fall of 2005, may have implications for PacifiCorp's earnings and cash flow. The current expectation is that permanent rules will be implemented during this summer.

In the last quarter, PacifiCorp and MEHC have negotiated two

key proposed settlements in Oregon and Utah that support the acquisition. Recently, it was announced that Wyoming and Washington have also completed settlements, meaning that settlements now exist in all six states. The settlements contain "most favored nation" clauses by which any state may ask the company to provide it with the terms and conditions negotiated in another. Final approval will require commission votes in all six states, which is scheduled to occur by the end of February. The Federal Energy Regulatory Commission (FERC), the Nuclear Regulatory Commission, and the Department of Justice (DOJ) have all approved the transaction. Berkshire Hathaway is expected to soon file its request with the DOJ seeking early termination of the waiting period for its conversion of MEHC convertible preferred stock.

Short-term rating factors.

Until the transaction closes, PacifiCorp's short-term ratings are based on the 'A-2' short-term ratings on Scottish Power plc and Scottish Power U.K. and reflect the expectations that, in the short term, the companies are expected to have ample internal liquidity. This is due to the steady, predictable net cash flow stream produced by the group's regulated businesses, the group's minimal debt maturities over the next few years, and Scottish Power's ample credit facility capacity. Cash and other short-term deposits, which amounted to about £920 million (\$1.16 billion) at Sept. 30, 2005, are held in a variety of quickly accessible funds. Full capacity exists under a \$500 million revolving credit facility due in 2010.

PacifiCorp currently provides for its own liquidity needs. Its cash and cash equivalent position was \$123.4 million as of Sept. 30, relative to \$199 million as of year-end fiscal 2005. In addition, it has an \$800 million commercial paper program, with \$296 million outstanding at the end of the third quarter. The program is backstopped by a revolving credit agreement that terminates in August 2010. As of Sept. 30, the facility was un-utilized and fully available.

The purchase agreement specifies that Scottish Power, via PacifiCorp Holdings Inc. (PHI), make a common equity contribution to PacifiCorp in quarterly amounts that total \$500 million for fiscal 2006. Considering the contributions against expected dividends, which are capped in the acquisition agreement, the net cash equity contribution the utility is expected to receive from Scottish Power via PHI is about \$285.2 million. In contrast, in fiscal 2005, PacifiCorp's dividends paid to PHI totaled about \$193 million, and no equity contributions were received.

Future maturities of \$120 million during the second half of fiscal 2006 are in line with historic obligations. At Sept. 30 (which is halfway through Scottish Power's fiscal year), PacifiCorp's capital expenditures totaled \$470 million. The utility has indicated that it expects total fiscal 2006 capital expenditures to be about \$1.1 billion. The acquisition agreement requires capital expenditures consistent with PacifiCorp's budget.

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BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

