-BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH-

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| IN THE MATTER OF THE APPLICATION OF | ) | DOCKET NO. 98-2035-04 |
| PACIFICORP AND SCOTTISHPOWER PLC | ) | UTAH DIVISION OF |
| FOR AN ORDER APPROVING THE ISSUANCE | ) | PUBLIC UTILITIES |
| OF PACIFICORP COMMON STOCK | ) | EXHIBIT NO. DPU 1.0 |

DIRECT TESTIMONY OF LOWELL E. ALT, JR.

FOR THE

DIVISION OF PUBLIC UTILITIES

DEPARTMENT OF COMMERCE

STATE OF UTAH

June 18, 1999

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

A. My name is Lowell E. Alt, Jr. I am Manager of the Energy Section for the Division of Public Utilities (Division) of the State of Utah Department of Commerce located at 160 East 300 South, Salt Lake City, Utah.

**Q. PLEASE DESCRIBE YOUR QUALIFICATIONS.**

A. My educational background and experience is summarized in Exhibit No. DPU 1.1.

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

A. To present the overall Division recommendation and discuss how we arrived at our recommendation. Division witnesses Mary Cleveland, Ron Burrup, Artie Powell, Ken Powell and Bob Maloney will discuss in more detail specific Division concerns and related recommendations.

**Q. WHAT SPECIFIC AREAS WILL BE ADDRESSED BY OTHER DIVISION WITNESSES?**

A. Mary Cleveland will discuss affiliate relations, access to information, corporate structure and asset transfers.

Ron Burrup will discuss costs and benefits of the merger, asset valuations, regulatory information needs, intra-company loans, dividends and capital budgets.

Artie Powell will discuss foreign currency risk, cost of capital, dividends, the acquisition premium, the Public Utilities Holding Company Act (PUHCA), and corporate structure.

Ken Powell will discuss impacts on employees and local and State economies, impact on integrated resource planning and acquisitions and existing PacifiCorp obligations.

Bob Maloney will discuss service quality and reliability.

**Q. WHAT STATUTORY OBLIGATION DOES THE DIVISION HAVE TO REPRESENT THE PUBLIC INTEREST?**

A. Section 54-4a-6 of the Utah Code provides the following objectives for the Division:

> In the performance of the duties, powers, and responsibilities committed to it by law, the Division of Public Utilities shall act in the public interest in order to provide the Public Service Commission with objective and comprehensive information, evidence, and recommendations consistent with the following objectives:
>
> (1) promote the safe, healthy, economic, efficient, and reliable operation of all public utilities and their services, instrumentalities, equipment, and facilities;
>
> (2) provide for just, reasonable, and adequate rates, charges, classifications, rules, regulations, practices, and services of public utilities;
>
> (3) make the regulatory process as simple and understandable as possible so that it is acceptable to the public; feasible, expeditious, and efficient to apply; and designed to minimize controversies over interpretation and application;
>
> (4) for purposes of guiding the activities of the Division of Public Utilities, the phrase “just, reasonable, and adequate” encompasses, but is not limited to the following criteria:
>
> (a) maintain the financial integrity of public utilities by assuring a sufficient and fair rate of return;
>
> (b) promote efficient management and operation of public utilities;
>
> (c) protect the long-range interest of consumers in obtaining continued quality and adequate levels of service at the lowest cost consistent with the other provisions of Subsection (4).
>
> (d) provide for fair apportionment of the total cost of service among customer categories and individual customers and prevent undue discrimination in rate relationships;
>
> (e) promote stability in rate levels for customers and revenue requirements for utilities from year to year; and
>
> (f) protect against wasteful use of public utility services.

Since these objectives are not prioritized and are sometimes conflicting, the Division must use judgement in balancing the objectives.

**Q. HOW DID THE CASE PROCEED AFTER THE APPLICATION WAS FILED WITH THE COMMISSION?**

A. The Public Service Commission (PSC) established a schedule based on input from the interested parties and then asked all parties to file a written statement of issues to be addressed in the case. A hearing was held on the issues and an Order was issued declaring that each party could bring up any issue but would assume the burden to show relevancy. The PSC Order also established that the standard of a net positive benefit would be used in determining whether the merger was in the public interest. Parties, including the Division, submitted discovery questions to PacifiCorp and ScottishPower (the Companies) to help in developing positions and testimony.

