

BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF THE APPLICATION)
OF IDAHO POWER COMPANY FOR)
AUTHORITY TO INCREASE ITS RATES)
AND CHARGES FOR ELECTRIC SERVICE)
TO ELECTRIC CUSTOMERS IN THE STATE)
OF IDAHO.)

CASE NO. IPC-E-03-13

IDAHO POWER COMPANY

DIRECT TESTIMONY

OF

DENNIS C. GRIBBLE

1 Q. Would you state your name, address and
2 present occupation?

3 A. My name is Dennis C. Gribble and my business
4 address is 1221 West Idaho Street, Boise, Idaho. I am
5 employed by Idaho Power Company as Assistant Treasurer.

6 Q. What is your educational background?

7 A. I graduated in 1975 from Boise State
8 University, Boise, Idaho, receiving a Bachelor of Business
9 Administration degree in Economics. In 1978, I graduated
10 from Boise State University, Boise, Idaho, with a Master in
11 Business Administration. In 1989, I completed the
12 University of Idaho's Public Utilities Executive Course in
13 Moscow, Idaho. I have also attended numerous seminars and
14 conferences on accounting and finance issues related to the
15 utility industry. I am a Certified Treasury Professional.

16 Q. Would you please describe your business
17 experience with Idaho Power Company?

18 A. I joined Idaho Power Company in 1979. In
19 June 1982, I transferred to the Finance and Reporting
20 Services Department as a Business Analyst. In June 1986, I
21 was promoted to a Business Analyst Supervisor. In March
22 1991, I was promoted to Manager of Financial Services. In
23 January 1992, I was promoted to Manager of Corporate
24 Accounting and Reporting. In 1996, I was promoted to
25 Controller-Financial Services and in May 1999 I was promoted

1 to my current position as Assistant Treasurer.

2 In the course of my duties with Idaho Power Company,
3 I have presented testimony to the Idaho Public Utilities
4 Commission and the Oregon Public Utility Commission.

5 Q. What are your duties as Assistant Treasurer
6 as they relate to the current proceeding?

7 A. I oversee the direct financial planning,
8 procurement, and investment of funds for Idaho Power, as
9 well as supervise corporate liquidity management.

10 Q. What are your financial activities and
11 responsibilities with respect to Idaho Power Company?

12 A. My activities and responsibilities include
13 various aspects of all the Company's financings and other
14 financial matters. With respect to long-term financings -
15 sale of bonds, preferred stock, and common stock - my
16 activities include development of financial plans with
17 senior officers, meeting with representatives of investment
18 banking firms that are interested in underwriting our
19 securities, discussions with rating agencies, assisting in
20 preparation of financial material including Registration
21 Statements filed with the Securities and Exchange
22 Commission, representing the Company at information meetings
23 for investment banking firms, reviewing recommendations on
24 bids received relative to the Company's financings and
25 recommending disposition of net proceeds. With respect to

1 short-term financings, these activities and responsibilities
2 include negotiation of lines of credit with commercial banks
3 and arranging for the sale of commercial paper.

4 Q. Are you in continual communication with
5 members of the financial community?

6 A. Yes. I am in constant contact with
7 individuals representing investment and commercial banking
8 firms, rating agencies, insurance companies, institutional
9 investment firms, and other organizations interested in
10 publicly traded securities, that actively follow IDACORP and
11 Idaho Power Company. In association with the Chief
12 Financial Officer and the Director of Investor Relations, my
13 responsibilities include keeping these persons informed of
14 the Company's financial condition, arranging meetings with
15 these people and Idaho Power's senior executive management,
16 and visiting with financial representatives in their
17 respective offices. These members of the investment
18 community have followed the electric utility industry for an
19 extended period of time and have a great deal of expertise
20 in the financial problems and prospects of utilities.

21 Through my continual contact with the financial
22 community, and review of investment banking analytical
23 reports and articles issued by these firms, I am able to
24 keep informed on trends, interest rates, financing costs,
25 security ratings, and other financial developments in the

1 public utility industry.