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February 2006

PacifiCorp Oregon

Financial Ratio Comparisons

| Peer Group | Return on Equity | | | | | | Return on Total Capital | | | | | |
|---|------------------|-------------------------|--------------|--------------|--------------|---------------|-------------------------|-------------------------|-------------|-------------|-------------|---------------|
| | Average | 12 months as of 2005 | 2004 | 2003 | 2002 | 2001 | Average | 12 months as of 2005 | 2004 | 2003 | 2002 | 2001 |
| Alliant Energy | 8.76 | 11.00 | 8.50 | 7.60 | 6.40 | 10.30 | 3.88 | 5.70 | 4.20 | 3.50 | 2.20 | 3.80 |
| Ameren | 11.82 | 10.90 | 10.10 | 11.40 | 12.20 | 14.50 | 5.44 | 5.60 | 4.50 | 5.20 | 5.00 | 6.90 |
| CH Energy Group | 8.98 | 8.40 | 8.70 | 9.10 | 8.30 | 10.40 | 5.22 | 4.60 | 5.10 | 5.50 | 5.00 | 5.90 |
| Con. Edison | 10.94 | 9.90 | 11.00 | 10.10 | 11.50 | 12.20 | 4.96 | 4.70 | 4.40 | 4.60 | 5.30 | 5.80 |
| Energy East Corp. | 10.02 | 8.80 | 9.20 | 8.20 | 10.50 | 13.40 | 3.46 | 3.60 | 3.60 | 3.20 | 3.00 | 3.90 |
| FPL | 12.90 | 12.30 | 12.20 | 13.00 | 13.40 | 13.60 | 5.08 | 5.10 | 5.10 | 5.20 | 3.50 | 6.50 |
| NSTAR | 13.46 | 13.20 | 13.30 | 13.50 | 13.90 | 13.40 | 4.55 | 4.50 | 4.80 | 4.70 | 4.20 | n.m. |
| Progress Energy | 11.20 | 8.90 | 9.80 | 11.90 | 13.10 | 12.30 | 3.76 | 3.70 | 4.00 | 4.60 | 3.10 | 3.40 |
| SCANA Corp | 11.80 | 11.70 | 12.50 | 12.40 | 11.70 | 10.70 | 5.93 | 4.90 | 4.90 | 4.70 | n.m. | 9.20 |
| Southern Company | 14.64 | 15.10 | 15.00 | 15.50 | 15.70 | 11.90 | 6.08 | 6.30 | 6.20 | 6.20 | 5.90 | 5.80 |
| Vectren Corp | 11.66 | 11.50 | 10.70 | 11.70 | 13.40 | 11.00 | 4.32 | 4.90 | 4.50 | 4.60 | 5.20 | 2.40 |
| Xcel Energy | 10.48 | 9.90 | 10.00 | 10.00 | 9.10 | 13.40 | 4.20 | 4.20 | 4.30 | 4.10 | n.m. | 4.20 |
| Average | 11.39 | 10.97 | 10.92 | 11.20 | 11.60 | 12.26 | 4.72 | 4.82 | 4.63 | 4.68 | 4.24 | 5.25 |
| | | | | | | | | | | | | |
| Average All Operating Utilities | 11.30 | 10.70 | 11.10 | 11.40 | 11.40 | 11.90 | 5.14 | 5.00 | 5.40 | 5.00 | 4.90 | 5.40 |
| | | | | | | | | | | | | |
| PacifiCorp | 4.78 | 6.50 | 7.00 | 4.40 | 8.90 | (2.90) | 2.34 | 2.80 | 3.00 | 2.50 | 4.50 | (1.10) |
| | | | | | | | | | | | | |
| Differences | | | | | | | | | | | | |
| PacifiCorp less Peer Group | (6.61) | (4.47) | (3.92) | (6.80) | (2.70) | (15.16) | (2.38) | (2.02) | (1.63) | (2.18) | 0.26 | (6.35) |
| PacifiCorp less All Operating Utilities | (6.52) | (4.20) | (4.10) | (7.00) | (2.50) | (14.80) | (2.80) | (2.20) | (2.40) | (2.50) | (0.40) | (6.50) |

Source: RRA Electric Utility Quality Measures: Ranking and Trends, dated January 3, 2006

