

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

In The Matter Of The Application of)
PacifiCorp and Scottish Power plc) Docket No. 98-2035-004
for an Order Approving the Issuance)
of PacifiCorp Common Stock)

SCOTTISH POWER

DIRECT TESTIMONY OF ROBERT D. GREEN

FEBRUARY 26, 1999

I.INTRODUCTION

- Q. Please state your name and business address.
- A. My name is Robert D. Green, and my business address is 500 NE Multnomah, Suite 900, Portland, Oregon.
- Q. By whom are you employed and in what capacity?
- A. I am employed by Scottish Power plc ("ScottishPower"), a Glasgow-based company in the United Kingdom ("U.K."). My title is Group Controller.
- Q. What are your responsibilities in your current position?
- A. My responsibilities are to oversee the state regulatory approval process.
- Q. What position will you hold with PacifiCorp after this transaction is closed?
- A. After the transaction is completed, I will be the Chief Financial Officer of PacifiCorp.
- Q. Please summarize your education and previous business experience.
- A. I was educated at Dulwich College, a private school in London. I then attended Oxford University, gaining a degree in mathematics. I am a U.K. qualified chartered accountant. I have worked in a variety of businesses in senior financial positions. I have previous experience working in Hong Kong and for companies such as ITT, ADT and Rank. In ScottishPower, which I joined in 1991, I have held a variety of senior financial posts including Finance Director of Manweb plc before being appointed as Group Controller in 1996.
- Q. Please summarize your direct testimony in this proceeding.
- A. After providing background information on the transaction, my testimony makes the following points:
- C Ratemaking Policy:** The transaction will over time lead to prices for customers that are lower than they would have been without the transaction.
 - C Financial Integrity:** PacifiCorp will benefit from ScottishPower's financial strength, which should over time lead to lower borrowing costs as the financial markets perceive PacifiCorp's improved financial position.
 - C Cost Allocations and Affiliate Transactions:** ScottishPower currently complies with strict cost allocation and reporting requirements agreed to with its regulators in the U.K., and is capable of complying with similar affiliate rules and cost allocation methodologies applied by this Commission. I will explain how these would apply to PacifiCorp.
 - C Access to Books and Records:** The transaction will have no impact on the Commission's access to PacifiCorp's books and records.
- I conclude by setting forth the conditions with which ScottishPower would comply in connection with regulatory approval of the transaction.
- Q. Please describe the transaction that will create the combined company, ScottishPower.
- A. ScottishPower proposes to merge with PacifiCorp by acquiring all of the outstanding common stock of PacifiCorp. Under the terms of the agreement, each PacifiCorp share will be exchanged tax-free for 0.58 American Depositary Receipts or 2.32 ordinary shares of ScottishPower. Before allowance for any buyback, this will give ScottishPower shareholders approximately 64% and current PacifiCorp shareholders approximately 36% ownership in the combined group. The combined company will be headquartered in Glasgow, Scotland and operate under the name of ScottishPower. Its U.S. headquarters

- will be located in Portland, Oregon. PacifiCorp will continue to operate in the U.S. under its current name and will still be headquartered in Portland, Oregon.
- Q. Are there other organizational changes that will occur in connection with the transaction?
- A. Yes. A holding company, or "HoldCo," will be formed in connection with the transaction. ScottishPower and PacifiCorp will both be subsidiaries of HoldCo. The existing organization charts for ScottishPower and PacifiCorp are shown on pages 1 and 2, respectively, of Exhibit SP __ (RDG-1). The anticipated organization chart for the new organization after the transaction is shown on page 3 of my Exhibit SP __ (RDG-1).
- Q. What is the accounting method that will be used for the transaction?
- A. The transaction will be accomplished through a share-for-share exchange for all of the issued and outstanding shares of PacifiCorp common stock in a transaction in which all outstanding debt obligations of PacifiCorp will remain. This form of transaction is required to be accounted for using the "purchase" method of accounting. The purchase method of accounting requires all assets and liabilities of PacifiCorp to be valued at fair market value at the time of closing of the transaction. After assigning fair market values to all identifiable assets and liabilities, any unallocated portion of the purchase price is recorded as goodwill.
- Q. What are the documents associated with the transaction?
- A. The Agreement and Plan of Merger ("Merger Agreement"), included as Appendix 1 to the Application, was entered into by ScottishPower and PacifiCorp on December 6, 1998. The Merger Agreement describes the reorganization transaction and the rights and responsibilities of the various entities. The Merger Agreement was subsequently amended, and the amended Merger Agreement will be substituted for the document included with the Application. Exhibit SP __ (RDG-2) is the confidential preliminary Proxy Statement. The final Proxy Statement will be provided once it is available.
- Q. Please briefly describe the Proxy Statement.
- A. The preliminary Proxy Statement describes the transaction to shareholders and includes notices of the Special Meetings of Shareholders at which shareholders will vote on the transaction. It is preliminary because the form was confidentially submitted to the Securities and Exchange Commission, and has not actually been issued to shareholders as of the date of preparation of this testimony.