2 Q. Are you a member of any professional
3 societies or associations?

4 A. Yes. I am a member of the Association for
5 Financial Professionals (AFP) and the Institute of
6 Management Accountants (IMA).

7 Through information received from attendance at
8 conferences and seminars of these and other utility
9 professional groups such as the Edison Electric Institute, I
10 am able to gain additional insights into the financial
11 developments affecting Idaho Power Company as well as the
12 electric utility industry.

13 Q. What is the purpose of your testimony in this
14 proceeding?

15 A. I am sponsoring testimony as to the point
16 estimate for Idaho Power Company's rate of return on common
17 equity, the embedded cost of long-term debt and preferred
18 stock, the use of an estimated year-end 2003 capital
19 structure, and the resultant overall cost of capital to be
20 used in these proceedings.

21 Q. What exhibits are you sponsoring?

22 A. I am sponsoring Exhibits numbered 12 through
23 15.

24 Q. What is the point estimate you recommend for
25 the rate of return on common equity for Idaho Power Company?

1 A. As I will discuss in further detail later in
2 my testimony, I have selected 11.2 percent as a reasonable
3 cost of equity for the Company, which falls at the mid-point
4 of Mr. Avera's recommended cost of equity range for Idaho
5 Power Company of 10.6 to 11.9 percent. The 11.2 percent is
6 also the minimum required fair rate of return considering
7 the Company's overall management efforts throughout these
8 last ten years as discussed by Mr. Keen and Ms. Fullen in
9 their testimony, as well as the Company's efforts to
10 economically refinance outstanding debt and preferred stock
11 securities in recent years.

12 Q. What is the overall cost of capital for Idaho
13 Power Company?

14 A. Based on an estimated year-end 2003 capital
15 structure provided to me by Ms. Smith, the embedded cost of
16 debt and preferred stock presented in my testimony, and
17 incorporating the 11.2 percent cost of equity, the resultant
18 overall cost of capital for Idaho Power Company is 8.334
19 percent.

20 Q. Mr. Avera indicates that his 10.6 to 11.9
21 percent recommended cost of equity range does not include
22 any additional basis points as an incentive to the Company
23 for its stewardship of the system and overall management
24 efforts described by Mr. Keen and Ms. Fullen nor for the
25 Company's efforts to economically refinance its securities.

1 What effect does this have on your 11.2 percent point
2 estimate for the rate of return on the Company's common
3 equity?

4 A. If the Commission selects a cost of equity
5 value that is less than the mid-point of the recommended
6 cost of Mr. Avera's recommended equity range, then the
7 Company will be penalized since the cost of equity range
8 derived by Mr. Avera does not include any such reward.

9 Q. Mr. Avera indicates in his testimony that
10 Idaho Power, when compared to the Western electric utility
11 industry and its selected comparable peer group, has a
12 greater share of specific risk. Do you agree with this
13 conclusion?

14 A. Yes. Financial analysts, bond rating
15 agencies, regulators, and other commentators in the
16 financial press continue to chronicle the increasing
17 volatility of change and risk in the western electric
18 utility industry. The Company, not unlike the majority of
19 the industry, also faces the prevalence of change and
20 uncertainty. Most observers agree that individual companies
21 tend to have increasingly less and less control of both the
22 pace and magnitude of this change and uncertainty. In
23 addition to the impact of the general electric utility
24 industry risk, Idaho Power Company faces very specific
25 risks.

1 level."

2 Q. Please describe the risks specific to a
3 predominately hydroelectric generating base subject to the
4 vagaries of weather and water.