PacifiCorp Oregon

Financial Ratio Comparisons

| Peer Group | Pretax Interest Coverage | | | | | | Fixed Charge Coverage | | | | | |
|--|--------------------------|-------------|-------------|-------------|-------------|-------------|-----------------------|-------------|-------------|-------------|-------------|-------------|
| | 12 months | | | | | | 12 months | | | | | |
| | Average | as of 2005 | 2004 | 2003 | 2002 | 2001 | Average | as of 2005 | 2004 | 2003 | 2002 | 2001 |
| Alliant Energy | 2.43 | 2.73 | 2.74 | 2.33 | 1.88 | 2.46 | 2.01 | 2.46 | 2.06 | 1.78 | 1.68 | 2.05 |
| Ameren | 4.31 | 4.43 | 3.96 | 3.84 | 4.21 | 5.12 | 2.97 | 3.09 | 2.83 | 2.65 | 2.95 | 3.33 |
| CH Energy Group | 4.18 | 4.91 | 5.16 | 4.45 | 3.67 | 2.72 | 2.90 | 3.27 | 3.24 | 2.88 | 2.54 | 2.55 |
| Con. Edison | 3.30 | 3.22 | 3.06 | 3.19 | 3.39 | 3.64 | 2.46 | 2.52 | 2.38 | 2.40 | 2.47 | 2.53 |
| Energy East Corp. | 2.53 | 2.43 | 2.78 | 2.24 | 2.37 | 2.85 | 1.84 | 1.88 | 1.85 | 1.68 | 1.76 | 2.01 |
| FPL | 4.00 | 3.20 | 3.35 | 4.30 | 4.50 | 4.66 | 3.13 | 2.78 | 2.80 | 3.21 | 3.55 | 3.33 |
| NSTAR | 2.78 | 2.87 | 3.00 | 2.84 | 2.49 | 2.72 | 2.09 | 2.16 | 2.20 | 2.11 | 2.00 | 1.96 |
| Progress Energy | 2.06 | 1.87 | 2.32 | 2.19 | 2.12 | 1.79 | 2.17 | 2.06 | 2.15 | 2.35 | 2.28 | 2.02 |
| SCANA Corp | 2.80 | 1.86 | 3.12 | 3.11 | 2.50 | 3.43 | 2.26 | 2.37 | 2.43 | 2.33 | 2.20 | 1.96 |
| Southern Company | 4.35 | 4.06 | 4.17 | 4.04 | 5.14 | 4.34 | 2.95 | 3.14 | 3.15 | 3.04 | 2.93 | 2.50 |
| Vectren Corp | 2.87 | 3.11 | 2.99 | 2.97 | 2.95 | 2.32 | 2.41 | 2.55 | 2.49 | 2.48 | 2.46 | 2.07 |
| Xcel Energy | 2.18 | 2.46 | 2.57 | 2.44 | 0.93 | 2.50 | 1.99 | 2.15 | 2.18 | 2.07 | 1.57 | 1.96 |
| Average | 3.15 | 3.10 | 3.27 | 3.16 | 3.01 | 3.21 | 2.43 | 2.54 | 2.48 | 2.42 | 2.37 | 2.36 |
| Note: Information unavailable from RRA on Empire District and MGE Energy, Inc. | | | | | | | | | | | | |
| Average All Operating Utilities | 3.79 | 3.94 | 4.06 | 3.64 | 3.81 | 3.48 | 2.66 | 2.85 | 2.90 | 2.58 | 2.58 | 2.41 |
| PacifiCorp | 2.28 | 2.53 | 2.40 | 2.05 | 3.25 | 1.19 | 1.59 | 1.87 | 1.89 | 1.46 | 2.07 | 0.64 |
| Differences | | | | | | | | | | | | |
| PacifiCorp less Peer Group | (0.87) | (0.57) | (0.87) | (1.11) | 0.24 | (2.02) | (0.84) | (0.67) | (0.59) | (0.96) | (0.30) | (1.72) |
| PacifiCorp less All Operating Utilities | (1.50) | (1.41) | (1.66) | (1.59) | (0.56) | (2.29) | (1.08) | (0.98) | (1.01) | (1.12) | (0.51) | (1.77) |

Source: RRA Electric Utility Quality Measures: Ranking and Trends, dated January 3, 2006

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

Exhibit Accompanying Direct Testimony of Bruce Williams on Reconsideration

February 2006

Fitch Ratings

FITCH LOWERS PPW SR UNSECURED DEBT TO 'BBB+'; OUTLOOK STABLE

Fitch Ratings-New York-31 January 2006: Fitch Ratings has lowered PacifiCorp's (PPW) credit ratings as indicated below:

- Issuer default rating to 'BBB' from 'BBB+';
- Senior secured to 'A-' from 'A';
- Senior unsecured to 'BBB+' from 'A-';
- Preferred stock to 'BBB' from 'BBB+'.

At the same time, Fitch has affirmed PPW's 'F2' short term rating. The Rating Outlook is Stable for all of PPW's long- and short-term debt and preferred securities. The rating action affects approximately \$4.4 billion of debt.

