



Oregon

Theodore R. Kulongoski, Governor

Public Utility Commission

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August 5, 2008

OREGON PUBLIC UTILITY COMMISSION
ATTENTION: FILING CENTER
PO BOX 2148
SALEM OR 97308-2148

RE: **Docket No. UE197** – In the Matter of **PORTLAND GENERAL ELECTRIC COMPANY** Request for a general rate revision.

Enclosed for electronic filing in the above-captioned docket is the Public Utility Commission Staff Direct Testimony on Cost of Capital.

/s/ Kay Barnes

Kay Barnes

Regulatory Operations Division

Filing on Behalf of Public Utility Commission Staff

(503) 378-5763

Email: kay.barnes@state.or.us

c: UE 197 Service List (parties)

**PUBLIC UTILITY COMMISSION
OF OREGON**

UE 197

STAFF DIRECT TESTIMONY OF

Bryan Conway

**In the Matter of
PORTLAND GENERAL ELECTRIC COMPANY
Request for a General Rate Revision.**

Cost of Capital

August 5, 2008

CASE: UE 197
WITNESS: Bryan Conway

**PUBLIC UTILITY COMMISSION
OF
OREGON**

STAFF EXHIBIT 700

Direct Testimony

August 5, 2008

1 **Q. PLEASE STATE YOUR NAME, OCCUPATION, AND BUSINESS**
2 **ADDRESS.**

3 A. My name is Bryan Conway. My business address is 550 Capitol Street NE
4 Suite 215, Salem, Oregon 97301-2551.

5 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND WORK**
6 **EXPERIENCE.**

7 A. My Witness Qualifications Statement is found on Exhibit Staff/701, Conway/1.
8 In addition, I have completed all of the required and elective coursework for a
9 Ph.D. in economics from Oregon State University. My fields of study were
10 Industrial Organization and Applied Econometrics. Further, I have testified
11 before the Commission in numerous occasions on topics related to electric,
12 gas and telecommunication utilities.

13 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

14 A. The purpose of my testimony is to describe and support the cost of capital
15 settlement that was reached by all parties to this proceeding.

16 **Q. DID YOU PREPARE AN EXHIBIT FOR THIS DOCKET?**

17 A. Yes. I prepared Exhibit Staff/701, consisting of one page and Exhibit Staff/702
18 consisting of two pages. Exhibit Staff/702 contains PGE's condensed
19 consolidated balance sheet and my witness qualifications statement.

20 **Q. HOW IS YOUR TESTIMONY ORGANIZED?**

21 A. First, I describe the settlement that was reached with the parties to this docket.
22 Second, I provide information on Portland General Electric Company's

1 (“PGE’s”) required rate of return and demonstrate that the settlement reached,
2 although a compromise by all parties, results in a fair and reasonable return.

3 **Q. PLEASE DESCRIBE THE SETTLEMENT.**

4 A. The settlement settles the contested issues related to PGE’s assumed capital
5 structure, embedded cost of debt, and cost of equity for rates effective on or
6 about January 1, 2009. Specifically, the parties to the Stipulation agree that
7 the required rate of return should be:

COMPONENT	% of CAPITAL	COST	WEIGHTED COST
Long Term Debt	50.00%	6.567%	3.284%
Preferred Stock	0.00%	0.000%	0.000%
Common Equity	50.00%	10.100%	5.050%
Total	<u>100.00%</u>		8.334%

13 **Q. WHAT WAS PGE’S LAST RATE OF RETURN AUTHORIZED BY THIS**
14 **COMMISSION?**

15 A. PGE’s current authorized rate of return authorized by this Commission is:

COMPONENT	% of CAPITAL	COST	WEIGHTED COST
Long Term Debt	50.00%	6.48%	3.240%
Preferred Stock	0.00%	0.000%	0.000%
Common Equity	50.00%	10.100%	5.050%
Total	<u>100.00%</u>		8.29%

1 **Q. PLEASE DISCUSS THE CAPITAL STRUCTURE BEING PROPOSED BY**
2 **THE PARTIES.**

3 A. The parties to the Stipulation propose that the capital structure remain at 50
4 percent equity and 50 percent debt.

