

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In the Matter of the Application of PacifiCorp
and Scottish Power plc for an Order
Approving the Issuance of PacifiCorp
Common Stock

Docket No. 98-2035-04

PacifiCorp

Direct Testimony of Richard T. O'Brien

February 26, 1999

INTRODUCTION

1 Q. Please state your name and business address.

2 A. My name is Richard T. O'Brien. My business address is 825 N.E. Multnomah,
3 Portland, Oregon.

4 Q. By whom are you employed and in what position?

5 A. I am employed by PacifiCorp as Executive Vice President and Chief Operating
6 Officer.

7 Q. Please summarize your education and business experience.

8 A. I received a bachelor's degree in economics from the University of Chicago and a
9 law degree from Lewis and Clark College, Northwestern School of Law. From
10 1983 to 1993 I served in various financial positions at NERCO, a former mining
11 and resource development subsidiary of PacifiCorp. In 1993 I was appointed Vice
12 President of Corporate Finance of PacifiCorp and in 1995 was appointed Senior
13 Vice President and Chief Financial Officer. I was appointed to my current
14 positions in 1998.

15 Q. What position will you hold with PacifiCorp after the transaction with Scottish
16 Power plc ("ScottishPower") is closed?

17 A. I will be the President and Chief Operating Officer of PacifiCorp.

TESTIMONY SUMMARY

19 Q. What is the purpose of your direct testimony in this proceeding?

20 A. The purpose of my testimony is to explain why PacifiCorp decided to pursue a
21 transaction with ScottishPower and why we believe that the proposed transaction
22 is in the public interest.

1 In summary, we decided to pursue the transaction with ScottishPower because we
 2 believe a combination with ScottishPower will enable PacifiCorp to become a top
 3 performing utility quicker, more fully and with a higher degree of certainty than if we
 4 were to attempt it alone. Our combination with ScottishPower is in the public interest
 5 because:

- 6 • The combination with ScottishPower will result in a financially stronger
 7 company than PacifiCorp standing alone;
- 8 • ScottishPower will add significantly to PacifiCorp's ability to improve its
 9 reliability, system operations and customer service;
- 10 • ScottishPower and PacifiCorp together will produce greater efficiencies,
 11 innovations and cost savings in PacifiCorp's operations;
- 12 • ScottishPower has demonstrated its commitment to employees and the
 13 communities it serves and will enhance PacifiCorp's efforts in these areas; and
- 14 • ScottishPower will complement and strengthen PacifiCorp's efforts in
 15 environmental stewardship and the development and marketing of green
 16 power.

17 In addition, ScottishPower will commit to a comprehensive set of system
 18 performance standards and customer service guarantees that address our
 19 customers' most important service quality and customer service concerns. These
 20 standards will set a new benchmark for U.S. utilities.

21 DESCRIPTION OF TRANSACTION

22 Q. Please describe the proposed transaction with ScottishPower that is the subject of
 23 this proceeding.

1 A. The transaction is set out in detail in the Agreement and Plan of Merger dated as
2 of December 6, 1998 (“Agreement”) which was included with our Application in
3 this proceeding. Since entering into the Agreement, ScottishPower has decided to
4 create a new holding company for ScottishPower and its subsidiaries.
5 ScottishPower and PacifiCorp have executed an Amended and Restated
6 Agreement and Plan of Merger (“Amended Agreement”) under which PacifiCorp
7 would become a wholly owned subsidiary of the new holding company
8 (“HoldCo”) and a sister company to ScottishPower.
9 Under the Amended Agreement, Merger Sub, an indirect, wholly-owned
10 subsidiary of HoldCo, will merge with and into PacifiCorp, with PacifiCorp
11 continuing in existence as the surviving corporation.
12 Outstanding PacifiCorp common stock will be exchanged, at the option of the
13 holder, for either HoldCo American Depository Shares (each such ADR
14 representing four HoldCo ordinary shares) or HoldCo ordinary shares. ADR’s
15 trade on the New York Stock Exchange and pay dividends converted to dollars.
16 HoldCo ordinary shares will trade on the London Stock Exchange and pay
17 dividends in pounds sterling.
18 As a consequence of the transaction, HoldCo will indirectly own all of the
19 outstanding common stock of PacifiCorp. However, following the transaction, the
20 existing stockholders of PacifiCorp will control approximately 36% of the
21 common stock of HoldCo.
22 Q. Please describe the stock issuance associated with this transaction.