The lowered ratings better reflect the company's operating cash flow and debt leverage measures, large capital spending program, and business risk profile. While a large majority of the utility's generating capacity mix is coal-fired, incremental load growth is expected to be met primarily by natural gas-fired resources. As a result, the company's natural gas requirements are likely to grow over time. Management has contracts in place to hedge its natural gas exposure through 2007, including fuel for the new Carrant Creek and Lake Side power plants, and has hydro hedges in place to mitigate in part its exposure to critical water conditions through September 2006. In addition, regulatory filings in the past year to implement fuel and purchase power cost adjustment mechanisms, if approved, would further mitigate commodity exposure. These filings are currently being considered by regulators in Wyoming, Washington, Utah and Oregon. Nonetheless, the mechanisms are not in place yet and exposure to high and rising natural gas fuel and purchase power costs could be significant, especially in the event of a sustained outage at a base-load generating facility during a period of peak demand. The ratings also consider PPW's above-industry average service territory growth, primarily in its eastern service territory, and significant planned investment in new plant and infrastructure to meet its load requirements, which are estimated to approximate \$1 billion per annum over the next five years.

The rating action and Stable Rating Outlook incorporate reasonable regulatory outcomes in pending and future rate proceedings and note the unfavorable final order issued in September 2005 by the Oregon commission in PPW's general rate case (GRC, discussed further below). The proposed sale of PPW by Scottish Power (SP; senior unsecured debt rated 'BBB+' by Fitch) to MidAmerican Energy Holdings Company (MEHC; senior unsecured debt rated 'BBB' by Fitch) is not a factor in the rating downgrade. In fact, Fitch views the change in ownership, if approved by regulatory authorities as expected by the end of March 2006, as a stabilizing factor for PPW's credit profile. Conversely, if the proposed sale to MEHC were to fail, the result would be uncertainty as to the future ownership of PPW, which in Fitch's view would be a negative credit development. The Stable Outlook also anticipates the equity infusion of approximately \$300 million net of dividends from its direct parent, PacifiCorp Holdings, Inc. (PHI), during the 2006 fiscal year. PPW is a direct subsidiary of PHI, which is a wholly-owned subsidiary of SP.

PPW's operating cash flow has been challenged by a lack of regulatory support and low returns in its six-state service territory and below normal hydroelectric conditions in five of the past six years (recent winter 2005-2006 precipitation statistics imply significantly improved hydrogeneration in 2006). Fitch continues to view regulation as a primary risk for PPW fixed income investors and recognizes progress made by SP management in improving its relations with its regulators. Moreover, Fitch assumes progress in this area will continue under new ownership. Regulatory progress is evidenced by constructive outcomes in PPW's multi-state process, the February 2005 Utah Public Service Commission GRC order authorizing a \$51 million rate increase, legislation enacted in Utah adopting a forward test year, and the pending power cost adjustment mechanism filings in Oregon, Washington and Wyoming.

However, the Oregon Public Utilities Commission's (OPUC) September 2005 order incorporating recently

enacted tax legislation (Senate Bill 408) in PPW's Oregon GRC is a serious matter for concern in Fitch's view. The OPUC has granted PPW's motion to rehear the order in its GRC with respect to the incorporation of Senate Bill 408, which reduced the \$52 million rate increase contemplated under settlement agreements reached by PPW with intervenor groups to approximately \$26 million. Rehearing proceedings are scheduled through May 2006, which together with the outcome of the Senate Bill 408, permanent rule making process will affect PPW's future earnings and cash flows.

The agreed sale of PPW by SP for approximately \$9.4 billion to MEHC, including the assumption of \$4.3 billion of net debt and preferred stock, announced May 24, 2005, has received clearance under Hart Scott Rodino and the approval of the Federal Energy Regulatory Commission and the Nuclear Regulatory Commission. Settlement agreements have been reached with the relevant parties in all six states PPW serves. The Utah Public Service Commission unanimously approved the acquisition of PPW by MEHC and issued its order Jan. 27, 2006. The Wyoming Public Service Commission has also approved the transaction and a final written order will be issued and become effective Feb. 10, 2006.

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Fitch's rating definitions and the terms of use of such ratings are available on the agency's public site, 'www.fitchratings.com'. Published ratings, criteria and methodologies are available from this site, at all times. Fitch's code of conduct, confidentiality, conflicts of interest, affiliate firewall, compliance and other relevant policies and procedures are also available from the 'Code of Conduct' section of this site.

BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

Exhibit Accompanying Direct Testimony of Bruce Williams on Reconsideration

February 2006



CLO



Credit FAQ: PacifiCorp's Rate Case Ruling

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Quick Links

Frequently Asked Questions

PacifiCorp (A-/Watch Neg/A-2) received a disappointing ruling from the Oregon Public Utilities Commission (OPUC) on Sept. 28, 2005, that cut in half the \$52.5 million retail rate increase negotiated as part of a stipulated settlement with various parties, including staff. The decision authorized just \$25.9 million, or a retail rate increase of about 3.2%, which became effective Oct. 4, 2005.

The \$26 million disallowance reflects adjustments the OPUC made in the amount of income taxes that PacifiCorp may collect in its retail electric rates related to recently enacted legislation, Senate Bill (SB) 408. Oregon constitutes about 30% of PacifiCorp's retail market. While the ruling is adverse for credit quality, no near-term rating action is foreseen at this time as Scottish Power supports PacifiCorp's ratings. Longer-term, there could be an adverse ratings action, depending on factors that are discussed in detail below.

Frequently Asked Questions

What is SB 408?

SB 408 addresses concerns that Oregon utilities may be collecting income tax expenses in retail electric and natural gas rates that are not ultimately paid by either the utility or its affiliate (such as a parent) to taxing authorities. A utility's federal and state income taxes are considered an operating expense for ratemaking purposes. In Oregon, as in many other states, retail rates are set at levels designed to cover operating expenses, including income taxes, over an agreed upon test period. But differences frequently arise between amounts that an electric or gas utility collects that are attributable to its stand-alone tax obligations and amounts that the consolidated company actually pays in taxes. Such differences arise for a number of reasons. For example, a utility's positive stand-alone tax obligation could be properly combined with the generation of income as well as losses within the parent company's federal tax return. Tax payments reflect all the combined income and loss positions of the consolidated entity.

The essence of SB 408 is that it overturns the precedent of calculating utility taxes on a stand-alone basis and instead requires the OPUC to track taxes collected by utilities in rates and compare this amount against taxes ultimately paid by the utility or the consolidated corporation to state, federal and

local governments. The legislation authorizes the establishment of a mechanism that automatically flows back to retail ratepayers any differences in income taxes collected versus income taxes actually paid by the filing company that are attributable to regulated operations.

The genesis of SB 408, which passed by a significant margin in the Oregon Legislature, has to do with issues surrounding Enron's ownership of Portland General Electric (PGE; BBB/Stable/-). Consumer advocates have charged that while the utility collected millions of dollars in retail rates for PGE's estimated tax obligations, offsetting losses in other Enron operations resulted in its paying no federal or state income taxes for several years. As a result, PacifiCorp has found itself drawn into a sensitive policy issue that has generated widespread concern throughout the state.

How does SB 408 affect PacifiCorp and Scottish Power?

SB 408 applies to investor-owned electric and natural gas utilities that are regulated by the OPUC and serve more than 50,000 customers. Other utilities that are potentially affected are PGE, Northwest Natural Gas (A+/Stable/A-1), Avista (BB+/Stable/B-1) and PacifiCorp.

While all four of these investor-owned utilities will be required to file tax information, those most vulnerable to actual income tax-based adjustments appear to be PGE and PacifiCorp. PacifiCorp's potential SB 408 tax adjustments stem principally from:

- The ability of its U.S. holding company to deduct interest expenses on its federal and state income tax filings, which it pays to Scottish Power in association with its acquisition indebtedness; and
- The U.S. holding company's ability to utilize tax deductions from PacifiCorp's non-regulated affiliates.

Scottish Power purchased PacifiCorp in 1999. Subsequent to the acquisition, Scottish Power created PacifiCorp Holdings Inc. (PHI), a non-operating, indirect, wholly owned subsidiary. PHI is the parent of PacifiCorp and of Scottish Power's three other U.S. subsidiaries, including PPM Energy.