5 A. Idaho Power Company and its customers have
6 long enjoyed the benefits of a hydroelectric based utility.
7 However, because of the heavy reliance on hydroelectric
8 generation, the Company's operations and resulting financial
9 condition can be significantly impacted by low water
10 conditions. Reduced hydroelectric generation resulting from
11 below normal water flows, compels the Company to use more
12 expensive thermal generation and/or purchased power to meet
13 the electrical needs of its customers. Although the Idaho
14 Public Utilities Commission (IPUC) grants recovery for the
15 majority of extraordinary purchased power costs through the
16 Company's Power Cost Adjustment Mechanism (PCA), the
17 recovery is less than 100 percent, is on a deferred basis,
18 and is subject to the regulatory process. Generally, the
19 investment community views the PCA mechanism as a positive
20 since it does allow for recovery of the majority of excess
21 net power supply costs. As a result of the 2000-2001
22 California energy crisis and four years of Northwest drought
23 conditions, the last three PCA rate proceedings (i.e., 2001,
24 2002, and 2003) have resulted in unprecedented increased net
25 power supply costs. Although originally conceived as a fair

1 sharing mechanism, the Idaho jurisdictional 10 percent
2 portion of the recent PCA proceedings borne by the Company's
3 shareholders has had a devastating impact on the earnings
4 capability of the Company. Unlike the more familiar fuel
5 cost adjustment mechanisms (for gas utilities) that recover
6 100 percent of the changes in base fuel costs, the Company's
7 PCA mechanism is viewed by the investment community as more
8 risky as a result of this sharing feature. The firm of
9 Ragen MacKenzie reported this impact in its February 25,
10 2002 IDACORP, Inc. research report (pg.6); "IDACORP
11 estimates that Idaho Power Company's earnings (2002) would
12 have been \$1.45 higher (\$1.27 negative impact from excess
13 power costs not included in the PCA adjustment and a write-
14 off of \$0.18 for excess power costs) without the negative
15 impact of higher power costs."

16 Q. Please describe the risks specific to the
17 renewal of federal licenses for its hydroelectric projects,
18 namely the Hells Canyon Complex that provides 40 percent of
19 the Company's total generating capacity.

20 A. Idaho Power Company is the only investor-
21 owned electric utility in the United States with 57 percent
22 of its generation derived from hydro generating facilities
23 under normal water conditions. With such a large portion of
24 the Company's generation resources based on hydro
25 facilities, a negative economic impact resulting from

1 renewing the Federal licenses of these facilities could have
2 a significant financial impact on the Company and the prices
3 its consumers pay for electricity. As part of this process,
4 the Company has and will file applications with the Federal
5 Energy Regulatory Commission (FERC) for new licenses on 92
6 percent of its hydro generating capacity. Once an
7 application is filed, the time frame to actually receive an
8 order from the FERC is unknown. The combination of an
9 unknown time frame to receive a new license along with a
10 financial impact that is difficult to quantify, lays the
11 foundation for a potentially large financial risk unique to
12 the Company. The Hells Canyon generating facilities
13 comprised of Hells Canyon, Oxbow, and Brownlee make up 68
14 percent of the Company's hydro generation capacity and 40
15 percent of its total generation capacity. The Hells Canyon
16 license application was filed in July of 2003. This process
17 moves at an extremely deliberate pace due to the large
18 number of interested parties involved in evaluating the
19 application. This makes the likelihood of a new Hells
20 Canyon facilities license being issued in 2005 remote. In
21 these types of delayed situations, historically the Company
22 has been given an annual license renewal (under the existing
23 old license) until the formal new license is issued. This
24 delay further reinforces the ambiguity of the ultimate
25 financial impact. For any particular generating facility,

1 the worst possible outcome would be the loss of the license
2 to a competing party. Along with the uncertainty as to the
3 eventual receipt of licenses and the costs involved in
4 preparing for the license applications, costs of protection,
5 mitigation and enhancement of natural resources (PME's)
6 related to these projects are also difficult to quantify.
7 The potential financial magnitude of these PME's and their
8 effect on the Company's low cost hydrogeneration resources,
9 threaten the financial stability of a company the size of
10 Idaho Power and the ultimate rates it must charge its
11 customers. These amounts will vary between each facility,
12 but in all cases they can be significant due to lost
13 capacity, less generation at a higher cost, and the
14 decreased ability of the Company to time and control water
15 flows. If the Company cannot generate when it is most
16 advantageous for the system, then some of the economic value
17 of the generation has been lost, even if the amount of total
18 generation does not change. Kevin Rose, an analyst with
19 Moody's Investor Services notes in his June 20, 2003 Opinion
20 update on Idaho Power Company (Pg. 2); "What Could Change
21 the Rating - DOWN....., Significant increases in relicensing
22 costs and/or stringent operational constraints imposed as
23 part of the license renewal process..."

