Public Service Commission of Utah

4th FLOOR, HEBER M. WELLS BUILDING, 160 EAST 300 SOUTH
P.O. BOX 45585, SALT LAKE CITY, UTAH 84145
TELEPHONE: (801) 530-6716

NORMAN H. BANGERTER
GOVERNOR

COMMISSIONERS
BRIAN T. (TED) STEWART, CHAIRMAN
BRENT H. CAMERON
JAMES M. BYRNE
EXECUTIVE STAFF DIRECTOR
DOUGLAS C. W. KIRK
COMMISSION SECRETARY
STEPHEN C. HEWLETT

September 15, 1987

Frank Davis, President
Utah Power and Light Company
P.O. Box 899
Salt Lake City, Utah 84110

Dear Mr. Davis:

Attached to our letter to you of August 6, 1987, was a draft memo prepared by our staff. That memo contained a preliminary list of information our staff considered necessary in order to perform an analysis of the proposed merger.

Subsequently, we asked our staff to refine this list. We asked them to do it in the form of questions or issue statements that would be more suggestive of what should actually be analyzed than was the preliminary list. We are enclosing a copy of this new memo for your consideration, and that of PacifiCorp as well, as you prepare to file an application requesting approval of the merger proposal.

As you well know, we are required to be very thorough in assessing the public interest implications of this unprecedented proposal. We intend to meet this responsibility, and to do so as expeditiously as possible. At the same time, we have no wish to cause an excessive regulatory burden. It is in this spirit that we forward the staff memo to you and would be happy to discuss it with you.

Sincerely,

B. Ted Stewart

Brian T. Stewart
Chairman

BTS/bw

Attachment

cc: David F. Bolender
President
Pacific Power & Light Co.

Division of Public Utilities
Committee of Consumer Services

Public Service Commission of Utah

4th FLOOR, HEBER M. WELLS BUILDING, 160 EAST 300 SOUTH
P.O. BOX 45585, SALT LAKE CITY, UTAH 84145
TELEPHONE: (801) 530-6716

NORMAN H. BANGERTER
GOVERNOR

COMMISSIONERS
BRIAN T. (TED) STEWART, CHAIRMAN
BRENT H. CAMERON
JAMES M. BYRNE

EXECUTIVE STAFF DIRECTOR
DOUGLAS C. W. KIRK

COMMISSION SECRETARY
STEPHEN C. HEWLETT

MEMORANDUM

TO: PUBLIC SERVICE COMMISSION

FROM: Staff

DATE: September 15, 1987

PREFACE

The Commission should give very serious consideration to the impact on UP&L's ratepayers of the proposed merger with PacifiCorp. In order to approve or disapprove the merger, we suggest that a complete economic analysis of the benefits and costs, plus who bears the burden or reaps the gains, be performed by UP&L and PacifiCorp. The basis for this analysis would be a comparison of the with-merger and the without-merger cases.

In the context of such an analysis, the issues set out below should be addressed, and all necessary supporting information should be provided. The analysis should be completed at the earliest possible date. We have confined this list to those issues and questions to which a Utah Power and/or PacifiCorp response should reasonably be expected.

The without-merger case would simply be UP&L as we know it. The company's history would be recounted only insofar as is necessary to explain the current situation and as it may bear on the future. The future itself would be described as evolving from the most likely pattern of investment, operational, organizational and regulatory decisions. In the with-merger case, this future would of course be modified by a new, more complex organizational structure and by a new pattern of management and regulatory decisions. To show what happens to UP&L's ratepayers in both cases would be the desired outcome of the analysis. A question of particular interest is the identification of sources of the claimed five to ten percent Utah rate reduction, its implications for other parts of the merged system, and the likely path of future electricity prices after the price reduction years are over.

The following questions are designed to elicit information from which resolutions of these major issues can be developed. Note that similar concerns arise several times in various contexts. This repetition is appropriate in emphasizing important relationships.

1. ORGANIZATIONAL STRUCTURE OF THE FIRM

Describe the existing corporate structure of PacifiCorp and PP&L.

Describe the relative merits (including cost, operational, risk, etc., considerations) of alternative organizational structures designed to increase the coordination between UP&L and PP&L.

If merger occurs, will UP&L be a separate entity, having its own distinct generation and transmission resources? Will it be separate operationally? Will it be separate financially?