II.RATEMAKING POLICY.RATEMAKING POLICY

- Q. In the Application, ScottishPower and PacifiCorp suggest the possibility of prices for PacifiCorp's customers that are lower than they otherwise would have been without the transaction. How will this be achieved?
- A. ScottishPower is committed to assist PacifiCorp in its efforts to improve customer service and system performance while keeping rates low. ScottishPower's previous experience in the U.K. in transforming regulated utility businesses gives us the confidence that we can replicate the experience with PacifiCorp. Our investments in systems and staff, along with implementing the process improvements that we found were successful in the U.K., gives us every reason to believe that we can mitigate the upward cost pressures inherent in this business. In addition, our ability to implement these measures in a way that will be more timely, more efficient, and with greater certainty of success due to our experience, will help to keep rates low over the long term.

- Q. In some of the mergers between U.S. utilities in the recent past, utility commissions have required price reductions or a commitment to freeze rates as a condition for approval. Is ScottishPower proposing to freeze or reduce rates as a result of this transaction?
- A. No. The benefits to customers from this transaction take the form of improvements in the quality of service and increased efficiency in operations, not rate adjustments. This transaction presents very limited opportunities for achieving immediate cost savings. Unlike most other U.S. utility mergers, there are no significant, redundant corporate operations to be eliminated, nor are there synergies to be obtained in combining operating systems. Over time, however, the improvements in operating performance achieved by ScottishPower will lead to cost savings resulting in rates lower than they would have been without the transaction.
- Q. Will there be any elimination of significant corporate functions currently performed by PacifiCorp?
- A. There will be some reduction in overlapping corporate functions, as described later in my testimony. In contrast to mergers between two U.S. operating utilities, however, this transaction does not present the opportunity to reduce a significant amount of costs through the elimination of redundant operations. ScottishPower will not, for example, eliminate the PacifiCorp headquarters function as part of this transaction. The small number of ScottishPower personnel that are anticipated to relocate to the U.S. means that, for the most part, corporate functions will continue to be undertaken by the current staff.
- Q. What do you mean by synergies in the combined operating systems?
- A. In the typical U.S. utility merger, the two combining utilities are serving adjacent areas. In these situations, there are immediately available synergies arising from the transaction. Transmission systems can be more efficiently utilized. Distribution systems can be combined and management structures streamlined. The legacy companies' generation portfolios can be re-evaluated and re-tooled to produce a more economical, lean generation mix. None of these circumstances is present in this transaction.
- Q. Will the steps that ScottishPower intends to take to reduce operating costs provide an ability to reduce rates for customers?
- A. At some point in the future, the efficiencies resulting from improved operating performance will mitigate future rate increases. ScottishPower has, to date, conducted only a high-level, preliminary benchmarking study to identify potential areas for cost reduction. This effort, however, was very preliminary in nature and insufficient to base any opinion or commitment to specific cost savings that will be forthcoming immediately. Without any firm assurances that such cost savings are available, it would be premature to reflect these hoped-for cost reductions in rates. As noted in the testimony of both Mr. Richardson and Mr. MacRitchie, the transformation we are proposing will take several years and require significant investment in people and systems.
- Q. How will the Commission be able to incorporate costs savings into rates in the future?
- A. The Commission will retain its ability to track PacifiCorp's future financial performance and will be able to use its ratemaking authority, when appropriate, to reflect these cost savings in rates. There is nothing about this transaction which will affect the Commission's ratemaking authority with respect to PacifiCorp.
- Q. How does ScottishPower propose to offer prices, over time, that will be lower than they would have been without the transaction?

- A. Three principles will guide ScottishPower's strategy on this point:
- C ScottishPower will reduce corporate costs and overheads, where possible, by streamlining support functions and selectively eliminating redundant activities.
 - C ScottishPower will achieve efficiencies in operational costs by an amount greater than could be achieved by PacifiCorp, as further described in Mr. MacRitchie's testimony.
 - C ScottishPower proposes to increase overall system performance and to enhance customer service. This improvement will undoubtedly require initial capital investment, but will over the longer-term produce efficiencies and lower costs.
- Using these principles as the basis for ScottishPower's strategy will produce prices lower than they would have been absent the transaction.