5 **Q. WHAT IS PGE'S CURRENT CAPITAL STRUCTURE?**

6 A. As of March 31, 2008, PGE had 51.4 percent shareholder equity and 48.6
7 percent long-term debt. PGE did not have any outstanding preferred stock.
8 See Portland General Electric's Form 10-Q, page 5, attached as Staff/702,
9 page 2.

10 **Q. IS A CAPITAL STRUCTURE COMPRISED OF 50 PERCENT EQUITY AND**
11 **50 PERCENT DEBT REASONABLE?**

12 A. Yes. A capital structure of 50 percent debt and equity was fully vetted by the
13 Commission in determining PGE's rates in 2007. Further, this capital structure
14 is in line with recent Commission decisions for other utilities such as Avista and
15 PacifiCorp.

16 **Q. PLEASE DISCUSS THE EMBEDDED COST OF LONG-TERM DEBT**
17 **BEING PROPOSED BY THE PARTIES.**

18 A. The parties to the Stipulation propose that the embedded cost of long-term
19 debt be 6.567 percent, as set forth in PGE's initial filing in this docket. This
20 represents an increase of 8.7 basis points over PGE's most recent authorized
21 cost of debt.

1 **Q. IS AN EMBEDDED COST OF LONG-TERM DEBT 6.567%**
2 **REASONABLE?**

3 A. Yes. While Treasury rates have declined modestly since the Commission
4 issued Order No. 07-015 in PGE's last rate case on January 12, 2007, spreads
5 in the corporate sector have increased such that the total cost of borrowing
6 appears to have increased slightly. At the time of Order No. 07-015, the
7 Moody's Seasoned Aaa rate was 5.41 percent and the Baa rate was 6.34
8 percent. As of June 20, 2008, the Moody's Seasoned Aaa rate was 5.72
9 percent and the Baa rate was 7.11 percent. These rates can be found at
10 [HTTP://WWW.FEDERALRESERVE.GOV/RELEASES/H15](http://www.federalreserve.gov/releases/h15).

11 **Q. WHAT DOES THE MOODY'S SEASONED RATE MEASURE?**

12 A. Moody's Aaa and Baa rates through December 6, 2001, are averages of Aaa
13 and Baa utility and Aaa and Baa industrial bond rates, respectively. As of
14 December 7, 2001, these rates are averages of industrial bonds only.
15 However, these still can be considered indicative of interest rate trends faced
16 by utilities.

17 **Q. WHAT IS THE AVERAGE MATURITY FOR MOODY'S SEASONED**
18 **RATES?**

19 A. Moody's tries to include bonds with remaining maturities as close as possible
20 to 30 years. Moody's drops bonds if the remaining life falls below 20 years, if
21 the bond is susceptible to redemption, or if the rating changes.

1 **Q. SINCE THE LAST RATE CASE, HAS THERE BEEN CHANGES TO PGE'S**
2 **OUTSTANDING DEBT?**

3 A. Yes. Some pollution control bonds were retired as well as some first mortgage
4 bonds. In addition, new debt was issued. Between the March 15, 2006 filing of
5 UE 180 and the February 27, 2008 filing of UE 197, PGE issued \$650 million in
6 new long-term debt. Additionally, PGE proposes to issue \$50 million of first
7 mortgage bonds in August, 2008; and two series of first mortgage bonds,
8 totaling \$250 million in gross proceeds, in 2009.¹

9 **Q. WHAT IS THE IMPACT OF THESE CHANGES?**

10 A. Staff analyzed these changes in the context of what was assumed in UE 180,
11 and the impact of these changes is to slightly raise PGE's cost of debt. This
12 further justifies the settlement of debt that slightly raises PGE's cost of debt for
13 ratemaking purposes.

14 **Q. DOES THE STIPULATION MEAN THAT YOU AGREE TO HOW PGE**
15 **CALCULATED ITS COST OF DEBT?**

16 A. No. Staff agrees that the overall cost of debt is reasonable, but it does not
17 necessarily agree to all of the inputs, such as the specific rate for pro forma
18 debt assumed in the calculation.

19 **Q. IN ORDER NO. 07-015, THE COMMISSION ORDERED SPECIFIC**
20 **ADJUSTMENTS TO PGE'S COST OF DEBT IN ORDER TO HOLD**
21 **CUSTOMERS HARMLESS FOR ENRON'S OWNERSHIP OF PGE. HAVE**

¹ See PGE Exhibit 901/Page 2.