**Q. PLEASE EXPLAIN THE STANDARD USED BY THE DIVISION IN EVALUATING THE MERGER APPLICATION.**

A. The PSC ordered that the appropriate standard to be used in evaluating the merger application is a net positive benefit to the public interest in the State of Utah. We understand this to mean that when all known costs and benefits related to the merger have been evaluated and netted that if there is a net positive benefit then the merger should be approved. The PSC, however, did not set the amount of the net positive benefit required for merger approval nor did they specifically define the public interest. The public interest normally considered by the Division involves those areas within the PSC's jurisdiction such as rates charged utility customers. This case demands a broader perspective, although we believe any proposed conditions would be limited by the Commission's enforcement authority. Consideration should be given to the impact on ratepayers, shareholders, employees, the State of Utah, its citizens and its general economy.

**Q. PLEASE SUMMARIZE THE KEY ISSUES OF THIS MERGER CASE?**

A. Following a review of all issues submitted by parties, we believe that the foremost concerns are that service quality and reliability may get worse and rates may go up as a result of the proposed merger. These concerns are followed by the concern that the Utah PSC's ability to regulate the merged company may be adversely impacted. The possibility of adverse impact on the State, communities and employees through loss of jobs, loss of local company presence and reduced support for community and economic development was also raised. Other parties have raised concerns about the environment, energy conservation, municipalization, retail competition and utility facilities.

**Q. PLEASE DESCRIBE THE DIVISION'S REVIEW OF THIS CASE.**

A. After reading the Companies' application, the Division held several internal staff meetings to develop a list of our concerns or issues. Our issues were derived from comparing our aforementioned statutory objectives with ideas of possible adverse consequences of the merger based on our experience and research. We divided the issues list into areas and assigned them to staff to investigate. We involved Division staff beyond just those appearing as witnesses in our review. Discussions of our concerns led to many questions unanswered by the Companies' application. This led to extensive discovery questions given to PacifiCorp and ScottishPower.

The Division held numerous internal staff meetings to discuss issues, status of discovery, information from other States and meetings with the Companies. We had discussions with some of the other parties about their concerns to make sure we had covered all possible issues. We reviewed and found valuable the discovery questions and responses of other parties such as the Utah Industrial Energy Consumers. We decided that discussions with other States involved with the merger might help us as well as them so we initiated a series of conference calls with Oregon, Wyoming, Idaho and Washington. These conference calls were very helpful as we exchanged ideas, information and discovery requests. We followed the merger activities in other States including reviewing their data requests and testimony. PacifiCorp and ScottishPower were very helpful in our investigation by providing quick responses to most data requests, by meeting with us on many occasions to discuss issues and by agreeing to our request for an all day workshop where all parties were able to ask informal questions of each Company witness. ScottishPower witness Robert Green's direct testimony in Utah provided a list of conditions that they were willing to accept if the merger were approved. ScottishPower witness Alan Richardson's Supplement Testimony expanded this list. We also reviewed the conditions imposed on PacifiCorp by the PSC in the 1988 Pacific Power/Utah Power merger Order. We asked the Companies in a data request which of the 1988 conditions they would accept as conditions if the ScottishPower merger were approved. We reviewed the merger conditions proposed by the Idaho Commission Staff as well as those included in the stipulation between the Wyoming Commission Staff and ScottishPower and PacifiCorp.

**Q. PLEASE DESCRIBE HOW THE DIVISION ARRIVED AT ITS OVERALL**

**RECOMMENDATION.**

A. While reviewing the information in the case, we soon realized that the ScottishPower merger posed new risks and that the conditions offered by ScottishPower and PacifiCorp in their direct testimony would be insufficient to remedy possible adverse outcomes. This merger is quite different from the previous merger in that benefits appear to be much smaller and are harder to quantify. The previous merger involved two operating companies with transmission ties that presented many opportunities for significant dollar savings (hundreds of millions) that were easier to quantify. This merger involves two companies in different countries separated by thousands of miles with some small quantifiable savings (ScottishPower guarantees only $10 million) possible in corporate overheads. The primary benefits identified by Division witnesses include the aforementioned $10 million, some evidence of improved management, possible improved financial strength and voluntary reliability performance standards and customer service guarantees. With smaller and less certain merger benefits, mitigating the risks becomes more important if the net positive benefit standard is to be met.

If possible adverse outcomes materialize, they could easily offset the small assured savings and result in a net harm to the public interest. ScottishPower tried to assure us that they could achieve significant efficiencies even though they would not guarantee them. Our statutory obligation to represent the public interest requires more than trust of a company with which we have limited knowledge and no experience. Division staff therefore began the process of determining if we could develop sufficient additional conditions to mitigate the risks and uncertainty that we felt would come with the merger. The Division has developed a list of conditions that attempts to mitigate the risks related to specific areas of the merger.

**Q. WHAT IS THE DIVISION'S POSITION ON THE PROPOSED MERGER?**

A. We recommend approval with conditions.

**Q. WHAT CONDITIONS DOES THE DIVISION BELIEVE ARE NECESSARY IF THE MERGER IS APPROVED?**

A. Our proposed conditions are summarized in Exhibit DPU 1.2. These conditions generally include and build on those proposed by ScottishPower and PacifiCorp. We recommend that the PSC require that the Companies accept these conditions in writing so that they would be enforceable.