24 In addition to the hydro relicensing risk, the
25 Company continually faces significant capital, operating and

1 other costs associated with compliance with current
2 environmental statutes, rules and regulations. These costs
3 may be even higher in the future as a result of, among other
4 factors, changes in legislation and enforcement policies and
5 the potential additional requirements imposed in connection
6 with the relicensing of the Company's hydroelectric
7 projects.

8 Q. Why do you say that a volatile wholesale
9 power supply market in the Western United States and
10 specifically the Northwest is specific to Idaho Power
11 Company?

12 A. The recent California energy crisis and its
13 unprecedented effects on the prices in the wholesale energy
14 markets, coupled with persistent drought in the Northwest
15 have specifically impacted the Company. These impacts are;
16 first, and as noted above, reduced access to the Company's
17 low cost hydroelectric generation, second, increased
18 reliance on the Company's thermal based generating
19 resources, and lastly, the heightened exposure to volatile
20 wholesale energy prices when the Company must rely on the
21 wholesale energy market to meet native load requirements.
22 When the Company is unable to utilize its hydro resources,
23 it must next turn to the wholesale markets or its own
24 thermal based resources. Typically pricing and availability
25 will determine these decisions. Over the last several

1 years, the Company's thermal fleet has been required to
2 supply a large amount of the resource deficit since the
3 wholesale energy market prices were extremely high and hydro
4 availability was low. Although these thermal resources have
5 been there when dispatched, these thermal resources are
6 aging and are requiring increased capital and O&M
7 expenditures just to maintain availability. As the
8 reliability of these thermal resources diminishes, either as
9 a result of age or over-utilization, the Company is further
10 at the mercy of a volatile western and northwest energy
11 market. Philip C. Adams, Banc One Capital Markets, Inc.,
12 describes this situation in his December 12, 2002 Update and
13 New Issue Review (Pg. 2), " Challenges: IPC is on its third
14 consecutive year of below-average water availability for
15 hydroelectric power. Its reliance on purchased power
16 remains higher than normal, forcing IPC to fund purchases in
17 anticipation of rate relief. IPC relies heavily on
18 hydroelectric power for its generating needs and can
19 experience a negative impact from adverse weather, such as a
20 low snow pack in the mountains above IPC reservoirs, or low
21 precipitation levels. As demand outstrips hydroelectric
22 capacity, more expensive coal and diesel facilities, along
23 with purchased power, are needed to make up the difference."

24 Q. Please describe the risks specific to the
25 Company's ability to recover significant capital investment

1 required for present and growing electrical requirements and
2 service reliability for its customers.

3 A. As the Company's system ages and customer
4 electrical requirements increase, additional investment is
5 required to meet reliability standards and the additional
6 demand on its electrical infrastructure. The Company's
7 latest forecast requires construction budgets of \$150
8 million in 2003; this budget will rise to \$675 million over
9 the next three years. Recovery of these investments
10 introduces an element of risk since; first, the need for the
11 Company's to attract capital, and second, recovery of these
12 investments will be on a deferred basis and subject to the
13 regulatory process. Kevin Rose, Moody's Investors Services,
14 identifies one of the Company's key credit challenges in his
15 June 20, 2003 Opinion Update as; "General rate increase
16 needed to recover costs of customer growth, additional
17 capacity needs and expansion of T&D system."

