- BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH -

In the Matter of the Application of UTAH POWER & LIGHT COMPANY and PC/UP&L MERGING CORP. (to be renamed PacifiCorp) for an Order Authorizing the Merger of Utah Power & Light Company and PacifiCorp into PC/UP&L Merging Corp., Authorizing the Issuance of Securities, Adoption of Tariffs and Transfer of Certificates of Public Convenience and Necessity and Authorities in Connection Therewith.)	DOCKET NO. 87-035-27 ORDER VACATING SUSPENSION ORDER OF MERGER APPROVAL DATED OCTOBER 26, 1988

ISSUED: December 13, 1988

Short Title: PacifiCorp/UP&L Merger - Reinstatement

SYNOPSIS

By this Order, the Commission vacates and sets aside its Suspension Order of October 26, 1988 and hereby reinstates its Order of September 28, 1988 in full effect. The Commission determines that the FERC's transmission conditions do not substantially diminish the anticipated merger benefits.

Appearances:

Sidney G. Baucom Thomas W. Forsgren Edward A. Hunter	For	Utah Power & Light
Robert S. Campbell Gregory B. Monson George M. Galloway	"	PC/UP&L Merging Corp.
Michael Ginsberg, Assistant Attorney General	"	Division of Public Utilities, Department of Business Regulation, State of Utah
Calvin L. Rampton Donald B. Holbrook Lee R. Curtis	"	Utility Shareholder Association of Utah

A. Wally Sandack Arthur Sandack Scott Hempling	"	United Mineworkers of America, District 22, et al.
Bruce Plenk	"	Salt Lake Community Action and Salt Lake Citizens Congress
Charles M. Darling, IV J. Patrick Berry Gerald M. Conder	"	AMAX Magnesium Corporation
Gary A. Dodge Richard D. Clayton Jill Neiderhauser	"	Geneva Steel and Basic Manufacturing and Technologies of Utah, Inc.
James A. Holtkamp William Richards	"	Utah Association of Municipal Power Systems and Washington City
Peter J. P. Brickfield Kenneth G. Hurwitz Andrew W. Buffmire Wiliam P. Schwartz	"	Nucor Steel, a Division of Nucor Corporation
Lynn W. Mitton	"	Deseret Generation & Transmission
Sandy Mooy, Assistant Attorney General	"	Committee of Consumer Services, Department of Business Regulation, State of Utah

BY THE COMMISSION:

On October 26, 1988, this Commission issued its Order suspending the Order of September 28, 1988, which approved with conditions the application of Utah Power & Light Company and PC/UP&L Merging Corp. for an order authorizing the merger of Utah Power & Light Company and PacifiCorp, Maine. This was done to enable us to analyze the conditions imposed by the Federal Energy Regulatory Commission (FERC) in its Order approving the merger. Our October 26, 1988 Order established a hearing for this purpose. Our intent was to determine the effect of the FERC Order on Utah;

remaining to the Merged Company, its shareholders and employees, and in particular to Utah ratepayers, following imposition of the FERC-ordered conditions.

Upon the issuance of the October 26, 1988 Order, we called for the submission of testimony, and an evidentiary hearing was held on November 8, 9, 28, 29 and 30, 1988. Testimony and evidence was submitted to the Commission by the Applicants, the Division of Public Utilities, the Committee of Consumer Services, the Utility Shareholders Association of Utah, AMAX Magnesium Corporation, Nucor Steel Corporation and Basic Manufacturing & Technologies of Utah, Inc. In addition, argument and cross-examination was heard from United Mine workers, et al., UAMPS, and Deseret Generation and Transmission Cooperative.

Having considered the testimony and evidence, the Commission herewith enters its Discussion, Findings, Conclusions and Order:

DISCUSSION

In our Order of September 28, 1988, approving the merger, we found net benefits would result in the area of system resources over a 20-year horizon and in the area of power supply over a five-year horizon, for the planning and operation of the merged system relative to the unmerged, stand-alone systems. This finding is reasonable on two grounds. First, it is expected that the Merged Company will face more attractive economic alternatives than are available to the stand-alone companies. Second, it is expected that the Merged Company will be subject to fewer constraints than would be the case for the stand-alone companies.

The Applicants asserted, and this Commission confirmed, that pricing of services provided by the utility system need not be considered in this merger hearing. Thus, neither the measurement of system-wide revenues and costs, nor an investigation of possible divisional pricing methods was deemed material to a determination of the merger's impact on the public interest of the State of Utah. We have stated our opinion that Utah regulatory agencies have the legal authority, resources, expertise, and willingness to ensure that retail ratepayers of Utah will share in the net benefits resulting from the merger. Our presumption is that a sharing of benefits will result in cost-based rates which will be lower in the future than they would be in the absence of the merger.