The interest that PHI pays to Scottish Power that is associated with an inter-company loan is deductible on the consolidated tax returns that PHI files on behalf of PacifiCorp and the other three subsidiaries. At fiscal year end March 31, 2005, PHI reflected an inter-company loan balance of about \$2.4 billion, and PHI paid to Scottish Power approximately \$160 million in related interest. This constituted a direct offset to PHI's consolidated tax liability, and thus reduced the consolidated group's taxable income. SB 408 will likely mean that until Scottish Power sells PacifiCorp, the utility could face future retail rate deductions induced by the automatic adjustment mechanism, unless PHI debt is reduced.

How is the automatic tax adjustment mechanism

expected to work?

SB 408 applies to income taxes collected from ratepayers and paid to governments beginning Jan. 1, 2006. The legislation specifies that beginning in 2005, utilities must file an annual tax report on October 15. For the three preceding fiscal years, the report must provide: A) the amount of taxes paid by the utility, or the consolidated entity's income taxes paid that are "attributable" to regulated operations; and B) the amount of taxes authorized for collection in the utility's retail rates. The lesser of item A is then compared to item B, and if the difference is at least \$100,000, an adjustment is triggered.

SB 408 appears to apply the adjustment symmetrically, allowing for the possibility of an increase in retail rates due to higher tax obligations of the stand-alone utility. But a concern from a credit perspective is that the OPUC may suspend the adjuster if it is found to have a materially adverse effect on ratepayers. This suggests that in its application, the mechanism would more commonly be used to reduce retail rates rather than to pass through rate increases to consumers. Many of the details of the mechanism are left to the OPUC.

When will the details of the mechanism be finalized?

The OPUC issued interim rules on Sept. 15 to enable the Oct. 15 filings. These rules have proved difficult to decipher and have sparked significant concern of the utilities, because there is a potential for unintended consequences. For example, the temporary rules seem to apply a tax adjustment even in cases where the consolidated tax payments far exceed the amount of taxes collected and paid by the utility. Troubling for the pending MidAmerican Energy Holdings Co. (MEHC) acquisition of PacifiCorp is interim rule language that would allow the OPUC to allocate the tax benefits of losses at unregulated affiliates owned by Berkshire Hathaway to Oregon ratepayers in the form of a rate reduction.

Permanent rules are expected to be in place by mid-January 2006. The content of these permanent rules will be critical for credit quality—open-ended rules that introduce a wide set of circumstances in which a rate reduction could be required will increase regulatory risk and potentially increase the variability of regulated cash flows. Also unknown is when the tax trigger should begin. It is PacifiCorp's position (and that of some intervenors) that filings made in 2005 and 2006 are to be used for information purposes only, and that only in late 2007 should the filings be used trigger an actual adjustment. But until permanent rules are in place, it is difficult to determine how the details will work.

How is it that SB 408 formed the basis of reductions in PacifiCorp's rate case?

Treatment of taxes was a contested issue in PacifiCorp's general rate case, and no stipulations were reached with parties on this issue. While the case was pending before the OPUC, SB 408 was passed on an emergency basis, which means the bill became effective when the state's governor signed it on Sept. 2, 2005. The Industrial Customers of Northwest Utilities (ICNU) argued that SB 408 should be

considered in the context of PacifiCorp's general rate case decision. The OPUC agreed.

Because it was not expected that the OPUC would apply the principles of SB 408 until after permanent rules were adopted for taxes paid after Jan. 1, 2006, the ruling was a surprise. The OPUC appears to have predicated its authority to apply SB 408 to the general rate case on the fact that PacifiCorp's retail rates are based on a forward 2006 test year, and therefore some portion of the authorized rate increase is to cover expected 2006 expenses, including income taxes. The OPUC noted in its decision that it is not "bound to maintain our practice of stand-alone calculations, particularly when a new statute comes into play." In reducing the settlement by half, the OPUC did not formally apply an adjustment mechanism but followed a methodology presented by the Citizen's Utility Board, a ratepayer advocate. More balanced rules proposed by staff were rejected.

What are the immediate credit implications for PacifiCorp?