18 Q. What is the status of Idaho Power Company's
19 bond ratings?

20 A. The following are the current First Mortgage
21 Bond (FMB), Preferred Stock, Commercial Paper (CP-short term
22 debt), and Rating Outlook ratings for Idaho Power Company:

	<u>Moody's</u>	<u>S. & P.</u>	<u>Fitch</u>
23			
24 General Corporate Rating	A3	A-	No Rating
25 FMB's	A2	A	A

1	Preferred	Baa2	BBB	BBB+
2	CP	P-1	A-2	F-1
3	Outlook	Negative	Stable	Stable

4 Q. Have the Company's ratings been under
5 pressure in recent years?

6 A. Yes. Although the bond ratings for the
7 Company's first mortgage bonds have remained intact, the
8 ratings on its preferred stock were changed due to a rating
9 agency philosophy that replaced preferred stock ratings with
10 a debt like standard. Accordingly, S&P has changed its
11 rating on the Company's short term debt from A-1 to A-2,
12 Moody's has the Company on a Negative Rating Outlook, and
13 S&P has moved the Company from a Positive to a Stable
14 Outlook. Moody's reasoned as follows; "IPC's rating outlook
15 is negative as the utility continues to cope with difficult
16 power supply markets in the region and prepares to seek a
17 base rate increase to bolster utility returns and cash flow.
18 Affiliate transaction issues with FERC and the IPUC have
19 been largely resolved without undue cost, although certain
20 internal compliance assessments still need to be completed."
21 Swami Ven Kataroman, Standard & Poor's, in his October 3,
22 2003 update, states: "Standard & Poor's now expects that
23 ratios will only meet expectations for the 'A-' rating and
24 may even be slightly weaker in the interim, as Idaho Power
25 continues to recover deferred power costs and face poor

1 water conditions in the Snake River and lower than expected
2 sales." The Company's S&P financial measurement benchmarks
3 reflect the financial pressure the Company faces in
4 maintaining its current ratings.

5 Q. What are the principal financial measurement
6 ratio benchmarks used by Standard and Poor's (S&P)?

7 A. The first benchmark is the funds from
8 operations (FFO) as a percent of average total debt. The
9 second principal benchmark is FFO interest coverage. Pre-
10 tax cash interest coverage is the third benchmark. The
11 fourth benchmark used by Standard and Poor's is the ratio of
12 total debt to total capital. In the first three benchmarks
13 higher scores are better, while in the fourth benchmark, a
14 lower score is better. These objective measurements are but
15 one set of tools that Standard & Poor's use in determining
16 the ultimate credit rating for a company. Other factors
17 that standard and Poor's considers are management
18 credibility and track record, forecasts provided by
19 management, and general overall judgment by the rating
20 agency committees.

21 Q. What are the Standard and Poor's electric
22 utility financial ratio benchmarks?

23 A. The Standard and Poor's electric utility
24 financial ratio benchmarks are set forth in Exhibit No. 12.

25 Q. How does Idaho Power Company's current (12

1 months ended June 30, 2003) S&P financial ratio benchmarks
2 compare with the mid-point ratio benchmarks for an "A" rated
3 electric utility with a level 4 business risk position (the
4 Company's current risk position).

5 A. The resulting ratios are as follows:

	<u>"A"</u>	<u>IPCo</u>
7 FFO/total debt (%)	30.5%-24.5%	24.4%
8 FFO interest coverage (x)	4.5x-3.8x	6.70x
9 Pretax interest coverage (x)	4.0x-3.3x	2.00x
10 Total debt/total capital (%)	43.0%-49.5%	52.9%

11 Q. What do the Company's current financial
12 benchmark ratios indicate regarding the Company's financial
13 condition?

14 A. Using a strict analytical approach, the
15 FFO/total debt ratio of 24.4 percent would warrant a high
16 "BBB" rating, the FFO interest coverage of 6.70x would yield
17 a high "AA" rating (this ratio will decline, however, due to
18 the recent reductions in PCA recovery), the Pretax interest
19 coverage of 2.00, would produce a high "BB" rating, and the
20 Total debt/total capital ratio of 52.9 percent, would score
21 a "BBB" rating. Rating agency analysts must and do take
22 into account qualitative aspects of a company, but a literal
23 interpretation of these quantitative financial benchmark
24 results would suggest a downgrade from the Company's current
25 "A" rating.