1 **THOSE ADJUSTMENTS BEEN CARRIED THROUGH INTO THIS**
2 **SETTLEMENT?**

3 A. Yes. Even though there is not agreement on how the result was calculated,
4 both PGE and Staff incorporated the specific Enron-related adjustments
5 reflected in Order No. 07-015 into its estimates that were the basis for the
6 settlement.

7 **Q. UNDER THE STIPULATION, IS PGE PRECLUDED FROM UPDATING ITS**
8 **COST OF DEBT LATER IN THIS CASE?**

9 A. Yes. This ensures that PGE bears the interest rate risk with respect to the cost
10 of new debt.

11 **Q. PLEASE DISCUSS THE COST OF EQUITY BEING PROPOSED BY THE**
12 **PARTIES.**

13 A. The parties to the Stipulation propose that the cost of equity be set at 10.1
14 percent.

15 **Q. IS AN AUTHORIZED COST OF EQUITY OF 10.1 PERCENT**
16 **REASONABLE?**

17 A. Yes. The most recent time the Commission has decided PGE's cost of equity
18 in a contested case was in 2007. In Order No. 07-015, PGE was awarded a
19 10.1 percent cost of equity. Since that time the Commission also ordered a
20 10.1 percent cost of equity for Cascade Natural Gas (Order No. 07-220). The
21 financial markets do not have appeared to have changed materially since that
22 time. As discussed previously, utility borrowing rates appear to be slightly
23 higher than the last time the Commission set PGE's cost of equity, but

1 Treasury Rates are slightly lower (e.g., the 30-year Treasury Rate as fallen
2 from 4.86% from January 2007 to 4.71% on June 20, 2008).

3 **Q. HAS THE MARKET'S PERCEPTION OF PGE'S RISKINESS CHANGED**
4 **SINCE THE LAST ORDER?**

5 A. It does not appear so based on current information. The Value Line Beta
6 listed for PGE is 0.85, which is the same Beta assumed by Staff in Docket UE
7 180 (ICNU assumed a Beta of 0.80) where the Commission adopted a 10.1
8 percent cost of equity.

9 **Q. WHAT DOES BETA MEASURE?**

10 A. Beta is a measure of the responsiveness of the expected return on a particular
11 financial security relative to movements in the average expected return on all
12 other securities in the market. In the capital-asset pricing model, the beta
13 coefficient (Beta) is taken as a measure of the market (or non-diversifiable) risk
14 of a particular security. The beta coefficient links the return on the security and
15 the average market return. Theoretically, assuming a risk-free rate equal to
16 zero, the average market risk of all securities is where $Beta = 1$, that is, a 10%
17 increase in market return is reflected as a 10% increase in the return of, say,
18 security A. If the expected return on, say, security B, is 20%, but there is an
19 expected market return of 10%, then this security has a $Beta = 2$ which
20 indicates a risk greater than the market. If security C has a $Beta = 0.5$, this
21 indicates a security less risky than the market in general.

1 **Q. WHAT IMPACT DOES THE COST OF CAPITAL SETTLEMENT HAVE ON**
2 **PGE'S INITIAL REVENUE REQUIREMENT FILED IN THIS DOCKET?**

3 A. The cost of capital settlement described in my testimony results in a revenue
4 requirement decrease of approximately \$12.9 million.

5 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

6 A. Yes.

CASE: UE 197
WITNESS: Bryan Conway

**PUBLIC UTILITY COMMISSION
OF
OREGON**

STAFF EXHIBIT 701

Witness Qualification Statement

August 5, 2008

WITNESS QUALIFICATION STATEMENT

NAME: Bryan A. Conway

EMPLOYER: Public Utility Commission of Oregon

TITLE: Administrator, Telecommunications Division

ADDRESS: 550 Capitol Street NE Suite 215, Salem, Oregon 97301-2115.

EDUCATION: B.S. University of Oregon, Eugene, Oregon
Major: Economics; 1991

M.S. Oregon State University, Corvallis, Oregon
Major: Economics; 1994

In addition, I have completed all of the required and elective coursework for a Ph.D. in economics from Oregon State University. My fields of study were Industrial Organization and Applied Econometrics.