**Q. WHY DOES THE DIVISION FEEL THESE CONDITIONS ARE NECESSARY?**

A. Each Division witness explains the reasons for the specific conditions they propose. Basically these conditions attempt to mitigate the risk of possible adverse outcomes that would otherwise wipe out the small assured benefits of the merger. We believe that these conditions sufficiently address the new risks such that we can expect a net positive benefit from the merger.

**Q. ARE ALL OF THE CONDITIONS EXPLAINED BY THE OTHER DIVISION WITNESSES?**

A. No. They explain most of our conditions. I will explain the rate cap condition as well the last two conditions on our summary exhibit.

**Q. WHAT IS THE RATE CAP CONDITION?**

A. We recommend a rate (revenue requirement) cap for a maximum of three years from the effective date of the PSC Merger Order. We offer two ideas for this rate cap. The first would limit rate increases above current levels to inflation increases based on a measure such as the Gross Domestic Product (GDP). The second would limit rate increases above current levels such that the rate of return on equity in Utah would not exceed that resulting from rates set in proceedings in any other PacifiCorp State. Both situations would of course require a full rate case to be held where rate increases are limited to the cap and rates may be reduced.

**Q. WHY DOES THE DIVISION BELIEVE A RATE CAP CONDITION IS NEEDED?**

A. We believe a rate cap is needed to sufficiently lock in savings from the merger so that a net positive benefit is more assured. This proposed merger, as mentioned earlier and discussed more fully in other Division testimony, is expected to bring very small assured benefits and large uncertainties and risk. A rate cap allows the risk of future merger benefits to ratepayers to be shared with PacifiCorp shareholders who will receive a merger benefit up front with the stock premium. The three year term would allow a sharing of risks until merger savings begin to occur. Other Division conditions should help mitigate this risk, but we felt that a rate cap was necessary for us to assure net positive benefits and therefore allow us to recommend approval of the merger.

**Q. CAN YOU PROVIDE EXAMPLES OF RISKS THAT A RATE CAP WOULD HELP MITIGATE?**

A. Even though the Companies have agreed that merger costs should not be recovered in rates, we are concerned that not all merger related costs including transition costs are or would be tracked. We are not sure that our proposed condition on asset valuations and the related impact on property taxes will provide complete protection. We are concerned about the possible adverse and difficult to predict impact on the economy from the potential loss of Utah jobs. We are concerned that our proposed conditions may not completely mitigate all possible risks of adverse outcomes. The penalties available if service quality and reliability deteriorate may not be adequate to assure a net positive benefit.

**Q. IS THE RATE CAP CONDITION REASONABLE?**

A. Yes because PacifiCorp has already agreed to one in Wyoming. Division witness Ron Burrup discusses the specifics of the Wyoming stipulations. Idaho Commission Staff has proposed that any benefit agreed to in any other State that would benefit Idaho should also be received in Idaho. This proposal could be interpreted to mean that they would want a rate cap like Wyoming.

**Q. PLEASE EXPLAIN THE OTHER TWO DIVISION CONDITIONS.**

A. We believe that rates in Utah should not increase as a result of the merger. PacifiCorp witness Richard O'Brien states in his direct testimony that the merger "...benefits will result in prices lower than they would be without the transaction." However, neither PacifiCorp nor Scottish Power have proposed such as a condition. We think it is fair to capture that promise in a binding condition.

In the previous Utah Power merger, the Utah PSC required that PacifiCorp shareholders assume all risks of less than full cost recovery due to different allocation methods among the Merged Company's various jurisdictions. We believe it is possible that differences in merged company treatment among the various jurisdictions may occur in the future and that the companies should not expect Utah ratepayers to be responsible for any shortfalls. This risk associated with the merger must belong to the shareholders. We therefore propose that ScottishPower and PacifiCorp must accept the risk of less than full recovery of costs if the Utah PSC orders any cost or revenue treatment, conditions or requirements that differ from those in other jurisdictions.

**Q. DOES THE DIVISION AGREE WITH THE SCOTTISHPOWER PROPOSAL TO HAVE PENALTIES PAID FOR NOT MEETING RELIABILITY GOALS PLACED IN THE PACIFICORP FOUNDATION?**

A. No. Our understanding is that there would be no assurances that the money would be used in Utah. Commission Rule R746-200-9 requires residential service rule related penalties to be used for low income energy assistance in Utah. We do not have a specific recommended use at this time and therefore recommend that the Commission defer a decision on this issue until such time as any penalty is due.

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

A. Yes.