STATE OF UTAH
OFFICE OF THE ATTORNEY GENERAL

JAN GRAHAM
ATTORNEY GENERAL

JAMES R. SOPER
Solicitor General

REED RICHARDS
Chief Deputy Attorney General

PALMER DEPAULIS
Director of Public Policy & Communications

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SERVICE COMMISSION

June 18, 1999

Julie Orchard
Secretary, Utah Public Service Commission
160 E. 300 So.
Salt Lake City, UT 84114

Re: Docket No. 98-2035-04 Utah Power & Light/Scottish Power Merger

Dear Julie,

Enclosed are the original and nine copies of the testimony of Lowell E. Alt, Mary H. Cleveland, Ronald L Burrup, William A. Powell, Kenneth B. Powell and Robert J. Maloney for the Division of Public Utilities. If you have any questions or concerns, please let me know.

Sincerely

Laurie L. Noda

Laurie L. Noda
Assistant Attorney General
Division of Public Utilities

PUBLIC AFFAIRS DIVISION • 160 EAST 300 SOUTH • P.O. BOX 140857, SALT LAKE CITY, UTAH 84114-0857
TELEPHONE (801) 366-0353 • FAX (801) 366-0352

I hereby certify that Thirty-five copies of Direct Testimony and Exhibits of Lowell E. Alt Jr., Ronald L. Burrrp, Mary H. Cleveland, Robert J. Maloney, William A. Powell and Kenneth B. Powell in the PacifiCorp Merger Case Docket Number 98-2035-04 were mailed or hand delivered on the 18TH day of June, 1999 to the following.

Michael Ginsberg
Assistant Attorney General
Division of Public Utilities
160 East 500 South, 5TH Floor
Salt Lake City UT 84111

Doug Tingey
Assistant Attorney General
Committee of Consumer Services
160 East 300 South, 5TH Floor
Salt Lake City UT 84111

Dr. Charles E Johnson
The Two Parties
1338 Foothill Boulevard, Suite 134
Salt Lake City UT 84108

Stephen R Randle
Randle Deamer Zarr Romrell & Lee, P.C.
139 East - South Temple Street, Suite 330
Salt Lake City UT 84111-1004

Peter J. Mattheis
Brickfield Burchette & Ritts PC
1025 Thomas Jefferson Street, N.W.
800 West Tower
Washington DC 20007

Dean S Brockbank
Brickfield Burchette & Ritts PC
1025 Thomas Jefferson Street, N.W.
800 West Tower
Washington DC 20007

Matthew J Jones
Brickfiels Buechette & Ritts PC
1025 Thomas Jefferson Street, N.W.
800 West Tower
Washington DC 20007

Curtis Broadbent - Controller
Nucor Steel
PO BOX 10
Plymouth UT 84330

Glen E Davis
Parsons Davies Kinghorn & Peters P.C.
185 South State Street Suite 700
Salt Lake City UT 84111

Bill Thomas Peters
Parsons Davies Kinghorn & Peters P.C.
185 South State Street Suite 700
Salt Lake City UT 84111

Jim Matheson
The Matheson Group
466 East 500 South suite 200
Salt Lake City UT 84111

Dr. Robert Malko
The Matheson Group
466 East 500 South suite 200
Salt Lake City UT 84111

David W Scofield
Parsons Davies Kinghorn & Peters P.C.
185 South State Street Suite 700
Salt Lake City UT 84111

Robert F Reeder
Parsons Behle & Latimer
One Utah Center
201 South Main Street
PO Box 45898
Salt Lake City UT 84116

William J Evans
Parsons Behle & Latimer
One Utah Center
201 South Main Street
PO Box 45898
Salt Lake City UT 84116

Lee R Brown, Vice President
Contracts, Human Affairs, Public &
Government Affairs
238 North 2200 West
Salt lake City UT 84116

Daniel Moquin
Assistant Attorney General
1594 West - North Temple Street, # 300
Salt Lake City UT 84116

Gary A Dodge
Parr Waddoups Brown Gee & Loveless
185 South State Street Suite 1300
Salt Lake City UT 84111-1536

Eric Blank
Land & Water Fund of the Rockies
2260 Baseline Suite 200
Boulder CO 80302

Robert Green - Group Controller
Scottish Power plc (REGULATION)
Kaiser Building, Suite 900
500 NE Multnomah
Portland OR 97232

Brian W Burnett
Callister Nebeker & McCullough
Gateway Tower East Suite 900
10 East - South Temple Street
Salt Lake City UT 84133

Lawrence H Reichman
Perkins Coie LLP
1211 SW Fifth Avenue Suite 1500
Portland OR 97204-3715

Anne E Eakin - VP Regulation
PacifiCorp
825 NE Multnomah Street
Portland OR 97332

D Douglas Larsen - Director
Regulatory Policy
PacifiCorp
One Utah Center Suite 2200
201 South Main Street
Salt Lake City UT 84140-2000

Edward A Hunter
Stoel RivesLLP
One Utah Center Suite1100
201 South Main Street
Salt Lake City UT 8411-4904

Steven W. Allred (ULCT)
Salt Lake City Corp.
451 South State Street, Suite 505
Salr Lake City UT 84111

Paul T Morris (ULCT)
3600 Constitution Blvd
West Valley City UT 84119

Roger O Tew, Esq. (ULCT)
60 South 600 East Suite 200
Salt Lake City UT 84102

Matthew F.McNulty, III, Esq. (UAMPS)
VanCott, Bagley, Cornwall & McCarthy
50 South Main Street Suite 1600
Salt Lake City UT 84145

Douglas O Hunter - General Manager
Utah Associated Municipal Power Systems
2825 East Cottonwood Parkway STE 200
Salt Lake City UT 84121

Dave Blackwell
Emery County Attorney
PO BOX 249
Castle Dale UT 84513

David F Crabtree
Deseret Generation & Transmission
5295 South 300 West Suite 500
Murray UT 84107

Betsy Wolf
Salt Lake Community Action Program
764 South 400 West
Salt Lake City UT 84101

Brian L Farr
Asst Attorney General
Community & Economic Development
P.O. Box 140857
Salt Lake City UT 84114-0857

Rick Anderson
Energy Strategies Inc.
39 Market Street Ste 200
Salt Lake City Ut 84101

Dennis Miller

17276

-BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH-

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.

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Division of Public Utilities
Utah PSC Docket No. 98-2035-04
Lowell E. Alt, Jr.
Exhibit No. DPU 1.1

EDUCATIONAL BACKGROUND

Bachelor of Science degree in Electrical Engineering (1967) and a Master's degree in Business Administration (1968) from West Virginia University
Electrical Engineering Honorary Society-Eta Kappa Nu
Registered Professional Engineer licensed in Utah and Pennsylvania.
Member Institute of Electrical and Electronics Engineers (IEEE)
Completed additional studies in utility economics and finance, utility regulation, cost of service, computer programming, and electric utility engineering.
Attended numerous conferences and seminars on utility regulation and management.

CURRENT POSITION

Manager of the Energy Section for the Utah Division of Public Utilities. I am responsible for managing the Division's work on electric and natural gas utilities.

PRIOR WORK EXPERIENCE

I started with the Division of Public Utilities as an Electric Rate Engineer in 1980. I was Chief Engineer from May 1983 until October 1995 when I became Manager of the Energy Section. I have testified before the Utah Public Service Commission in electric cases on interim rates, rate design, cost-of-service, and return on equity; in telephone cases on cost-of-service and in natural gas cases on customer charges and service extensions. I have completed numerous cost-of-service studies of various utilities including Utah Power & Light, U.S. West Communications, Moon Lake REA, Raft River REA, Wells REA, Dixie Escalante REA, Flowell REA, Strawberry Water Users Association, Sandy City Water and White City Water Company. I worked for Pennsylvania Power and Light Company from 1968 to 1980. My last positions there were Distribution Senior Engineer-Substations and Senior Tariff Analyst.

Division of Public Utilities
Utah PSC Docket No. 98-2035-04
Lowell E. Alt, Jr.
Exhibit No. DPU 1.2

Summary List of Division Merger Conditions

ISSUE	CONDITION
	1. PacifiCorp/ScottishPower shall agree to all commitments and conditions as included in Witness Alan Richardson's Supplemental Testimony Exhibit AVR-1 EXCEPT as modified by the following Division proposed conditions:
The corporate structure of the merged companies is unknown and there is no methodology in place for the allocation of ScottishPower's corporate costs to PacifiCorp.	2. Within 30 days of the completion of the merger ScottishPower/PacifiCorp shall file a proposed cost allocation methodology with the Utah Public Service Commission for its approval. Cost allocation methodologies shall comply with the following principles: a. For all costs allocated to PacifiCorp from the ScottishPower group, ScottishPower must demonstrate a benefit to PacifiCorp. b. Cost allocations shall be based on generally accepted accounting standards, that is, that in general, direct costs shall be charged to specific PacifiCorp subsidiaries wherever possible and shared or indirect costs shall be allocated based upon the primary cost-driving factors. c. ScottishPower shall have in place timekeeping and project management systems adequate to support the allocation of executives' costs. d. An audit trail shall be maintained such that all costs allocated can be specifically identified along with their origination and adequately supported. Failure to adequately support any allocated cost may result in denial of its recovery in rates.

		e. Costs which have been denied recovery in rates had they been incurred by PacifiCorp regulated operations will likewise be denied recovery whether they are allocated directly or indirectly through subsidiaries in the ScottishPower group. f. Any corporate cost allocation methodology, and subsequent changes thereto, must be approved by the Utah Commission. ScottishPower will assume the risk for the Utah Commission approval and adoption of corporate cost allocation methodologies which differ from those adopted by OFFER or any other U.S. regulatory jurisdiction.
ScottishPower has guaranteed a $10 million savings in corporate costs. However, the basis from which this savings is measured will determine whether or not any of the guaranteed savings is realized by ratepayers.	3.	The achievement of the $10 million guaranteed savings shall be measured from PacifiCorp's 1999 actual corporate costs, normalized and adjusted so as to reflect only those costs that would be included in rates. All costs related to the ScottishPower merger shall also be excluded.
Both ScottishPower & PacifiCorp have committed to recording merger "transaction" costs below the line. However, there are merger related costs that have not been classified as "transaction" costs.	4.	All merger related costs incurred by PacifiCorp and ScottishPower shall be recorded below the line.
The most recently proposed corporate	5.	Any diversified holdings and investments (e.g., non-utility business or foreign utilities) of ScottishPower and

structure would create a U.S. registered holding company to facilitate further acquisitions by ScottishPower in the U.S. This potential diversification creates more risk.	PacifiCorp shall not be held by PacifiCorp, the entity for utility operations. 6. ScottishPower/PacifiCorp shall be required to notify the Utah Commission subsequent to ScottishPower plc's Board approval and as soon as practicable following any public announcement of and acquisition of a regulated or non-regulated business representing 5% or more of the market capitalization of ScottishPower plc.
Potential for affiliate transactions to result in cross-subsidization of other members of the ScottishPower group by PacifiCorp, the regulated utility.	7. ScottishPower shall be required to comply with PacifiCorp's Transfer Pricing Policy. 8. The Merged Company shall notify the Commission, and provide sufficient information and documentation to the Commission, prior to the implementation of plans (1) to form an affiliate entity for the purpose of transacting business with the electric divisions of PacifiCorp, (2) to commence new business transactions between an existing affiliate and the electric utility divisions of PacifiCorp, (3) to dissolve an affiliate which has transacted any substantial business with such divisions, (4) to enter into new business ventures or expand existing ones, or (5) to merge, combine, transfer stock or assets of any part or all of the Merged Company. 9. The Merged Company shall provide notification of all asset transfers to or from PacifiCorp, its affiliates, or subsidiaries in accordance with current PSC rules (PSC R746-401).
Potential divestiture of PacifiCorp's utility activities.	10. The Applicants shall be required to provide notification of and file for Commission approval of the divestiture, spin-off, or sale of any integral utility assets or functions.
Access to books, records and personnel affects PSC's ability to effectively regulate PacifiCorp.	11. Establish agreed upon procedures by which Division staff can have access to documentation supporting the purpose and/or circumstances attributable to costs charged to PacifiCorp.

	12. The holding company(s) and subsidiaries' employees, officials, directors, or agents shall be available to testify before the Utah Commission to provide information relevant to matters within the jurisdiction of the Utah Commission. 13. The Utah Commission should establish procedures by which the Public Service Commission and Division staffs, or their authorized agents can obtain needed access to subsidiary books and records, other relevant documents, data and records. Failure to provide adequate supporting documentation of costs may result in those costs being denied rate recovery. Requests by the Utah Commission, the Division, or their authorized agents shall be deemed presumptively valid, material and relevant, with the burden falling to ScottishPower/PacifiCorp to prove otherwise. ScottishPower/PacifiCorp shall reserve the right to challenge any such request before the Utah Commission and shall have the burden of demonstrating that any such request is not valid, material or relevant. In addition, ScottishPower/PacifiCorp shall pay for the expense incurred by Utah regulatory personnel in accessing corporate records and personnel located outside of the state of Utah.
Risk that the $10 million in merger savings will not be realized in rates	14. A 2001 Informational Filing shall include a full description, calculation (with supporting work papers) and dollar identification (both total PacifiCorp and Utah's share) of merger savings. This filing shall include in the adjusted revenue requirement calculation any merger savings achieved, applying established Utah ratemaking practices. The allocated share of merger savings shall not be less than the Utah allocated share of the $10 million of estimated PacifiCorp corporate savings, assuming that the closing date of the PacifiCorp/Scottish Power merger occurs in 1999. If the closing date of the PacifiCorp/Scottish Power merger does not occur in 1999, PacifiCorp/Scottish Power may make an appropriate adjustment in the $10 million of estimated PacifiCorp corporate savings to reflect the delay in the closing of the merger. In either event, if the annual amount of PacifiCorp corporate savings exceed $10 million,

	the higher amount of actual savings will be used. The $10 million in PacifiCorp corporate savings will apply notwithstanding the fact that foreign exchange variations in the costs charged will fall into PacifiCorp. The promised $10 million net reduction is permanent and guaranteed whether or not it is actually achieved. 15. No later than six months after the closing date of the merger, ScottishPower and PacifiCorp will file the merger transition plan with the Commission. The plan will include the items described in Mr. MacRichie's Oregon rebuttal testimony.
Risk that intra-company loans may disadvantage electric operations.	16. PacifiCorp and ScottishPower shall apply to the Commission for approval of intra-company loan agreements.
Risk that dividend payments may interfere with construction obligations.	17. For two years following the merger, PacifiCorp shall file a cash flow summary (or other evidence) with its dividend report, showing that service will not be impaired by payment of the dividend.
Risk that asset revaluation may be used to increase property tax expense which is used in setting rates.	18. Scottish Power agrees that asset revaluation resulting from the merger shall not be used as a basis to increase property taxes or other taxes or existing contract costs for the purpose of setting rates in the Utah jurisdiction.
Risk that state regulators will not maintain their ability to adequately regulate the merged company.	19. General and Financial reports - To be filed with the PSC: a. FERC form 1 - Total Company & Utah b. Annual and quarterly reports to shareholders c. Semi Annual reports showing Utah and total company operating results, allocation factors, coal reports, demand side management report, production costs modeling, peak loads by jurisdiction, normalizing adjustments and work papers, d. Monthly financial and operating reports e. Securities and Exchange Commission Reports 10-Q

	and 10K, quarterly and annual. f. Annual class cost of service studies g. Monthly Energy Information Administration Form EIA-826 h. Annual affiliated interest report i. Five year financial plan and forecast of financial condition, filed annually for the total company, PacifiCorp division, and the Utah jurisdiction.
Gains or losses on foreign transactions can occur due to exchange rate changes. The Financial Accounting Standards Board (FASB) has rules governing such transactions.	20. ScottishPower shall follow the generally accepted accounting standards regarding foreign operations and exchange. Namely, FASB 52.
The Public Utility Holding Company Act of 1935 (PUHCA) came about largely due to wide spread abuses and the inability of state commissions to regulate large, multi-jurisdictional holding companies.	21. Unless otherwise approved by the PSC, the following apply: For ratemaking purposes, a hypothetical capital structure will used to determine the correct costs of capital. The capital structure shall be constructed using a group of A-rated electric utilities comparable to PacifiCorp. 22. Within thirty days after the approval of the merger PacifiCorp/ScottishPower shall provide a detailed report indicating PacifiCorp's proportionate share of the Holding company's total assets, total operating revenues, operating and maintenance expense, and number of employees. Subsequent to this initial report, this information shall be included as part of the PacifiCorp's semi-annual filing with the Commission. 23. Until approved by the Commission in a separate proceeding, PacifiCorp shall maintain separate debt and, if outstanding, preferred stock. 24. PacifiCorp shall apply to the Commission for approval of debt issuances.

	25. PacifiCorp/ScottishPower agrees not to assert in any future Utah proceeding that the provisions of PUHCA or the related Ohio Power v FERC case preempt the Commission's jurisdiction over affiliated interest transactions and will explicitly waive any such defense in those proceedings. 26. PacifiCorp/ScottishPower shall provide a copy of any SEC filed lobbying reports.
Despite ScottishPower's promises, there is a risk that the cost of capital could increase as a result of the merger.	27. If ScottishPower is able to lower the costs of capital, then those savings shall be reflected in rates in a timely manner. If, however, the cost of capital increases as a result of the merger, ScottishPower's shareholders will bear that cost.
PacifiCorp shareholders have been offered a substantial premium. If just a portion of this premium were to get into rates, the promised $10 million in savings would be completely dwarfed.	28. Rates will be set based upon original and not revalued costs; any premium paid by ScottishPower for PacifiCorp stock will be disregarded for ratemaking purposes.
ScottishPower's informal assurances to provide a service package do not establish enforceable accountability for achieving service results.	29. Continuously meet performance standards, provide service guarantees, and do not allow underlying outages to increase above current levels.
ScottishPower's plans to fund a maximum of $55 million in network	30. Fund network expenditures from efficiency savings and redirected internal funding; report funding sources and expenditures against the $55 million estimate.

expenditures from as yet unidentified efficiencies and internal funding sources are subject to a high degree of uncertainty.	
It is not possible to accurately determine outage levels with the current outage reporting system.	31. Implement Prosper, an automated reporting system, no later than 12 months after the merger transaction and also operate the current reporting system in parallel until actual outage levels are accurately and reliably determined.
Agreeing on outage levels using inaccurate and unreliable outage data can result in irresolvable differences between ScottishPower management and Division staff.	32. Measure outage-reduction performance against agreed to (by management and Division Staff) outage levels at the time Prosper is installed and audited -- or defer to the Commission on such.
ScottishPower's proposed use of IEEE criteria in defining an extreme event requires engineering judgements about what "exceeds design limits" and what constitutes "extensive damage." Reasonable engineers may differ on these matters.	33. Define"extreme event" as outside three standard deviations of the average number of daily incidents during the previous calendar year.
It is not possible to accurately determine outage levels with the current outage reporting	34. Audit, upon request, to determine actual outage levels – after correcting for under or inaccurate recording.

system. Whether ScottishPower can effectively implement an accurate reporting system is uncertain.	
ScottishPower may more efficiently reduce statewide outage levels by focusing limited investments in highly populated areas. Already high outage levels in sparsely populated high-cost rural areas could rise.	35. Report, each quarter, outage levels against internal outage targets on a district, circuit, and (where feasible) individual customer basis.
ScottishPower's standards package does not include *performance standards* for field responses. The Company may achieve its standards package at the expense of services not consider important enough to include in its service package.	36. Continue with meter set and meter test internal field response targets in Northern Utah. Establish internal field response targets where none currently exist. Report performance against all targets on a quarterly basis.
In the past, PacifiCorp has had a multitude of system breakdowns in handling calls during wide scale outages.	37. Report, during wide-scale outages, internal call-handling targets and results: average answer speeds, hold times, and busy indications.
In pursing efficiencies, ScottishPower may be especially pressed to	38. Report, each quarter, district data showing credits to customers for failures to meet guaranteed service outcomes.

adequately fund timely field responses in high – cost rural service territories.	
Management practices vary widely among PacifiCorp's Utah districts. Under such circumstances, managers may have a variety of interpretations regarding guarantee requirements.	39. Implement and tariff a dispute resolution process for dealing with guaranteed service outcomes failures on a fair and consistent basis.
Expensive resource acquisitions may cause rates to go up unnecessarily.	40. ScottishPower will continue to produce Integrated Resource Plans every two years, according to the current schedule and current PSC rules. 41. ScottishPower's commitment to develop an additional 50MW of renewable resources is conditioned on those resources meeting the cost effectiveness standards of the IRP then in place.
Commitment to employees	42. For the two years following the final approval of the merger, Utah PacifiCorp employee benefits will be held stable per the ScottishPower/PacifiCorp merger agreement.
Other conditions do not completely assure a net positive benefit.	43. Rate (revenue requirement) increases would be limited for a maximum of three years to either inflation increases as measured by the GDP or to increases such that the Utah rate of return on equity would not exceed that resulting from proceedings in any other PacifiCorp State. Both situations would require a full rate case where increases are limited to the cap and rates may be reduced.

	44. Conditions or benefits agreed to by ScottishPower or PacifiCorp in other jurisdictions that would benefit Utah shall also be received by Utah. 45. Rates in Utah shall not increase as a result of the merger. 46. 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 that in other jurisdictions.

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UTAH PUBLIC
SERVICE COMMISSION

-BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH-

In the Matter of the Application of	)	Docket 98-2035-04
PACIFICORP and SCOTTISH POWER	)	Division of Public Utilities
PLC for an Order Approving the Issuance	)	Testimony of Ronald L. Burrup
of PACIFICORP common stock	)	Exhibit No. DPU 3.0 (RLB)

June 18, 1999

Q PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A My name is Ronald L Burrup, I am employed by the Utah Division of Public Utilities (Division) as a Technical Consultant. My business address is 160 East 300 South, Heber Wells Building, Salt Lake City, Utah

Q HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION?

A Yes, on a number of occasions. My qualifications are shown on the attached Exhibit No. DPU RLB 3.1.

Q WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS CASE?

A The purpose of my testimony is to recommend conditions to address the Division's concerns in several areas such as merger savings and costs, asset valuation, intra-company loan agreements, dividend payments, and financial reporting requirements. The specific merger conditions that I recommend are shown in bold type. They are also shown separately on Exhibit No. DPU RLB 3.5.

Q PLEASE EXPLAIN WHAT YOU REVIEWED IN CONNECTION WITH THIS APPLICATION?

A I reviewed public and internal financial statements of PacifiCorp and ScottishPower, financial projections, estimates of cost savings, due diligent reports, , board minutes, reports of financial analysts and consultants, and the prospectus to shareholders. I also reviewed the data requests and responses of the Division, other parties in Utah and other states. In addition, I participated in frequent discussions with other states and attended presentations by ScottishPower and PacifiCorp in Oregon and Utah.

MERGER SAVINGS AND COSTS

Q IS THIS MERGER SIMILAR TO THE 1989 MERGER OF UTAH POWER AND PACIFIC POWER?

A No, in some ways it is the opposite. In the 1988 merger, the applicants made a concerted effort to quantify every conceivable merger savings. Merger savings were specifically identified year by year and by area for both companies. The companies provided forecasts and detail on each area of merger savings. The merger savings were estimated to be $481 million in the first 5 years. In 1989 Utah Power reported a return on equity of 15.5% in the Utah jurisdiction, so merger savings were reflected in a series of rate reductions.

In the present case the applicants are vague about specific merger savings. They claim that merger savings haven't been quantified, that this will occur after the merger. Only $10 million in merger savings have been specifically identified from PacifiCorp and none from Scottish Power. When this $10 million is allocated to Utah, it amounts to about $3.5 million. This is less than one half of one percent of Utah's annual tariff revenues of $822 million. This lack of specificity about merger savings means that there are more unknowns. This merger is not as clearly a "good deal" like the 1989 merger.

Q WHAT IS YOUR CONCLUSION REGARDING MERGER COSTS AND SAVINGS?

A The applicants commit to $10 million in merger savings by the third year after the transaction closes. My opinion is that the $10 million is understated, and that greater consolidation savings can be achieved. This represents only 22% of PacifiCorp's 1998 budget for these services. This does not include any savings in the same service areas for Scottish Power. Nor does this included any savings from benchmarking and implementation of best practices.

Q HAVE OTHERS ESTIMATED MERGER SAVINGS TO BE GREATER THAN $10 MILLION?

A Yes, Warburg Dillion Read (WDR), an investment banker in the UK issued a 45 page report in December 1998, on the Scottish Power/PacifiCorp merger. They estimated that Scottish Power could achieve merger savings of $200 million annually. I prepared Exhibit No. DPU RLB 3.2 that shows their estimate of target merger cost reductions on the bottom line. WDR bases their estimates on Scottish Power's track record at ManWeb and Southern Water, and on WDR's observation that "UK wires and generation productivity appears to be 22-55% higher than in PacifiCorp[1]".

Q HAS MR. RICHARDSON INDICATED THAT MERGER BENEFITS MAY BE SIGNIFICANTLY GREATER?

A Yes, in his supplemental testimony filed on April 16, 1999, Mr. Richardson states

[1]Warburg Dillon Read, report December 1998, page 24

on page 8 lines 11 through 13 the following.

> Apart from the corporate costs reductions, we are confident that we will achieve additional significant cost savings in the future, although their magnitude cannot be quantified.

Q WHAT CONDITION WOULD YOU RECOMMEND TO INSURE THAT THE $10 MILLION IN BENEFITS IS REALIZED?