III.FINANCIAL INTEGRITY.FINANCIAL INTEGRITY

- Q. What effect will the transaction have on the ability of PacifiCorp to issue debt on reasonable terms?
- A. The effect of the transaction, if any, should be positive, as PacifiCorp will become part of a larger, financially stronger entity. As a direct result of the announcement of the merger, the credit rating agencies placed PacifiCorp's ratings on "CreditWatch" with positive implications, which suggests the potential for an upgrade in PacifiCorp's debt ratings. This provides some indication that the cost of PacifiCorp's borrowings can be expected to be lower after the transaction.
- Q. What economic and financial indicators do investors review in assessing a company's financial integrity?
- A. In assessing a company's financial integrity, investors examine the economic forces that affect a company's business risk, including its competitive position, its operations and management and its regulation. Investors also review financial risk through measures such as interest coverage, capital structure, cash flow adequacy and financial flexibility.
- Q. In your opinion, how would the transaction affect investors' perception of PacifiCorp's financial integrity?
- A. The impacts of the transaction on PacifiCorp should be positive, given ScottishPower's financial strength. Measured by market capitalization of approximately \$12 billion currently--and which will be approximately \$18 billion after the transaction--ScottishPower is among the 20 largest investor-owned electric utilities in the world. As of September 30, 1998, ScottishPower had assets of approximately \$9.5 billion and shareholder equity of approximately \$2.9 billion. For its fiscal -year ended March 31, 1998, ScottishPower had revenues of approximately \$5.0 billion. ScottishPower maintains a strong financial position through significant internal cash flow generation and a conservative balance sheet.
- Q. What is ScottishPower's debt rating?
- A. ScottishPower's bond rating as of December 1998 was rated Aa3 (Review Neg.) by Moody's and A+ (Watch Neg.) by Standard & Poor's.
- Q. Is there any plan to retire the long-term debt of PacifiCorp?
- A. No.
- Q. Will ScottishPower maintain separate debt ratings for PacifiCorp?
- A. Yes, so long as PacifiCorp debt remains outstanding.

- Q. Will the transaction affect the capital structure of PacifiCorp?
- A. Yes, we intend to strengthen the capital structure of PacifiCorp. We are proposing an actual capital structure equivalent to that of comparable, A-rated electric utilities in the U.S., with a common equity ratio for PacifiCorp of not less than 47%.
- Q. In summary, what impact will the transaction have on PacifiCorp's financial condition?
- A. The transaction should have little, if any, impact upon PacifiCorp's financial integrity in the short run. Over the longer term, PacifiCorp's integration into a larger, financially stronger organization should be viewed favorably by debtholders and rating agencies, and should result in lower borrowing costs.

IV.COST ALLOCATIONS AND TRANSACTIONS WITH AFFILIATES.COST ALLOCATIONS AND TRANSACTIONS WITH AFFILIATES

COST ALLOCATION ISSUESALLOCATION ISSUES

- Q. Is ScottishPower familiar with corporate cost allocation issues?
- A. Absolutely. We are used to dealing with cost allocation issues in the U.K. We have to allocate costs among our four main regulated businesses, ScottishPower, Manweb, Southern Water, and Scottish Telecom. When allocating these costs, we have to work with the U.K. regulators to arrive at a mutually acceptable result. We expect a similar process will occur in the U.S. and are ready to work with the Commission to ensure a fair result for all stakeholders.
- Q. How are common or corporate costs allocated to the various companies and organizations, or various subsidiaries and affiliates within ScottishPower?
- A. Generally, ScottishPower allocates costs to its affiliates in a manner similar to that employed by U.S. utilities, by applying a range of cost allocation bases that would include assessment of workload, usage statistics, salaries and net assets. For example, Human Resources costs are allocated to all businesses in proportion to their total employee costs, and Information Systems Division costs are, for the most part, allocated on the basis of usage.
- Q. Are there any exceptions to this basic rule?
- A. The only variation to the above relates to the allocation of Corporate Costs to Southern Water. The reason for the exception is that the basis formerly used to allocate corporate costs prior to the acquisition was inappropriate to the circumstances, as it would have charged Southern Water with a level of corporate overhead such that its corporate costs would have increased. It was agreed with the U.K. regulatory authorities that the amount of corporate overhead costs allocated would be lower than the corporate overheads borne by Southern Water prior to the acquisition. The remaining costs would then be allocated to the other group companies as described above.
- Q. Does ScottishPower intend to allocate corporate expenses to PacifiCorp upon completion of the transaction?
- A. Yes. We will allocate a share of all the corporate costs to PacifiCorp based on the allocation techniques described above.
- Q. Will PacifiCorp's corporate costs increase as a result of the allocation of ScottishPower's costs?
- A. No. PacifiCorp will bear lower corporate costs than is currently the case.