Describe the proposed structure of the merged companies in complete detail and explain why it was selected.

Identify the benefits due to the merger which cannot be realized by continued operation of the companies as separate entities.

If PacifiCorp (PP&L) now is organized as a set of functionally separate "profit centers", is this in any sense a precursor to a breakup of the utility into separate distribution, transmission and generation companies? Under what conditions might such a breakup occur, and what is the probability that such might occur within five years? 10 years?

2. JURISDICTION

If merger occurs, how will jurisdictional revenue requirement be determined?

If merger occurs, discuss future intentions for Utah Power's Energy Balancing Account.

UP&L has FERC jurisdictional customers; PacifiCorp apparently does not, or does not treat them separately for cost allocation purposes. If merger occurs, how will this situation be reconciled?

If merger occurs, how do you propose to have each state analyze areas such as least-cost planning. If the geographic scope is extended by the merger to a regional level, should the analysis be elevated to inter-utility planning where the capacity expansion plans of both utilities must be taken into consideration? How would you propose the various commissions can jointly develop some type of regionally integrated (or disintegrated) least-cost planning strategy?

How does UP&L intend to assure this and other commissions that the utility will not in any way subsidize the non-utility operations of PacifiCorp? Are both utilities prepared to accede to a reasonable set of conditions governing such matters as treatment of expenses, allocations of costs, access to books and records, no uncompensated lending of creditworthiness, protection from risk, and the like (similar to the conditions imposed in the ENI case), should the commission find such conditions necessary?

3. FINANCIAL ISSUES

Describe the current and expected future financial status of the company with and without the merger, paying attention to capital structure--components, ratios, and rates of return, and financial ratios.

Describe sources and applications of funds, with and without merger.

Report dividend policies and payout ratios as far back historically as is necessary to explain current and expected future practices, with and without the merger.

Summarize such information as may now exist concerning the bond rating effects of merger and the UP&L case without the merger.

What effect on cost of capital will the merger have? Compare to UP&L case without the merger, taking into consideration all aspects of risk, business and financial, especially as may be affected by the diversified nature of PacifiCorp.

What tax considerations arise from the proposed merger? Comparing UP&L with and without the merger, what differences in concepts, applications, as well as dollars can reasonably be expected?

If merger occurs, UP&L apparently will lose all direct access to capital markets. How can the Utah Commission be assured the Utah operation will have adequate access to capital? What is the expected regulatory authority regarding utility investment? How will the construction budget be determined (i.e. who makes the investment decisions) and needed construction financed? Describe, showing differences between the with- and without-merger cases. How will financial policies work in the new corporate structure?

4. CURRENT AND PROSPECTIVE LOADS AND LOAD SHAPES

a. Jurisdictional Loads and Forecasts

What are the current and recent historical peak load levels and total energy sales experienced by the two companies separately?

What would current and recent historical coincident peak loads and total electrical energy sales have been for the companies combined?

What is the current and recent historical customer class mix of the two companies?

Numbers of customers?
Energy sales distribution?
Class peak loads?
Coincident peaks?

What would these proportional mixes have been in a combined company?

What methods and models are used to project jurisdictional energy sales and peak loads? At what geographic and customer class resolution do they operate? What are the major independent variables? What if any role is played by load control-load management considerations?

b. Off-System Sales of Energy and Capacity

Describe the current and recent historical role of each company in off-system transactions providing capacity and energy to other utilities: firm, economy, surplus. What would the likely role have been if the companies had been combined during this period?

What would the future of each company be in these markets separately? What is the expected future of the combined company in these markets?

How are off-system sales of surplus energy and capacity projected?

How are off-system firm sales of energy and capacity projected?

c. Load Diversity

Describe specific load shape diversity opportunities which exist between UP&L and PP&L and which can be exploited to achieve cost savings. How do the two utilities complement each other and how are these complementarities to be exploited?

d. Industrial/Commercial Self-Generation "Bypass"

What is the potential impact of industrial/commercial self-generation "bypass" on:

UP&L's system?
PP&L's system?
The merged system?

How would UP&L separately, and the merged entity, respond to self-generation?