A The following paragraph would resolve the Divisions's concerns. It is similar to paragraph 4 from the Wyoming stipulation (included as Exhibit No. DPU RLB 3.3

> **A 2001 Informational Filing shall include a full description, calculation (with supporting work papers) and dollar identification (both total PacifiCorp and Utah's share) of merger savings. This filing shall include in the adjusted revenue requirement calculation any merger savings achieved, applying established Utah ratemaking practices. The allocated share of merger savings shall not be less than the Utah allocated share of the $10 million of estimated PacifiCorp corporate savings, assuming that the closing date of the PacifiCorp/Scottish Power merger occurs in 1999. If the closing date of the PacifiCorp/Scottish Power merger does not occur in 1999, PacifiCorp/Scottish Power may make an appropriate adjustment in the $10 million of estimated PacifiCorp corporate savings to reflect the delay in the closing of the merger. In either event, if the annual amount of PacifiCorp corporate savings exceed $10 million, the higher amount of actual savings will be used. The $10 million in PacifiCorp corporate savings will apply notwithstanding the fact that foreign exchange variations in the costs charged will fall into PacifiCorp.**

Q IN OCTOBER 1998, PACIFICORP ANNOUNCED A "REFOCUS" PROGRAM AIMED AT IMPROVING FINANCIAL PERFORMANCE THROUGH COST REDUCTIONS AND REFOCUSING ON THE CORE BUSINESS. DO YOU BELIEVE PACIFICORP CAN ACHIEVE THE SAME LEVELS OF COST

REDUCTIONS THROUGH THIS PROGRAM WITHOUT THE MERGER?

A. No. It is my opinion that real change in financial performance and customer service will only come through a change in senior management. I agree with the Warburg Dillion Read report that concluded PacifiCorp has "attractive assets but these have been undermanaged, resulting in a significant loss of shareholder confidence in management". In addition, the current "refocus" effort does not include any of the customer service guarantees included in the ScottishPower proposal.

ScottishPower, on the other hand, has proven management expertise in operating a vertically integrated electric utility, and has demonstrated its success in reducing costs and increasing customer service.

Q PRIOR TO THE MERGER, HAVE YOU EVER HEARD PACIFICORP MANAGEMENT REFER TO BENCHMARKING OR BEST PRACTICES?

A No.

Q IS BENCHMARKING A USEFUL TOOL FOR AN ORGANIZATION TO USE TO IMPROVE ITS PERFORMANCE?

A. I believe it is. The American Productivity and Quality Center and the Strategic Planning Institute Council on Benchmarking have adopted a written Benchmarking Code of Conduct. It states:

> Benchmarking - the process of identifying and learning from best practices anywhere in the world - is a powerful tool in the quest for continuous

improvement.

Benchmarking accelerates change by 1) using tested methods 2) identifying areas of improvement, 3) convincing skeptics and 4) involving process owners[2].

Q HOW DOES THE APPLICANT PROPOSE TO RECORD MERGER RELATED COSTS?

A In the 1989 merger, the costs were split between customers and shareholders. In this merger, applicants have "promised to exclude from our books for ratemaking purposes" costs ScottishPower and PacifiCorp will incur to complete the tranasction[3]. The total transaction costs for PacifiCorp are estimated to be $50 million. ScottishPower has not finalized its cost estimates for the transaction[4]. The PacifiCorp transaction costs to date ($13.2 million in 1998) have been charged below the line to Account 426[5]. If merger related costs are not accurately identified and excluded from rates, they could easily surpass the $10 million in merger savings. Division witness Mary Cleveland discusses merger costs in her direct testimony in more detail.

ScottishPower has stated that its transaction costs will be capitalized and

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[2] Source: PriceWaterhouseCooper, Benchmarking: A Manager's Guide and American Productivity and Quality Center

[3] Supplemental testimony of Alan Richardson, page 8

[4] ScottishPower response to Idaho PUC data request number 22

[5] PacifiCorp's response to Idaho PUC data request number 13

amortized over several years and that these costs will be borne by shareholders and not considered to be costs for recovery from customers.

Q SCOTTISH POWER HAS STATED THAT IT WILL MAKE ADDITIONAL INVESTMENTS TO IMPROVE CUSTOMER SERVICE. WILL THESE INVESTMENTS INCREASE COSTS?

A No. Scottish Power has committed to reducing already existing PacifiCorp capital or operating budgets by a similar amount to implement customer service improvements without increasing costs[6]. The table below shows PacifiCorp's domestic electric operations estimated construction budget for 1999 through 2001 (in millions).

Type of facility	1999	2000	2001
Distribution	$168	$180	$180
Production	120	87	113
Mining	31	33	52
Transmission	50	51	51
Other	110	63	66
Total	$479	$414	$462

The $32 million in capital expenditures described in Mr. Alan Richardson's supplemental testimony, is to be spent over 5 years to improve customer service. It represents only about 1-2% of the existing capital budgets ($6.4 million per year divided by $479 million construction budget). It is reasonable to assume that capital budgets will

[6] See Alan Richardson's supplemental testimony page 7 lines 6 through 23.

not increase as a result of these expenditures.

INTRA-COMPANY LOANS AND DIVIDEND PAYMENTS

Q WHAT ADDITIONAL RISK DOES THE MERGER PRESENT TO UTAH CUSTOMERS?

A There are two areas of additional risk that I see. First is the risk that intra-company loans may be unfair to electric operations. The Commission has already approved an intra-company loan agreement between PacifiCorp electric operations and the other PacifiCorp subsidiaries. At the end of 1998 PacifiCorp had in excess of $500 million in cash or cash equivalent. Scottish Power should reapply for approval of intra-company loan agreements stating what rates and limits apply to future intra-company loans.

The second area of risk is in dividend payment policy. State statutes require notification by a gas or electric utility prior to payment of a dividend. Historically the utilities have written a letter to the Commission containing the information required by the statute. The statute states:

> If the commission, after investigation, shall find that the capital of any such corporation is being impaired or that its service to the public is likely to become impaired or is in danger of impairment, it may issue an order directing such utility corporation to refrain from payment of said dividend until such impairment is made good or danger of impairment is avoided. UCA 54-4-27

In 1998, PacifiCorp's cash flow from operations (after dividend payment) covered only about half of the cash requirements for construction and repayment of maturing long term debt[7]. The capital budgets through 2001 also indicate a continuing need for capital in excess of cash flows from operations. To insure that dividend payments do not interfere with the need for capital, PacifiCorp should file additional information with the dividend payment notification required under the statute, for at least the next two years. The additional information may be in the form of a cash flow summary showing cash sources and needs. The following merger condition will resolve these two concerns.

PacifiCorp and Scottish Power shall apply to the Commission for approval of intra-company loan agreements. For two years following the merger, PacifiCorp shall file a cash flow summary (or other evidence) with its dividend report, showing that service will not be impaired by payment of the dividend.

REVALUATION OF ASSETS

Q FOLLOWING THE MERGER, THE ASSETS OF PACIFICORP WILL BE REVALUED BY SCOTTISH POWER. DOES THIS IMPOSE ANY ADDITIONAL RISK?

A Yes. Scottish Power has stated that the revaluation will not change rate base values at PacifiCorp. However, revaluation may impact operating expenses. Mr. Malko

[7] Securities and Exchange Commission Form 10-K/A, Dec. 31, 1998, page 41

appearing on behalf of Emery County recommends that the Commission defer any ruling on asset revaluation to the jurisdiction of the Utah State Tax Commission[8]. This recommendation adds significant risk for customers. Property taxes in the 1997 test year were $83 million. If the Utah State Tax Commission increases property taxes based on asset revaluation, this alone could easily surpass the $10 million in merger savings. Customers would be left with additional merger costs in excess of the $10 million merger benefits, courtesy of the Utah State Tax Commission which has no jurisdiction over the merger. I recommend that the Commission adopt the following condition to address this significant risk.

Scottish Power agrees that asset revaluation resulting from the merger shall not be used as a basis to increase property taxes or other taxes or existing contract costs for the purpose of setting rates in the Utah jurisdiction.

Q. IN THE 1989 MERGER THE COMMISSION REQUIRED CERTAIN REPORTING REQUIREMENTS. WHAT ARE THE REPORTING REQUIREMENTS THAT YOU RECOMMEND BE ADOPTED IN THIS MERGER?

A I recommend that reporting requirements from the prior merger be continued. These reports are not unduly burdensome. PacifiCorp has been filing them with the Division and Commission for the past 10 years. These reports relate to maintaining the

[8] Testimony of J.Robert Malko, June 9, 1999, page 8, Docket 98-2035-04

state's ability to adequately regulate the merged company.

General and Financial reports to be filed with the Commission

a) **FERC form 1**
b) **Annual and quarterly reports to shareholders**
c) **Semi Annual reports showing Utah and total company operating results, allocation factors, coal reports, demand side management report, production costs modeling, peak loads by jurisdiction, normalizing adjustments and work papers,**
d) **Monthly regulatory financial and operating reports**
e) **Securities and Exchange Commission Reports 10-Q and 10K, quarterly and annual.**
f) **Annual class cost of service studies**
g) **Monthly Energy Information Administration Form EIA-826**
h) **Annual affiliated interest report**
i) **Five year financial plan and forecast of financial condition, filed annually for the total company, PacifiCorp division, and the Utah jurisdiction.**

Q IF THIS COMMISSION APPROVES THE MERGER AND SCOTTISHPOWER SUBSEQUENTLY AGREES TO CONDITIONS THAT BENEFIT OTHER JURISDICTIONS, SHOULD THOSE CONDITIONS ALSO APPLY IN UTAH?

A Yes, conditions or benefits agreed to by ScottishPower or PacifiCorp in other jurisdictions that create a benefit for a jurisdiction, should also be received by Utah customers.

Q CAN YOU GIVE SOME EXAMPLES?

A Yes, ScottishPower recently filed rebuttal testimony in Oregon that included more specific conditions that should also apply in Utah. In Mr. MacRichie's Oregon rebuttal testimony at page 3, he states.

"No later than six months after the closing date of the merger, ScottishPower and PacifiCorp will file the merger transition plan with the Commission".

This plan should also be filed with the Utah Commission. Also Mr. Green states in his Oregon rebuttal testimony the following.

"The promised $10 million net reduction is permanent and guaranteed whether or not we actually achieve it, and I am providing a methodology whereby this net reduction can be tracked and verified".

I recommend the following merger condition.

No later than six months after the closing date of the merger, ScottishPower and PacifiCorp will file the merger transition plan with the Commission. The plan will include the items described in Mr. MacRichie's Oregon rebuttal testimony. The promised $10 million net reduction is permanent and guaranteed whether or not it is actually achieved.

Q COULD YOU EXPLAIN THE GENERAL TERMS OF THE WYOMING STIPULATION?

A Scottish Power and PacifiCorp signed a stipulation with the Wyoming Consumer Advocate Staff (CAS). The role of the CAS is to represent the public interest, as viewed by the whole body of citizens of Wyoming. They do not represent the views of only a few specific classes of customers. The CAS entered into two different stipulations, the first is with Scottish Power and PacifiCorp and addresses merger conditions. It is attached as Exhibit No. DPU RLB 3.3.

The second agreement is between PacifiCorp and the CAS regarding rate filings in 1999 and 2000. This agreement is referenced in the merger stipulation in paragraph 3. The second agreement is attached as Exhibit No. DPU RLB 3.4.

Q. WHAT POSITION DID THE WYOMING CAS TAKE CONCERNING THE MERGER?

A. The CAS believed that there were a great deal of uncertainities[9] about the provision of service following the merger. However, those uncertainties cut both ways and there could be some very positive results coming from the merger. The CAS determined that by approving the merger with conditions it could deal with the uncertainties. I agree, in principle, with the statement made in the testimony of Denise Parrish.

> While there is no certainty, it is the CAS's belief that PacifiCorp customers will be no worst off, and will likely be better off, with the PacifiCorp/Scottish Power merger (and accompanying conditions), than without it.[10]

Q WHAT WERE THE CONDITIONS REGARDING RATES AGREED TO BY THE CAS AND PACIFICORP?

A Denise Parrish describes the agreement in her testimony as follows:

> In general, the separate agreement, which has been filed for informational purposes with the Commission separate and apart from this docket,

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[9] Testimony of Denise Parrish, Wyoming Docket No. 20000-EA-98-141, page 8

[10] Testimony of Denise Parrish, Wyoming Docket No. 20000-EA-98-141, page 11

> imposes a cap on the amount of rate relief that PacifiCorp can request in Wyoming in 1999 and 2000. It does not limit the CAS's review of the requested relief, nor does it limit the CAS advocating a lesser amount of rate relief than requested by PacifiCorp. In exchange for this rate limitation, the CAS has agreed to work with the companies to expedite the rate case process and has agreed to continue to work with the company on the review of its proposed depreciation modifications and on the review of interjurisdictional allocations. Finally, the agreement discussed limitations on rate increases to any particular class of service, so as to mitigate the impact of the increases on customers while still moving toward cost of service rates.[11]

The agreement caps the amount of rate increase PacifiCorp can seek in Wyoming in 1999 at $12 million, which is a 4.4% rate increase, and in the year 2000 the limit is capped at $8 million, a 2.9% rate increase, plus the impact of any change in depreciation.

Q IS THE RATE AGREEMENT AN IMPORTANT PART OF THE MERGER PROCEEDING IN WYOMING?

A Yes, Denise Parrish links the two agreements in her merger testimony.

> The rate agreement is an important consideration in this proceeding, since it shows that PacifiCorp is willing to continue to show a reasoned approach to phasing-in rate increases, and that the merger itself is not driving huge rate increases in order to immediately get returns to more appropriate levels. This agreement is in the public interest since it limits the size of the rate increase that will be requested in the next two years, even though PacifiCorp believes that it could justify a much larger increase.[12]

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[11] Testimony of Denise Parrish, Wyoming Docket No. 2000-EA-98-141, page 16

[12] Denise Parrish, Wyoming Docket No. 2000-EA-98-141, page 16-17

Q DOES THAT CONCLUDE YOUR DIRECT TESTIMONY?

A. Yes.

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Ronald Burrup

EMPLOYMENT

Public Utility Technical Consultant — **Years Employed : 1976 - present**
DEPARTMENT OF COMMERCE, DIVISION OF PUBLIC UTILITIES — SALT LAKE CITY, UTAH

Review and analyze accounting, statistical and economic data and assist in the development of policy for regulated utilities. Conduct independent research and apply theories in matters pertaining to utility accounting, rates, mergers, contracts, and operations. Write requests for proposals and administer contracts with venders. Present positions as oral and written testimony as an expert witness and negotiate settlements. Lead groups of other professionals in specific tasks.

Received Department of Commerce Highest Level Performers Award in 1995 and 1996, received Department Incentive Awards, and Exceptional performance reviews each year from 1991 to 1996.

Insurance Adjuster — **Years Employed : 1973 - 76**
INSURANCE COMPANY OF NORTH AMERICA — SALT LAKE CITY, UTAH

Conduct investigations into insurance claims and negotiate settlements with claimants

U. S. Army Officer — **Years Employed : 1971 - 73**
U. S. ARMY, QUARTERMASTER CORP — FT. LEE, VIRGINIA

Train and supervise enlisted personnel.

EDUCATION

Certified Public Accountant — **Year Attained : 1983**
LICENSED BY THE STATE OF UTAH (MEMBER AICPA) — SALT LAKE CITY, UTAH

Master of Public Administration — **Years Attended: 1979 - 81**
BRIGHAM YOUNG UNIVERSITY — PROVO, UTAH

B. S. Business Administration — **Years Attended: 1965 - 70**
BRIGHAM YOUNG UNIVERSITY — PROVO, UTAH

Utah Division of Public Utilities
Witness: Ronald L. Burrup
Exhibit No. DPU RLB 3.2

PacifiCorp Merger Cost Savings

Warburg Dillion Read Report on Cost Savings

PacifiCorp EBIT Model (earnings before income taxes)

		1998	1999	2000	2001	2002	2003
	Energy Sales (GWh)						
1	Wholesale	117,695	141,233	169,480	189,818	212,596	238,107
2	Retail	47,072	48,155	49,262	50,395	51,554	52,740
3	Total	164,767	189,388	218,742	240,213	264,150	290,847
	Average Price (cents)						
4	Wholesale	2.60	2.60	2.60	2.63	2.65	2.68
5	Retail	4.96	4.84	4.84	4.84	4.84	4.84
	Income Statement (millions)						
6	Wholesale	3,060	3,672	4,406	4,985	5,639	6,378
7	Retail	2,336	2,333	2,386	2,441	2,497	2,555
8	Total Operating Revenues	5,396	6,005	6,792	7,426	8,136	8,933
	Expenses						
9	Fuel	470	479	490	501	513	524
10	Purchased Power	3,045	3,610	4,336	4,895	5,543	6,264
11	Other Operations	289	256	264	273	281	290
12	Maintenance	187	185	191	197	199	201
13	Depreciation	396	396	404	417	430	444
14	Admin & General, other	229	227	207	197	200	200
15	Other taxes	100	99	101	104	106	109
16	Total electric expenses	4,716	5,252	5,993	6,584	7,272	8,032
	Target Savings 15% of Controllable Costs						
17	Fuel	71	72	74	75	77	79
18	Other Operations	43	38	40	41	42	44
19	Maintenance	28	28	29	30	30	30
20	Admin & General, other	34	34	31	30	30	30
	Total Target cost reductions	176	172	173	175	179	182

Source: Warburg Dillion Read Report, December 1998, Appendix 2, and page 26 and 27

BEFORE THE PUBLIC SERVICE COMMISSION OF WYOMING

In the Matter of the Joint Application of PacifiCorp and Scottish Power plc for Approval of a Reorganization of PacifiCorp as a Wholly-Owned Subsidiary of ScottishPower plc	DOCKET NO. 20000-EA-98-141 (RECORD NO. 4660)

STIPULATION

This Stipulation ("Stipulation") is entered into among PacifiCorp ("PacifiCorp"), Scottish Power plc ("Scottish Power") and the Consumer Advocate Staff of the Wyoming Public Service Commission ("CAS").

BACKGROUND

A. PacifiCorp is an Oregon corporation and an electric public utility in the state of Wyoming. PacifiCorp provides retail electric service in the states of California, Idaho, Oregon, Utah, Washington and Wyoming.

B. Scottish Power is public limited company in Scotland. Scottish Power provides retail electric service in the United Kingdom and, through its subsidiaries, also provides telecommunications and water and waste water services.

C. The CAS consists of employees of the Wyoming Public Service Commission ("Commission") who have been authorized by the Commission to act as a party to this proceeding. The CAS, in fulfilling its statutory mandate to promote the best interest of the citizens of the state or a broad class of citizens, appears as a party separate and distinct from the Commission in this proceeding.

D. On December 31, 1998, PacifiCorp and Scottish Power filed an Application with the Commission requesting approval of a reorganization of PacifiCorp pursuant to which PacifiCorp would merge with a subsidiary of Scottish Power. PacifiCorp would be the survivor of the merger and would become an indirect, wholly-owned subsidiary of Scottish Power.

E. PacifiCorp, Scottish Power and the CAS have met to discuss the proposed merger and resolve outstanding issues. This Stipulation constitutes the negotiated resolution of issues between PacifiCorp and Scottish Power, on the one hand, and the CAS on the other hand.

TERMS OF STIPULATION

The terms and conditions of this Stipulation are set forth below. Upon acceptance of these terms and conditions by PacifiCorp/Scottish Power, the CAS will recommend that the

Commission approve the Application in this docket as soon as possible within the procedural limits of this Docket. The CAS will include this recommendation in its prefiled direct testimony and will support its recommendation in this Docket.

1. PacifiCorp/Scottish Power agree to all commitments and conditions as included in their application in Docket No. 20000-EA-98-141 and the accompanying testimony and exhibits, except as modified in this Stipulation.

2. The capital requirements of PacifiCorp, as determined to be necessary to meet its obligation to serve the public, shall be given a high priority by the Board of Directors of the parent holding company and the utility.

3. Scottish Power acknowledges that PacifiCorp has entered into an agreement with the CAS regarding Wyoming rate filings in 1999 and 2000. Scottish Power agrees to honor that agreement. To ensure that planned cost savings resulting from the merger of Scottish Power and PacifiCorp are flowed through to Wyoming customers in a timely fashion, PacifiCorp/Scottish Power shall make an informational earnings filing in Wyoming in June 2001 (the "2001 Informational Filing") in accordance with the terms of this Stipulation. PacifiCorp/Scottish Power will have the burden of demonstrating that the 2001 Informational Filing appropriately reflects the terms of this Stipulation. The 2001 Informational Filing will include a full rate class cost of service review.

4. The 2001 Informational Filing shall include a full description, calculation (with supporting work papers) and dollar identification (both total PacifiCorp and Wyoming's share) of merger savings. This filing shall include in the adjusted revenue requirement calculation any merger savings achieved, applying established Wyoming ratemaking practices. The allocated share of merger savings shall not be less than the Wyoming allocated share of the $10 million of estimated PacifiCorp corporate savings, assuming that the closing date of the PacifiCorp/Scottish Power merger occurs in 1999. If the closing date of the PacifiCorp/Scottish Power merger does not occur in 1999, PacifiCorp/Scottish Power may make an appropriate adjustment in the $10 million of estimated PacifiCorp corporate savings to reflect the delay in the closing of the merger. In either event, if the actual amount of PacifiCorp corporate savings exceeds $10 million, the higher amount of actual savings will be used. The $10 million in PacifiCorp corporate savings will apply notwithstanding the fact that foreign exchange variations in the costs charged will fall into PacifiCorp.

5. The 2001 Informational Filing shall include a full description, calculation (including supporting work papers) and dollar identification (both total PacifiCorp and Wyoming's share) of any capital cost additions and administrative cost additions and operating cost additions, that are specifically related to actions or expenditures associated with the Scottish Power/PacifiCorp merger transition plan that are reflected in the adjusted revenue requirement calculation.

6. The 2001 Informational Filing shall include a showing that the requested cost of capital is no greater than that which PacifiCorp could have achieved on its own. Specifically, no

capital financing costs (either debt or equity) should increase by virtue of the fact that Scottish Power is a foreign operating utility operating in a competitive market with diverse holdings. An acceptable cost of equity capital study would be one developed by only including companies comparable to PacifiCorp (e.g., companies with primarily domestic operations in primarily monopoly environments).

7. The 2001 Informational Filing shall include a showing that no costs related to the approval of the merger or the establishment of the necessary corporate structure (pursuant to PUHCA) have been included in the adjusted revenue requirement, including the acquisition premium or amortization thereof. This showing shall include a description of how the merger approval costs were identified and recorded to assure their exclusion from jurisdictional rates.

8. In each rate proceeding filed with the Commission, PacifiCorp/Scottish Power shall make a showing that any additions of renewable resources to the rate base or the revenue requirement first appearing in that rate proceeding are prudent investments.

9. No later than six months after the closing date of the merger, PacifiCorp/Scottish Power will file with the Commission and the CAS the merger transition plan including anticipated time lines, actions anticipated necessary to implement the merger and the proposed benefits, the estimated associated capital and expense expenditures and anticipated workforce changes. PacifiCorp/Scottish Power will file any written modifications to the transition plan that occur within five years after the merger closing date.

10. The CAS and PacifiCorp/Scottish Power will work together to establish the baselines related to the network performance standards. If the CAS and PacifiCorp/Scottish Power fail to agree by October 1, 1999, on the appropriate baselines, all agree to abide by the Commission's decision regarding the appropriate baselines.

11. The proposed network performance standards, customer service performance standards, and customer guarantees will be reviewed after two years of experience with these standards to see if any modifications may need to be made to better maintain or improve network reliability, network safety, and customer satisfaction. In this regard, no later than July 1, 2002, PacifiCorp/Scottish Power will file with the Commission and all intervenors in this Docket a report detailing the companies' experience with the established standards and any proposed changes thereto. Pending any changes resulting from this report, the existing service standards and customer guarantees would remain in place.

12. PacifiCorp/Scottish Power agree that if PacifiCorp's network performance falls below baseline levels, PacifiCorp/Scottish Power will present a report as soon as practicable to the Commission explaining the deterioration in performance and will commit to an accelerated action plan (including required financial expenditures) to cure the deterioration in performance. In such an event, PacifiCorp/Scottish Power will carry the burden of demonstrating the prudence of their management of the system and the associated recoverability of their expenditures.

13. In addition to their network and customer service performance standards, PacifiCorp/Scottish Power agree to comply with any service standards adopted by the Commission. The CAS acknowledges, however, that the penalties associated with the PacifiCorp/Scottish Power network and customer service performance standards will not apply to any service standards adopted by the Commission. The provisions of this paragraph will not affect any penalties adopted by the Commission as part of any rules.

14. Any penalties paid by the companies as a result of failure to meet their proposed service standards in Wyoming, excluding penalties paid directly to customers, shall be paid directly to EnergyShare of Wyoming to benefit low income energy customers.

15. PacifiCorp/Scottish Power will provide an annual report to the Commission, for the five years following close of the merger, showing the reliability of the system on a statewide basis. This report shall include SAIDI data for the year. The first such report shall be filed on or before September 1, 2001.

16. For three years following the closing date of the merger, PacifiCorp/Scottish Power will report to the Commission, as soon as practicable prior to issuance, each debt or equity issuance made by PacifiCorp or Scottish Power, plc in excess of $75 million and having a term greater than one year. This report shall include the amounts, terms and conditions of the issuance, to the extent known, and the anticipated impact, if any, on the capital structure of PacifiCorp and Scottish Power.