In the short run, Standard & Poor's is taking no rating action. Critical to understanding this decision is the fact that PacifiCorp's current 'A-' corporate credit rating (CCR) is based on the consolidated credit quality of Scottish Power. Thus, a rating action, if it were to occur, would reflect the impact of the OPUC rate case decision and the future risks of SB 408 on the consolidated operations.

PacifiCorp represents about 45% of Scottish Power's operating profit, with the Oregon market being the second-largest service area behind Utah. Scottish Power produced about £1.2 billion (or \$2.2 billion) of funds from operations (FFO) in fiscal 2005 (ending March 31), so the pre-tax \$26 million disallowance represents about 1% of consolidated cash flows. Thus, the immediate consequences of the rate case are nominal from the consolidated perspective. Key consolidated cash flow ratios for fiscal 2005 were appropriate for the rating, with funds from operation (FFO) interest coverage of about 4.0x and adjusted FFO to total debt of 20%.

What are the longer-term credit implications?

In the long run, the credit implications are more complex, and will be a function of a number of unknowns. For example, until permanent rules are in place, it is difficult to assess the full impact of SB 408 on future utility financial performance. In addition, PacifiCorp has vigorously disputed OPUC's application of SB 408 to the rate case proceeding, calling the OPUC decision premature, ill advised, and possibly illegal. If the company takes legal action regarding the rate case and prevails, it could recoup the rate reductions, though not for some time, and SB 408 will continue to apply to future revenues earned by the utility. Also, while the legislation applies only to Oregon, there is potential for this issue to become a policy concern in other states, especially in Utah, which is PacifiCorp's largest market, accounting for 40% of the company's retail electric revenues. On Oct. 6, 2005 the Committee of Consumer Services issued a letter calling on

the Utah Public Service Commission to investigate consolidated tax issues.

Most importantly, Scottish Power is in the process of selling PacifiCorp. As a result, PacifiCorp's ratings are on CreditWatch with negative implications, reflecting PacifiCorp's weak credit metrics, which would not support its current CCR were it rated on a stand-alone basis. The OPUC decision will reduce after-tax cash flows by about \$16 million. And absent any changes in PHI's debt and tax arrangements, stand-alone performance will be weaker than forecast. These impacts could be ephemeral, if it is completed. However, the extent to which SB 408 may impact PacifiCorp following the sale to MEHC is also uncertain and is dependent on the permanent decision. For example, given the broad nature of Berkshire's businesses, it is likely that loss-making companies will exist in any given year, which under the temporary rules could result in rate reductions to Oregon customers.

What effect could this have on the sale of PacifiCorp to MEHC?

While the parties have made no public statements in this regard, it is clear that the legislation could influence whether MEHC proceeds with the sale because the permanent rules have the potential to affect the future profitability of PacifiCorp. MEHC's offer was made before SB 408 was passed and, since then, it has closely followed the developments. After the temporary rules were announced, MEHC met with multiple parties, including the state governor. The company's public statements have expressed significant concern about the interim rules. Standard & Poor's is monitoring the situation and will comment further as conditions warrant.

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BEFORE THE PUBLIC UTILITY COMMISSION
OF THE STATE OF OREGON

PACIFICORP

Exhibit Accompanying Direct Testimony of Bruce Williams on Reconsideration

February 2006



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January 6, 2006

STATE REGULATORY EVALUATIONS

As part of RRA's regulatory research effort, we evaluate the regulatory climates of 49 states and the District of Columbia. The evaluations are assigned from an investor perspective and indicate the relative regulatory risk associated with the ownership of securities issued by the jurisdiction's electric, gas, and telephone utilities. Each evaluation is based upon our studies of the numerous factors affecting the regulatory process in the state, and is changed as major events occur which cause us to modify our view of the regulatory risk accruing to the ownership of utility securities in that individual jurisdiction. We also review our evaluation when we issue State Regulatory Reviews, and when we publish quarterly comparative evaluations. The majority of factors that we consider are discussed in *Focus Notes*, State Regulatory Reviews, Final Reports, or Regulatory Updates. We also consider information obtained from contacts with commission, company, and government personnel in the course of our research. The final evaluation reflects our assessment of the probable level and quality of the earnings to be realized by the state's utilities as a result of regulatory, legislative, and court actions.