As a consequence of the conditions imposed on the Merged Company by the FERC in its approval of the merger, the Merged Company will now face greater constraints on the design, costs, usage and revenues associated with its transmission assets. We expect the effect of these constraints will not be confined to transmission assets but will impact the investment and usage of all assets of the merged system.

Additionally, the merger will no longer result in a greater availability of economic alternatives than would be available to the stand-alone companies. Instead, the Merged Company will face a different set of economic alternatives.

The FERC's conditions affect a complex transmission system. Yet Applicants have chosen not to request clarification of ambiguous and undefined basic terms and concepts used by the FERC, such as capacity and cost. Instead, Applicants have asserted

definitions and meanings on the record in this case which cannot with certainty be said to be correct.

The Applicants'--and especially Utah Power's--abrupt turn-about on decades of planning, investment and operational policy and practice is more than merely a curiosity. During the recent period of rapid growth (and double-digit inflation) the Company chose to continue its policy of capitalizing on its fortuitous geographic location between low-cost supplies of electricity in the Northwest and high-cost markets in the Southwest by building high-capital cost, low-operating cost, base load coal plants. Relying on its transmission system, it built no intermediate cycling or peaking plants, arguing that the system was and would be optimal as a result of the off-system transactions made possible by all of this. The FERC conditions are completely absent any analysis of this historical practice and the potential negative impact on Utah Power or its ratepayers.

To effectuate the merger, the Applicants quickly determined to submit to the FERC conditions, relinquishing control of the transmission system. The reason given is an assumption that the market is changing and just-completed calculations by the Applicants show that the FERC conditions are not so onerous as to significantly diminish the projected amount of merger benefits. According to Applicants' new analysis, there remains enough transmission capacity to pursue the majority of the off-system opportunities that are the basis for optimizing an all base load system, enough to make the off-system sales and purchases that are the basis of much of the merger benefits, and enough to serve the forecast requirements of native load. Applicants testified that

native load includes all retail customers, present and future, firm and interruptible, within Utah Power's certificated territory.

We are of the opinion that there will be added risks as a result of the FERC conditions. The record reflects that there is added risk and this risk translates into costs that will be borne by someone. The Applicants estimate, assuming no loss of load due to the FERC conditions, the costs will be at least $1 million per year over the first five years. Under more severe conditions the parties have indicated a far greater magnitude, but we have no actual quantification. Applicants' testimony suggests that this additional risk will be borne by the ratepayers of the Merged Company. We do not agree that the risk of added cost occasioned by the FERC Order and conditions should be borne exclusively by ratepayers, particularly Utah ratepayers. To the extent such costs are not allocated to and recovered from the beneficiaries of the FERC-imposed conditions, there will be a presumption that such costs and associated revenue requirements will not be borne by Utah ratepayers.

The future of the electric utility industry is highly uncertain. Our sense of this is of course heightened by the FERC action and Applicants' ready acceptance of it. This is a source of discomfort to us. The FERC's disregard for the interests of the Applicants and its ratepayers in the name of an ill-defined and unanalyzed concept of economic efficiency, as well as for the jurisdiction of the states, is of great concern, the more so when its actions and rationale suggest presence of an agenda which is

yet unspecified and for which the national dialogue is as yet unresolved.

Despite uncertain future economic and institutional circumstances, our principle by which risk is to be shared remains the regulatory objective of providing reliable service to retail ratepayers at minimum cost with the shareholders afforded the opportunity to earn a reasonable rate of return. For this return, the shareholders are expected to bear some risk on their capital investment, and in this specific case, bear some risk of the merger and of going forward with the merger under the uncertainty created by the FERC conditions.

One specific area of concern on which there is very little in this record involves the statements of the Applicants concerning their intent to close this transaction prior to final orders from regulatory bodies. This is of concern to us when there are petitions pending before FERC for rehearing, clarification, and modification, the outcome of which is unknown. We see this as a potential risk, although the extent of such risk is unquantifiable and unknown.

What happens if the merger is consummated, changes are made to parts of UP&L's Utah operations (moved out of state--or additional operations moved in state) and the merger is then denied, leaving the Applicants to unscramble people and properties, including transmission rights? Will the surviving entity be able to operate efficiently or will it be encumbered by conditions and restraints? Although we will not condition our approval on waiting for final orders from all of the regulatory bodies, we do

believe any such risk should be borne by shareholders, and not Utah ratepayers.