17. Until approved by the Commission in a separate proceeding upon the filing of an application, PacifiCorp shall maintain separate debt and, if outstanding, preferred stock ratings.

18. Despite the alternative corporate structures shown in the PacifiCorp and Scottish Power proxy statements, PacifiCorp and Scottish Power shall advocate before the Securities and Exchange Commission, shareholders, and other jurisdictions, a corporate structure that contains a holding company as a parent and does not include a new separate entity to provide corporate services, as proposed in the Amended and Restated Merger Agreement. PacifiCorp and Scottish Power agree to keep the CAS informed and consult with the CAS regarding any recommendations by jurisdictional regulatory bodies to include a separate entity to provide corporate services in the post-merger corporate structure. If a change in the proposed corporate structure as reflected in the Amended and Restated Merger Agreement, including the current PacifiCorp corporate structure, (i) is mandated in merger-related proceedings by a jurisdictional regulatory body other than Wyoming or shareholders or (ii) becomes advisable in the future, PacifiCorp/Scottish Power shall so advise the Commission and the CAS in writing, within 30 days, along with the perceived or anticipated associated changes to allocations or other matters that may be required by the changed corporate structure. PacifiCorp/Scottish Power and the Commission and its Staff will support before the Securities and Exchange Commission and other appropriate regulatory authorities continuation of the PacifiCorp's state divisional operation and interjurisdictional allocation of costs.

19. No later than June 18, 1999, PacifiCorp/Scottish Power shall file with the Commission a written procedure which proposes a process for coordination and conflict resolution between and among United States and United Kingdom regulators concerning cost allocation and affiliate transaction issues. This document shall be provided to or made available to the other state jurisdictions upon its filing with the Commission. The Commission will cooperate in good faith in the resolution of cost allocation and affiliate transaction issues.

20. Any diversified holding and investments (e.g., non-utility business or foreign utilities) of Scottish Power and PacifiCorp shall be held in separate company(ies) other than PacifiCorp, the entity for utility operations. Ring fence provisions shall be provided for each of these diversified activities. This condition shall not prohibit the holding of diversified businesses and investments by affiliates of PacifiCorp, such as PacifiCorp Group Holdings Company.

21. No later than June 18, 1999, Scottish Power/PacifiCorp shall provide the CAS and other jurisdictional state rate regulators a proposed methodology for the allocation of corporate and affiliate investments, expenses, and overheads and a statement of where each of the Scottish Power principal corporate departments will sit in the corporate structure. This document would constitute a draft of what is to be filed regarding cost allocations with the Securities and Exchange Commission. No later than October 15, 1999, PacifiCorp/Scottish Power shall schedule a conference/meeting with state and other interested regulators to discuss the proposed corporate and affiliate cost allocation methodology.

22. No later than 90 days after the closing date of the merger, Scottish Power/PacifiCorp shall file its proposed corporate and affiliate cost allocation methodology with the Securities and Exchange Commission, OFFER, and OFWAT.

23. Within 30 days of receiving all state, federal, and foreign regulatory approvals of the final corporate and affiliate cost allocation methodology, a written document setting forth the final corporate and affiliate cost methodology shall be submitted to the Commission and the CAS as a compliance filing related to this merger application. On an on-going basis, the Commission shall also be notified of anticipated or mandated changes to the corporate and affiliate cost allocation methodologies.

24. Where a market for goods or services or assets exists, PacifiCorp/Scottish Power shall allow the Commission to assert the more advantageous of cost or market pricing standard for affiliate transactions for ratemaking purposes.

25. PacifiCorp/Scottish Power agree not to cross-subsidize between the regulated and non-regulated businesses or between any regulated businesses.

26. In recognition of the limited resources of the Commission, PacifiCorp/Scottish Power agree to consider in good faith any request of the Commission for PacifiCorp/Scottish Power to assume financial responsibility for the costs of an audit of cost allocations and affiliated transactions between the utility and non-regulated businesses. The Commission shall be entitled to select the auditors for any such audit. PacifiCorp/Scottish Power's share of the cost of any

such audit shall not exceed $50,000 in any 12-month period unless otherwise agreed by PacifiCorp/Scottish Power. Scottish Power will cooperate fully with such audits.

27. PacifiCorp/Scottish Power agrees to provide access to books and records (including those of the parent or affiliate companies) required to be accessed to verify or examine transactions directly affecting PacifiCorp's regulated utility operations and such books and records shall be provided at a United States location in English. PacifiCorp/Scottish Power will provide conversions to United States dollars as appropriate. Administratively, requests for such books and records made by the Commission, its staff or its authorized agents, shall be deemed presumptively valid, material and relevant. PacifiCorp/Scottish Power reserve the right to challenge any such request before the Commission and shall have the burden of demonstrating that any such request is not valid, material or relevant.

28. PacifiCorp/Scottish Power shall maintain the necessary books and records so as to provide an audit trail for all corporate or affiliate transactions that impact the PacifiCorp regulated utility operations.

29. PacifiCorp/Scottish Power shall not assert in any future Wyoming proceeding that the provisions of the Public Utility Holding Company Act of 1935 or the related Ohio Power v FERC case preempt the Commission's jurisdiction over affiliated interest transactions and will explicitly waive any such defense in those proceedings.

30. On an annual basis on or before July 1st of each year, PacifiCorp shall file an affiliate transactions report which includes the following: an organizational chart showing the parent company and all subsidiaries; a narrative description of each affiliate with which PacifiCorp does business; the revenue for each affiliated entity with which PacifiCorp does business; a report of transactions between each affiliate and PacifiCorp; and a description of any intercompany loans. Additionally, PacifiCorp/Scottish Power shall not assert in any Wyoming proceeding preemption by a United Kingdom or other foreign regulator over cost allocations or affiliate interest transactions.

31. PacifiCorp/Scottish Power shall notify the Commission subsequent to Scottish Power's board approval and as soon as practicable following any public announcement of any acquisition of a regulated or nonregulated business representing 5% or more of the market capitalization of Scottish Power, plc.

32. On an annual basis on or before July 1st, PacifiCorp shall provide the Commission with a report detailing the utility's proportionate share of the holding company's (i) total assets; (ii) total operating revenues; (iii) operating and maintenance expense; and (iv) number of employees.

33. In the event the Public Utility Holding Company of 1935 is repealed, PacifiCorp/Scottish Power shall, within 60 days of the date of the repeal, discuss with the Commission and the CAS how cost allocation and affiliate transaction commitments contained in this Stipulation need to be modified in light of that circumstance.

34. In the event that PacifiCorp/Scottish Power do not comply with the above conditions, the Commission may make appropriate ratemaking adjustments to give full effect to these conditions. The Commission may exercise its authority to make, for retail ratemaking purposes, adjustments for misallocations of costs from nonregulated business to PacifiCorp/Scottish Power.

35. Nothing in this Stipulation shall preclude the Commission from participating in related proceedings before the Federal Energy Regulatory Commission or the United States Securities and Exchange Commission.

36. PacifiCorp/Scottish Power may request confidential treatment for any information or documents filed with the Commission or the CAS, or made available to them or their agents, in compliance with these conditions. Any request for confidential treatment will be handled as provided in Section 120 of the Commission's Rules of Practice and Procedure.

GENERAL TERMS AND CONDITIONS

37. PacifiCorp, Scottish Power and the CAS agree that this Stipulation represents a compromise in the positions of the parties. As such, evidence or conduct or statements made in the negotiation and discussion phases of this Stipulation shall not be admissible as evidence in any proceeding before the Commission or a court.

38. In the event the Commission materially changes this Stipulation or imposes additional, material conditions in approving the Application, or this Stipulation is otherwise disapproved by any court of competent jurisdiction, then neither the Commission nor any party to this Stipulation shall be bound or prejudiced by the terms of this Stipulation and each party shall be entitled to file any application, testimony and tariffs it chooses, to cross-examine witnesses and in general to put on such case as it deems appropriate.

39. PacifiCorp, Scottish Power and the CAS agree that this Stipulation is in the public interest and that all of its terms and conditions are fair, just and reasonable.

40. All negotiations relating to this Stipulation are privileged and confidential, and no party shall be bound by any position asserted in the negotiations, except to the extent expressly stated in this Stipulation. Execution of this Stipulation shall not be deemed to constitute an acknowledgment by any party of the validity or invalidity of any particular method, theory or principle of regulation, and no party shall be deemed to have agreed that any principle, method or theory of regulation employed in arriving at this Stipulation is appropriate

for resolving any issue in any other proceeding. No findings of fact or conclusions of law other than those stated herein shall be deemed to be implicit in this Stipulation.

Dated: May __, 1999

CONSUMER ADVOCATE STAFF
OF THE WYOMING PUBLIC
SERVICE COMMISSION

edna Young

By ______________________
David Lucero
Attorney for Consumer Advocate Staff

PACIFICORP

By ______________________
James F. Fell
Stoel Rives LLP

By ______________________
Brent R. Kunz
Hathaway, Speight & Kunz, LLC

SCOTTISH POWER PLC

By ______________________
Paul J. Hickey
Hickey, MacKey, Evans & Walker

RICHARD T. O'BRIEN
Executive Vice President and
Chief Operating Officer

.E. Multnomah, Suite 2000
nd, Oregon 97232
813-7217
503) 813-7250

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To Ron Burrup	Date 6/3 # of pages ▶ 2
Co./Dept. Utah.	From Denise Parrish
Phone #	Co. Wy PSC
Fax # 801-530-6512	Phone #
	Fax #

PACIFICORP

Utah Division of Public Utilities
Witness: Ronald L. Burrup
Exhibit No. DPU RLB 3.4

May 20, 1999

Mr. David J. Lucero
Consumer Advocate Staff
Wyoming Public Service Commission
Hansen Bldg., Suite 300
2515 Warren Avenue
Cheyenne, WY 82002

Re: PacifiCorp Rate Filing Plan

Dear Dave:

This letter documents the agreement reached between PacifiCorp and the Consumer Advocate Staff of the Commission (the "Consumer Advocate Staff") as a result of our discussions of PacifiCorp's rate case filing plan.

1. Consumer Advocate Staff would be willing to work with PacifiCorp on an expedited process or time frame for receiving rate relief during 1999 and 2000 if the amount of the revenue requirement requested is substantially less than what PacifiCorp would ask for in fully litigated, all-encompassing rate proceedings. Specifically, the Consumer Advocate Staff would be willing to work with PacifiCorp toward the implementation of a rate plan which would provide for an initial rate change (the "1999 Application") effective no later than January 1, 2000 and a second rate change (the "2000 Rate Application") effective no sooner than 12 months after the effective date of the rate change under the 1999 Rate Application if:

   a. The 1999 Rate Application, including direct testimony, is filed no later than July 30, 1999 and preferably earlier.

   b. The proposed Wyoming annual revenue increase for the 1999 Rate Application does not exceed $12,000,000 and the proposed Wyoming annual revenue increase for the 2000 Rate Application does not exceed $8,000,000 plus the effect of any revisions to PacifiCorp's depreciation rates approved by the Wyoming Public Service Commission in Docket No. 20000-ER-98-140. The 2000 Application will include an updated analysis of PacifiCorp's earnings. Nothing in this agreement precludes PacifiCorp from demonstrating revenue requirement deficiencies greater than these amounts. The Consumer Advocate Staff reserves the right to investigate the 1999 Rate Application and the 2000 Rate Application to ensure that the requested revenue increase is justified.

c. The proposed revisions to depreciation rates are not included in the revenue requirement computations in the 1999 Rate Application.

d. Unless the Consumer Advocate Staff agrees otherwise, there is no inclusion in either the 1999 Rate Application or the 2000 Rate Application, or in any rate application PacifiCorp might file in Wyoming in 2001, of any shift in state cost allocations from the recent Utah allocation and rate cases in which the Utah Commission moved to the fully rolled-in allocation method (in other words, the Modified Accord method will be the allocation method used). The Staff of the Wyoming Public Service Commission will continue to participate in good faith in interjurisdictional allocation task force meetings to develop new cost allocations in response to the Utah Commission's move to a fully rolled-in allocation method.

e. PacifiCorp will attempt in its proposed rate design in the 1999 Application and the 2000 Rate Application to balance the proper cost of service considerations with the impact on customers. This may require that cost of service rates not be achieved in these cases, while making an attempt to move in that direction, in order to mitigate the impact on any one customer class. However, the percentage increase assigned to any customer class in either of these cases will not exceed twice the average annual increase.

2. The pending depreciation revision case (Docket No. 20000-ER-98-140) shall continue to be analyzed and considered by the Consumer Advocate Staff but on its own time line and in a way unrelated to the 1999 Rate Application. The Consumer Advocate Staff shall endeavor to complete the depreciation revision case in time for PacifiCorp's 2000 Rate Application.

If this letter accurately reflects our agreement, please date, sign and return the enclosed copy of this letter. If you have any questions, please do not hesitate to call me.

Very truly yours,

Richard T. O'Brien

Richard T. O'Brien

Agreed this 25 4th day of May, 1999.

CONSUMER ADVOCATE STAFF OF THE
WYOMING PUBLIC SERVICE COMMISSION

By David J. Lucero

David J. Lucero
Attorney for Consumer Advocate Staff

17274

Utah Division of Public Utilities
Witness: Ronald L. Burrup
Exhibit No. DPU RLB 3.5

SUMMARY OF CONDITIONS: Ronald L. Burrup

Risk that the $10 million in merger savings will not be realized in rates	**A 2001 Informational Filing shall include a full description, calculation (with supporting work papers) and dollar identification (both total PacifiCorp and Utah's share) of merger savings. This filing shall include in the adjusted revenue requirement calculation any merger savings achieved, applying established Utah ratemaking practices. The allocated share of merger savings shall not be less than the Utah allocated share of the $10 million of estimated PacifiCorp corporate savings, assuming that the closing date of the PacifiCorp/ScottishPower merger occurs in 1999. If the closing date of the PacifiCorp/ScottishPower merger does not occur in 1999, PacifiCorp/Scottish-Power may make an appropriate adjustment in the $10 million of estimated PacifiCorp corporate savings to reflect the delay in the closing of the merger. In either event, if the annual amount of PacifiCorp corporate savings exceed $10 million, the higher amount of actual savings will be used. The $10 million in PacifiCorp corporate savings will apply notwithstanding the fact that foreign exchange variations in the costs charged will fall into PacifiCorp** **No later than six months after the closing date of the merger, ScottishPower and PacifiCorp will file the merger transition plan with the Commission. The plan will include the items described in Mr. MacRichie's Oregon rebuttal testimony. The promised $10 million net reduction is permanent and guaranteed whether or not it is actually achieved.**

Risk that intra-company loans may disadvantage electric operations or that dividend payments may interfere with construction obligations.	**PacifiCorp and Scottish Power shall apply to the Commission for approval of intra-company loan agreements. For two years following the merger, PacifiCorp shall file a cash flow summary (or other evidence) with its dividend report, showing that service will not be impaired by payment of the dividend.**
Risk that asset revaluation may be used to increase property tax expense which is used in setting rates.	**Scottish Power agrees that asset revaluation resulting from the merger shall not be used as a basis to increase property taxes or other taxes or existing contract costs for the purpose of setting rates in the Utah jurisdiction.**
Risk that state regulators will not maintain their ability to adequately regulate the merged company.	**General and Financial reports to be filed with the Commission** **a) FERC form 1** **b) Annual and quarterly reports to shareholders** **c) Semi Annual reports showing Utah and total company operating results, allocation factors, coal reports, demand side management report, production costs modeling, peak loads by jurisdiction, normalizing adjustments and work papers,** **d) Monthly financial and operating reports** **e) Securities and Exchange Commission Reports 10-Q and 10K, quarterly and annual.** **f) Annual class cost of service studies** **g) Monthly Energy Information Administration Form EIA-826** **h) Annual affiliated interest report** **i) Five year financial plan and forecast of financial condition, filed annually for the total company and PacifiCorp.**

17268

-BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH-

IN THE MATTER OF THE APPLICATION OF	)DOCKET NO. 98-2035-04
PACIFICORP AND SCOTTISH POWER PLC	)UTAH DIVISION OF PUBLIC UTILITIES
FOR AN ORDER APPROVING THE	)EXHIBIT NO. DPU 2.0
ISSUANCE OF PACIFICORP COMMON STOCK)	

DIRECT TESTIMONY OF MARY H. CLEVELAND

FOR THE

DIVISION OF PUBLIC UTILITIES

DEPARTMENT OF COMMERCE

STATE OF UTAH

June 18, 1999

I. QUALIFICATIONS

Q. PLEASE STATE YOUR NAME FOR THE RECORD.

A. Mary H. Cleveland.

Q. BY WHOM ARE YOU EMPLOYED AND WHAT IS YOUR BUSINESS ADDRESS?

A. I am employed by the Utah Department of Commerce, Division of Public Utilities (Division). My business address is 160 East 300 South, Suite 400, Salt Lake City, Utah, 84114.

Q. WHAT IS YOUR POSITION?

A. Utility Regulatory Analyst.

Q. BRIEFLY DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL BACKGROUND.

A. I hold a Bachelor of Business Administration, as well as a Master of Business Administration, from the University of Missouri-Kansas City. In addition I have regularly attended the National Association of Regulatory Utility Commissioners (NARUC) Staff Subcommittee on Accounts meetings and have served on the NARUC Securities and Exchange Commission (SEC) Subcommittee. I have participated extensively in PacifiCorp's

Integrated Resource Planning process. I also participated in the IndeGO Pricing Work Group and served as a non-member representative on the IndeGO Steering Committee.

I have approximately eighteen years of utility regulatory experience, both as a consultant and as an employee of state regulatory agencies. I have participated in regulatory proceedings in the states of Alaska, Arizona, Connecticut, Kansas, Missouri, New Mexico, Ohio, Utah and Wisconsin. I have also testified before the Kansas Supreme Court.

I am a licensed Certified Public Accountant in the state of Kansas and I am a member of the Institute of Certified Public Accountants. Further details regarding my background are provided in Exhibit No. DPU 2.1.

II. PURPOSE OF TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. My testimony will address the following areas as they relate to the proposed transaction between ScottishPower and PacifiCorp (Applicants): 1) corporate cost allocations; 2) affiliate transactions; and 3) access to books and records. For each of these areas I shall discuss issues and/or concerns arising from the proposed transaction which could potentially impact the Division's ability to carry out its statutory responsibilities with respect to the regulation of PacifiCorp and recommend conditions which the Division believes will serve to mitigate those issues and concerns.

Q. IN GENERAL WHAT IS THE OVERALL RISK YOU ARE ATTEMPTING TO MITIGATE?

A. In a recent joint paper, "Regulatory Issues Associated with Multi-Utilities" (May 1998), by the Directors General of Electricity Supply, Gas Supply, Telecommunications and Water Services; the Director General of Electricity Supply (Northern Ireland) and the Director General of Gas (Northern Ireland), the concerns which arose in connection with the proposed PacifiCorp acquisition of Eastern Electricity (The Energy Group) were summarized:

> "In competitive markets, if a company runs into financial difficulties, the customers can move elsewhere. But customers of monopoly utilities have no such facility. Regulators need, therefor, to be satisfied that monopoly utility license holders have the appropriated financial and managerial resources to finance their activities and meet their license and statutory obligations. Where the monopoly utility is part of a larger group, whether or not a multi-utility, there is a risk that decisions will not be taken solely in the interests of the regulated company and its customers, but will be influenced by the wider ambitions of the group. There is a risk that a licensee will be denied the resources to meet its obligations."

The question before the Monopolies and Mergers Commission in this instance was whether the existing license requirements, taken together with the existing powers of the regulator, were sufficient to meet these concerns. The tables have now turned with PacifiCorp becoming acquired, but the question remains the same. As regulators we need to impose requirements on this new entity to ensure that we have sufficient powers to protect the public interest.

Q. HOW DID YOU IDENTIFY THE ISSUES AND CONCERNS YOU ARE ABOUT TO ADDRESS?

A. I reviewed the application filed by PacifiCorp and ScottishPower filed on December 31, 1998, as well as the supporting testimonies subsequently filed on February 26, 1999. I issued a series of data requests seeking information about ScottishPower as well as the transaction and reviewed data requests issued by other parties to this proceeding. I reviewed ScottishPower's annual reports, filings before the Securities and Exchange Commission (SEC) as well as other publicly available data. I might add that we were generally precluded from reviewing ScottishPower's future budgetary information and plans as they were considered to be highly sensitive and proprietary.

Additionally, I gained a knowledge of the regulatory environment in which ScottishPower operates by reviewing consultation papers published by the United Kingdom (U.K.) regulator, the Office of Electricity Regulation (OFFER). I also examined filings made by ScottishPower before OFFER.

III. CORPORATE STRUCTURE / COST ALLOCATIONS

Q. DOES CORPORATE STRUCTURE PLAY AN IMPORTANT ROLE IN THE ALLOCATION PROCESS?

A. Yes, the corporate structure will determine to a large degree how individual members of the corporate group interrelate with each other and the extent to which they transact business among themselves. As such it will influence the number of entities within the group who's costs are allocated among other members of the group as well as the extent and complexity of affiliate transactions.

Q. WHAT CORPORATE STRUCTURE IS PROPOSED FOR THE MERGED COMPANIES?

A. The proposed corporate structure for the merged companies has been and continues to be a moving target. To date, to the best of my knowledge, there have been three proposed corporate structures. Originally, as filed pursuant to the Agreement and Plan of Merger entered into by ScottishPower plc, NA General Partnership, and PacifiCorp, dated December 6, 1998 (Merger Agreement), PacifiCorp was to have been a subsidiary of ScottishPower along with Manweb, Scottish Telecom and Southern Water. However, to address concerns of the U.K. Director General of Electricity Supply (DGES), ScottishPower agreed to establish a holding company for the ScottishPower group. The establishment of the holding company is reflected in the Amended and Restated Agreement and Plan of Merger entered into by New ScottishPower plc, ScottishPower plc, NA General Partnership, and PacifiCorp, dated February 23, 1999 (Amended Merger Agreement). Under the Amended Merger Agreement, PacifiCorp would be a subsidiary of the holding company. The Amended Merger Agreement also established a Service Company. Subsequently on May 14, 1999, yet another proposed corporate structure was provided to the Wyoming Consumer Advocate

Staff, as part of a letter of commitment by ScottishPower, plc witness Robert Green. Under this proposal there would be two holding companies, a United States registered holding company; as well as the U.K. holding company. According to ScottishPower plc witness Robert Green a United States registered holding company would facilitate further acquisitions by ScottishPower plc in the United States (Response to CAS interrogatory 7.204).

As proposed the merger will create a registered holding company. Thus, ultimately the Security and Exchange Commission (SEC) will approve a corporate structure under the Public Utilities Holding Company Act of 1935 (PUHCA). However, ScottishPower has taken the position that the merger does not have to be approved by the SEC under PUHCA. Following completion of the merger, however, ScottishPower plans to register as a holding company as required under Section 5 of the PUHCA. PUHCA requirements are addressed by Division witness Artie Powell

Therefore, the final corporate structure is unknown at this time. This is a significant issue since, as I mentioned previously, the corporate structure can impact the number of corporate allocations. The more complex the corporate allocations, the more difficult it may become to maintain an audit trail regarding those allocations.

Q. HAS SCOTTISHPOWER PROPOSED A METHODOLOGY FOR ALLOCATING CORPORATE COSTS?

A. No. Originally ScottishPower committed to provide an analysis of its proposed allocation of corporate costs within three months of the completion of the transaction (Direct Testimony of Robert D. Green, February 26, 1999, page 10, lines 1 - 2). However, ScottishPower has now committed to file a draft proposed cost allocation methodology no later than June 18, 1999. This commitment is contained in Term 21 of the proposed Stipulation among PacifiCorp ("PacifiCorp"), ScottishPower plc (ScottishPower) and the Consumer Advocate Staff of the Wyoming Public Service Commission (CAS), which reads as follows:

> "No later than June 18, 1999, ScottishPower/PacifiCorp shall provide the CAS and other jurisdictional state rate regulators a proposed methodology for the allocation of corporate and affiliate investments, expenses, and overheads and a statement of where each of the ScottishPower principal corporate departments will sit in the corporate structure. This document would constitute a draft of what is to be filed regarding cost allocations with the Securities and Exchange Commission. No later than October 15, 1999, PacifiCorp/Scottish Power shall schedule a conference/meeting with state and other interested regulators to discuss the proposed corporate and affiliate cost allocation methodology"

ScottishPower has verbally made a similar commitment to the Division.

Q. HOW DOES SCOTTISHPOWER CURRENTLY ALLOCATE CORPORATE COSTS TO ITS SUBSIDIARIES?

A. In response to a data request ScottishPower stated that it currently allocates costs to its subsidiaries by applying a range of allocation bases that include assessment of workload, usage statistics and net assets (Response to DPU interrogatory S1.6). In subsequent conversations with ScottishPower it was implied that net assets were used to allocate corporate overheads which were not attributable on a usage basis, although this may have only applied to Southern Water which is regulated by the Office of Water Services (OFWAT).

Subsequently, in reviewing a recent OFFER Consultation Paper, "Review of Public Electricity Suppliers 1996 - 2000: Distribution Price Control Review" (May 1999), I became aware of an accounting guideline known as CSC 194, introduced before privatization, that sets out guidance on cost allocations. Per CSC 194, corporate overheads which by their nature are not assignable on a usage basis should be assigned on salaries and net assets, **measured on a current cost basis.** I have placed emphasis "on a current cost basis" since PacifiCorp's net assets are measured on a historical cost basis for regulatory purposes.