5. RESOURCES

a. Current Generation Resources

Describe each company's current complement of generation resources -- include energy source (coal, gas, oil, hydro, nuclear, etc.); typical operation mode (base load, intermediate, peaking, cold reserve, etc.); availability (seasonal, year around, etc.); joint ownership characteristics and related operational constraints, if any; other operational peculiarities, if any.

What is each company's current reserve capacity (MW and percent of peak load)? What are their desired reserve margins? What actions have been or are being taken to deal with excess reserves? How long are excesses expected to persist?

What would current reserve capacity be for a combined company? How long would any combined company excess capacity persist? What actions would be contemplated to deal with excess capacity?

Describe each company's current and recent historical reliance on off-system generation sources -- include type of transaction (energy, capacity, firm, non-firm, purchase, exchange); providing utility; which utility provides reserve (buyer or seller).

How would the combined companies have behaved differently with respect to off-system sources than they did separately as described in response to the above?

b. Expected Future Generation Resources

Describe each company's expected future capacity expansions (type, timing) and their future expected reliance on off-system resources if they remain separate entities.

Delineate specific changes in future capacity expansions and off-system resource use that can be exploited to reduce costs for a combined company. Quantify the cost reductions that can be achieved through these opportunities.

c. Cogeneration and Small Power Production under PURPA

What is the potential impact of cogeneration and small power production on:

UP&L's system?
PP&L's system?
The merged system?

Will the merger result in any significant changes in either utilities' QF market? For example, will avoided cost prices be based on system-wide avoided capacity and energy costs? What is PP&L's philosophy towards cogeneration and small power production?

6. TRANSMISSION AND INTERCONNECT FACILITIES

a. Control Areas

Describe the control areas and operating divisions of each company.

How would either control areas or operating divisions be affected by the merger?

b. Control Area Relationships

Describe the existing transmission and interconnect facilities between the control areas of UP&L and PP&L.

Describe the existing transmission and interconnect facilities between the control areas of UP&L and PP&L with the control areas of other utilities.

c. Expected Future Transmission System

In the absence of a merger, describe the expected future expansion of each company's transmission system including interconnect facilities.

With a merger, describe the expected future expansion of the merged company's transmission system. Detail the opportunities afforded by the merger for increased coordination in the use of generation resources and transmission system.

How is the level of investment in transmission and interconnect facilities affected by the presence of a merger?

To what extent does the merger provide an opportunity to substitute new transmission facilities for new generation resources in the planning of peak capacity expansion?

Quantify the benefits and other costs of increased coordination between the merged companies including:

Economic Dispatch of Generating Resources
Transmission Line Losses
System Reliability

d. Wheeling

Describe the opportunities for bulk power sales and transfers, including source and destination, available to the merged company.

Detail the merged company's wheeling policy regarding access to transmission by other utilities.

How are prices and terms of wheeling services of the merged company to be determined? If the answer is FERC, how would the merged company be treated differently than the separate companies are now?

7. IMPACT OF CHANGING RELATIVE ENERGY PRICES (ELECTRICITY, NATURAL GAS, COAL, OIL, HYDRO, ETC.) ON END-USE MARKETS AND THE COST OF GENERATION

What policies or practices are being considered by UP&L and PP&L, with and without merger, to counter the effects of low growth in the service territories?

What would be the impact of increasing oil and gas prices on UP&L separately and on the merged companies?

Consider:

Surplus sales
Jurisdictional industrial and commercial sales
QF and self-generation responses

8. BENEFITS AND COSTS OF THE PROPOSED MERGER

a. Peak Capacity Expansion Plan

Quantify the change in the present value of the expected costs of future generation and transmission capacity with and without the merger.

b. Expected Future Operating Costs

Quantify the change in the expected annual operating costs of generation resources and transmission system for the next three to five years with and without the merger.

c. Benefits and Costs of Off-System Transactions

Quantify the change due to the merger of:

Expected revenues obtained from wheeling
Expected revenues and costs of surplus sales and purchases of off-system capacity and energy

d. Customer Class Costs and Derived Prices

Quantify the expected net costs of providing service with the allocation of such costs to jurisdictions and customer classes.

Given forecast loads, derive the implicit price, i.e. expected cost per unit of output, for each customer class.

e. Discuss the Benefits and costs of the Merger with respect to the Interests of:

Ratepayers of UP&L
Shareholders of UP&L
Employees of UP&L
State of Utah in general
Other