value of 13.37 percent. This adjustment further increased Rothschild's DCF estimate to 10.13 percent. Finally, we correct Rothschild's inputs for the stock purchase date and price set at February 28, 2001, and adjust his M/B accordingly. This produces a final adjusted DCF estimate of 10.53 percent.

Together, these two adjusted estimates produce a cost of equity range of 10.53 to 10.95 percent, with a mid-point of 10.74 percent. We round this number to 10.75 percent. We find that this average of 10.75 percent is an appropriate cost of equity for the comparable group of electric utilities. We conclude, however, that this figure should be adjusted for PGE, whose capital structure contains a substantially higher percentage of common equity than the average for the comparative group of electric utilities.

It is well understood by finance practitioners and theoreticians that the cost of equity drops as the percentage of common equity in the capital structure increases. Because the average amount of common equity in the capital structure of the comparable group of electric companies was 45.14 percent compared to 52.16 percent for PGE, it necessarily follows that PGE has a lower cost of equity. PGE's capital structure is therefore less risky, and its cost of common equity should be adjusted accordingly.

The question therefore becomes how much of an adjustment should be made. This record contains varying estimates that the cost of equity for regulated electric utilities decrease anywhere from 4 to 13.8 basis points for each one percent increase in the level of common equity in the capital structure. We find Rothschild's proposed 25 basis point reduction to be a reasonable adjustment to account for the above average percentage of common equity in PGE's capital structure. Contrary to PGE's arguments, this reduction does not constitute a "penalty." Rather, it is simply an adjustment to acknowledge PGE's reduced financial risk due to its increased level of common equity in its capital structure. Reliance on the stipulation in docket UM 814 is reasonable for the purpose of establishing a capital structure for PGE. The stipulation, however, cannot reasonably be used to argue for an ROE that does not correspond to the adopted capital structure.

Accordingly, we will adopt this adjusted average of 10.50 percent as an appropriate and reasonable cost of equity for PGE.[47] Evidence shows that this award will allow PGE to maintain a reasonable financial structure and attract capital at a reasonable cost. Using this figure in connection with other stipulated capital costs and the company's capital structure, which we find reasonable and adopt, yields a rate of return for PGE of 9.09 percent.

Capital Component	Ratio	Cost	Weighted Cost
Long-term Debt	46.32 %	7.508 %	3.48 %
Preferred Stock	1.53 %	8.432 %	0.13 %
Common Equity	52.16 %	10.50 %	5.48 %
Total	100.00 %		9.09 %

Finally, we close this subject with a short discussion on efforts expended in this docket to fix a reasonable ROE for PGE. ROE determinations have always been a fundamental

[47] Given this conclusion, we need not address PGE's argument that Staff's ROE recommendation, if adopted, would impair the company's bond ratings.

Portland General Electric
Composite Cost of Capital
Test Year Based on 12 Months Ending 12/31/02

	Average Outstanding *	Percent	Percent Cost	Weighted Average Cost
Long Term Debt	$887,900	46.32%	7.80%	3.61%
Preferred Stock	$29,250	1.53%	8.43%	0.13%
Common Equity	$999,781	52.16%	11.50%	6.00%
Composite Cost of Capital	$1,916,931	100.00%		9.74%

* Represents the Average of the Month End Balances

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