However, in its May 1999 Consultation Paper, OFFER, noting that the application of CSC 194 results in approximately 90% of corporate overheads being assigned to the Distribution function and questioning whether this is a reasonable reflection of the usage of corporate assets and staff, has proposed a new methodology for allocating corporate overheads. The proposed methodology would allocate corporate overheads based on four measures: 1) turnover (e.g. revenues); 2)historic cost operating profit; 3) employee numbers; and 4) historic cost net assets; giving equal weight to each. Comments on this proposal are due to OFFER by July 2, 1999. So, as is the corporate structure a moving target, the methodology for allocating corporate overheads employed by the U.K. regulator has likewise become a moving target.

This is problematic since PacifiCorp will reallocate to its subsidiaries corporate overheads allocated from ScottishPower. PacifiCorp currently allocates corporate overheads on the basis of three factors: 1) operating expenses, 2) number of employees and 3) historic cost net assets; giving equal weight to each. PacifiCorp's allocation methodology differs significantly from OFFER's current methodology and in some respect from OFFER's newly proposed methodology. The use of two different allocation methodologies will result in the allocation by PacifiCorp to it subsidiaries differing amounts of ScottishPower's corporate overheads than ScottishPower's allocation methodology actually attributed to the PacifiCorp subsidiaries.

Q. DO YOU KNOW WHEN OFFER WILL DECIDE ON THE ALLOCATION METHODOLOGY?

A. Not precisely, however, since the Distribution rates to which the proposed allocation methodology applies are scheduled to go into effect in April 2000, I would suspect that a decision would be made prior to April 2000. I would also suspect that ScottishPower may have a vested interest in having the same cost allocation methodology adopted by both OFFER and the U.S. regulators. Therefore, I would not be surprised if the proposed cost allocation that ScottishPower has committed to file on June 18, 1999, is similar to that proposed by OFFER.

Q. SHOULD THE UTAH COMMISSION APPROVE A COST ALLOCATION METHODOLOGY IN THIS PROCEEDING?

A. No, to do so at this time would premature. At this time the corporate structure, which can impact the number of and complexity of cost allocations, is unknown. The Division has not had an opportunity to examine the corporate costs which ScottishPower currently allocates to its subsidiaries, nor will we have access to ScottishPower's books and records until the merger is consummated. Furthermore, the establishment of a cost allocation methodology is only necessary when and if the merger is consummated. Currently the proposed transaction is in the approval process. However, the Utah Commission should require ScottishPower/PacifiCorp to file a proposed cost allocation methodology for its approval within 30 days following completion of the merger.

Although the establishment of a cost allocation methodology is a moot issue at this time, the principles governing any cost allocation methodology are not. These principles should constitute a merger condition.

Q. WHAT ARE THE PRINCIPLES?

A. The Utah Commission should require that a benefit to PacifiCorp be shown for any costs allocated to it from ScottishPower.

Cost allocations should be based on generally accepted accounting standards, that is, that in general, direct costs should be charged to specific PacifiCorp subsidiaries wherever possible and shared or indirect costs should be allocated based upon the primary cost-driving factors.

Corporate executives' costs are the most difficult to allocate fairly since they do not routinely provide the same services on a consistent basis. Therefore, the Utah Commission should require timekeeping and project management systems adequate to support the allocation of such costs. This condition was ordered by the Utah Commission in the Utah Power & Light and PacifiCorp merger, Docket No. 87-035-27.

An audit trail should be maintained such that all costs allocated can be specifically identified along with their origination and adequately supported. Failure to adequately support any allocated cost may result in denial of its recovery in rates.

Costs which would have been denied recovery in rates had they been incurred by PacifiCorp regulated electric operations should likewise be denied recovery whether they are allocated directly or indirectly through subsidiaries in the ScottishPower group. This is consistent with the Utah Commission's order in Mountain Fuel Supply (Docket No. 93-057-01):

> "We find that donations, dues, lobbying expenses and political contributions that are disallowed for cost recovery when funded directly by Mountain Fuel are not recoverable when included in affiliate charges."

Finally, any corporate cost allocation methodology and subsequent changes thereto must be approved by the Utah Commission. ScottishPower will assume the risk for the Utah Commission approval and adoption of cost allocation methodologies which differ from those adopted by OFFER or any other U.S. regulatory jurisdiction. A similar condition was ordered by the Utah Commission in the Utah Power & Light and PacifiCorp merger, Docket No. 87-035-27.

Q. DOES SCOTTISHPOWER CURRENTLY HAVE IN PLACE TIME REPORTING OR PROJECT MANAGEMENT SYSTEMS ADEQUATE TO SUPPORT THE ALLOCATION OF EXECUTIVES' COSTS?

A. No. ScottishPower classifies these costs as corporate overhead and allocates them along with all other corporate overhead costs (Response to DPU interrogative S7.17)

Q. HOW DOES PACIFICORP CURRENTLY TRACK EXECUTIVES' TIME?

A. Each executive completes a profile designating the percentage of time he or she expects to spend on various projects. These percentages are then used to allocate the executive's cost to those projects. Executives do not fill out time sheets. Profiles are updated annually, as new projects are added, or when the percentage of time an executive spends on certain projects significantly changes.

The Division has examined these executive profiles by reference to the executive's expense accounts and travel itineraries. The Oregon staff performed a detail audit of executives' time by examining appointment calendars etc.

Q. SCOTTISHPOWER HAS COMMITTED TO A NET $10 MILLION REDUCTION IN CORPORATE COSTS THREE YEARS SUBSEQUENT TO THE COMPLETION OF THE MERGER. WHAT IS THE BASIS FOR THIS REDUCTION?

A. The net $10 million reduction assumes a $15 million savings being achieved in PacifiCorp's corporate costs due to the elimination of duplicate functions arising as a result of the merger and a $5 million increase in Scottish Power's corporate costs recognizing there will be some increase to the remaining function after duplication has been eliminated. This was based on a high level analysis of various corporate functions. No detail analysis of where the savings will actually be achieved has been made. Such an analysis will be done as part of the transition plan.

Q. WHAT IS THE BASE FROM WHICH SCOTTISHPOWER PROPOSES THE $10 MILLION SAVINGS IS TO BE MEASURED?

A. Per ScottishPower, the base from which the corporate duplication savings will be deducted is the 1999 actual regulated corporate costs (Response to Division interrogatory S14.15).

Q. DOES THE DIVISION FIND THIS BASE TO BE ACCEPTABLE?

A. No. Not all actual costs charged to regulated operations are allowed for ratemaking purposes. Examples would include the executive Long Term Incentive Plan (LTIP); any incentive compensation based on the achievement of financial goals; the totality of extraordinary expenses, some of which would be deferred and amortized over a number of years. Thus, using a base of 1999 actual charges from which to measure the net $10 million savings does not guarantee that such savings will be recognized by ratepayers. To the extent reductions were achieved in costs not allowed for ratemaking, stockholders would benefit, not ratepayers. The use of actual costs charged to regulated operations as a base for measuring the achievement of the $10 million guaranteed savings does not translate into a corresponding benefit for ratepayers.

Q. FROM WHAT BASE SHOULD THE $10 MILLION SAVING BE MEASURED?

A. The achievement of the $10 million guaranteed savings should be measured from PacifiCorp's 1999 actual corporate costs, normalized and adjusted so as to reflect only those costs that would be included in rates. Any costs related to the ScottishPower merger should also be excluded. Absent the merger these costs would not have been incurred. Therefore they are not reflective of PacifiCorp's corporate operating costs prior to the merger. The inclusion of merger related costs will increase the base from which the savings are measured and since they are non-reoccurring will increase the savings reported. Reported merger savings should only be attributable to increased efficiencies. Additionally, ScottishPower witness Robert D. Green has testified that "the $10 million in annual savings to which we are committed will not be affected by currency exchange risk". (Rebuttal Testimony of Robert D. Green, Before the Public Utility Commission of Oregon, June 2, 1999, pg. 4). The Division likewise concurs, that currency exchange risk should not enter into the calculation of the guaranteed $10 million annual savings.

Q. HASN'T PACIFICORP RECORDED ALL MERGER RELATED COSTS BELOW THE LINE?

Q. No, PacifiCorp only committed to record "transaction" costs below the line. There are several categories of personnel costs, which although related to and would not be incurred absent the merger, are not considered to be"transaction"costs by PacifiCorp. These include costs associated with: 1) the PacifiCorp Executive Severance Plan (the Executive Plan); 2) payments to directors; 3) retention and bonus incentives and 4) the recognition pool.

The Executive Severance Plan provides for the payment of enhanced severance benefits if, during the 24-month protection period following the completion of the merger, a participant (A) is terminated by PacifiCorp "without cause" or (B) resigns within two months after a "material alteration in position". A "material alteration in position" means the occurrence of any of the following: (1) a change in reporting relationship to a lower level; (2) a material reduction in the scope of duties and responsibilities; (3) a material reduction in authority; (4) a material reduction in compensation; or (5) relocation of the participant's work location to an office more than 100 miles from the participant's office or more than 60 miles from the participant's home. Mr. O'Brien is eligible for enhanced severance benefits if he resigns for any reason no earlier than 12 month and no later than 14 months after the merger.

Executives who qualify for enhanced payment of severance benefits under the Executive Plan will receive:

(A) severance pay in an amount equal to two and one-half times (three times for Mr. O'Brien) the Executive's "annual cash compensation";

(B) an additional payment to compensate the Executive for the effect of any excise tax if change-in-control benefit payments would result in the imposition of such excise tax under section 4999 of the Internal Revenue Code;

(C) continuation of subsidized health insurance for the Executive, spouse and qualified dependants from 6 to 24 months depending on length of service; and

(D) a minimum of 12 months of executive officer outplacement services.

There are 27 executives covered by the Executive Plan. It is our understanding that the potential maximum cost for severance pay alone is approximately $17 million.

Included among the executives covered by the Executive Plan are Messrs. O'Brien, Steinberg, Bohling and Topham. The estimated amount of change in control severance benefit for each of these executives (calculated based on compensation as of March 1, 1999 and without regard to any additional payment to compensate for the effect of any excise tax) are as follows: Mr. O'Brien - $1,832,400; Mr. Steinberg - $1,199,500; Mr. Bohling - $1,129,500 and Mr. Topham - $1,129,500 (Scottish Power Circular to Shareholders, p.96).

Promptly following completion of the merger each non-executive director on PacifiCorp's Board will receive a special payment of $50,000 in recognition of his or her years of service and contributions. The decision to make these payments was made after the Merger Agreement was executed.

Additionally, a very small number of employees have retention agreements that payout if they are employed on the date the merger is consummated. Even if the merger is not consummated these employees will receive one-half of the payout. This program could cost up to $7 million.

In addition PacifiCorp has established an employee recognition pool in the amount of $8.5 million. Payments made to employees from the recognition pool may be merger related. To date $2.9 million has been awarded from the recognition pool. The $2.9 million was recorded on PacifiCorp's books in 1998.

Q. ARE THERE ANY OTHER COSTS RELATED TO THE MERGER WHICH WILL BE INCURRED BY PACIFICORP?

A. Yes. The ScottishPower Circular to Shareholders identifies two additional costs to be bourn by PacifiCorp: 1) the stamp duty reserve tax and 2) special cash payments to PacifiCorp Preferred Shareholders.

PacifiCorp's obligation with respect to the stamp duty tax is described on page 10 of the ScottishPower Circular to Shareholders:

> "Stamp duty reserve tax of an amount equal to 1.5% of the issue price of New Shares issued in the Merger in the form of New ADSs will be payable. Based on the market price for the ScottishPower Shares on 27 April 1999 (being the latest practicable date prior to the publication of this document), and on the assumption that all New Shares issued in the Merger are issued in the form of New ADSs, stamp duty reserve tax of approximately £54.64 million would be payable. Any such tax will be paid by PacifiCorp."

Special cash payments are to be made to PacifiCorp Preferred Shareholders for voting in favor of the Merger as well as in favor of increasing the amount of unsecured indebtedness which PacifiCorp may issue. Per the ScottishPower Shareholders Circular:

> "If the Merger is approved at the PacifiCorp annual meeting and all regulatory approvals for the Merger required under the Merger Agreement have been obtained. PacifiCorp will make a special cash payment of $1.00 per share ($.025 per share for the $1.16, $1.18 and $1.28 series) to each PacifiCorp Preferred Shareholder on the PacifiCorp Record Date that voted in favour of the Merger. These

> special cash payments will be paid out of PacifiCorp's general funds, promptly after receipt of the last regulatory approval for the Merger but prior to the Merger . . .
>
> Under the articles of incorporation of PacifiCorp, the amount of unsecured debt that PacifiCorp may issue is limited to 30%, of the total secured indebtedness of PacifiCorp, its capital and surplus. PacifiCorp is seeking consent of the PacifiCorp Preferred Shareholders to increase the amount of unsecured indebtedness which PacifiCorp may issue from time to time. PacifiCorp believes that the unsecured debt consent is key to meeting the objectives of flexibility and favourable cost structure and therefore if the unsecured debt consent is approved, PacifiCorp will make a special cash payment in the amount of $1.00 per share ($.025 per share for $1.16, $1.18 and $1.28 series) to each PacifiCorp Preferred Shareholder on the PacifiCorp Record Date that voted in favour of the unsecured debt consent. If the unsecured debt consent is approved, special cash payments will be paid out of PacifiCorp's general funds, promptly after the PacifiCorp annual meeting. . .
>
> The special cash payments referred to above, in aggregate, would not exceed approximately $5 million.
>
> In addition, certain dealer solicitation fees will be payable by PacifiCorp in relation to the resolutions referred to above which, in aggregate, would not exceed $4 million."

Additionally based on the proposed transaction's structure approximately $268.2 million of PacifiCorp's credit facilities supporting tax exempt debt issuances will be in default requiring PacifiCorp to refinance. ScottishPower believes that $45 million could be "easily amended" prior to closing, thereby reducing PacifiCorp's refinancing requirements.

Q. IS IT THE DIVISION'S POSITION THAT THESE OTHER MERGER COSTS SHOULD BE RECORDED BELOW THE LINE?

A. Yes. But for the merger, PacifiCorp would not have incurred these costs. PacifiCorp has indicated that the employee recognition pool may be an exception, but it was established by PacifiCorp's Board in conjunction with the Board's decision to proceed with the ScottishPower transaction and therefore at the onset appears to be merger related. The Division plans to examine the employee recognition pool further in conjunction with its audit of PacifiCorp's 1998 results of operations with particular emphasis on the $2.9 million employee recognition expenditure included in the 1998 results. The Division considers all of the other costs to be merger related.

As testified to by Division witness Artie Powell, stockholders are receiving the "premium". Therefore, stockholders should bear the associated merger costs. As a conditional of this merger, all merger related costs should be recorded below the line.

Q. DO YOU HAVE ANY CONCERNS REGARDING THE PROPOSED CORPORATE STRUCTURE?

A. Yes, the most recently proposed corporate structure would create a U.S. registered holding company to facilitate further acquisitions by ScottishPower in the United States. This potential diversification creates more risk.

Utility ratepayers have no choice but to take service from the monopoly utility. The

Division believes ratepayers should not be compelled to be partners in an enterprise over which they have no control. Subsidiary activities and operations should be as far removed as possible from the regulated utility enterprise and sufficient safeguards and controls put in place to assure that ratepayers do not inadvertently bear any risks associated with diversification. Therefore, any diversified holdings and investments (e.g., non-utility business or foreign utilities) of ScottishPower and PacifiCorp should not be held by PacifiCorp, the entity for utility operations.

Additionally, ScottishPower/PacifiCorp should be required to notify the Utah Commission subsequent to ScottishPower plc's Board approval and as soon as practicable following any public announcement of and acquisition of a regulated or non-regulated business representing 5% or more of the market capitalization of ScottishPower plc.

IV. AFFILIATE TRANSACTIONS

Q. HOW WILL THE PROPOSED CORPORATE STRUCTURE AFFECT THE COMMISSION'S ABILITY TO REGULATE AFFILIATED TRANSACTIONS?

A. Subsequent to the merger, contracts for goods and services among affiliated companies as well as the allocation of common overhead costs will be governed under PUHCA. The SEC, under PUHCA has a standard of pricing affiliated transactions "at cost". There is some question as to whether the SEC, under PUHCA, would have the authority to pre-empt state regulatory authority over the pricing of affiliated transactions in a registered holding company system. In Ohio Power Co. v. FERC, 954 F.2d 779 (D.C. Cir.), cert. denied, 113 S. Ct. 483 (1992) (Ohio Power), the court asserted precedence of the SEC's "at cost" rules over the Federal Energy Regulatory Commission's (FERC) use of lower of cost or market pricing for coal received by a utility subsidiary from its affiliated coal company. The utility subsidiary was forced to pay for the coal "at cost", which was 30% over market coal prices. Although this case has never been tested, it raises the issue as to whether the SEC's "at cost" standard can prevent state regulators from exercising authority over the pricing of affiliate transactions in a registered holding company system. Therefore, as a condition of this merger, ScottishPower/PacifiCorp should not assert in any future Utah proceeding that the provisions of the Public Utility Holding Company Act of 1935 or the related Ohio Power v FERC case preempt the Utah Public Service Commission's jurisdiction over affiliated interest transactions and will explicitly waive any such defense in those proceedings.

Q. WHAT OTHER ISSUES ARE RAISED BY AFFILIATE TRANSACTIONS?

A. Affiliate transactions have the potential to result in cross-subsidization of affiliates by the regulated utility. In the U.S., PUHCA prevents affiliates from charging prices above "cost" to other entities within the registered holding company's group, however, there may be instances where the "cost" of an affiliate good or service exceeds what the utility would pay in the market for the same good or service. In these instances the utility's payment of "cost" would result in a subsidy to the affiliate. To prevent the potential for cross-subsidization all goods and services provided either directly or indirectly by affiliates within the ScottishPower group should be priced at the lower of cost or market, where cost may include a return on investment no greater than the most recently authorized utility rate of return. The Utah Commission has made its policy in this area quite clear:

> "Our policy, stated in our Order in the prior rate case, 89-057-15, and elsewhere, is that affiliate billings should not include a rate of return greater than we authorize for the utility. Otherwise, transactions with affiliates would be a means of increasing return beyond that allowed, and ratepayers, other things being equal, would pay more for utility service than we have found just and reasonable. We have consistently ordered revisions where necessary to reduce the rate of return component of affiliate billings to that authorized for the utility." (Order in Docket No. 93-057-01, pgs. 69-70).

It is unclear whether conditions similar to the PUHCA "cost" restriction or the lower of cost or market criteria apply equally in the U.K. to services provided members of the wider group of companies of which the utility is a part. OFFER's May 1999 Consultation Paper states:

> "Certain PESs have structured themselves in such a way that services used by the distribution business are provided outside the distribution business but within the wider group of companies of which distribution is a part. Examples of this include the provision of transport fleets and non-operational property. Typically, the charge for the provision of the service includes an element of profit. Many of the businesses making recharges have little or no trade outside the group. An effect of this appears to be an increase in distribution

> business costs and the transfer of profits from the regulated business to elsewhere in the group. OFFER's consultants are removing the margins from recharges from other companies in the group, except where those companies presently carry out a significant element of their trade externally to the group, presently assumed to be 50 per cent or more."

Thus, it would appear as if in the U.K. services received from affiliates who provide at least 50% of their trade externally to the group are not necessarily priced at the lower of cost or market, or even at "cost" for that matter.

This could be problematic, particularly if these affiliates provide services at the corporate level, the costs of which are reallocated to ScottishPower subsidiaries. It may even violate the requirements of PUHCA. Perhaps this is why there has been much debate as to whether PUHCA requirements would extend to ScottishPower's U.K. subsidiaries.

Q. DOES PACIFICORP HAVE A POLICY REGARDING THE PRICING OF GOODS AND SERVICES PROVIDED BY THE UTILITY TO ITS SUBSIDIARIES AND AFFILIATES?

A. Yes, as a condition of the Utah Power / PacifiCorp merger, PacifiCorp was required to file for Commission approval a Transfer Pricing Policy. The Transfer Pricing Policy as approved by the Utah Commission is attached as DPU Exhibit 2.2. Under this policy goods and services provided by the utility are to be priced at a rate which covers all associated costs, including a return on investment no greater than the most recently authorized utility rate of return. This condition should also apply to ScottishPower.

Q. DOES PACIFICORP HAVE A POLICY REGARDING THE TRANSFER OF ASSETS AMONG AFFILIATES?

A. Yes. Utility assets transferred to affiliates are priced at the greater of fair market value or net depreciated book value. Assets acquired by Electric Operations from affiliated companies are transferred at the lesser of fair market value or the net depreciated book value. This policy was established in PacifiCorp's Transfer Pricing Policy as a condition of the Utah Power / PacifiCorp merger. This condition should also apply to ScottishPower.

Q. DO YOU HAVE ANY INDICATION THAT SCOTTISHPOWER INTENDS TO DIVEST ANY OF PACIFICORP'S UTILITY ACTIVITIES OR FUNCTIONS?

A. ScottishPower has no current plans to divest any of PacifiCorp's utility activities or functions. However, this does not mean that divestiture of utility activities or functions will never occur. In its prepared response to the Department of Trade & Industry (DTI) on the future of gas and electric operations, ScottishPower stated:

> "... greater unbundling of transmission and distribution activities, such as metering and connections, ... is welcome. This will enable the more efficient players to succeed and, in so doing, deliver lower prices and improved services to consumers ... the regulator should encourage the development of separate competitive business serving the regulated core monopolies at market rates." (Response to the DTI Consultation Paper on the Future of Gas and Electric Regulation,

Nov. 16, 1998, pg. 3)

After its hostile take-over of Manweb, ScottishPower transferred Manweb's second-tier (e.g. wholesale) sales to ScottishPower. Suppose a similar decision was made, transferring PacifiCorp's wholesale sales function to its non-regulated subsidiary PacifiCorp Power Marketing (PPM). Restrictions are necessary to assure that integral functions are not reorganized into independent profit centers for the benefit of stockholders at the possible detriment of ratepayers.

Q. WHAT CONDITIONS SHOULD THE COMMISSION IMPOSE TO ASSURE THAT RATEPAYERS ARE NOT HARMED BY DIVESTITURE OF INTEGRAL UTILITY FUNCTIONS?

A. The Applicants should be required to provide notification of and file for Commission approval of the divestiture, spin-off, or sale of any integral utility assets or functions. My legal counsel, Michael Ginsberg, has advised me that legal precedent for this requirement was established by the Wexpro decision.

Q. SHOULD ANY OTHER CONDITIONS BE PLACED ON AFFILIATED TRANSACTIONS?

A. Yes. The following conditions were implemented in the PacifiCorp / Utah Power merger and should apply equally to the ScottishPower transaction.

A. The Merged Company shall notify the Commission, and provide sufficient information and documentation to the Commission, prior to the implementation of plans (1) to form an affiliate entity for the purpose of transacting business with the electric divisions of PacifiCorp, (2) to commence new business transactions between an existing affiliate and the electric utility divisions of PacifiCorp, (3) to dissolve an affiliate which has transacted any substantial business with such divisions, (4) to enter into new business ventures or expand existing ones, or (5) to merge combine, transfer stock or assets of any part or all of the Merged Company.

B. ScottishPower shall file an annual affiliated interest report.

C. The Merged Company shall provide notification of all asset transfers to or from PacifiCorp, its affiliates, or subsidiaries in accordance with current PSC rules (see in particular PSC R746-401).

V. ACCESS TO BOOKS AND RECORDS

B. WHAT CONCERNS DOES THE DIVISION HAVE REGARDING ACCESS TO RELEVANT DOCUMENTS AND RESPONSIBLE INDIVIDUALS?

A. ScottishPower witness Robert D. Green stated in his testimony, that "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." However, ScottishPower has not stated to what extent the Utah Commission and Division will have access to relevant materials in the possession of the holding company(s), their subsidiaries, or to officers and employees.

PacifiCorp's corporate functions reside in the operating company. Thus, all corporate costs are readily available for our review and examination, as these costs are recorded as part of electric operations and allocated out to PacifiCorp's subsidiaries. Additionally we are able to interview corporate officers and employees regarding corporate expenditures and allocations as needed. The proposed merger will necessitate the need to audit transactions between PacifiCorp and its parent company, ScottishPower; and possibly subsidiaries of ScottishPower. Not only will this involve the examination of an additional set(s) of books and records, but books and records which are located outside of the U.S. and are not recorded according to U.S. Generally Accepted Accounting Principles (GAAP).

Additionally, we have become cognizant of documents which we routinely examine in our reviews of PacifiCorp, that will not be readily made available in the U.K. For example, the outside auditors workpapers in the U.K. are not made available. Thus, it will be necessary to establish agreed upon procedures by which Division staff can have access to documentation supporting the purpose and/or circumstances attributable to costs charged to PacifiCorp.

Q. WHAT CONDITIONS DO YOU RECOMMEND TO ADDRESS THE ISSUE OF ACCESS TO BOOKS AND RECORDS?

A. Consistent with the Utah Commission's order In the Matter of the Investigation of the Creation of a Holding Company (Questar) by Mountain Fuel Supply Company (Docket No. 84-057-10), the holding company(s) and subsidiaries' employees, officials, directors, or agents shall be available to testify before the Utah Commission to provide information relevant to matters within the jurisdiction of the Utah Commission.