EXPERIENCE: Starting in October 1998, I have been employed by the Public Utility Commission of Oregon. I am currently the Administrator of the Telecommunications Division. My responsibilities include leading research and providing technical support on a wide range of policy issues for telecommunications utilities. My previous position was the Program Manager of the Economic & Policy Analysis Section where my responsibilities included leading research and providing technical support on a wide range of policy issues for electric, telecommunications, and gas utilities. I have testified before the Commission on policy and technical issues in UG 132, UE 115, UE 116, UE 170, UE 179, UE 180 and have been the Summary Staff Witness in UP 158, UP 168, UP 165/170, UX 27, UX 28, UM 967, UM 1041, UM 1045, UM 1121, UM 1206, UM 1209, and UM 1283.

OTHER EXPERIENCE: I am currently an adjunct faculty member Chemeketa Community College teaching principles of economics.

From September 2002 through June 2006, I was a faculty member of the University of Phoenix teaching various economics courses.

From January 1998 through September 2000, I was a part time instructor at Linn-Benton Community College teaching principles of economics.

From July 1992 through June 1994, I was a graduate teaching assistant at Oregon State University teaching introductory principles of economics.

CASE: UE 197
WITNESS: Bryan Conway

**PUBLIC UTILITY COMMISSION
OF
OREGON**

STAFF EXHIBIT 702

**Exhibits In Support of
Direct Testimony**

August 5, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2008**
- OR**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____**

Commission File Number: 1-5532-99

PORTLAND GENERAL ELECTRIC COMPANY

(Exact name of registrant as specified in its charter)

Oregon
(State or other jurisdiction of
incorporation or organization)

93-0256820
(I.R.S. Employer
Identification No.)

**121 SW Salmon Street
Portland, Oregon 97204
(503) 464-8000**

(Address of principal executive offices, including zip code,
and Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Number of shares of common stock outstanding as of April 30, 2008 is 62,532,232 shares.

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PORTLAND GENERAL ELECTRIC COMPANY AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in millions)
(Unaudited)

	<u>March 31,</u> <u>2008</u>	<u>December 31,</u> <u>2007</u>
<u>ASSETS</u>		
Current assets:		
Cash and cash equivalents	\$ 51	\$ 73
Accounts and notes receivable, net	233	178
Unbilled revenues	79	92
Assets from price risk management activities	202	64
Inventories, at average cost	60	64
Other current assets	53	67
Total current assets	678	538
Electric utility plant, net	3,147	3,066
Other property and investments:		
Nuclear decommissioning trust	46	46
Non-qualified benefit plan trust	63	69
Miscellaneous	17	19
Total other property and investments	126	134
Regulatory assets	252	304
Other noncurrent assets	66	66
Total assets	\$ 4,269	\$ 4,108
<u>LIABILITIES AND SHAREHOLDERS' EQUITY</u>		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 273	\$ 227
Liabilities from price risk management activities	99	101
Other current liabilities	49	40
Deferred income taxes	40	-
Accrued taxes	28	23
Total current liabilities	489	391
Long-term debt	1,256	1,313
Regulatory liabilities	727	574
Deferred income taxes	234	279
Non-qualified benefit plan liabilities	88	86
Accumulated asset retirement obligations	88	91
Other noncurrent liabilities	57	58
Total liabilities	2,939	2,792
Commitments and contingencies (see notes)		
Shareholders' equity:		
Common stock, no par value, 80,000,000 shares authorized; 62,532,232 and 62,529,787 shares issued and outstanding as of March 31, 2008 and December 31, 2007, respectively	647	646
Accumulated other comprehensive loss	(4)	(4)
Retained earnings	687	674
Total shareholders' equity	1,330	1,316
Total liabilities and shareholders' equity	\$ 4,269	\$ 4,108

See accompanying notes to condensed consolidated financial statements.

CERTIFICATE OF SERVICE

UE 197

I certify that I have this day served the foregoing document upon all parties of record in this proceeding by delivering a copy in person or by mailing a copy properly addressed with first class postage prepaid, or by electronic mail pursuant to OAR 860-13-0070, to the following parties or attorneys of parties.

Dated at Salem, Oregon, this 5th day of August, 2008.



Kay Barnes
Public Utility Commission
Regulatory Operations
550 Capitol St NE Ste 215
Salem, Oregon 97301-2551
Telephone: (503) 378-5763

**UE 197
Service List (Parties)**

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