ScottishPower intends to apply cost allocation principles analogous to those utilized with Southern Water. These principles will be applied by assigning a fixed sum to PacifiCorp such that the overall PacifiCorp head office costs will go down.

- Q. How much will PacifiCorp's current corporate costs be reduced?
- A. By the end of the third year following the closing of the transaction, ScottishPower expects to achieve approximately \$15 million of annual cost savings in corporate costs which, when offset by \$5 million of cost increases, will produce a net reduction of \$10 million annually in corporate costs. ScottishPower will commit to reflecting this reduction in PacifiCorp's results of operations.
- Q. When do you anticipate that ScottishPower will advise the commission of its proposed allocation procedures?
- A. ScottishPower will provide an analysis of its proposed allocation of corporate costs within three months of completion of the transaction. We will commit to filing this analysis and proposed allocations with each Commission.
- Q. Will ScottishPower's cost allocation principles change as a result of the transaction?
- A. No, we will continue to apply the same cost allocation principles. Because of the corporate structure following the transaction--with the creation of HoldCo as the parent to both ScottishPower and PacifiCorp--many of these cost allocation issues will fall within the scope of affiliated interest activities. As a result, different approval procedures may need to be followed. We are not proposing to change the substantive cost allocation principles, however.

AFFILIATE TRANSACTIONSTRANSACTIIONS

- Q. Please describe the nature of the types of transactions that currently occur between ScottishPower and its affiliates and subsidiaries.
- A. ScottishPower has a structure typical of a large company, and accordingly there are several types of transactions that occur between the various affiliates within the ScottishPower group. By far the greatest number of transactions is with Scottish Telecom. When Scottish Telecom provides telecom services throughout the group to all other affiliates and all other subsidiaries and ScottishPower itself, these services are provided at market rates.
- Q. Is this the general rule for transactions between affiliates--that goods and services are supplied at market rates?
- A. Yes.
- Q. How is the market rate for the provision of services determined?
- A. The market rate is determined on the basis of its assessment of how it charges in the external market.
- Q. Have you identified the type of transactions that would occur between ScottishPower and/or any of its affiliates and PacifiCorp subsequent to the completion of this transaction?
- A. As discussed above, because of the structure of the transaction and the creation of HoldCo, a number of cost allocation issues fall within the scope of affiliated interest activities. Other than this category of activities, however, we do not

- expect that a material number of affiliate transactions involving PacifiCorp will take place following the completion of the transaction.
- Q. Please explain why the number of transactions will not be material.
- A. Scottish Telecom, the affiliate I mentioned earlier, operates solely within the U.K. and there are no plans for Scottish Telecom to operate within the U.S. The same holds true with respect to the other electric and/or regulated operations of the other affiliates and subsidiaries of ScottishPower. The other main affiliates within the ScottishPower group are Southern Water, which supplies water and wastewater services to customers in the southeast of England, and Manweb, which provides electricity services to customers in northwest England and North Wales. Given the geographic separation between these affiliates and PacifiCorp, there will be very few, if any, transactions between them.
- Q. For those transactions that do occur, how will ScottishPower determine the price?
- A. In the absence of any alternative treatment prescribed by the Commission, we would propose that transactions of goods and services between affiliated interests be priced at market rates, in accordance with our practice as described above. In the case of cost allocations which become affiliated interest activities only because of the structure of the transaction, we propose that an at-cost basis be used, as is currently the case under the cost allocation principles outlined above.
- Q. Please describe the regulatory oversight that exists in the U.K. with respect to the treatment of affiliated transactions with Scottish Telecom.
- A. ScottishPower must provide reports on a regular basis to our regulators which explain the transactions that occur between the affiliates in the ScottishPower group.
- Q. What other types of information must be supplied to the regulatory authorities in the U.K. with respect to the affiliate transactions?
- A. ScottishPower is required to submit regulated accounts, which are very detailed accounts supplied to our regulators with a complete analysis setting out all the monetary transfers between one affiliate and another.
- Q. Have the bases for those transfers been audited?
- A. Yes. The bases of all those transactions are audited by our external auditors, and then submitted to the regulators. Rather than undertaking their own audit of those transactions, our regulators have always relied on our auditors.
- Q. Has ScottishPower and/or its affiliates or subsidiaries ever been challenged by regulators with respect to the procedures and policies associated with accounting for the affiliate transactions between any of the subsidiaries?
- A. Not to my knowledge. Our regulators routinely review and discuss affiliate transactions with us on a periodic basis. In connection with this oversight, we provide regular information when and as requested.
- Q. How would you summarize ScottishPower's approach to affiliate transactions ?
- A. ScottishPower is familiar with and, as a matter of course, complies with regulatory oversight of its affiliate transactions. We currently operate in an environment which includes such oversight, and we fully expect to satisfy similar requirements imposed by the states in which PacifiCorp operates.