The Utah Commission should establish procedures by which the Public Service Commission and Division staffs, or their authorized agents can obtain needed access to subsidiary books and records, other relevant documents, data and records. Failure to provide adequate supporting documentation of costs may result in those costs being denied rate recovery. Requests by the Utah Commission, the Division, or their authorized agents shall be deemed presumptively valid, material and relevant, with the burden falling to ScottishPower/PacifiCorp to prove otherwise. ScottishPower/PacifiCorp shall reserve the right to challenge any such request before the Utah Commission and shall have the burden of demonstrating that any such request is not valid, material or relevant. In addition, ScottishPower shall pay for the expense incurred by Utah regulatory personnel in accessing corporate records and personnel located outside of the state of Utah.

VII. SUMMARY OF CONDITIONS

Q. WOULD YOU PLEASE PROVIDE A SUMMARY OF THE MERGER CONDITIONS YOU ARE PROPOSING.

Q. The merger conditions I am proposing are:

1) Within 30 days of the completion of the merger ScottishPower/PacifiCorp shall file a proposed cost allocation methodology with the Utah Public Service Commission for its approval.

2) Cost allocation methodologies shall comply with the following principles:

   a) For all costs allocated to PacifiCorp from the ScottishPower group, ScottishPower must demonstrate a benefit to PacifiCorp.

   b) Cost allocations should be based on generally accepted accounting standards, that is, that in general, direct costs should be charged to specific PacifiCorp subsidiaries wherever possible and shared or indirect costs should be allocated based upon the primary cost-driving factors.

   c) ScottishPower should have in place timekeeping and project management systems adequate to support the allocation of executives' costs.

d) An audit trail be maintained such that all costs allocated can be specifically identified along with their origination and adequately supported. Failure to adequately support any allocated cost may result in denial of its recovery in rates.

e) Costs which would have been denied recovery in rates had they been incurred by PacifiCorp regulated electric operations will likewise be denied recovery whether they are allocated directly or indirectly through subsidiaries in the ScottishPower group.

f) Any corporate cost allocation methodology and subsequent changes thereto must be approved by the Utah Commission.

3) ScottishPower will assume the risk for the Utah Commission approval and adoption of corporate cost allocation methodologies which differ from those adopted by OFFER or any other U.S. regulatory jurisdiction.

4) The achievement of the $10 million guaranteed savings should be measured from PacifiCorp's 1999 actual corporate costs, normalized and adjusted so as to reflect only those costs that would be included in rates. Any costs related to the ScottishPower merger should also be excluded.

5) Any diversified holdings and investments (e.g., non-utility business or foreign utilities) of ScottishPower and PacifiCorp shall not be held by PacifiCorp, the entity

for utility operations.

6) ScottishPower/PacifiCorp should be required to notify the Utah Commission subsequent to ScottishPower plc's Board approval and as soon as practicable following any public announcement of and acquisition of a regulated or nonregulated business representing 5% or more of the market capitalization of ScottishPower plc.

7) ScottishPower/PacifiCorp should not assert in any future Utah proceeding that the provisions of the Public Utility Holding Company Act of 1935 or the related Ohio Power v FERC case preempt the Utah Public Service Commission's jurisdiction over affiliated interest transactions and will explicitly waive any such defense in those proceedings.

8) ScottishPower should be required to comply with PacifiCorp's Transfer Pricing Policy. (Exhibit No. DPU 2.2).

9) The Applicants should be required to provide notification of and file for Commission approval of the divestiture, spin-off, or sale of any integral utility assets or functions.

10) The Merged Company shall notify the Commission, and provide sufficient information and documentation to the Commission, prior to the implementation of plans (1) to form an affiliate entity for the purpose of transacting business with the electric divisions of PacifiCorp, (2) to commence new business transactions between an existing affiliate and the electric utility divisions of PacifiCorp, (3) to dissolve an affiliate which has transacted any substantial business with such divisions, (4) to

enter into new business ventures or expand existing ones, or (5) to merge combine, transfer stock or assets of any part or all of the Merged Company.

11) ScottishPower shall file an affiliated interest report annually.

12) The Merged Company shall provide notification of all asset transfers to or from PacifiCorp, its affiliates, or subsidiaries in accordance with current PSC rules (see in particular PSC R746-401).

13) Establish agreed upon procedures by which Division staff can have access to documentation supporting the purpose and/or circumstances attributable to costs charged to PacifiCorp.

14) The holding company(s) and subsidiaries' employees, officials, directors, or agents should be available to testify before the Utah Commission to provide information relevant to matters within the jurisdiction of the Utah Commission.

15) The Utah Commission should establish procedures by which the Public Service Commission and Division staffs, or their authorized agents can obtain needed access to subsidiary books and records, other relevant documents, data and records. Failure to provide adequate supporting documentation of costs may result in those costs being denied rate recovery. Requests by the Utah Commission, the Division, or their authorized agents shall be deemed presumptively valid, material and relevant, with the burden falling to ScottishPower/PacifiCorp to prove otherwise. ScottishPower/PacifiCorp shall reserve the right to challenge any such request before

the Utah Commission and shall have the burden of demonstrating that any such request is not valid, material or relevant. In addition, ScottishPower shall pay for the expense incurred by Utah regulatory personnel in accessing corporate records and personnel located outside of the state of Utah.

16) All merger related costs incurred by PacifiCorp and ScottishPower shall be recorded below the line.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

Yes.

17269

RESUME
MARY H. CLEVELAND

EDUCATION:

BBA-Accounting: University of Missouri-Kansas City, 1971
MBA-Accounting: University of Missouri-Kansas City, 1974

HONORS:

Beta Gamma Sigma

CPA STATUS:

Licensed in Kansas

EMPLOYMENT:

Mar. 1998 to present: Utah Division of Public Utilities
160 East 300 South, Suite 400
Salt Lake City, UT 84114

Position: Utility Regulatory Analyst IV

Description: Primarily responsibilities include reviewing utilities' affiliated transactions and accounting for regulated and non-regulated activities. Also review gas procurement activities, participate in rate case investigations, prepare written testimony and testify before the Utah Public Service Commission.

Aug. 1991 to Mar. 1998: Utah Committee of Consumer Services
160 East 300 South, Suite 408
Salt Lake City, UT 84114

Position: Utility Regulatory Analyst IV

Description: Represented residential, small commercial and agricultural customers in utility matters. Monitored, assessed and reported on current issues facing the utility industry. Planned and conducted audits of both gas and electric utilities in conjunction with rate applications, prepared written testimony and testified before the Utah Public Service Commission. Assignments included participation in the IndeGO (proposed independent system operator for the Northwest region)

Pricing Work Group and Steering Committee, evaluating PacifiCorp's integrated resource planning process, participating in PacifiCorp's Demand-Side Management Advisory Group, and assisting in the evaluation of PacifiCorp's stranded cost exposure. Also evaluated gas procurement activities of Questar Gas.

Oct. 1988 - Aug. 1991: Utah Division of Public Utilities
160 East 300 South
Salt Lake City, UT 84114

Position: Utility Rate Engineer

Description: Participated in audits of utilities in conjunction with rate applications, prepared written testimony and testified before the Utah Public Service Commission. Evaluated and prepared written recommendations on utility tariff and special contract filings. Assisted in the evaluation of the PacifiCorp and Utah Power & Light merger.

Apr. 1985 - Oct. 1988: LMSL, Inc.
10955 Lowell
Overland Park, KS 66210

Position: Senior Regulatory Consultant

Description: Participated in rate case investigations and other special studies on behalf of state utility commissions, prepared written testimony and testified in various proceedings.

Aug. 1983 - Apr. 1985: Troupe Kehoe Whiteaker and Kent
800 Penn Tower Building
3100 Broadway
Kansas City, MO 64111

Position: Senior Regulatory Consultant

Description: Local CPA firm specializing in regulated industries. Work included rate case investigations, preparation of written testimony and testifying before various state regulatory commissions. Also participated in year-end financial audits of small independent telephone companies and rural electric companies and assisted in tax return preparation.

Mar. 1981 - Aug. 1983: Kansas Corporation Commission
Utilities Division
1500 S.W. Arrowhead Road
Topeka, KS 66604-4027

Position: Senior Utility Regulatory Auditor

Description: Planned and conducted audits of utilities in conjunction with rate case applications, prepared written testimony and served as an expert witness in rate hearings before the Commission.

Aug. 1977 - Mar. 1981: University of Kansas Medical Center
Institutional Research & Planning / Budget Office

Position: Analyst / Accountant

Description: Conducted special operational and long-range planning studies. Work involved programming with SPSS, SAS and Mark IV; program documentation and report writing.

Jun. 1973 - Aug. 1977: Midwest Research Institute
425 Volker
Kansas City, MO 64110

Position: Operations Analyst

Description: Performed operational audits and developed management information systems for a variety of clients. Also conducted workshops on long-range planning. Work involved programming with FORTRAN and SPSS, program documentation and report writing.

Apr. 1969 - Jun. 1973: University of Missouri - Kansas City
Library Accounting / Acquisitions
5100 Rockhill Road
Kansas City, MO 64110

Position: Accountant

Description: General accounting, budget preparation and fiscal reporting.

MEMBERSHIPS:

American Institute of Certified Public Accountants.

National Association Regulatory Utility Commissioners Subcommittee on Accounts SEC Subcommittee.

TRANSFER PRICING POLICY

GENERAL

It is the policy of PacifiCorp Electric Operations (the "Company") to engage in transactions with affiliated companies when appropriate. In so doing, the Company will establish transfer prices which are both advantageous to electric customers and fair to affiliated companies. Special care will be taken to assure that the transactions are of an appropriate nature and do not have the appearance of self-dealing or cross-subsidization of nonutility operations by utility customers.

For the purpose of setting transfer prices, all affiliate transactions will be considered to fall into one of two categories -- transfers of assets and exchanges of goods and services. The term "transfer of assets", as used in this policy, refers to the disposition or acquisition of utility property for which cost recovery has been obtained from electric customers or for which future cost recovery will be sought. The issues to be considered in setting transfer prices are described below.

TRANSFERS OF ASSETS

A. **Transfers of Utility Assets to Affiliated Companies**

When it becomes necessary to dispose of utility assets, the interests of utility customers are protected by obtaining the highest possible price for those assets. Therefore, it is Company policy that if surplus utility assets are transferred to affiliates, the transfer price will be the greater of fair market value or net depreciated book value. Fair market value is defined as the cost of comparable assets available from non-affiliated companies, determined in accordance with corporate procurement policies and procedures.

B. **Transfers of Affiliated Company Assets to the Utility**

When acquiring utility assets, the interest of utility customers are protected by obtaining the assets at the lowest possible price. Therefore, assets acquired by Electric Operations from affiliated companies will be transferred at the lesser of fair market value, as defined above, or the net depreciated book value on the records of the affiliated company.

EXCHANGES OF GOODS AND SERVICES

A. **Goods and Services Provided to the Utility by Affiliates**

In accordance with the Company's procurement policies and procedures, the market price shall be used to cost goods and services sold by an affiliated company to Electric Operations. Market price is defined as the lowest evaluated cost of comparable goods and services available from non-affiliated companies as determined by competitive bidding or justified otherwise as required by the Company's procurement policy. With respect to competitive bidding, it is understood that in determining the "lowest evaluated cost of comparable goods and services", factors such as technical expertise, performance capabilities, safety, convenience and minimization of related costs, etc. may be as or more important than lowest bid price.

If the goods and services provided by an affiliate are not required to be competitively bid under the terms of the Company's procurement policies and procedures, the transaction will be priced at the affiliate's actual cost. Cost in this case may include a return on the affiliate's investment at a rate no greater than the utility's most recently authorized overall rate of return.

B. **Goods and Services Provided to Affiliates by the Utility**

Goods and services provided by Electric Operations to affiliated companies will be priced at a rate which covers all associated costs, including a return on investment.

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-BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH-

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UTAH PUBLIC SERVICE COMMISSION

In the Matter of the Application of PacifiCorp And Scottish Power for an Order Approving The Issuance of PacifiCorp Common Stock	DOCKET NO. 98-2035-04 UTAH DIVISION OF PUBLIC UTILITIES

TESTIMONY OF ROBERT J. MALONEY, WITNESS 6

SERVICE QUALITY AND ADDED VALUE --

FOR THE DIVISION OF PUBLIC UTILITIES

DEPARTMENT OF COMMERCE

STATE OF UTAH

June 18, 1999

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Exhibits

INTRODUCTION

Q PLEASE STATE YOUR NAME AND OCCUPATION.

A My name is Robert J. Maloney. I work within the Division of Public Utilities (Division). My title is Management Analyst.

Q WHAT ARE YOUR PURPOSES IN TESTIFYING IN THIS DOCKET?

A My purposes are: 1. Compare service standards and service targets currently in place with ScottishPower's proposed service package. 2. Identify services not addressed through ScottishPower's proposal. 3. Describe a ***possible*** positive benefit attributable to a merger. 4. Recommend eleven conditions enabling the Commission to transfer some risks from customers to shareholders.

Q WHAT HAVE BEEN YOUR RESPONSIBILITIES OVER THE PAST SEVERAL YEARS RELATIVE TO YOUR TESTIMONY IN THIS DOCKET?

A During 1992 through 1995, I analyzed the service results of US West's reengineering efforts. This involved reporting customers' most significant service requirements and the Company's continuing failures to meet these requirements.

During 1995 through 1998, I analyzed PacifiCorp's and Questar's service results. I examined internal service targets, performance results, and customer feedback regarding performance. These efforts led to both Companies voluntarily providing quarterly service quality monitoring reports to the Division of Public Utilities.

Q PLEASE DESCRIBE YOUR EARLIER WORK EXPERIENCE RELATIVE TO YOUR TESTIMONY IN THIS DOCKET.

A I have analyzed regulated public utility operations and services for twenty-one years. During 1978 through 1986, I worked for the Missouri Public Service Commission as a Management Services Specialist. Since 1986 I have worked within the Division as a Management Analyst. This has involved conducting management evaluations, including customer service evaluations, of telephone, electric, and gas utilities. I have also monitored the work of consultants conducting utility management audits.

Q5 WHAT IS YOUR EDUCATIONAL BACKGROUND?

A In 1970, I completed an Associates of Art Degree in Business Administration; in 1972, a Bachelor of Arts degree in Business Management; in 1974, a Master of Business Administration degree. I am certified by The Institute of Internal Auditors as Certified Internal Auditor and the American Society for Quality Control, as a Certified Quality Auditor.

SUMMARY

Q WOULD YOU PLEASE SUMMARIZE YOUR TESTIMONY?

A Yes, I will. I have identified a ***possible*** positive benefit associated with ScottishPower's proposed service package and funding of network improvements. I have also identified service outcomes not addressed in the Company's proposed service package.

Service outcomes not addressed in the Company's proposed package include call handling during wide scale outages, outage levels on the weaker (not weakest) circuits within Utah, and field responses for such services as meter sets and meter tests in the districts. Deterioration in these service outcomes could offset a possible positive benefit.

To enhance the probability that customers realize a positive benefit (or value), I recommend the Company formally commit to eleven conditions. I recommend these conditions because Title 54-7-25 subjects the Company to penalties unless it can provide convincing reasons why it should not pay penalties for failing to meet the conditions. The Commission will thereby have a means for enforcing service adequacy.

The conditions require the Company to:

- Achieve their proposed service package and fund such from as yet unidentified efficiencies and internal sources.

- Set internal targets for handling calls during wide-scale outages; provide quarterly reports showing performance against the targets.

- Set internal outage targets for districts, circuits, and individual customers; provide quarterly reports showing performance against the targets.

- Set internal field response targets for districts and individual customers; provide quarterly reports showing performance against the targets.

What gets measured and reported generally improves, or at least does not deteriorate. It is possible Scottish Power will not set internal targets, set unreasonably lax internal targets, or let performance deteriorate for services not included in their service package. Should any of these three outcomes occur, Title 54-4-18 empowers the Commission to ascertain and fix reasonable service standards. However, we need local service reports to determine when and where service is inadequate.

I believe Scottish Power should set reasonable internal service targets, achieve the targets, and report quarterly progress. Doing so will allow the Division and the Company to meet the requirements of Title 54-4a-6 (3), which states:

> ***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.***

Meeting the eleven commitments includes effectively implementing the service standards package, adequately funding network and other service improvements from as yet unidentified efficiencies and internal resources. Meeting the commitments also includes setting internal targets, maintaining or improving performance for services not included in their service package, and providing quarterly reports showing performance against the targets.

A STANDARDS COMPARISON

Q DOES THE COMMISSION HAVE THE AUTHORITY TO ESTABLISH SERVICE STANDARDS?

Yes, Title 54-4-18 indicates the Commission has the power to ascertain and set reasonable service standards. R746-100-15 explains the Commission's rulemaking procedures.

Q WHAT ARE THE DIVISION'S RESPONSIBILITIES RELATIVE TO SERVICE ADEQUACY?

A Title 54-4a-6 indicates the Division is responsible for providing objective and comprehensive evidence and recommendations to the Commission consistent with its objectives. One of the Division's objectives, as stated in Subsection (4) (c), is to 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).

To provide the Commission with objective and comprehensive recommendations concerning service quality and adequacy, the Division must have access to service outcome data at the local level. By local level, I mean district, circuit, and, where feasible, individual customer level.

Q WHY HAVE YOU REVIEWED, IN ANSWERING THE TWO PREVIOUS QUESTIONS, THE COMMISSION'S POWER'S AND THE DIVISION'S RESPONSIBILITIES CONCERNING SERVICE STANDARDS?

A I have reviewed the Commission's powers and the Division's responsibilities concerning service standards because Utah has relatively few end-user service standards in place. Captive customers suffer the unfavorable consequences if both a utility and a regulatory agency take a lackadaisical approach to service quality. It is critical that we have the data to determine where and when enforceable standards are needed.

Q WOULD YOU COMPARE SCOTTISHPOWER'S PROPOSED END USER PERFORMANCE STANDARDS WITH CURRENT STANDARDS AND TARGETS?

A Yes, I will. Exhibit 6.1, which follows, shows ScottishPower's proposed standards, Utah's associated standards, and PacifiCorp's associated internal targets.

Exhibit 6.1 – Proposed Performance Standards Compared			
Service Standard	**Proposed by Scottish Power**	**Utah Existing**	**PacifiCorp Internal Target**
1) SAIDI: System Availability (interruption duration) 2) SAIFI: System Reliability (interruption frequency)	Reduce *underlying* outages by 10% by 2005	R745-310-5: design, construct, maintain, & operate facilities to give adequate & continuous service. (also, see Title 54-3-1)	Provide adequate and continuous service – no specific targets except statewide averages as reflected in the Quarterly Service Quality Standards Report filed with DPU.
3) MAIFI: System Momentaries (outages under five minutes)	Reduce underlying momentaries by 5% by 2005	"	"
4) Worst Performing Circuits	Each year, identify the five worst performing circuits in Utah. Reduce outages 20% within 2 years	R746-310-4 (C): utility shall inspect. (D): Maintenance – NESC to be met or exceeded.	Each year, identify the five worst performing circuits in each of Northern and Southern Utah. Meet NESC – no specific targets.
5) Supply Restoration	80% within 3 hours	None	Restore as expeditiously as possible with safety in mind – no specific targets.
6) Telephone Service Levels	80% within 30 seconds; by Jan. 2002, 80%with 10 seconds	None	Answer 80% of calls in 45 seconds. Also, on average, answer all calls within 65 seconds.
7) Resolve Commission Complaints	Investigate/respond: within 3 bus. days; investigate/respond within 4 hours for disconnects; resolve 90% within 30 days.	R746-310-3.B.4 – fully and promptly investigate. R746-200-7: DPU has 5 bus. days to investigate and attempt to resolve complaint.	Utah complaints – attempt to resolve in 5 business days – starting to track investigation and response within 3 business days.
Sources: ScottishPower 5/27/99 handout; RJM's DPU V36 – Status of UP&L's efforts to define service adequacy; PC's reply to DR18.1; Utah Public Utility Laws 1998 - 1999			

Q WHAT ARE THE KEY BENEFITS OF SCOTTISHPOWER'S SEVEN PROPOSED PERFORMANCE STANDARDS?

A Key benefits may include:

- Scottish Power has ***voluntarily*** committed to achieve a number of reliability standards, service standards, and guarantees that are of high importance to customers.

- The Commission will have an ability to enforce ***quantified*** reliability standards, service standards, and guarantees.

- Eventual outage reductions will lead to a estimated $60 million continuing annual savings in customers' power outage costs.

- The Company will accurately record and report outages.

Q WOULD YOU COMPARE SCOTTISHPOWER'S PROPOSED INDIVIDUAL CUSTOMER GUARANTEES WITH CURRENT STANDARDS AND TARGETS?

A Yes. Exhibit 6.2, which follows, includes ScottishPower's proposed guarantees, Utah's associated standards, and PacifiCorp's associated internal targets.

Exhibit 6.2 – Proposed Guarantees Compared

Customer Guarantees -- Proposed by ScottishPower: Eight separate guarantees with associated payment to customers for failure to meet standard. $50 payment to customer for failure to meet time frame. $100 for commercial customer for CG1 and CG7. (Note: In the following, where days are given they are business days.)

Service Standard	Proposed by Scottish Power	Utah Existing	PacifiCorp Internal Targets
CG1 – Restoring Supply	Restoration w/in 24 hrs due to fault on Company's system. Additional penalties for each additional 12 hour period.	R746-310-5: facilities to be constructed, operated & maintained to render adequate & continuous service.	As expeditiously as possible with safety in mind – no specific targets
CG2 -- Keep appointments	Keep all mutually agreed to appointments. Beginning 2001, customer will be offered a morning (8 a.m. to 1 p.m.) or an afternoon (12 noon to 5 p.m.) appointment.	None	See appointment target for new extensions (CG4 below) -- otherwise no specific target.
CG3 -- Switching on initial power (connecting)	Will activate within 24 hours of customer request.	None	If no construction, target is to switch on power within 24 hours. Where meter sets required, switch on 90% within five days, after receipt of government inspections.
CG4 New Extensions	Call customer w/in 2 days to schedule an estimator appointment. Provide estimate w/in: five days for work not requiring network change; w/in 15 days for work requiring network change.	None	Respond back to customer in days. Meet with customer w/in 5 days. No target for providing estimate.
CG5 – Bill Inquiries	Investigate and respond w/in 15 days of customer's request.	R746-310-2.5 – provide phone number on bill for customers to call w/questions.	No specific target.
CG6 – Cust. Meter Problem	Investigate/respond within 15 bus. days of customer's request.	R746-310-3.B.4 – upon written request, promptly test; report to customer.	Northern Utah only -- test meter within five business days of customer's request.
CG7 Planned interruption	Give customer at least 48 hours notice.	R746-310-2.G.2 – provide reasonable notice of planned interruption	Provide reasonable notice – no specific targets.
CG8 Power quality complaints	Explain in writing w/in 5 bus. days or investigate w/in 7 calendar days.	R746-310-2.F.1 – fully/promptly investigate a complaint.	No specific target.

Sources: Alan Richardson's supplemental direct testimony; RJM's DPU V36 – Status of UP&L's efforts to define service adequacy; PC's reply to DR18.1.

Q WHAT ARE THE KEY BENEFITS OF SCOTTISHPOWER'S EIGHT PROPOSED INDIVIDUAL CUSTOMER GUARANTEES?

- Scottish Power acknowledges customer inconvenience. The Company has agreed to credit a customer whenever it does not meet a guarantee.

- Senior management will have a tool with which to hold employees accountable for improving service quality.

- Each guarantee is quantified. It is therefore possible to determine whether the Company meets the guarantee requirement.

A POSITIVE BENEFIT

Q DOES SCOTTISHPOWER'S INTERNALLY FUNDED SERVICE PACKAGE TOGETHER WITH ACCURATE, ACTIONABLE QUARTERLY REPORTING CONSTITUTE A POSITIVE BENEFIT IN THE PUBLIC INTEREST?

A Yes, if the Company can both cost effectively implement the service package and provide accurate reports showing that service outcomes not included in the package do not deteriorate.

ScottishPower can show they are accountable by formalizing their commitment. Formalizing their commitment involves agreeing to eleven conditions. The first set of conditions, conditions one and two, requires ScottishPower to implement the service package without exceeding the network expenditure commitments described in their testimony.

The second set, conditions three through ten requires ScottishPower to provide data that accurately depicts actual service outcomes at useful/actionable levels of detail for districts, circuits, and individual customers. Condition eleven requires ScottishPower to establish/tariff a dispute resolution process.

With accurate actionable reports, and using its powers under Title 54-4-18, the Commission will be able to order corrective action if service deteriorates in Utah or in parts of Utah.

ENFORCEABLE SERVICE QUALITY CONDITIONS

Q WHY DO YOU RECOMMEND THAT SCOTTISHPOWER FORMALLY COMMIT TO MEET EACH OF ELEVEN CONDITIONS?

A Formally agreeing to meet each of eleven conditions shifts some of the risk ScottishPower will not meet approved merger conditions from customers to shareholders. ScottishPower becomes subject to the penalties upon failure to meet Commission approved merger conditions.

Title 54-7-25 states that the Company becomes subject to a penalty of not less than $500 or more than $2,000 for failing to comply with a Commission order. Each violation is a separate and distinct offense. In the case of a continuing violation, each day's continuance is a separate offense.

Possible financial penalties provide incentives to meet the conditions in a timely and effective manner. The Commission may, after allowing the Company due process, impose financial penalties if Scottish Power fails to meet any one of the eleven conditions.