1 A. To accomplish the transaction, PacifiCorp will issue new common stock to
2 facilitate the merger of Merger Sub with and into PacifiCorp. Under the
3 Amended Agreement, upon the closing all shares of PacifiCorp common stock
4 will be canceled and retired, and PacifiCorp will issue new common stock to an
5 entity wholly-owned by HoldCo. PacifiCorp will thereafter continue to exist as an
6 indirect, wholly-owned subsidiary of HoldCo and will be an affiliate of
7 ScottishPower.

8 **REASONS FOR THE TRANSACTION**

9 Q. Why did PacifiCorp enter into this transaction with ScottishPower?

10 A. We entered into this transaction because we believe a combination with
11 ScottishPower represents the best and quickest way for PacifiCorp to achieve its objectives
12 of providing top quality service to its customers and a reasonable return to its shareholders.
13 We are also persuaded that a combination with ScottishPower would be in the best interests
14 of our employees and the communities we serve.

15 Q. Please explain your objective of becoming a top quality electric service provider.

16 A. We have been convinced for several years that in order to prosper in the changing
17 domestic electricity markets, a utility's services and costs must meet world class
18 standards. Business customers are becoming global in their operations and will expect
19 world class performance from their electricity suppliers. Suppliers who do not meet these
20 expectations will not succeed.

21 Providing world class performance does not mean that PacifiCorp must become
22 global in scope. Instead, it requires that PacifiCorp provide a level and quality of service

1 that is on a par with the best electric service providers in the world, and that it accomplish
2 this objective without compromising its low prices.

3 Our pursuit of a combination with The Energy Group was done to a significant
4 degree for the purpose of aiding us in our effort to become a world class electric service
5 provider. When it became apparent that transaction could not be done, or could only be
6 done at too high a cost, we abandoned it in favor of focusing on our core electricity
7 business in the western United States. We were prepared to try to become a top
8 performing electric service provider entirely on our own. We recognized the difficulty of
9 this task and understood that it would require many years to accomplish.

10 Despite our decision to focus on our core electricity business, we remained
11 convinced that our customers would be served best by a large, stable enterprise able to
12 offer the most competitive prices while providing customer service and reliability that
13 reflect the world's best practices. Similarly, our shareholders would be advantaged by
14 owning a part of such an enterprise.

15 Q. How does the ScottishPower transaction fit with your objective of becoming a top
16 performing electric service provider?

17 A. The ScottishPower transaction will bring to bear the combined experience, skill,
18 innovation and commitment of PacifiCorp and ScottishPower in the areas of electric
19 power supply and operations, customer service, community involvement, employee
20 relations and environmental stewardship. We are in the same business and share the
21 same objectives. We do not need to realign the objectives of either party.

22 ScottishPower is an excellent partner for PacifiCorp. Our assets, views and
23 objectives are complementary. ScottishPower is fully committed to our focus on the core

1 electricity business in the western United States and to our goal of providing world class
2 service. They have a proven and enviable record as a utility system operator. They are
3 innovative in their approach to the electricity business, particularly to system performance
4 and customer service issues, which are increasingly important. They have already
5 developed programs targeting areas in which PacifiCorp seeks to improve, including
6 service reliability, computer systems and customer care.

7 ScottishPower has already demonstrated that it is both skillful and agile in
8 transforming utilities into world class performers. By combining the experience and
9 skills ScottishPower has developed in the United Kingdom with PacifiCorp's own
10 experience and skills, we expect to achieve our operations and customer service
11 objectives faster, more fully and with more certainty than if we were to attempt it alone.

12 **BENEFITS OF THE TRANSACTION**

13 Q. How will the transaction benefit PacifiCorp customers?

14 A. Through the transaction, we will create a balanced and strong enterprise that can
15 provide the highest level of service to our customers while maintaining or
16 improving PacifiCorp's low costs. ScottishPower is a leader in efficient, reliable
17 operations and customer service. We expect that the ScottishPower experience
18 and excellence can be brought to PacifiCorp so that the two companies together
19 can provide service to our customers that reflects the best practices in the world.