1 Q. What are the implications to the Company of
2 increasingly more stringent risk assessments by rating
3 agencies and the Company's current financial benchmark
4 ratios?

5 A. Without adequate rate relief and more normal
6 water conditions, it is uncertain as to how long the Company
7 can maintain an "A" rating. Although many Investor-Owned
8 Utilities (IOU's) find a "BBB" or "BBB+" acceptable, the
9 Company believes that maintaining a strong "A" rating is
10 essential. The Company must maintain its ability to attract
11 capital in the ultra-competitive investing environment.
12 Idaho Power is not a large electric utility and when matched
13 against other utility investment opportunities, the Company
14 lacks the benefit of broad investment analyst coverage.
15 Unless a strong single "A" rating is maintained; the absence
16 of broad investment analyst coverage and the small size of
17 the Company could prove to great an obstacle for the Company
18 to overcome in its efforts to raise capital. A "BBB" rating
19 for the Company would mean a 50-55 basis point annual
20 increase on newly issued long-term debt and prevent the
21 Company from accessing the low-cost short-term commercial
22 paper (CP) market. Without access to the CP market, the
23 Company will pay an added 70-80 basis points for short-term
24 debt. In simple terms, a strong "A" rating is critical for
25 Idaho Power to maintain its independence and attract lower

1 cost capital as the Company enters into a period of
2 substantial investment requirements.

3 Q. Is Idaho Power also affected by rating
4 agencies imputing debt onto its balance sheet due to
5 purchased power contracts?

6 A. Yes. Like other electric utilities, when the
7 Company adds to its rate base, it must use some portion of
8 shareholder equity to fund the investment. The Company must
9 maintain its equity component above a certain level as it
10 continues this investment process. Or as the debt levels
11 increase, the Company will face the threat of a bond
12 downgrading. Conversely, when the Company enters into
13 contracts for purchased power, an obligation that is not
14 reflected in its financial statement, an increase in equity
15 to maintain credit quality is not automatic. This lack of
16 required equity funding as an offset to the debt-like
17 obligation of purchase power contracts, results in an off
18 balance sheet risk. For financial commitments that do not
19 appear on the balance sheet, financial analysts and rating
20 agencies impute the debt and interest equivalents on the
21 financial statements of the Company to achieve a more
22 accurate picture of the risk associated with their
23 investment. The added equity needed to offset this imputed
24 debt and interest represents the effect that long-term
25 purchase power commitments have on the cost of capital. Any

1 increase in the long-term obligation of a utility related to
2 its capacity and energy resources will have to be backed by
3 an appropriate amount of equity in the eyes of the
4 investment community.

5 Q. In their testimony, Mr. Keen and Ms. Fullen
6 describe Company and management efforts in the areas of
7 stewardship of the system, customer service, and demand-side
8 management. Is there anything in the area of financing
9 activity that you feel deserves similar recognition?

10 A. Yes. In addition to the areas discussed in
11 detail by Mr. Keen, the Company has taken numerous
12 opportunities to refund various issues of both long-term
13 debt and preferred stock on a cost effective basis. This has
14 resulted in significantly lower embedded costs than would
15 otherwise have been the case. At the last Idaho general
16 rate case, the Company's overall cost of debt capital was
17 8.024 percent and the effective cost of preferred stock was
18 6.083 percent. As will be shown later in my testimony, the
19 Company's current cost of debt capital is 5.983 percent and
20 the effective cost of preferred stock is 6.534 percent. The
21 primary driver for the small increase in the effective cost
22 of preferred stock was the removal of the \$50 million
23 variable rate auction preferred stock that was redeemed in
24 August 2002. This redemption was due to a different
25 preferred stock rating criteria that placed added pressure

1 on the ability of this market to avoid a failed auction
2 process. The resulting financing efforts by the Company are
3 reflected by the overall cost of capital at the last Idaho
4 general rate case of 9.199 percent being reduced to the
5 current cost of capital of 8.334 percent that is proposed in
6 this filing.