Together, Title 54-7-25 and the approved merger conditions enable the Commission to shift some of the risk of failing to meet approved merger conditions from customers to shareholders.

EXPLANATIONS OF SERVICE QUALITY MERGER CONDITIONS

Q CONDITION #1. WHY DO YOU RECOMMEND THE COMPANY CONTINUOUSLY MEET PERFORMANCE STANDARDS, PROVIDE SERVICE GUARANTEES, AND NOT ALLOW UNDERLYING OUTAGES TO INCREASE ABOVE CURRENT LEVELS?

A Formally committing to meet performance standards and provide service guarantees establishes accountability. It also provides the Commission with enforcement tools it does not currently have.

Title 54-7-25 makes any utility violating a Commission order under title 54 subject to a penalty of not less than $500 nor more than $2,000 for each offense. Each violation is a separate offense. Each day's continuance is also a separate offense.

I therefore recommend the Commission require the Company to:

- Formally agree to effectively implement their proposed service package.

- File tariffs specifying the five network performance standards, two customer service performance standards, and eight guarantees listed in their proposed package.

- Formally agree to not allow "underlying" (exclusive of extreme events) outages to increase above current levels during any of the next five years.

- Formally agree to update the aforementioned standards and service guarantees during 2004 and each year thereafter.

Q **CONDITION #2. WHY DO YOU RECOMMEND THAT THE COMPANY FUND NETWORK EXPENDITURES FROM EFFICIENCY SAVINGS AND REDIRECTED INTERNAL FUNDING; REPORT FUNDING SOURCES AND EXPENDITURES AGAINST THE $55 MILLION ESTIMATE?**

A Doing so will help address the risk the Company will be ineffective in identifying efficiencies and internal funding sources. On page one, lines 17 through 21 of Mr. Alan Richardson's supplemental testimony, Mr. Richardson indicates:

The $55 million which we have estimated we will spend over the next five years to implement the proposed service standards package is not an incremental cost, but will be achieved through efficiencies within the existing spending plans of PacifiCorp. Overall costs will therefore not increase as a result of these expenditures, as they will be offset by efficiencies we will achieve in PacifiCorp's operations.

Formally conditioning the merger on funding network improvement expenditures through identifying efficiencies or internal funding sources shows that Scottish Power accepts accountability and provides the Commission with a means of enforcing performance.

Q **CONDITION #3. WHY DO YOU RECOMMEND THE COMPANY IMPLEMENT PROSPER, AN AUTOMATED REPORTING SYSTEM, NO LATER THAN 12 MONTHS AFTER THE MERGER TRANSACTION – AND ALSO OPERATE THE CURRENT OUTAGE REPORTING SYSTEM IN PARALLEL UNTIL ACTUAL OUTAGE LEVELS ARE ACCURATELY AND RELIABLY DETERMINED?**

A I recommend the Company commit to implement Prosper, an automated outage reporting system, no later than 12 months after the transaction because:

- Scottish Power has indicated they could implement Prosper in twelve to eighteen months.

- PacifiCorp's current outage reporting system understates outages. Scottish Power's January 1999 audit of the PacifiCorp's current system showed outages were underreported by 20% to 30%. PacifiCorp did not challenge the audit findings. It is not presently possible to accurately determine outage baseline and measure outage reductions against that baseline.

- It is as possible for customers to lose $60 million in outage costs as it is possible for them to gain $60 million in outage savings. On page four lines 22 through page five line ten, in his supplemental direct testimony, Mr. Richardson discusses a $60 million annual savings in customers' power outage costs. Mr. Richardson indicates the saving will be realized if the Company achieves the targeted outage reductions. If, of the otherhand, outages begin to increase, even by only a few percentage points, customers will begin to incur significant additional power outage costs – in tens of millions of dollars.

  We need accurate and reliable outage data at the earliest possible time to determine actual outage levels. We also need the data to expeditiously enforce penalties if outages begin to increase.

- We need accurate outage data to identify where and when outages may increase due to inadequate network investment and maintenance. With the $55 million cap on network investments, Scottish Power may be pressed to cut costs – especially in high cost sparsely populated areas. This is certainly possible if ScottishPower is unable to realize the as yet unidentified efficiencies and alternative internal funding.

I recommend the Company operate the current outage reporting systems in parallel because Prosper implementation is uncertain. Even highly inaccurate outage data is better than no data.

Q CONDITION #4. WHY DO YOU RECOMMEND THE COMPANY MEASURE OUTAGE-REDUCTION PERFORMANCE AGAINST OUTAGE LEVELS AGREED TO (BY MANAGEMENT AND DIVISION STAFF) OUTAGE LEVELS AT THE TIME PROSPER IS IMPLEMENTED AND AUDITED – OR DEFER TO A COMMISSION DECISION ON SUCH?

A As previously indicated under condition #3, PacifiCorp's current outage reporting system is highly inaccurate. There is no way to determine actual outage levels until the Company installs Prosper, an automated outage reporting system.

Based upon ScottishPower's estimates, accurate outage reports will not be available for from 18 to 30 months after the merger transaction. This estimate includes 12 to 18 months to implement Prosper and another six to 12 months to ensure accuracy by the employees responsible for recording outages.

ScottishPower has concluded present reporting systems understate outages by 20% to 30%. Scottish Power determined such by conducting an audit of the accuracy of PacifiCorp's outage reporting system during January 1999. PacifiCorp has not challenged these findings.

ScottishPower also indicates that annual variations greater than 5% in underlying outages suggest problems in recording accuracy. PacifiCorp's outage reports show annual variations significantly larger than 5%.

Eventually, Scottish Power expects reporting accuracy to be close to 100%. However, in reply to data requests inquiring about expected reporting accuracy, Scottish Power provided no dates.

The Commission can decide baseline outage levels for determining whether Scottish Power meets its 60 month outage reduction targets. I recommend this occur if the Division and Company do not agree on baseline outage levels within 18 months of the transaction.

Q CONDITION #5. WHY DO YOU RECOMMEND THE COMPANY DEFINE "EXTREME EVENT" AS OUTSIDE THREE STANDARD DEVIATIONS OF THE AVERAGE NUMBER OF DAILY INCIDENTS DURING THE PREVIOUS CALENDAR YEAR?

A The three standard deviations criterion can be audited and enforced. Also, in the United Kingdom, ScottishPower and Manweb define extreme storm as any incident outside three standard deviations of the daily average.

Unfortunately, ScottishPower has proposed both the three standard deviations criterion as well as the Institute of Electrical and Electronic Engineers (IEEE) definition of an extreme storm. The IEEE definition includes: 1. Exceeds the design limits of the power system, and 2. Extensive damage to the electric power system. Both these criteria require an engineering judgment. Reasonable engineers may differ as to what exceeds design limits and what is extensive damage.

The three standard deviations criterion alone allows no exceptions, judgmental or otherwise. Use of the criterion is consistent with title 54-4a-6 (3). This statute states a Division objective of making 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. The two aforementioned IEEE criteria are not consistent with this statute.

Q CONDITION #6. WHY DO YOU RECOMMEND THE COMPANY AUDIT, UPON REQUEST, TO DETERMINE ACTUAL OUTAGE LEVELS – AFTER CORRECTING FOR UNDER OR INACCURATE REPORTING?

A Verifiable audits may provide a way to determine actual outage levels as ScottishPower implements new outage recording and reporting systems. Customers will realize an estimated $60 million annual savings in outage costs only if the Company reduces outages by the targeted amounts -- from actual current levels. We need audits to determine when reported levels become the same as actual levels.

Q CONDITION #7. WHY DO YOU RECOMMEND THE COMPANY REPORT, EACH QUARTER, OUTAGE LEVELS AGAINST INTERNAL OUTAGE TARGETS ON A DISTRICT, CIRCUIT, AND (WHERE FEASIBLE) INDIVIDUAL CUSTOMER BASIS?

A Outage levels for worst-performing districts are often significantly higher than statewide outage levels. Exhibit 6.4, following page 26 of this testimony, shows outage levels for the worst performing districts as compared with statewide outage levels for each of years 1990 through 1998.

In reviewing Exhibit 6.1, please note that the Delta District during 1998 had an average of 197 minutes of interruption minutes per customer (excluding extreme storms, prearranged outages, and transmission outages). The 1998 statewide average was only about 92 minutes. Also, please note that: 1. Interruption minutes are averaged across all customers, not only affected customers. 2. Since 197 minutes is an average, a large number of circuits within the Delta District have interruptions of longer than 197 minutes duration.

Exhibit 6.3, which follows, shows the number of circuits and customers experiencing more than 151 interruption minutes during 1998. One hundred fifty-one minutes is more than double the 1992 – 1996 statewide average of 68 minutes.

Exhibit 6.3 – Numbers of Utah Customers Having High Outage Levels During 1998

Range of Interruption Minutes Per Customer	Numbers of Circuits	Numbers of Customers
600 to 10,890 minutes	22 circuits	4,666 customers
361 to 584 minutes	40 circuits	13,039 customers
240 to 357 minutes	75 circuits	50,309 customers
151 to 237 minutes	74 circuits	50,165 customers
Totals	211 circuits	118,179 customers

Notes: 1. The numbers of minutes per customer in the left column are calculated by dividing total interruption minutes by *all* customers. The numbers of interruption minutes per *affected* customer are larger than the numbers of interruption minutes in the left column. 2. The 1998 statewide (underreported) interruption per customer average was about 92 minutes.

Source: Revised response to DPU PC17.6

Tracking outage levels on district, circuit, and individual customer bases will help show the extent customers, including those in rural service territories, receive reliable service.

ScottishPower is familiar with the approach. In the United Kingdom, the Company is considering internal targets wherein they "look at:"

- Each individual situation wherein a customer experiences more than seven outages per year.

- Each community situation wherein a community experiences more than four outages per year.

Once installed, ScottishPower's Prosper system will have the ability to track individual customer and district outage levels. I believe our regulatory agency should use this capability to assure adequate reliability for all customers.

Q **CONDITION #8. WHY DO YOU RECOMMEND: THE COMPANY CONTINUE WITH METER SET AND METER TEST INTERNAL FIELD RESPONSE TARGETS IN NORTHERN UTAH? ESTABLISH INTERNAL FIELD RESPONSE TARGETS WHERE NONE CURRENTLY EXIST? REPORT PERFORMANCE AGAINST ALL INTERNAL FIELD RESPONSE TARGETS ON A QUARTERLY BASIS?**

A Tracking field-response intervals on a district basis will allow the Commission to address the risk some customers, especially rural customers, don't receive timely responses to field requests.

ScottishPower's service standards package does not include field response performance standards for setting meters, testing meters, reconnecting after disconnecting for non-payments, or other field responses. Northern Utah Operations, however, has set internal targets for setting and testing meters.

There is a risk ScottishPower will achieve its standards package at the expense of services it did not consider important enough to include in its standard package. This is so because the Company plans to fund their network improvement package through identifying efficiencies within existing spending plans and internal funding sources.

Q CONDITION #9. WHY DO YOU RECOMMEND THE COMPANY REPORT, DURING WIDE-SCALE OUTAGES, INTERNAL CALL-HANDLING TARGETS AND RESULTS: AVERAGE ANSWER SPEED, HOLD TIMES, AND BUSY INDICATIONS?

Large numbers of customers are especially interested in accurate, up-to-date outage information during wide-scale outages. They want to know the Company is aware of the outage and when their service will be restored.

During a November 6, 1998 wide-scale outage, PacifiCorp experienced a multitude of system breakdowns in handling a large volume of incoming outage calls. However, call-handling performance during a wide-scale outage on April 23, 1999 showed the average answer speed was ten seconds. With a disciplined focus, it is possible to effectively manage call handling during wide scale outages.

PacifiCorp currently uses a 15-minute customer wait time as a threshold for conducting a diagnostic of call-handling breakdowns during wide-scale outages. The Company otherwise has no internal targets for diagnosing call-handling breakdowns.

I recommend conditioning the merger on management's establishing targets for handling calls during wide-scale outages because:

- Customers place a high value on useful outage information during wide-scale outages.

- PacifiCorp has had past breakdowns in handling calls during wide-scale outages.

- PacifiCorp's current 15-minute customer wait time threshold is too lax from customers' perspectives.

Q CONDITION #10. WHY DO YOU RECOMMEND THE COMPANY REPORT, EACH QUARTER, DISTRICT DATA SHOWING CREDITS TO CUSTOMERS FOR FAILURES TO MEET GUARANTEED SERVICE OUTCOMES?

Reporting customer credits on a district basis enables our regulatory agency to address the risk that rural customers in high cost service territories may experience a disproportionately large percentage of inadequate services.

Unless Company management closely monitors service outcomes, customers residing in high-cost rural service territories could experience deteriorating services. This is possible because ScottishPower is committed to funding network improvements by identifying as yet unidentified efficiencies and internal funding. Under such circumstances, funding adequate services in high-cost rural service territories may become an increasingly formidable challenge.

Q CONDITION #11. WHY DO YOU RECOMMEND THE COMPANY IMPLEMENT AND TARIFF A DISPUTE RESOLUTION PROCESS FOR DEALING WITH GUARANTEED SERVICE OUTCOME FAILURES ON A FAIR AND CONSISTENT BASIS?

A As ScottishPower indicated on line ten, page 29 of the Moir-MacLaren-Rockney Oregon rebuttal testimony, implementing a dispute resolution process matches ScottishPower's intentions and is similar to the way ScottishPower operates its guarantee program in the United Kingdom.

Also, management practices vary widely among PacifiCorp's Utah districts. Under such circumstances, managers may have a variety of interpretations regarding guarantee requirements.

Most importantly, an effective dispute resolution process would enable the Company to treat customers fairly and consistently. Customers will continue to have the prerogative of filing informal or formal complaints with the Commission.

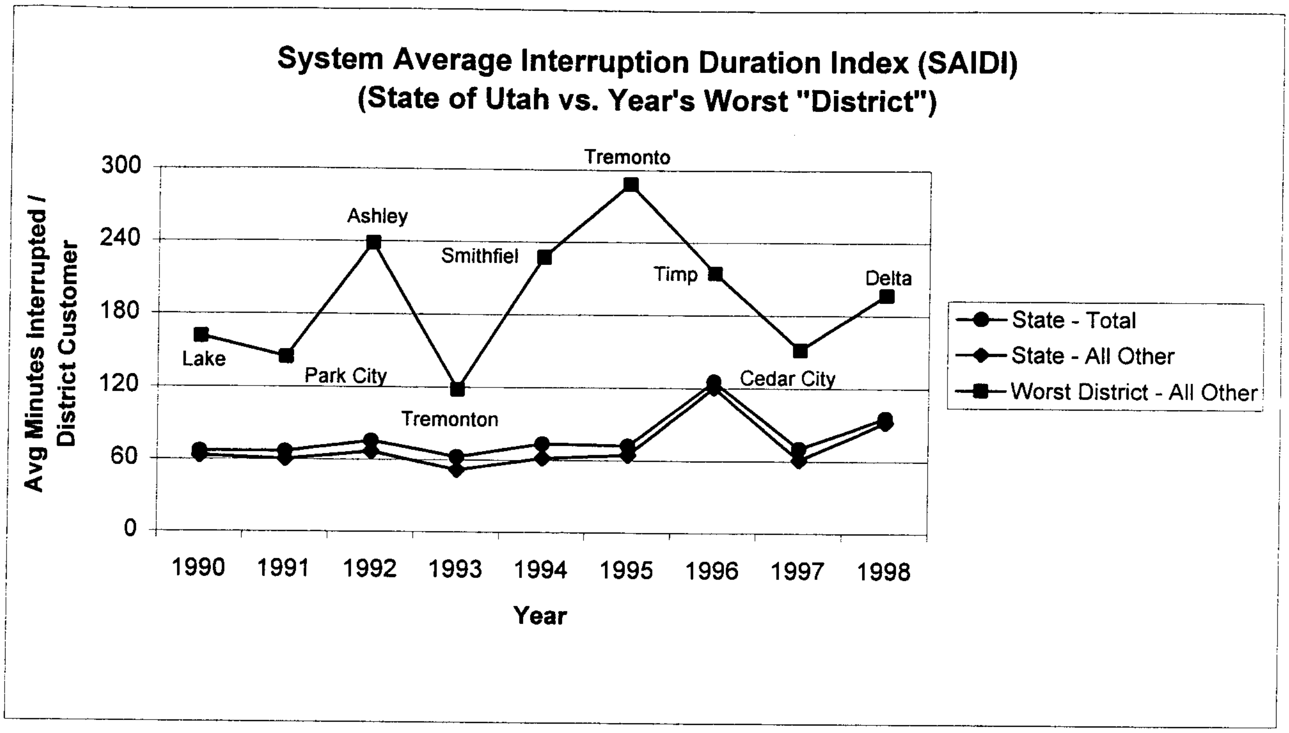
Q DOES THIS CONCLUDE YOUR TESTIMONY?

A Yes, it does.

EXHIBIT 6.4
SUMMARY OF ELEVEN SERVICE QUALITY ISSUES AND CONDITIONS

Issue	**Condition**
1. ScottishPower's informal assurances to provide a service package do not establish enforceable accountability for achieving service results.	1. Continuously meet performance standards, provide service guarantees, and do not allow underlying outages to increase above current levels.
2. ScottishPower's plans to fund a maximum of $55 million in network expenditures from as yet unidentified efficiencies and internal funding sources are subject to a high degree of uncertainty.	2. Fund network expenditures from efficiency savings and redirected internal funding; report funding sources and expenditures against the $55 million estimate.
3. It is not possible to accurately determine outage levels with the current outage reporting system.	3. Implement Prosper, an automated reporting system, no later than 12 months after the merger transaction and also operate the current reporting system in parallel until actual outage levels are accurately and reliably determined.
4. Agreeing on outage levels using inaccurate and unreliable outage data can result in irresolvable differences between ScottishPower management and Division staff.	4. Measure outage-reduction performance against agreed to (by management and Division Staff) outage levels at the time Prosper is installed and audited -- or defer to a Commission on such.
5. ScottishPower's proposed use of IEEE criteria in defining an extreme event requires engineering judgements about what "exceeds design limits" and what constitutes "extensive damage." Reasonable engineers may differ on these matters.	5. Define "extreme event" as outside three standard deviations of the average number of daily incidents during the previous calendar year.
6. It is not possible to accurately determine outage levels with the current outage reporting system. Whether ScottishPower can effectively implement an accurate reporting system is uncertain.	6. Audit, upon request, to determine actual outage levels – after correcting for under or inaccurate recording.
7. ScottishPower may more efficiently reduce statewide outage levels by focusing limited investments in highly populated areas. Already high outage levels in sparsely populated high-cost rural areas could rise.	7. Report, each quarter, outage levels against internal outage targets on a district, circuit, and (where feasible) individual customer basis.
8. ScottishPower's standards package does not include *performance standards* for field responses. The Company may achieve its standards package at the expense of services not consider important enough to include in its service package.	8. Continue with meter set and meter test internal field response targets in Northern Utah. Establish internal field response targets where none currently exist. Report performance against all internal field response targets on a quarterly basis.
9. In the past, PacifiCorp has had a multitude of system breakdowns in handling calls during wide scale outages.	9. Report, during wide-scale outages, internal call-handling targets and results: average answer speeds, hold times, and busy indications.
10. In pursing efficiencies, ScottishPower may be especially pressed to adequately fund timely field responses in high – cost rural service territories.	10. Commit to report, each quarter, district data showing credits to customers for failures to meet guaranteed service outcomes.
11. Management practices vary widely among PacifiCorp's Utah districts. Under such circumstances, managers may have a variety of interpretations regarding guarantee requirements.	11. Implement and tariff a dispute resolution process for dealing with guaranteed service outcomes failures on a fair and consistent basis.

Exhibit 6.5 --
System Average Interruption Duration Index
State of Utah Vs. Year's Worst District (1990 to 1998)



Avg Minutes Interrupted / State Customer				
	State of Utah		Worst District - All Other	
Year	State - All Other	State - Total	Max. - All Other	District
1998	91.980	95.880	196.800	Delta
1997	60.780	70.440	151.320	Cedar City
1996	120.408	125.520	214.620	Timp
1995	64.500	72.240	288.480	Tremonton
1994	61.740	73.620	227.400	Smithfield
1993	51.540	62.340	118.380	Tremonton
1992	66.600	75.660	238.440	Ashley
1991	60.300	66.660	144.360	Park City
1990	63.300	66.900	161.400	Lake
AVG	71.239	78.807	193.467	

= Data modified by DPU to match data provided by Scottish Power in Docket # 98-2035-04

Category Descriptions:

"All Other" - **This category <u>excludes</u> data related to Extreme Storms, Pre-arranged Outages, and Transmission outages (defined as a transmission fault causing outages on other circuits serving retail customers).**

"Total" - **This category <u>includes</u> all data, i.e. no data exclusions.**

Data Source: Pacificorp Response to DPU Data Request PC 1.4, Docket # 98-2035-01

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UTAH PUBLIC SERVICE COMMISSION

– 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 Division of Public Utilities Exhibit No. DPU 4.0

DIRECT TESTIMONY OF WILLIAM A. POWELL

DIVISION OF PUBLIC UTILITIES

UTAH DEPARTMENT OF COMMERCE

June 18, 1999

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LIST OF EXHIBITS

INTRODUCTION

Q: Please state your name and business address.

A: My name is William A. Powell Jr., but most people know me as Artie. My business office is at 160 E. 300 S., Salt Lake City, Utah, 84114.

Q: By whom are you employed and what is your official title?

A: I'm employed by the Utah State Department of Commerce, Division of Public Utilities. My official title is *Utility Economist*.

Q: Please summarize your education and other experience relevant to the current proceedings.

A: I earned a Doctorate degree in economics from Texas A&M University with emphasis in econometrics and public finance. I have published several papers in professional journals including, "A Decision Support System for In-sample Simultaneous Equations System Forecasting Using Artificial Neural Networks," published in *Decision Support Systems* (1994), and "Detecting Abnormal Returns Using the Market model with Pretested Data," published in the *Journal of Financial Research* (1996). Since 1987, I have taught undergraduate and graduate courses in economics, econometrics, and statistics. And I currently teach as an adjunct professor for Weber State University. For the past 3 ½ years I have been employed with the Division as an economist, and have attended several conferences on various aspects of regulation and restructuring in the electric industry. In the summer of 1996, I completed the NARUC Annual Regulatory Studies Program held at Michigan State University. A Vita detailing more of my experience is attached as Exhibit No. DPU 4.4.

SCOPE OF TESTIMONY

Q: For whom are you testifying?

A: I am testifying on behalf of the Division of Public Utilities (Division or DPU).

Q: What is the scope of your testimony?

A: My testimony will cover aspects dealing with:

- Foreign Currency Risk;
- The Public Utility Holding Company Act of 1935;

- The Cost of Capital; and
- The Acquisition Premium.

SUMMARY OF TESTIMONY

Q: Please summarize your testimony and major conclusions or recommendations.

A: Neither ScottishPower nor PacifiCorp's direct or supplemental testimony is overwhelming. In fact, the degree of unsubstantiated claims is enough to stagger all but the most sanguine supporter. In place of the usual quantitative evidence, ScottishPower encrusts their testimony with pleas to "trust" them. While trust may be a substantial ingredient in British regulatory practice, this trust, if it exists, would be the result of a long history between ScottishPower and British regulators. Given that a similar history has not been developed in Utah, caution may well prove to be the "better part of valor."[1] With some trepidation, therefore, I offer the following conclusions and recommendations.

Benefits of the Merger

First, it appears that ScottishPower is a financially stronger entity than PacifiCorp. And this could benefit PacifiCorp shareholders and ratepayers. Prior to the merger announcement, PacifiCorp was on a credit watch with a negative designation. After the merger announcement, PacifiCorp was placed on a credit watch with a positive designation. According to representatives at Standard and Poor's Financial Services, if the merger goes through, PacifiCorp's debt rating may be upgraded. Lower debt cost, if they materialize, would be a benefit of the merger. Given the capital structure ordered in the most recent rate case with PacifiCorp, one-half percentage point (50 basis points) in the weighted cost of capital is worth approximately $17 million in PacifiCorp's total revenue requirement.

Merger Concerns and Conditions

Second, it is possible that gains or losses on foreign transactions can occur. These transaction losses and gains are the effect of exchange rate changes on transactions denominated in a foreign

[1] William Shakespeare, *King Henry IV,* Act 5, Scene 4.

currency. The Financial Accounting Standards Board (FASB) has rules governing such transactions. Therefore, I propose that:

> ScottishPower follow the generally accepted accounting standards regarding foreign operations and exchange. Namely, FASB 52.

Third, the Public Utility Holding Company Act of 1935 (PUHCA) came about largely due to wide spread abuses and the inability of state commissions to regulate large, multi-jurisdictional holding companies. Therefore, in order to ensure that the Commission can effectively regulate the merged company, I propose that:

> PacifiCorp/ScottishPower agrees not to assert in any future Utah proceeding that the provisions of PUHCA or the related Ohio Power v FERC case preempt the Commission's jurisdiction over affiliated interest transactions and will explicitly waive any such defense in those proceedings.[2]

> In the event that PUHCA is repealed or modified, PacifiCorp/ScottishPower agrees not to seek any preemption under any subsequent modification or repeal of PUHCA until such time as the Commission can fully review its regulatory position or authority.[3]

> Within thirty days after the approval of the merger, PacifiCorp/ScottishPower should provide a detailed report indicating PacifiCorp's proportionate share of the Holding company's total assets, operating revenues, operating and maintenance expense, and number of employees. Subsequent to this initial report, this information should (could) be included as part of PacifiCorp's semi-annual filing with the Commission.[4]

> For ratemaking purposes, until otherwise approved by the Commission, a hypothetical capital structure will be used to determine the correct costs of

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[2] ScottishPower has agreed to this condition in Wyoming. See, *Wyoming Stipulation*, Condition Number 29.