RRA maintains three principal rating categories: Above Average, Average, and Below Average. We endeavor to maintain an approximately equal number of ratings above the average and below the average. Within the principal rating categories, the numbers 1, 2, and 3 indicate relative position. The designation 1 indicates a stronger rating; 2, a mid-range rating; and, 3, a weaker rating.

Our last "State Regulatory Evaluations" was published October 5, 2005, at which time, we noted two ratings changes; in response to increased politicization of the regulatory process, we lowered our rating of Illinois to Below Average/1 from Average/3 (see FN 9/23/05); and, in recognition of constructive rate decisions for three of the major investor-owned utilities, we raised our rating of Georgia regulation to Average/1 from Average/2. At this time we are raising our rating of the California regulatory climate to Average/2 from Average/3 in recognition of more constructive policies, in particular, the California Public Utilities Commission's December 2005 authorization of above-average equity returns for 2006 for the state's major energy utilities (see the Final Report 12/29/05). In addition, we are lowering our rating of Oregon regulation to Average/2 from Average/1 due to the potential negative ramifications of Senate Bill (SB) 408, enacted in September 2005, that requires the flow through of consolidated tax savings to ratepayers (FN 1/6/06).

Our state regulatory evaluations are not to be confused with our "Tier" classifications, in which we categorize 49 states and the District of Columbia based on relative progress toward electric industry restructuring. For further detail, refer to the October 20, 2004 Special Report entitled *Electric Industry Restructuring Update*, which is revised weekly on our website www.rra-focus.com.

NOTE: RRA Regulatory Evaluations are provided for the use of our clients only. Please do not disseminate these ratings outside your organization.

RRA-REGULATORY FOCUS

-2-

January 6, 2006

Above Average

1

2
Alabama
Florida
Indiana
North Carolina
Wisconsin

3
Mississippi
Virginia

Average

1

Delaware
Georgia
Iowa
Maryland
Massachusetts
South Carolina
Tennessee
Washington

2
California*
District of Columbia
Hawaii
Kentucky
Michigan
Minnesota
Nebraska
New Jersey
New York
North Dakota
Ohio
Oklahoma
Oregon**
Rhode Island
South Dakota

3
Arizona
Arkansas
Colorado
Connecticut
Idaho
Kansas
Louisiana
Maine
Missouri
New Hampshire
New Mexico
Pennsylvania
Utah
Wyoming

Below Average

1

Illinois
Montana
Nevada
Texas
Vermont
West Virginia

2

3

ALPHABETICAL LISTING

Alabama - AA/2
Arizona - A/3
Arkansas - A/3
California - A/2*
Colorado - A/3
Connecticut - A/3
Delaware - A/1
Dist. of Col. - A/2
Florida - AA/2
Georgia - A/1
Hawaii - A/2
Idaho - A/3
Illinois - BA/1

Indiana - AA/2
Iowa - A/1
Kansas - A/3
Kentucky - A/2
Louisiana - A/3
Maine - A/3
Maryland - A/1
Massachusetts - A/1
Michigan - A/2
Minnesota - A/2
Mississippi - AA/3
Missouri - A/3
Montana - BA/1

Nebraska - A/2
Nevada - BA/1
New Hampshire - A/3
New Jersey - A/2
New Mexico - A/3
New York - A/2
North Carolina - AA/2
North Dakota - A/2
Ohio - A/2
Oklahoma - A/2
Oregon - A/2**
Pennsylvania - A/3

Rhode Island - A/2
South Carolina - A/1
South Dakota - A/2
Tennessee - A/1
Texas - BA/1
Utah - A/3
Vermont - BA/1
Virginia - AA/3
Washington - A/1
West Virginia - BA/1
Wisconsin - AA/2
Wyoming - A/3

* Revised upward since October 5, 2005.

** Revised downward since October 5, 2005.

CERTIFICATE OF SERVICE

I hereby certify that I served a true and correct copy of the foregoing document in Docket UE 170 on the following named person(s) on the date indicated below by email and first-class mail addressed to said person(s) at his or her last-known address(es) indicated below.

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