7 Q. Would you please comment on page 1 of Exhibit
8 No. 13?

9 A. Page 1 of Exhibit No. 13 details the
10 calculation of the Idaho Power Company capital structure for
11 long-term debt, preferred stock, and common equity balance
12 resulting from the Company's estimated year end 2003 capital
13 structure as provided to me by Ms. Smith.

14 Q. Earlier in your testimony you indicated that
15 you have used an estimated 2003 financial result in arriving
16 at the overall cost of capital for the Company. Why have
17 you selected this particular capital structure?

18 A. The estimated year end 2003 financial results
19 as provided to me by Ms. Smith reflect the Company's best
20 estimate at this time of the 2003 year-end capital
21 structure. The Commission can update the capital structure
22 to incorporate known and measurable changes as this
23 proceeding progresses to reflect an actual year-end 2003
24 capital structure. Mr. Avera, in his testimony, has
25 indicated that the capital structure submitted on page 1 of

1 my Exhibit No. 13 is reasonable and is consistent with
2 comparable companies in the industry.

3 Q. The capital structure presented on page 1 of
4 Exhibit No. 13 incorporates changes to the Company's normal
5 financial reporting of its capital structure. Could you
6 please discuss the rationale for the variance?

7 A. For financial reporting purposes the American
8 Falls Bond Guarantee and the Milner Dam Note Guarantee are
9 included in the long-term debt portion of the capital
10 structure. For ratemaking purposes the interest costs
11 associated with both the American Falls and the Milner debt
12 securities are covered as operating and maintenance ("O&M")
13 expenses. Even with these exclusions, the capital structure
14 presented in my Exhibit No. 13 is reasonable in light of
15 industry and rating agency criteria.

16 Q. Would you please comment on page 1 of Exhibit
17 No. 14?

18 A. Page 1 of Exhibit No. 14 details the
19 calculation of the embedded cost of debt used in the
20 estimated year-end 2003 capital structure. The embedded
21 cost of debt is 5.983 percent.

22 Q. Does the Company utilize variable rate
23 securities in its long-term capitalization?

24 A. Yes, the Company currently utilizes several
25 variable rate securities in its long-term capitalization.

1 These securities are the County of Sweetwater Variable Rate
2 Series 1996B (\$24.2 million), and 1996C (\$24.0 million)
3 Pollution Control Bonds, and the Port of Morrow Variable
4 Rate Pollution Control Bonds (\$4.36 million). Also, the
5 Company intends to refinance its \$49.8 million, 8.30 percent
6 Humboldt County Pollution Control Revenue bonds in October,
7 2003 by issuing new \$49.8 million of variable rate bonds.
8 These securities are listed on lines 12, 13, 14, and 15 of
9 page 1 on Exhibit No. 14.

10 Q. Would you please describe the variable rate
11 nature of these variable rate pollution control bonds?

12 A. These variable rate pollution control bonds,
13 although considered long-term securities, have features that
14 allow the Company to take advantage of rates applicable to
15 short term securities. The County of Sweetwater Pollution
16 Control Variable Rate Bonds Series B and C (Bridger Variable
17 Rate Bonds) reset the interest rate on a daily basis. The
18 Port of Morrow Pollution Control Variable Rate Bonds
19 (Boardman Variable Rate Bonds) reset the interest rate on a
20 weekly basis. The proposed Humboldt Pollution Control
21 Revenue Bonds (Valmy Variable Rate Bonds) will reset their
22 interest rate every 35 days. The Bridger Variable Rate
23 Bonds daily rate interest rate is determined each business
24 day by a Remarketing Agent by examining tax-exempt
25 obligations comparable to the Bridger Variable Bonds known

1 to have been priced or traded under the then-prevailing
2 market conditions that would be the lowest rate which would
3 enable the Remarketing Agent to sell the Bridger Variable
4 Rate Bonds. Likewise, on a weekly basis the Boardman
5 Variable Rate Bonds weekly interest rate is determined the
6 first day of a weekly period by a Remarketing Agent by
7 examining tax-exempt obligations comparable to the Boardman
8 Variable Bonds known to have been priced or traded under the
9 then-prevailing market conditions that would be the lowest
10 rate which would enable the Remarketing Agent to sell the
11 Boardman Variable Rate Bonds. The new Valmy Variable Rate
12 Bonds are designed to reset their interest rate every 35
13 days via a dutch auction process (lowest bid received by an
14 Auction Agent that covers the bonds outstanding) to reflect
15 the current market conditions.