[3] This condition is very similar to one ScottishPower has agreed to in Wyoming. See, *Wyoming Stipulation*, Condition Number 33.

[4] This is similar to a condition ScottishPower has already agreed to in Wyoming. See, *Wyoming Stipulation*, Condition Number 32.

> capital. The capital structure shall be constructed using a group of A-rated electric utilities comparable to PacifiCorp.[5]
>
> Until otherwise approved by the Commission in a separate proceeding, PacifiCorp shall maintain its own debt and, if outstanding, preferred stock.
>
> PacifiCorp shall apply to the Commission for approval of debt issuances.
>
> PacifiCorp and ScottishPower shall provide the Commission with a copy of any lobbying reports filed at the SEC.
>
> Additional conditions that ensure the Commission's ability to effectively regulate the new company are proposed by DPU witnesses Mary Cleveland (DPU Exhibit No. 2.0) and Ron Burrup (DPU Exhibit No, 3.0). Specifically, witness Mary Cleveland has proposals dealing with affiliate transactions, allocations, and access to books and records. Witness Ron Burrup has proposals dealing with reporting and filing requirements, dividends, and inter-company loans. I concur with these conditions.

Fourth, despite ScottishPower's promises, there is a risk that the cost of capital could increase as a result of the merger. While it is likely that PacifiCorp's debt cost will be lower with the merger than without, it can be argued that the cost of equity will be higher as a result of the merger. Therefore, I propose that:

> If ScottishPower is able to lower the costs of capital, then those savings shall be reflected in rates in a timely manner. If, however, the cost of capital increases as a result of the merger, ScottishPower's shareholders will bear that cost.

Fifth, ScottishPower has offered PacifiCorp shareholders a substantial premium as part of the merger agreement. Given current conditions, the premium is approximately $878 million. If just a portion of this premium were to find its way into rates, the promised $10 million in savings would be completely dwarfed. Therefore, I propose that:

[5] This condition is an adaptation of that proposed by ScottishPower. See, *ScottishPower, Direct Testimony of Robert D. Green*, February 26, 1999.

> Rates will be set based upon original and not revalued costs; any premium paid by ScottishPower for PacifiCorp stock will be disregarded for ratemaking purposes. Nor will ratepayers bear any costs of the transaction.[6]

Q: Does that conclude the summary of your direct testimony?

A: Yes it does.

FOREIGN CURRENCY RISK

Q: You indicated that your testimony would cover four areas: foreign currency risk, PUHCA, the cost of capital, and the acquisition premium. Will you please explain what you mean by foreign currency risk.

A: Certainly. Foreign currency risk refers to the potential losses or gains on transactions between ScottishPower and PacifiCorp. These transaction losses and gains are the effect of exchange rate changes on transactions denominated in a foreign currency. From PacifiCorp's perspective, the foreign currency is British pounds, and from ScottishPower's perspective, the foreign currency is American dollars.

Q: How do you propose to mitigate this risk?

A: PacifiCorp should follow generally accepted accounting principles in dealing with foreign transactions. Specifically, DPU witness Mary Cleveland (exhibit no. DPU 2.0) proposes that, cost allocations should be based on generally accepted accounting standards, and that an audit trail should be maintained such that all allocated costs can be identified. Furthermore, witness Cleveland proposes that, failure to adequately support any allocated cost may result in denial of its recovery in rates. I concur with these proposals.

Q: Are these reasonable proposals?

---

[6] This condition is an adaptation of that proposed by ScottishPower. See, *ScottishPower, Rebuttal Testimony of Robert D. Green*, Before the Oregon Public Utility Commission, UM 918, June 2, 1999.

A: Yes. The (American) Financial Accounting Standards Board (FASB) has a rule which covers foreign currency transactions: FASB 52. A summary of this rule is attached to my testimony as exhibit number DPU 4.2. Under this rule, foreign currency conversions or the losses and gains on foreign currency transactions are specifically identified. And, therefore, should be easy to track for ratemaking purposes.

Q: How are exchange rates determined?

A: In general, exchange rates are set in competitive markets for foreign currency. For every currency there is a market in which the exchange rate is set by the interaction of demand and supply for that currency. As events unfold in the respective economies, demand and supply for the currencies will fluctuate and, therefore, the exchange rates will change. This change or volatility can be quite dramatic.

Q: When you say dramatic, what do you mean?

A: The change in the exchange rate can be substantial, even over short periods of time. For example, over the five year period from February 26, 1980 to February 26, 1985, the exchange rate increased by 116%. Similar trends can be seen in the five and one half year period since 1993. The exchange rate fell from .71 on February 12, 1993 to .58 on October 8, 1998, a -18% change. While over the next seven month period the exchange rate increased by 6.9%. This volatility leads to the potential loses and gains mentioned above and, presumably, is one reason behind FASB 52.

PUBLIC UTILITY HOLDING ACT OF 1935

Q: What bearing does the Public Utility Holding Company Act (PUHCA) have on the proposed merger?

A: The merger applicants have stated that a merged holding company will be formed, registered with the Security Exchange Commission (SEC), and be regulated by the SEC under PUHCA like any other registered public utility holding company in the U.S. Regulation by the SEC could provide Utah ratepayers protection against abuses that state regulators may have little control over.

Alternatively, SEC methods designed to address abusive practices may work to the detriment of Utah ratepayers or PacifiCorp shareholders.

Q: What are your concerns?

A: In general, PUHCA came about as a result of wide spread abuse of the holding company structure and lack of effective regulation. PUHCA was designed to curb these abuses and provide state commissions, as well as federal regulators, the means to effectively regulate the large holding companies that came to dominate the electric industry after the turn of the century. Without PUHCA, or some similar legislation in place, it seems unlikely that the Commission could effectively regulate a large holding company, let alone one of international scope.

Q: How is PacifiCorp currently regulated?

A: From what I understand, PacifiCorp's retail operations as they relate to rates are regulated by six state commissions: California, Idaho, Oregon, Utah, Washington, and Wyoming. PacifiCorp's wholesale rates and transmission operations are regulated by the FERC. Each of the states conducts its own regulatory procedures. For instance, in Utah the DPU conducts a semi-annual audit of PacifiCorp and files a report with the Commission as to the reasonableness of rates. These procedures serve as the front line of the regulatory process for the states.

In addition, some inter-state agreements are sometimes used to coordinate regulatory activities between the states. These interstate agreements, however, are between the staffs of the various states and are not binding on the six state commissions. For example, since the last merger the staffs of the various states have participated in the PacifiCorp Inter-Jurisdictional Task Force on Allocations (PITA). Recently, the staff of the DPU determined that Utah's interests were no longer being met under the PITA agreement. The DPU (and other state agencies) recommended that the Commission adopt a plan to move to full rolled-in rates on a shorter time table than allowed under the PITA agreement. The Commission concurred and issued such an order in 1998.

Q: How will the regulation of PacifiCorp be effected if the merger is approved?

A: Under the current regulatory structure, state commissions are bound only by state law. However, assuming that ScottishPower will form a registered holding company, the SEC could assume authority over affiliate transactions, corporate structure, cost allocations, diversification, and financial transactions. SEC decisions are likely to be quite different than those made by the Commission and, therefore, could harm Utah ratepayers or PacifiCorp shareholders.

Q: But hasn't ScottishPower agreed not to claim preemption of affiliate transactions under PUHCA?

A: Yes it has. However, according to a Wyoming Consumer Advocate Staff witness, Lou Ann Westerfield, the decision rendered in the Ohio Power case "casts doubt on the ability of states to avoid being pre-empted"[7] by the SEC.

Q: If the SEC does preempt the states in their jurisdictional authority, wouldn't the states still have the right to intervene in SEC proceedings?

A: Yes they would. But how effective this would be is questionable. According to Wyoming Consumer Advocate Staff witness, Lou Ann Westerfield, the SEC has not held a hearing under PUHCA in the last eleven years. Instead of hearings, "the SEC staff makes its recommendations . . . based on the exchange of paper pleadings . . . [bypassing] the traditional evidentiary process."[8]

Even if these concerns turn out to be unwarranted, we are still faced with the possible repeal of PUHCA in the near future. Since President Carter's administration there has been a strong movement in the United States toward deregulation. So far we have witnessed the deregulation of the airline, trucking, and banking industries. We have also seen limited deregulation in both the telecommunications and natural gas industries. Furthermore, and more to the point at hand, there is a strong movement in the United States to restructure the electric industry. (Both the Energy Policy Act of 1992 and the Telecommunications Act of 1996 allow exemptions under PUHCA).

Q: What is it that PUHCA provides for the states?

A: According to a report prepared by the Energy Information Administration (EIA),[9] major abuses of

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[7] See, Direct testimony of Lou Ann Westerfield, Wyoming Consumer Advocate Staff, Docket No. 20000-EA-98-141, pp. 9, 29-31.

[8] See, Direct testimony of Lou Ann Westerfield, Wyoming Consumer Advocate Staff, Docket No. 20000-EA-98-141, p. 31.

[9] *The Public Utility Holding Company Act of 1935: 1935 - 1992*, Energy Information Administration, U.S. Department of Energy, DOE/EIA-0563, January 1993.

the holding company system lead to passage of the Public Utilities Holding Company Act of 1935. EIA classifies the abuse in five areas: (1) Abuses of the holding company structure, (2) unwarranted inflation of securities and capital assets, (3) inappropriate inter-company financial practices and transactions, (4) excessive fees for services, and (5) destructful competition for control of strategic operating companies. As I mentioned above, PUHCA provided safeguards against these abuses and also provided state and federal regulators the means to effectively regulate large holding companies.

Q: Will you please summarize each of these five abuses?

A: Certainly.

ABUSE 1: ABUSE OF THE HOLDING COMPANY STRUCTURE

"Holding companies," according to EIA, "were established through the process of pyramiding." Pyramiding is defined as stacking or interposing one or more sub-holding companies between the parent holding company and its operating companies. EIA sites two major reasons for pyramiding. First, by manipulating the capital structures of the various subholding companies, control of the operating companies could be achieved with relatively small investments. Second, small increases in the value of the operating company's assets dramatically increases the amount of income accruing to the holding company.

"The result of pyramiding," again according to EIA, "was that the . . . holding company's principal interest was in the increased profits of the operating companies. . . . Customer service and reliability were secondary considerations. In addition, consumers often paid rates which were felt to be unfair because [ratepayers] were, in effect, subsidizing speculative ventures."

The aforementioned EIA report provides an excellent example of how this abuse might work.

ABUSE 2: UNWARRANTED INFLATION OF SECURITIES AND CAPITAL ASSETS

Another common practice directly linked to pyramiding is the inflation or writeup of securities and capital assets. These writeups are primarily the result of (1) inflating constructing cost; (2) internally selling subholding and operating companies shares above their market value; and (3) overly optimistic projections of savings and earning power. The primary beneficiaries of these practices are the shareholders of the holding company.

ABUSE 3: INTER-COMPANY FINANCIAL PRACTICES AND TRANSACTIONS

Prior to the passage of PUHCA it was argued that the holding company could "milk" the operating companies in at least three ways:

- By lending money to the operating company at above market rates.
- By requiring unjustifiably high dividends from the operating company.
- By borrowing money from the operating company in exchange for an unsecured note.

ABUSE 4: EXCESSIVE FEES FOR SERVICES

By virtue of its control over the operating company, the holding company is in a position to both require the purchase of its services and to charge excessive fees for services rendered. Ratepayers are harmed when the excessive fees find their way into rates.

ABUSE 5: COMPETITION FOR CONTROL OF STRATEGIC OPERATING COMPANIES

To ensure their position, holding companies sought to purchase potential competitors. The increased competition naturally drove up the price of the securities of the targeted company. In order to purchase the targeted companies, holding companies turned to investment bankers. The investment bankers, whose primary interest was in making a profit, encouraged the holding companies to use debt and fixed return preference shares to finance the purchase. This practice contributed to the "financial instability of the holding companies by driving up their debt to equity ratios and saddling them with significant fixed costs."

Q: What remedies does PUHCA provide these abuses?

A: The afore mentioned EIA report classifies the provisions of PUHCA into seven categories: (1) Regulation of Security Issues, (2) Acquisition of Securities, (3) Limitations on Intra-system Transactions, (4) Accounts, Records, and Filing Reports, (5) Limitations on Political Activity; (6) Elimination of Uneconomical Holding Companies; and (7) Removal of Needless Complexities.

Q: Will you please summarize these remedies?

A: Certainly.

REMEDY 1: REGULATION OF SECURITY ISSUES

In addition to complying with any issuance restrictions imposed by the state in which the holding company was organized, PUHCA prohibited the holding company from issuing any securities without receiving prior approval from the SEC. PUHCA also provides guidelines for the SEC to follow in approving security issuances:

- Approved securities should not create an improper risk for the holding company.
- Fees and commissions associated with the sale of securities should be reasonable.
- Approved securities should not be detrimental to the public interest, utility investors, or consumers.
- Only those securities which are "reasonably adapted" to the existing holding companies securities' structure were to be approved.
- Approved securities should reflect the earning power of the holding company, be necessary, and promote economic and efficient operation of the holding company.

REMEDY 2: ACQUISITION OF SECURITIES

In addition to complying with any restrictions imposed by the state in which the holding company was organized, PUHCA prohibited the holding company from acquiring any securities without receiving prior approval from the SEC. PUHCA also provides guidelines for the SEC to follow in approving security acquisitions:

- The acquisition would not unduly complicate the capital structure of the holding company.
- The holding company must demonstrate that the acquisition would bring about a more efficient and integrated utility.
- Fees and commissions associated with the acquisition would be reasonable and reflect the earning potential of the utility's assets.
- Any approved acquisition would not lead to a concentration (i.e., market power) that would be harmful to the general public, investors, or ratepayers.

REMEDY 3: LIMITATIONS ON INTRA-SYSTEM TRANSACTIONS

PUHCA specifically forbids some of the activities that were meant to "milk" the operating companies. Operating companies are not permitted to:

- Make unsecured loans to the holding company.
- Pay excessive dividends to the holding company.

In addition, holding companies are restricted to providing only engineering and managerial services to the operating company, and these services must be provided at cost.

REMEDY 4: ACCOUNTS, RECORDS, AND FILING REPORTS

PUHCA authorizes the SEC to require such reports as it sees are necessary to promote the public interest and to protect investors and consumers.

REMEDY 5: LIMITATIONS ON POLITICAL ACTIVITIES

Holding companies are prohibited from promoting candidates for public office, or supporting political parties or their agencies. Holding companies must also report all political lobbying activities to the SEC.

REMEDY 6: ELIMINATION OF UNECONOMICAL HOLDING COMPANIES

The holding company must be integrated – interconnected or at least capable of interconnection – and operated as a consolidated system. In addition to promoting efficiency, the purpose of this provision was to restrict the holding company to operations within only one state or a few contiguous states. This would, hopefully, promote effective regulation by the state commissions.

REMEDY 7: THE REMOVAL OF NEEDLESS COMPLEXITIES

PUHCA effectively limited the corporate structure to two layers of holding companies. Furthermore, PUHCA provided that the voting power of security holders be fairly distributed.

In summary, let me quote at length from the EIA report:

> What permitted the growth of the utility holding companies was basically the lack of effective regulation. States were unwilling or unable to regulate the

> large holding companies that came to dominate the utility business after the turn of the century. The holding company approach led to pyramiding. The result of pyramiding was the extensive use of bonds and preference shares which paid fixed returns as a means of financing the acquisition of operating companies and other holding companies. This growth in debt and fixed interest payments required to service the debt made the holding companies more vulnerable to the business cycle.
>
> Holding companies were also felt to have abused the system by the use of questionable Inter-company transactions and the charging of exorbitant service fees to subsidiary companies. The excessive fees . . . were then capitalized into the accounts of the holding company which in turn inflated the operating utility's book value and caused the rates charged to the customers to increase. The result was unrealistic prices for the holding companies securities. The desire of the holding companies to continue to acquire operating utilities and other holding companies caused them to purchase these entities at prices well above the market value.[10]

Q: Do you have any proposals to ensure that the remedies included in PUHCA continue even if PUHCA is repealed, and to ensure that state regulation is not preempted by less effective federal remedies?

A: Yes I do.

First, to mitigate abuse of the holding company structure and unwarranted inflation of securities and capital assets, I propose that,

> For ratemaking purposes, until other wise approved by the Commission, a hypothetical capital structure will be used to determine the correct costs of capital. The capital structure shall be constructed using a group of A-rated electric utilities comparable to PacifiCorp.

---

[10] *The Public Utility Holding Company Act of 1935: 1935 - 1992*, Energy Information Administration, U.S. Department of Energy, DOE/EIA-0563, January 1993, p. 11.

> Within thirty days after the approval of the merger, PacifiCorp shall provide a detailed report indicating PacifiCorp's proportionate share of the ScottishPower's total assets, operating revenues, operating and maintenance expense, and number of employees. Subsequent to this initial report, this information should (could) be included as part of PacifiCorp's semi-annual filing with the Commission.[11]

> Until approved by the Commission in a separate proceeding, PacifiCorp shall maintain its own debt and, if outstanding, preferred stock.

> PacifiCorp shall apply to the Commission for approval of debt issuances.

> In addition to these proposals, DPU witness Ron Burrup (Exhibit Number DPU 3.0) proposes, and I concur, that,

> The merged company shall file annually a five year financial plan and forecast of financial condition for the total company, PacifiCorp division, and the Utah jurisdiction.

Second, to mitigate abuse of inter-company financial practices and transactions and excessive fees for services, I concur with witness Ron Burrup (exhibit number 3.0) that,

> For two years following the merger, PacifiCorp shall file a cash flow summary with its dividend report, showing that service will not be impaired by payment of the dividend.

> PacifiCorp and ScottishPower shall apply to the Commission for approval of intra-company loan agreements. For two years following the merger, PacifiCorp shall file a cash flow summary (or other evidence) with its dividend report, showing that service will not be impaired by payment of

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[11] This is similar to a condition ScottishPower has already agreed to in Wyoming. See, *Wyoming Stipulation*, Condition Number 32.

the dividend.

In addition to this proposal, DPU witness Mary Cleveland (Exhibit Number DPU 2.0) proposes, and I concur, that,

ScottishPower/PacifiCorp should be required to notify the Utah Commission subsequent to ScottishPower plc's Board approval and as soon as practicable following any public announcement of and acquisition of a regulated or non-regulated business representing 5% or more of the market capitalization of ScottishPower plc.

The Applicants should be required to provide notification of and file for Commission approval of the divestiture, spin-off, or sale of any integral utility assets or functions.

The Merged Company shall notify the Commission, and provide sufficient information and documentation to the Commission, prior to the implementation of plans (1) to form an affiliate entity for the purpose of transacting business with the electric divisions of PacifiCorp, (2) to commence new business transactions between an existing affiliate and the electric utility divisions of PacifiCorp, (3) to dissolve an affiliate which has transacted any substantial business with such divisions, (4) to enter into new business ventures or expand existing ones, or (5) to merge combine, transfer stock or assets of any part or all of the Merged Company.

The Merged Company shall provide notification of all asset transfers to or from PacifiCorp, its affiliates, or subsidiaries in accordance with current Public Service Commission (PSC) rules (see in particular PSC R750-401).

Establish agreed upon procedures by which Division staff can have access to documentation supporting the purpose and/or circumstances attributable to costs charged to PacifiCorp.

The holding company(s) and subsidiaries' employees, officials, directors, or agents shall be available to testify before the Utah Commission to provide information relevant to matters within the jurisdiction of the Utah Commission.

The Utah Commission shall establish procedures by which the Public Service Commission and Division staffs, or their authorized agents can obtain needed access to subsidiary books and records, other relevant documents, data and records. Failure to provide adequate supporting documentation of costs may result in those costs being denied rate recovery. Requests by the Utah Commission, the Division, or their authorized agents shall be deemed presumptively valid, material and relevant, with the burden falling to ScottishPower/PacifiCorp to prove otherwise. ScottishPower/PacifiCorp shall reserve the right to challenge any such request before the Utah Commission and shall have the burden of demonstrating that any such request is not valid, material or relevant. In addition, ScottishPower shall pay for the expense incurred by Utah regulatory personnel in accessing corporate records and personnel located outside of the state of Utah.

Finally, to ensure against preemption of Commission authority, I propose that,

PacifiCorp/ScottishPower agrees not to assert in any future Utah proceeding that the provisions of PUHCA or the related Ohio Power v FERC case preempt the Commission's jurisdiction over affiliated interest transactions and will explicitly waive any such defense in those proceedings.[12]

In the event that PUHCA is repealed or modified, PacifiCorp/ScottishPower agrees not to seek any preemption under any subsequent modification or repeal of PUHCA until such time as the Commission can fully review its

[12] ScottishPower has agreed to this condition in Wyoming. See, *Wyoming Stipulation*, Condition Number 29.

regulatory position or authority.[13]

PacifiCorp and ScottishPower shall provide the Commission with a copy of any lobbying reports filed at the SEC.

Q: Are these reasonable conditions for the merger?

A: Yes, I believe they are.

Despite the "good old-boy" feeling projected by ScottishPower, history has taught us that there are strong incentives for firms to abuse the holding company structure. I can't help but recall the words of the father of economics and philosopher of the Scottish Enlightenment, Adam Smith, who said:

> People of the same trade seldom meet together, even for the merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices.[14]

These conditions provide several benefits. First, they remove, or at least expose, the incentives for abuse of the multi-tiered holding company structure. Second, it is not ScottishPower's stated intent to circumvent such requirements as they intend to be regulated as a registered public utility holding company. Finally, in combination with the other conditions proposed by the Division, they will provide the Commission with means to effectively regulate PacifiCorp.

Q: Are these conditions adequate to ensure that the Commission can effectively regulate PacifiCorp in the future?

A: In general, yes. However, the SEC still needs to look at this merger and grant its approval.

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[13] This condition is very similar to one ScottishPower has agreed to in Wyoming. See, *Wyoming Stipulation*, Condition Number 33.

[14] Adam Smith, *An Inquiry Into the Nature and Causes of the Wealth of Nations*, The Glasgow Edition, Liberty Classics, 1981, p. 145

Therefore, the Division reserves the right to revisit these issues in the event that either: (1) Conditions of the merger imposed by the SEC are either in conflict with conditions proposed by the Division or make it difficult to effectively regulate PacifiCorp, (2) Scottish Power requests an exemption, either in whole or part, to the provisions set out in PUHCA, or (3) PUHCA is repealed or modified.

COST OF CAPITAL

Q: What concerns do you have relating to the cost of capital?

A: The cost of capital may actually increase as a result of the merger.

ScottishPower indicates that they expect the cost of capital to be lower in the long-run than what would be the case if the merger does not take place.[15] ScottishPower has, however, offered little or no evidence to support their optimism. In the absence of such evidence, one must take seriously arguments that support the possibility that the cost of capital may actually go up after – as result of – the merger.

One such argument is that the U.K. electric market, as a result of deregulation, is more competitive than the U.S. market and, thus, inherently more risky. If investors actually impute relatively more risk to the U.K. market, then, according to economic and financial theory, they will expect or demand a higher return on their investment. If, therefore, the cost of capital for the combined firm is simply a blend of the current capital costs of PacifiCorp and ScottishPower, PacifiCorp's effective cost of capital could actually increase.

Q: Do you have any proposals regarding the cost of capital?

A: Yes. If ScottishPower is able to lower the costs of capital, then those savings shall be reflected in rates in a timely manner. If, however, the cost of capital increases as a result of the merger, ScottishPower's share holders will bear that cost.

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[15] See Company's Response to Wyoming Consumer Advocate Staff, Third Data Request, Question No. 82 .

Q: Is there any evidence to support your contention that the cost of capital could change, or possibly increase, as a result of the merger?

A: Yes there is. However, since the weighted cost of capital is determined by both equity and debt costs, I would like to answer that question in two corresponding parts.

PART I: EQUITY

The simple or basic Discounted Cash Flow (DCF) model indicates that the expected or required return on an investment is equal to the dividend yield plus the rate of growth in the dividend. That is,

$$\begin{aligned} \textit{Required Return} &= \textit{Dividend Yield} + \textit{Dividend Growth} \\ &= \frac{D}{P} + g \end{aligned}$$

where D is the dividend (usually defined as being paid in the next period), P is the current stock price, and g is the dividend growth rate. Generally speaking, the riskier an investment is, the greater will be the required rate of return.

Using information gathered from several sources,[16] the difference in the required return (on equity) for ScottishPower and PacifiCorp may be as great as 5.6%, which indicates that investors view ScottishPower as an inherently riskier investment than PacifiCorp.

Another indication of the comparative risk of PacifiCorp and ScottishPower, and thus the required return sought by investors, can be inferred from the Capital Asset Pricing Model (CAPM).

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[16] Dividend yields for both PacifiCorp and Scottish (5.78% and 4.52% respectively) were gathered from Yahoo Finance, June 5, 1999. Since PacifiCorp's dividend has not change since, at least, before June 1994, PacifiCorp's dividend growth rate was assumed to be zero. ScottishPower's estimated dividend growth rate, 6.84%, was calculated from actual dividends as reported on ScottishPower's Web site: http://www.scottish.power.plc/aboutus, *Five Year Financial Summary.*

According to the underlying theory,[17] the systematic risk of a stock's return can be measured by the beta (β) coefficient in the model

$$k_e = r_f + \beta(r_m - r_f)$$

where k_e is the return required by investors, r_f is a risk-free rate of return, and r_m is the market rate of return as measured by a well diversified portfolio of stocks. Thus, beta measures the relative risk or variability of a stock to that of a well diversified portfolio of stocks.