This hearing allowed the Commission to again inform the parties that it is in receipt of many additional written and verbal anonymous communications concerning the proposed merger, mainly from employees. As we stated in our September 28, 1988 Order, Applicants urged that the merger is in the best interest of its shareholders, ratepayers and employees. In an effort to dispel some employee concerns and to reiterate our concern, we again questioned Presidents Bolander and Davis on what the Merged Company's attitude and intent toward its employees would be. The Commission specifically asked for responses to its conditions and expectations expressed in the September 28, 1988 Order. Both Presidents affirmed that they were willing to abide by the spirit and intent of the conditions and expectations. They acknowledged employee concerns and indicated a desire to reduce these concerns. We conclude that no additional conditions are necessary in this area.

The Commission has no intention of interfering with the employee-employer relationship, but does fully expect compliance with our Order. To that end, prior to, or at least when specific instances of potential violation of the spirit and intent of our Order occur, the Merged Company will present to the Commission the method by which they plan to deal with these instances. The Commission is in no position to hear all such potential cases and would therefore encourage the establishment of a method including the possible use of an independent third party acceptable to the Commission to hear specific complaints and to make periodic

reports to both the Commission and the Merged Company. We note that this is but one possibility. The Company may advocate others.

Numerous parties have advocated that the Commission require, as a condition of merger approval, the Merged Company to make good its intent that systemwide rolled-in rates be established at a time certain. Applicants strongly oppose this condition. Because we have the regulatory authority to establish rates on a rolled-in cost basis in the Utah jurisdiction when such rates are appropriate, it is not necessary for us to condition our approval of the merger in this way. We will, however, require Applicants to provide testimony and analysis in the upcoming allocation and/or general rate proceedings showing when and under what conditions rolled-in rates should be established.

Despite these misgivings and concerns, based on the record in this hearing, we will reaffirm our approval of the merger. The record shows that although there are increased risk and reduced total benefits, substantial net benefits are expected to remain. But our feelings of discomfort and uncertainty are such that if we knew exactly how to do it we could surely add further conditions. Instead, however, we hereby state our intentions to monitor this Company's future performance, on the basis of the information flow we have provided for, and state that there will be a presumption that additional costs arising from these FERC conditions will not be borne by the Applicants' Utah jurisdictional ratepayers. Specifically,

1. If the FERC conditions result in increased municipalization that harms Utah retail ratepayers, Applicants

will have the burden of proving that it is not a result of the merger.

2. We put the Applicants and the FERC on notice that the Commission considers it unacceptable that revenue obligations for the Utah ratepayer may result from actions taken solely to comply with the FERC conditions which do not clearly and measurably benefit the Utah ratepayer. It is our intention that the beneficiaries of the FERC conditions will bear these additional costs.
3. There is a presumption that any additional costs incurred by non-recovery from those benefitted by FERC conditions will not be recovered from Utah ratepayers.
4. We will require annual accounting of incremental costs of the FERC conditions to be submitted in the Merged Company's annual cost of service filings. In addition, Applicants shall identify wheeling as a separate revenue class for the Merged Company and its divisions.
5. We intend to adopt a process for monitoring the impacts of the FERC conditions on the interruptible customers of the Merged Company, along the lines proposed by Nucor in this hearing.
6. It is our intention to protect the Merged Company's native load vis a vis any wheeling customers of the Merged Company.
7. Applicants shall propose a specific timetable and method for systemwide rolled-in rates in our upcoming allocation and/or general rate proceeding.

8. The risk of proceeding with the merger absent final regulatory approvals must be borne by the Applicants and their shareholders.

FINDINGS AND CONCLUSIONS

1. The testimony reflects that the positive benefits of the merger, as found by this Commission in its September 28, 1988 Order, are not substantially diminished after weighing the impact of the FERC-ordered conditions. All worst-case scenarios presented and analyzed on this record sustain this conclusion.

2. While this Commission is concerned about the legal and administrative policies of the FERC Order regarding access to the Applicants' transmission systems, there are nonetheless substantial net positive benefits to be achieved by the merger.

3. It is in the public interest that the conclusions and reporting requirements set forth in the Discussion section be adopted.

4. It is in the public interest that the Suspension Order of October 26, 1988 be vacated and set aside and that the Order of September 28, 1988 be in full force and effect.