20 Q. Did PacifiCorp pursue the transaction with ScottishPower in the expectation that
21 retail energy markets would soon be deregulated in the states where it serves?

22 A. No. While deregulation may ultimately be pursued in PacifiCorp's jurisdictions,
23 this was not the motivation for our wishing to take advantage of ScottishPower's

1 skills and experience. Efficiency, customer service and community involvement
2 are important regardless of the extent of regulation an electric utility faces. It is
3 our belief that if a company can provide superior customer and community service
4 in a deregulated environment, and at the same time be profitable and more
5 efficient, it has a lot to offer to a utility still subject to cost-of-service regulation. If
6 deregulation comes, we will be much better prepared for it as a result of our
7 affiliation with ScottishPower.

8 Q. Please comment on the system and customer service improvements you expect
9 will result from the transaction.

10 A. In their testimony, Messrs. Richardson and Moir describe a number of
11 improvements and explicit commitments that ScottishPower is prepared to make
12 regarding PacifiCorp's system performance and customer service. The system
13 performance commitments include improving system availability and reliability,
14 improving the worst performing circuits in each state on an annual basis,
15 improving the restoration of the system following outages and improving the
16 company's overall responsiveness to customers. The customer service
17 commitments include an array of individual service guarantees accompanied by
18 payments to customers for failure to perform. The nature and breadth of these
19 commitments and the fact that the customer service standards are backed up by
20 meaningful guarantees is unprecedented in the electric utility industry in the U.S.
21 I believe these standards will be the most comprehensive offered by any investor-
22 owned U.S. utility. They address all of the most important system performance
23 and customer service concerns. These standards will be of great value to

1 PacifiCorp's customers and will set a new benchmark for U.S. utilities. It is clear
2 to us that ScottishPower not only has unique operating experience but also a
3 unique understanding of the critical value of service quality and customer service.

4 Q. Couldn't PacifiCorp implement these service quality and customer service
5 standards without the proposed transaction?

6 A. Perhaps, but not as soon, not as fully and not with as high a probability of success.
7 As I said earlier, we looked into what we could accomplish on our own and how long it
8 would take us to accomplish our objectives after we abandoned The Energy Group
9 transaction. ScottishPower is willing to guarantee material service quality and customer
10 service improvements because it has accomplished these sorts of gains before. Lacking
11 this experience, PacifiCorp simply could not commit to achieving improvements this
12 substantial or this broad on this short a time schedule. I also expect that PacifiCorp could
13 not achieve these improvements as economically as it will be able to do in combination
14 with ScottishPower.

15 Our objectives are to raise our service to the highest levels while at the same time
16 maintaining or improving PacifiCorp's low costs. In combination, these are daunting
17 tasks, but ones we believe are necessary to serve our customers and survive in an
18 increasingly competitive industry. Our transaction with ScottishPower is a sign that we
19 are serious about these objectives and committed to achieving them quickly, fully and
20 economically.

21 Q. How will the benefits that you expect be reflected in PacifiCorp's prices?

22 A. Let me state first that improvements in service reliability, operational efficiencies
23 and customer service are extremely important and beneficial to customers in and

1 of themselves. These improvements require significant up-front investments and
2 their cost reduction benefits will be realized over a longer term. That said, I would
3 expect, based upon ScottishPower's experience in the U.K., that its involvement
4 with PacifiCorp's operations will result in significant efficiencies and cost savings
5 by the end of the five-year period discussed in Mr. MacRitchie's testimony.

6 In the normal course, as cost savings are realized they will be reflected in
7 PacifiCorp's cost of service for ratemaking purposes. Following the initial period
8 of service quality and customer service improvements, cost savings will begin to
9 occur and will reduce the need for price increases. These benefits will result in
10 prices lower than they would be without the transaction.

11 Q. Would it be appropriate for the Commission to require guaranteed price
12 reductions as a condition to approving the transaction between PacifiCorp and
13 ScottishPower?