16 Q. Please comment on the derivation of the
17 effective cost of the interest rates for the Pollution
18 Control Bonds listed on lines 12, 13, 14, and 15 on page 1
19 of Exhibit No. 14?

20 A. Page 2 of Exhibit No. 14 is a chart that
21 depicts the Bond Market Association (BMA) Municipal Swap
22 Index for the last 10 years. The BMA Municipal Swap Index,
23 produced by Municipal Market Data (MMD), is a 7-day high-
24 grade market index comprised of tax-exempt Variable Rate
25 Demand Obligations (VRDO's) from MMD's extensive database.

1 The Index was created in response to industry participants'
2 demand for a short-term index to accurately reflect activity
3 in the VRDO market. In 1991, The Bond Market Association
4 established a Market Index Subcommittee to analyze the need
5 for such an index, and determined a solution. MMD worked
6 closely with The Bond Market Association to determine
7 appropriate criteria on which to base the index. Issuers,
8 investment bankers and other market participants need an
9 efficient way to monitor the market on a regular basis. The
10 index provides a consistent, superior means of tracking
11 market movements as they occur.

12 Pages 3, 4, 5, and 6 of Exhibit No. 14 show the
13 Company's spreads (difference of the Company's actual
14 variable rate, plus or minus, when compared to the BMA
15 Municipal Swap Index) over the BMA Municipal Swap Index for
16 the Bridger Variable Rate Bonds and the Boardman Variable
17 Rate Bonds since the life of these bonds, plus an estimate
18 for the Valmy Variable Rate Bonds.

19 In light of the volatility in short-term interest
20 rates, I determined that an average of the 10 year BMA
21 Municipal Swap Index, plus an average of the Company's
22 spreads since the inception of these variable rate bonds,
23 should be used in calculating the cost of these securities.
24 This is a conservative approach in that, there are a
25 significantly larger amount of data points at the low end of

1 the 10-year cycle and the trough covers a relatively high
2 percentage of this cycle.

3 The average of the 10 BMA Municipal Swap Index is
4 3.04 percent, the average Company spreads for the Bridger
5 Variable Rate Bond Series B is -.07%, the Bridger Variable
6 Rate Bond Series C is -.12%, the Boardman Variable Rate Bond
7 is .94%, and the Valmy Variable Rate Bonds is .61% (includes
8 amortization of call premium, spread over BMA index, broker
9 dealer fees, and insurance costs). The resulting coupon
10 rates used for these variable rate securities are:

11 Bridger Variable Rate Bond Series B - 2.97%

12 Bridger Variable Rate Bond Series C - 2.92%

13 Boardman Variable Rate Bond - 3.98%

14 Valmy Variable Rate Bond is - 3.65%

15 Q. Would you please comment on Exhibit No. 15?

16 A. Exhibit No. 15 details the calculation of the
17 embedded cost of preferred stock used in the forecasted 2003
18 capital structure. The embedded cost of preferred stock is
19 6.534 percent.

20 Q. What is the overall weighted cost of capital
21 when you incorporate the respective costs?

22 A. The overall weighted cost of capital for
23 revenue requirement purposes in this proceeding is 8.334
24 percent. This is based on a 5.993 percent embedded cost of
25 debt; a 6.534 percent embedded cost of preferred stock; and

1 the 11.2 percent rate of return on common equity.

2 Q. Does this conclude your direct testimony in
3 this case?

4 A. Yes, it does.