ORDER

NOW, THEREFORE, IT IS HEREBY ORDERED that the Suspension Order of October 26, 1988 is vacated and that the Report and Order of the Commission dated September 28, 1988, except as modified herein, is reaffirmed.

DATED in Salt Lake City, Utah this 13th day of December, 1988.

(SEAL) /s/ Brent H. Cameron, Commissioner

/s/ James M. Byrne, Commissioner

ATTEST:

/s/ Stephen C. Hewlett
Commission Secretary

CONCURRENCE OF CHAIRMAN BRIAN T. STEWART

I concur in the decision of my fellow Commissioners to vacate the Suspension Order of October 26, 1988 and reaffirm our Report and Order of September 28, 1988. However, I must respectfully disagree on the issue of whether there should be any possibility that the costs that may result from the FERC conditions should be "netted out" against merger benefits, in effect resulting in such costs being borne by the ratepayers. I believe that the Commission should make it clear in this Order that such FERC imposed costs will not be borne by Utah retail ratepayers, but rather will be borne solely by FERC jurisdictional customers or shareholders.

As stated clearly in this Order, the Commission recognizes that additional risks and costs will flow from the FERC conditions. The extent of such risks and costs is undetermined. One of the reasons that little concrete value can be placed on the

FERC conditions is because the Applicants have chosen to plow headlong into culmination of the merger without hesitating for a moment to seek clarification of the terms and conditions of the FERC Order necessary to quantify their value or the risks they create. I believe that one of the reasons the Applicants are so casual about the FERC conditions is that they presume the risks and costs will be borne by the ratepayers. Such a presumption is clearly reflected in the testimony presented to this Commission.

I fear that by leaving a loophole in this Order, that is, by stating that it is only a presumption that the Utah jurisdictional ratepayers will not have to bear a portion of the costs of the FERC conditions, the Commission is altering the motivation of the Merged Company when it comes to implementation of the FERC conditions.

Stated plainly, the Applicants have already demonstrated a cavalier attitude towards a FERC power-grab and a willingness to abandon summarily its long defended control over its own transmission system. In light of such an attitude, my fear is that if the merged Company believes that it has any likelihood that it will be able to pass through to retail ratepayers the costs that flow from implementation of the FERC conditions, it will not demonstrate the necessary motivation to fight FERC over definitions and terms and practices that will have real impacts. If, on the other hand, such impacts are going to be passed on to the shareholders, the Merged Company's motivation may be very different.

In addition, I believe that to the extent any ratepayers should bear the costs of the FERC conditions, it should be FERC jurisdictional ratepayers. I am greatly offended by the FERC

Orders in this case. I believe that this federal agency has clearly overstepped its authority in this matter. States' rights have been trampled. Orderly consideration of the major transmission issues facing this nation has been aborted. But if the FERC insists upon extorting acceptance of these conditions as a condition of approval, let its jurisdictional ratepayers pay the price.

In short, I wish that the Commission's Order would make it clear that all costs that flow from the FERC conditions will not be borne by retail ratepayers in our jurisdiction.

/s/ Brian T. Stewart, Chairman

COMMENTS OF COMMISSIONER BRENT H. CAMERON

I acknowledge and sympathize with Chairman Stewart's concerns over the FERC imposed conditions. However, I want to clarify my own concept of imposing the additional risk of Applicants' acceptance of the FERC conditions on the FERC jurisdictional customers and how protection of the Utah ratepayer will occur.

I consider the Order as a statement of regulatory policy and intent that known risks accepted by the Applicants which were not heretofore considered in our September 28, 1988 Order are risks to the Applicants.

I do not consider the Order as a complete prohibition in the future of weighing those costs and balancing them against merger benefits. I believe the Merged Company bears the burden of con-

vincing the Commission by a preponderance of the evidence in a future proceeding that such costs should be balanced against actual merger benefits.

Our Order, as a matter of regulatory policy and intent, should be looked at as a guideline, but who bears what costs must and can only be assessed during a future proceeding analyzing the events and conditions present at that time.

Traditional regulatory concepts provide that the equity owner be afforded a reasonable opportunity to earn a fair rate of return. To put the equity owners at absolute risk while shifting most, if not all benefits, to the ratepayers implies higher authorized rates of return to compensate for this additional risk. I would prefer that benefits be shared as an incentive to encourage efficiency and fairness. For this merger to be successful, all parties must benefit. We have established conditions to protect ratepayers and employees. The FERC has established conditions to benefit wholesale customers and competitors. Equity owners must also be given the ability to reasonably share in the benefits and I don't believe each and every possible precondition should be imposed upon them.