14 A. No. Most regulatory proceedings involving utility mergers have related to
15 transactions that are principally motivated by the opportunity to capture savings or
16 efficiencies resulting from the consolidation of two domestic operating companies. In
17 these sorts of transactions, the parties have typically quantified potential savings as part of
18 their decision to pursue the transaction and their savings estimates are reasonably precise.
19 Examples of these sorts of transactions are the 1989 merger of PacifiCorp and Utah
20 Power & Light Company and the 1997 merger of Puget Sound Power & Light Company
21 and Washington Energy Company. In these circumstances, commissions have required
22 some measure of price reductions to reflect the projected savings that have been
23 quantified by the parties and have served as the basis for the commission's approval.

1 The present transaction does not involve the consolidation of two operating
2 companies and is not principally motivated by potential operating improvements
3 and savings. Even if one adopts the view that the standard for Commission
4 approval requires “positive net benefits” to customers, the expectation that this
5 transaction will result in better and more reliable service is more than enough to
6 constitute positive net benefits to customers.

7 Q. How will the transaction benefit PacifiCorp’s employees?

8 A. PacifiCorp’s employees will have opportunities to work for a fast-growing,
9 financially-stable, competitive and innovative company. As detailed in the
10 testimony of Mr. Kelly, ScottishPower has a superb reputation in regard to the
11 training opportunities and other benefits it offers its employees. Many of these
12 opportunities, as well as international employee exchanges, will be available to
13 PacifiCorp employees. ScottishPower also works responsibly and collaboratively
14 with unions and has committed to honoring all existing labor agreements.

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1 Q. How will the transaction benefit the environment?

2 A. Like PacifiCorp, ScottishPower is a leader in the industry in developing policies,
3 programs and incentives for “green” energy, particularly wind turbines. PacifiCorp is the
4 leading purchaser of wind power facilities in the western United States outside of
5 California. PacifiCorp also is the largest supplier to the leading green marketer in
6 California and has the only operating geothermal facility serving the northwest. In
7 collaboration with environmental, consumer and regulatory groups, PacifiCorp
8 incorporated renewable resource incentives into its alternative form of regulation in
9 Oregon.

10 The combination with ScottishPower will strengthen PacifiCorp’s resources
11 dedicated to environmental programs and the goal of becoming a leading developer and
12 marketer of green energy. As Mr. Richardson testifies, ScottishPower will commit to
13 implementing internal processes and systems that emphasize improving environmental
14 performance in PacifiCorp’s operations, filing “green resource” tariffs in each state,
15 contributing \$100,000 to the Bonneville Environmental Foundation, developing an
16 additional 50 MW of renewable resources and studying a possible expansion of the
17 Blundell geothermal project. PacifiCorp alone would not undertake all of these initiatives
18 simultaneously and could not accomplish them as quickly as we can with the help of
19 ScottishPower.

20 Q. What about the communities in which PacifiCorp provides electric service?

21 A. Mr. Kelly describes in his testimony the active role that ScottishPower has taken
22 in its local communities. A very tangible community benefit is reflected in the
23 Agreement, and retained in the Amended Agreement, where ScottishPower has

1 agreed add \$5 million to the PacifiCorp Foundation, increasing its endowment by
2 approximately 12.5% to \$45 million. These funds will be available for charitable
3 use throughout the PacifiCorp service territories.

4 Both ScottishPower and PacifiCorp are committed to developing, maintaining and
5 improving their local presence in PacifiCorp's service territories. Following the
6 closing of the transaction, the new U.S. headquarters for ScottishPower will be
7 located in Portland, Oregon. PacifiCorp will still be headquartered in Portland
8 and will continue to have significant functions led from Salt Lake City, Utah.

9 While PacifiCorp will continue to be operated as an integrated utility,
10 ScottishPower respects the unique histories of Pacific Power and Utah Power and
11 expects to draw on the strengths of these histories in forging its community
12 relationships. It has done the same with Manweb and Southern Water, the two
13 utilities it acquired in the U.K.

14 More broadly, as a result of the transaction, PacifiCorp will be financially stronger
15 and better able to survive and prosper in a changing electricity industry. We
16 recognize that PacifiCorp is an important economic contributor to many
17 communities in the western United States. The size and financial stability this
18 transaction will bring to PacifiCorp will assure that we will be around performing
19 that role for many years to come.

20 Q. Does this conclude your direct testimony?

21 A. Yes.

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