V.ACCESS TO BOOKS AND RECORDS.ACCESS TO BOOKS AND RECORDS

- Q. Where will the books, records, documents and other information relating to PacifiCorp be located?
- A. The books, records, documents and other information relating to PacifiCorp will be located in Portland, Oregon, and will continue to be available to the Commission upon request at PacifiCorp's offices in Portland, Salt Lake City, Utah, and elsewhere in accordance with current practice.
- Q. Will the Commission have reasonable access to the books, records, documents and other information which pertain to transactions between PacifiCorp and all its affiliated interests?
- A. Yes. ScottishPower and PacifiCorp shall provide the Commission with copies of or access to all books of account, as well as all documents, data and records of their affiliated interests, which pertain to transactions between PacifiCorp and all its affiliated interests.
- Q. Will the Commission have reasonable access to the books, records, documents and other information which pertain to the bases for charges from ScottishPower to PacifiCorp?
- A. Yes. The Commission will have access to and may examine the records of ScottishPower and those of its subsidiaries which are the bases for charges to PacifiCorp. ScottishPower agrees to cooperate fully with such Commission examination.
- Q. What are the written accounting policies and procedures that will be applied to regulated utility operations after the transaction?
- A. PacifiCorp will keep its existing accounting policies and procedures applicable to the regulated utility operations in place after the transaction. These policies and procedures will allow PacifiCorp to report regulated results using the Federal Energy Regulatory Commission System of Accounts, and ensure that PacifiCorp will comply with all Commission accounting rules.

VI.PROPOSED CONDITIONS.PROPOSED CONDITIONS

- Q. Based on your testimony, can you summarize the conditions which ScottishPower would propose in connection with regulatory approval of the transaction?
- A. Yes. We propose the following conditions:
1. To determine the reasonableness of allocation factors used by ScottishPower to assign costs to PacifiCorp and amounts subject to allocation or direct charges, the Commission or its agents may audit the records of ScottishPower which are the bases for charges to PacifiCorp. ScottishPower will cooperate fully with such Commission audits.
 2. ScottishPower and PacifiCorp will provide the Commission access to all books of account, as well as all documents, data and records of their affiliated interest, which pertain to any transactions between PacifiCorp and its affiliated interests,
 3. PacifiCorp will maintain its own accounting system, separate from ScottishPower's accounting system. All PacifiCorp financial books and records will be kept in Portland, Oregon, and will continue to be available

to the Commission upon request at PacifiCorp's offices in Portland, Salt Lake City, Utah, and elsewhere in accordance with current practice.

4. ScottishPower and PacifiCorp will exclude all costs of the transaction from PacifiCorp's utility accounts.
 5. PacifiCorp will maintain separate debt and, if outstanding, preferred stock ratings.
 6. ScottishPower and PacifiCorp will provide the Commission with unrestricted access to all written information provided to common stock, bond, or bond rating analysts, which directly or indirectly pertains to PacifiCorp.
 7. ScottishPower and PacifiCorp agree to comply with all existing Commission statutes and regulations regarding affiliated interest transactions, including timely filing of applications and reports.
 8. ScottishPower will not subsidize its activities by allocating to or directly charging PacifiCorp expenses not authorized by the Commission to be so allocated or directly charged.
 9. Neither ScottishPower nor PacifiCorp will assert in any future Commission proceeding that the provisions of the Public Utility Holding Company Act of 1935 preempt the Commission's jurisdiction over affiliated interest transactions.
- Q. Does this conclude your testimony?
- A. Yes, it does.