Publicly available information indicates that ScottishPower's beta coefficient may be as much as five times that of PacifiCorp's.[18] This also indicates that investors view ScottishPower as a riskier investment than PacifiCorp. Thus, there is a potential that PacifiCorp's cost of equity capital could increase as a result of the merger.

PART II: DEBT

Prior to the merger announcement, PacifiCorp was on "credit watch" with a "negative" designation. According to Standard and Poor's own definition, a credit watch,

> Highlights the potential direction of a short — or long – term rating. . . . Ratings appear on credit watch when . . . an event or a deviation from an expected trend occurs and additional information is necessary to evaluate the current rating. A listing, however, does not mean a rating change is inevitable.

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[17] The following discussion of the CAPM is adopted from William F. Shughart, William F. Chappell, and Rex L. Cottle, *Modern Managerial Economics*, South-Western Publishing Company, Cincinnati, Ohio, 1994.

[18] As of June 7, 1999, Market Guide reported PacifiCorp's β as 0.19 (See Market Guide, Comparison Report for PacifiCorp, http://yahoo.marketguide.com/mgi/ratio/6820N.html). The value of ScottishPower's β, 0.91, was obtained from, *Review of Public Electric Suppliers 1998-2000, Distribution Price Control Review*, Offer, May, 1997.

A positive designation, again according to Standard and Poor's, means that a rating may be increased while a negative designation means that a rating may be decreased. In other words, absent the merger announcement, PacifiCorp's debt rating would likely have decreased, increasing the cost of debt financing.

At or near the time of the merger announcement, however, Standard and Poor's rating service placed PacifiCorp on "credit watch" with a "positive" designation, while ScottishPower was placed on credit watch with a negative designation. According to recent news releases, Standard and Poor's affirms both ratings. Both PacifiCorp and ScottishPower are to remain on credit watch, PacifiCorp with a positive designation and ScottishPower with a negative designation. Standard and Poor's currently rates ScottishPower's long term debt at "A+" and PacifiCorp's at "A." If Standard and Poor's does re-rate both companies, the likely outcome would be an "A" or "A+" rating for the combined company. In any event, Standard and Poor's believes that "its long-term ratings on ScottishPower will not fall below single-'A'"[19] if the merger is completed. We can expect, therefore, that PacifiCorp's debt rating will, at least in the short-run, stay the same or improve slightly if the merger goes forward. If the merger does not take place, it is likely that, in the absence of any changes on PacifiCorp's part, PacifiCorp's bond rating will be downgraded.[20]

How the potential changes in the cost of equity and debt play out after the merger is uncertain at this point. If debt costs go down, but equity costs go up, then the overall cost of capital may decrease, increase, or stay the same depending on the relative weight assigned to each. Since ScottishPower has not presented convincing evidence that it can lower the cost of capital after the merger, it seems reasonable to hold the shareholders at risk for increases in the weighted cost of capital that result from the merger.

Q: Can you quantify the effect of a change in the weighted cost of capital?

A: Every 100 basis points in equity return is worth approximately $17 million in PacifiCorp's revenue

[19] "S&P affirms, may still cut, ScottishPower," Reuter's News Release, Yahoo Finance, June 7, 1999, http://biz.yahoo.com/rf/990607.

[20] Raymond Leung, a rating analyst with Standard and Poor's New York office, confirmed over the phone (June 7, 1999) that PacifiCorp's bond rating would likely be downgraded absent the merger.

requirement. In other words, if the cost of equity goes up by 1%, PacifiCorp's revenue requirement will increase by about $17 million, an amount that easily dwarfs the $10 million in savings promised by ScottishPower. An increase in equity costs, however, could potentially be offset by a corresponding decrease in the cost of debt.

For example, suppose we have a capital structure that is 49% debt and 51% equity with costs 7.5% and 10.5% respectively. The weighted cost of capital for this example is equal to 9.04%.

Table 1

Weighted Cost of Capital

	Percent	Cost	Weighted
debt	49.00%	7.50%	3.68%
equity	51.00%	10.50%	5.36%
			9.04%

Assuming the capital structure does not change, if the cost of equity changes, the offsetting change in the cost of debt is given by

$$\begin{aligned} \Delta C_d &= -\frac{E}{D} * \Delta C_e \\ &= (-1.41) * \Delta C_e \end{aligned}$$

where Δ is read as "the change in," C_e is the cost of equity, C_d is the cost of debt, D is the percent of debt, and E is the percent of equity. If the cost of equity increases by 1%, to prevent the weighted cost of capital changing, the cost of debt must decrease by 1.41%. If the cost of debt decreases by more than 1.41%, the weighted cost of capital would likewise decrease. If the cost of debt decreases by less than the 1.41%, the weighted cost of capital would increase as a result of the increase in the cost of equity. Without an offsetting change in the cost of debt, a 1% increase in the cost of equity is equivalent to a 0.51% (1%*51%) increase in the weighted cost of capital.

Using the currently authorized capital structure, and assuming the preferred stock percentage and cost stay the same, every 1% increase in the cost of equity would have to be met by a 1.02% decrease in the cost of debt to maintain the weighted cost of capital at the currently authorized rate of 8.84%. If, as a result of the merger, PacifiCorp's debt financing costs remain about the same as they are now, then a 1% increase in equity cost would mean a 0.476% increase in the weighted cost of capital. Again, a 0.476% increase in the weighted cost of capital would be equivalent to a $17 million increase in PacifiCorp's revenue requirement. Any decrease in the cost of debt would offset any potential increases in the cost of equity.

ACQUISITION PREMIUM

Q: What concerns do you have concerning the acquisition premium?

A: According to current market conditions, the acquisition premium may be as much as or more than $878 million. If even a small portion of this amount were to find its way into rates, the $10 million in promised savings would be dwarfed.

Q: Do you have a proposal regarding the acquisition premium?

A: Just that which ScottishPower has stated:

> Rates will continue to be set based upon the original (not revalued) costs, and any premium paid by ScottishPower for PacifiCorp stock will be disregarded for ratemaking purposes. . . They will never bear any costs associated with it. Nor will ratepayers bear any costs of this transaction.[21]

Q: Do you believe this is a reasonable condition?

A: As long as ScottishPower commits to making all the necessary books and records available to

[21] See, Robert D. Green, "ScottishPower Rebuttal Testimony of Robert D. Green," Before the Public Utility Commission of Oregon, June 2, 1999, UM 918.

regulators, I believe this is a reasonable condition.

Q: You indicated that the acquisition premium may be as much as $878 million. How did you come to that figure?

A: The acquisition premium is defined as any price paid in excess of market value of PacifiCorp's stock. The premium is calculated as the difference between the purchase price of PacifiCorp's outstanding shares minus the market value of PacifiCorp's outstanding shares. ScottishPower has proposed purchasing PacifiCorp's outstanding shares at a rate of .58 American Depository Shares (ADS) for each PacifiCorp share. Each ADS represents four ordinary shares. So the swap is equal to 2.32 ScottishPower shares for each PacifiCorp outstanding share. Therefore, we can write the premium as,

$$Prem = \left[0.58 * Price_{sp} - Price_{pc}\right] * Shares$$

where $Price_{sp}$ is the price of the ADS; $Price_{pc}$ is the price of PacifiCorp's common shares; and Shares is the number of PacifiCorp's outstanding shares. Thus there are three factors that influence the premium: the two share prices and the total number of shares outstanding.

On the day the merger was announced, December 7, 1998, PacifiCorp's share price was $19.50, ScottishPower's ADS price was $43.50. With approximately 285,000,000 outstanding shares at the time of the merger announcement, the premium would be $1.6 billion. By June 4, 1999, however, both share prices had fallen dramatically. The closing prices for PacifiCorp and ScottishPower were, respectively, $18.69 and $37.31. Given 297,334,000 current outstanding shares, the premium would be $878 million.

Table 2

Acquisition Premium

	SP ADS Price	PC Stock Price	Shares Outstanding	New PC Stock Price	Premium Per Stock	Premium Percent	Premium Total
12/7/98	$43.50	$19.50	285,000,000	$25.23	$5.73	29.38%	$1,633,050,000
6/4/99	$37.31	$18.69	297,334,000	$21.64	$2.69	15.81%	$878,250,303

Q: Can the acquisition premium increase or decrease between now and the time the merger is likely to close?

A: Yes. However, the difference in ScottishPower's stock price and that of PacifiCorp's should remain fairly constant until the merger is completed. Therefore, I assume that the magnitude of the premium will remain in the neighborhood of $800 million to $1 billion.

Q: Can you explain why this may be the case?

A: Yes. Stock prices reflect the investors expectations about the present value of future cash flows. Since ScottishPower has announced their intention of purchasing PacifiCorp's Stock at .58 ADS to 1 share of PacifiCorp stock, and since some time has intervened since the announcement, investors have incorporated the information in their valuations. Sellers of PacifiCorp stock will demand, as part of the price of the stock, the premium they could receive if they held onto the stock. Likewise buyers of PacifiCorp stock should be willing to pay a price that includes the known premium. The two stocks then, should, after some initial adjustments, begin to track one another. This is apparently what is happening.

Immediately after the merger announcement, both share prices briefly increased, but then began to fall within a matter of weeks. This trend continued until around the first of May when both share prices began to increase. (See DPU Exhibit 4.3, Figures 1 and 2) Interestingly, but not surprisingly, since the announcement the prices of the two stocks have been closely tracking one another. Over the five month period prior to the merger announcement, the correlation coefficient for the two stock's prices was -0.44, after the announcement, the correlation increased to 0.95. Without any further announcements, this trend or correlation in the two prices will continue until the merger is closed.

Table 3

Stock Price Correlation: PacifiCorp and ScottishPower

	Before the Merger Announcement July 1, 1998 to December 4, 1998	**After the Merger Announcement December 7, 1998 to June 4, 1999**
Correlation Coefficient	-0.44	0.95

The number of outstanding shares, however, may change over the intervening period. As this occurs, the total premium will also change. I'm assuming that the change in the number of outstanding shares will not change by much and, thus, the total premium will remain around the current $878 million.

Q: In your opinion, does the acquisition premium have any implications for stranded costs?

A: Yes, I believe it does.

A stock's price, as I indicated before, reflects the investors expectations about the present value of future cash flows. If ScottishPower is willing to pay a premium for PacifiCorp's stock, the implication is that they anticipate earnings to be greater in the future than is indicated by the current price (i.e., absent the merger) of PacifiCorp's stock. This is essentially the argument put forth by a couple of authors in a recent article:

> Since most utilities already enjoy a market price that is 150% or more above book value, merger-related premiums clearly contemplate future earnings from other than regulated operations, where profits are limited by

book value.[22]

In the present case, the anticipated future earnings may be a simple expansion by ScottishPower into another regulated market, as much as it is in anticipation of future restructuring in the United States.

In either case, the willingness of ScottishPower to pay an acquisition premium may be an indication that PacifiCorp would not face any stranded costs if the electric industry were restructured.

As is well known, however, stranded costs is a very controversial topic and need not be decided here in these proceedings.

Q: Does this conclude your direct testimony?

A: Yes it does.

[22] Robert P. Knickerbocker and Florence K.S. Davis, "The Acquisition Premium: A U-Turn in Merger Policy?," *Public Utilities Fortnightly*, May 15, 1999, p. 45.

ATTACHMENTS

DPU EXHIBIT NUMBER DPU 4.1:

MERGER BENEFITS AND PROPOSED MERGER CONDITIONS

Merger Benefits

It appears that ScottishPower is a financially stronger entity than PacifiCorp. And this could benefit PacifiCorp shareholders and ratepayers. Prior to the merger announcement, PacifiCorp was on a credit watch with a negative designation. After the merger announcement, PacifiCorp was placed on a credit watch with a positive designation. According to representatives at Standard and Poor's Financial Services, if the merger goes through, PacifiCorp's debt rating may be upgraded. Lower debt cost, if they materialize, would be a benefit of the merger. Given the capital structure ordered in the most recent rate case with PacifiCorp, one-half percentage point (50 basis points) in the weighted cost capital is worth approximately $17 million in PacifiCorp's total revenue requirement.

Concerns and Proposed Merger Conditions

Concern: Foreign Currency Risk

It is possible that gains or losses on foreign transactions can occur. These transaction losses and gains are the effect of exchange rate changes on transactions denominated in a foreign currency. The Financial Accounting Standards Board (FASB) has rules governing such transactions.

Proposed Condition

ScottishPower shall follow the generally accepted accounting standards regarding foreign operations and exchange. Namely, FASB 52.

Concern: PUHCA

Proposed Conditions

The Public Utility Holding Company Act of 1935 (PUHCA) came about largely due to wide spread abuses and the inability of state commissions to regulate large, multi-jurisdictional holding companies.

For ratemaking purposes, a hypothetical capital structure will used to determine the correct costs of capital. The capital structure shall be constructed using a group of A-rated electric utilities comparable to PacifiCorp.

Within thirty days after the approval of the merger PacifiCorp/ScottishPower should provide a detailed report indicating PacifiCorp's proportionate share of the Holding company's total assets, total operating revenues, operating and maintenance expense, and number of employees. Subsequent to this initial report, this information should (could) be included as part of PacifiCorp's semi-annual filing with the Commission.

Until approved by the Commission in a separate proceeding, PacifiCorp shall maintain its own debt and, if outstanding, preferred stock.

PacifiCorp shall apply to the Commission for approval of debt issuances.

PacifiCorp/ScottishPower agrees not to assert in any future Utah proceeding that the provisions of PUHCA or the related Ohio Power v FERC case preempt the Commission's jurisdiction over affiliated interest transactions and will explicitly waive any such defense in those proceedings.

In the event that PUHCA is repealed or modified, PacifiCorp/ScottishPower agrees not to seek any preemption under any subsequent modification or repeal of PUHCA until such time as the Commission can fully review its regulatory position or authority.

PacifiCorp and ScottishPower shall provide the Commission with a copy of any lobbying reports filed at the SEC.

Concern: Cost of Capital

Despite ScottishPower's promises, there is a risk that the cost of capital could increase as a result of the merger.

Proposed Conditions

If ScottishPower is able to lower the costs of capital, then those savings shall be reflected in rates in a timely manner. If, however, the cost of capital increases as a result of the merger, ScottishPower's shareholders will bear that cost.

Concern: Acquisition Premium

Sottish Power has offered PacifiCorp shareholders a substantial premium as part of the merger agreement. Given current conditions, the premium is approximately $878 million. If just a portion of this premium were to find its way into rates, the promised $10 million in savings would be completely dwarfed.

Proposed Conditions

Rates will be set based upon original and not revalued costs; any premium paid by ScottishPower for PacifiCorp stock will be disregarded for ratemaking purposes. Nor will ratepayers bear any costs of the transaction.

DPU EXHIBIT NUMBER DPU 4.2:

FASB NO. 52 , *FOREIGN CURRENCY TRANSLATION*[23]

"Application of this Statement will affect financial reporting of most companies operating in foreign countries. The differing operating and economic characteristics of varied types of foreign operations will be distinguished in accounting for them. Adjustments for currency exchange rate changes are excluded from net income for those fluctuations that do not impact cash flows and are included for those that do. The requirements reflect these general conclusions:

"The economic effects of an exchange rate change on an operation that is relatively self-contained and integrated within a foreign country relate to the net investment in that operation. Translation adjustments that arise from consolidating that foreign operation do not impact cash flows and are not included in net income.

"The economic effects of an exchange rate change on a foreign operation that is an extension of the parent's domestic operations relate to individual assets and liabilities and impact the parent's cash flows directly. Accordingly, the exchange gains and losses in such an operation are included in net income.

"Contracts, transactions, or balances that are, in fact, effective hedges of foreign exchange risk will be accounted for as hedges without regard to their form.

"More specifically, this Statement replaces FASB Statement No. 8, *Accounting for the Translation of Foreign Currency Transactions and Foreign Currency Financial Statements,* and revises the existing accounting and reporting requirements for translation of foreign currency transactions and foreign currency financial statements. It presents standards for foreign currency translation that are designed to (1) provide information that is generally compatible with the expected economic effects of a rate change on an enterprise's cash flows and equity and (2) reflect in consolidated statements the financial results and relationships as measured in the primary currency in which each entity conducts its business (referred to as its "functional currency").

"An entity's functional currency is the currency of the primary economic environment in which that entity

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[23] *Summary of Statement No. 52 Foreign Currency Translation*, Financial Accounting Standards Board, http://www.rutgers.edu/Accounting/raw/fasb/.

operates. The functional currency can be the dollar or a foreign currency depending on the facts. Normally, it will be the currency of the economic environment in which cash is generated and expended by the entity. An entity can be any form of operation, including a subsidiary, division, branch, or joint venture. The Statement provides guidance for this key determination in which management's judgment is essential in assessing the facts.

"A currency in a highly inflationary environment (3-year inflation rate of approximately 100 percent or more) is not considered stable enough to serve as a functional currency and the more stable currency of the reporting parent is to be used instead.

"The functional currency translation approach adopted in this Statement encompasses:

"14.Identifying the functional currency of the entity's economic environment

"15.Measuring all elements of the financial statements in the functional currency

"16.Using the current exchange rate for translation from the functional currency to the reporting currency, if they are different

"17.Distinguishing the economic impact of changes in exchange rates on a net investment from the impact of such changes on individual assets and liabilities that are receivable or payable in currencies other than the functional currency

"*Translation adjustments* are an inherent result of the process of translating a foreign entity's financial statements from the functional currency to U.S. dollars. Translation adjustments are *not* included in determining net income for the period but are disclosed and accumulated in a separate component of consolidated equity until sale or until complete or substantially complete liquidation of the net investment in the foreign entity takes place.

"*Transaction gains and losses* are a result of the effect of exchange rate changes on transactions denominated in currencies other than the functional currency (for example, a U.S. company may borrow Swiss francs or a French subsidiary may have a receivable denominated in kroner from a Danish customer). Gains and losses on those foreign currency transactions are generally included in determining net income for the period in which exchange rates change unless the transaction hedges a foreign currency commitment or a net investment in a foreign entity. Intercompany transactions of a long-term investment nature are considered part of a parent's net investment and hence do not give rise to gains or losses."

DPU EXHIBIT NUMBER DPU 4.3:

STOCK PRICES FOR SCOTTISHPOWER AND PACIFICORP

Figure 1

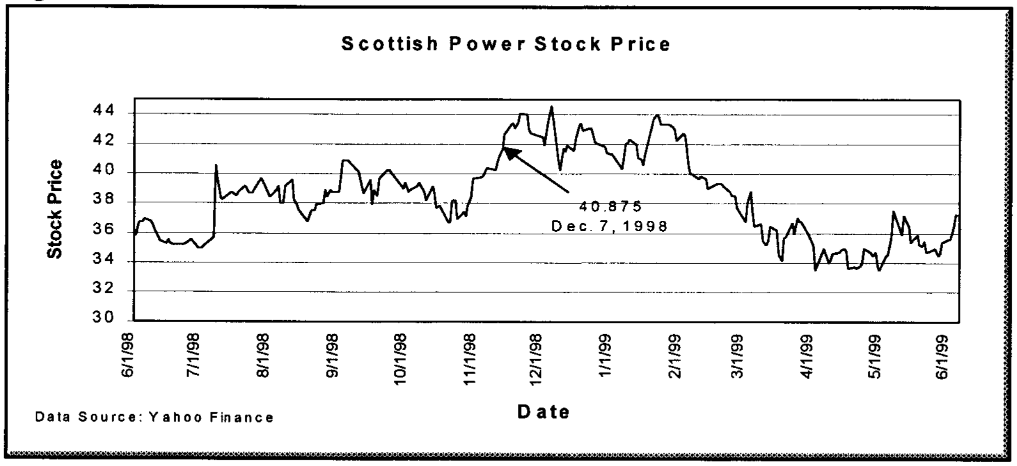
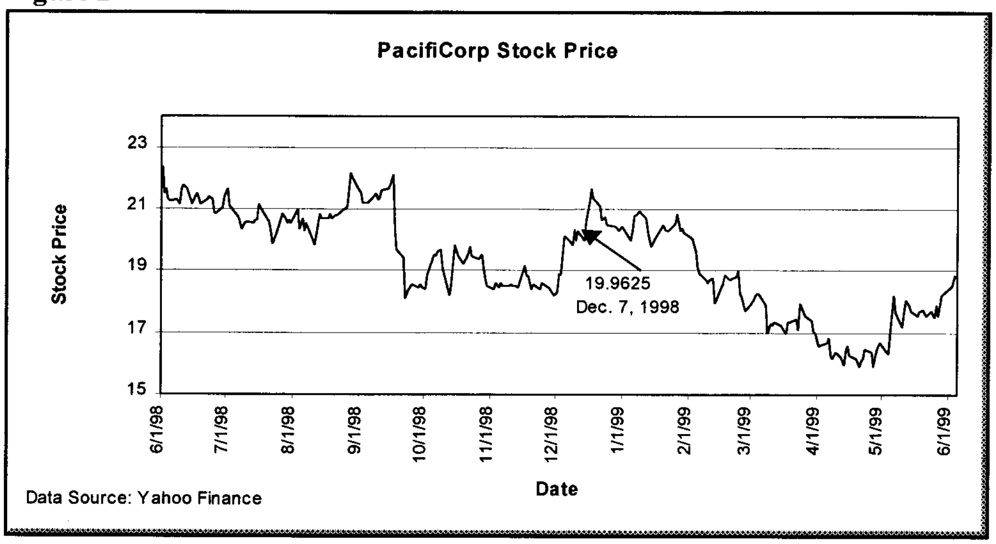


Figure 2



Immediately after the merger announcement both share prices briefly increased, but then began to fall within a matter of weeks. This trend continued until around the first of May when both share prices began to increase. Since the announcement the prices of the two stocks have been closely tracking one another. Over the five month period prior to the merger announcement the correlation coefficient for the two stock's prices was -0.44, after the announcement the correlation increased to 0.95.

DPU EXHIBIT NUMBER DPU 4. 4:

VITA WILLIAM A. POWELL, PH.D.

CURRENT POSITION **Utility Economist**

Division of Public Utilities

Department of Commerce, State of Utah

Salt Lake City, Utah 84114;

(801) 530-6032; wpowell@br.state.ut.us

EDUCATION

Doctorate of Philosophy (Economics) **1993**

Texas A&M University, College Station, Texas

Thesis: Reduced Form Estimation in Partially Specified Simultaneous Equations Models

Major: Econometrics

Minor: Public Finance and Risk and Uncertainty

Bachelor of Science **1985**

Weber State University, Ogden, Utah

Major: Economics

Minor: Business and Psychology

PROFESSIONAL TRAINING

NARUC Annual Regulatory Studies Program **1996**

Michigan State University

Two course in regulatory theory, procedures, and practices.

Professional Conferences

I have attended several professional conferences covering a wide variety of regulatory topics.

EXPERIENCE

Utility Economist **1996 - Present**

Utah State Division of Public Utilities

Responsibilities

- Negotiate settlements with utilities and interveners.
- Propose, evaluate and advance new regulatory theories and procedures.
- Conduct, economic research and analysis to assist in the development of policy for utility regulatory issues.
- Prepare recommendations, present written and oral testimony, and assist counsel in cross examination of other witnesses.
- Conduct independent studies related to regulatory issues including, economic analysis, rate design, cost of service, quality control, etc.

Adjunct Professor of Economics **1996-Present**

Weber State University, Ogden, Utah

Teaching Responsibilities

- Survey of Economics
- Principles of Micro and Macro Economics
- Quantitative Methods for Business and Economic

Assistant Professor of Economics **1989-1995**

University of Mississippi, Oxford, Mississippi

Teaching Responsibilities

- Graduate Courses:

  Applied Microeconomics, Applied Statistics and Regression Analysis, Econometrics, and Mathematical Statistics

- Undergraduate Courses:

  Principles of Economics, Microeconomics, and Statistics

- Course Coordinator for Undergraduate Statistics Courses

Committee Assignments

- Qualifying Theory Exams
- MBA Program Review
- Econometrics Field Exam
- Undergraduate Program and Effectiveness Assessment

Graduate Research/Teaching Assistant **1985-1990**

Texas A&M University, College Station, Texas

Responsibilities

- Teaching undergraduate economics courses
- Helping conduct and evaluate research for Dr. Robert Basmann and Dr. Raymond Battalio

PROFESSIONAL ACTIVITIES

- Text Book Reviewer
- Referee (past), Journal of Economic Education
- Discussant, Southern Economic Association Meetings
- Member of the American and Southern Economic Associations
- Invited Questioner, Educational Testing Service, GRE Economics Subject Exam

RESEARCH

- "Detecting Abnormal Returns Using the Market Model with Pretested Data," with Steven Graham and Wendy Pirie, *Journal of Financial Research*, Spring 1996, pp. 21-40.
- "Do Students Go to Class? Should They? Comment," with William F. Shughart, *Journal of Economic Perspectives*, Summer 1994, pp. 208-210.
- "A Decision Support System for In-Sample Simultaneous Equations Systems Forecasting Using Artificial Neural Networks," with Lou Caporaletti, Bob Dorsey, and John Johnson, *Decision Support Systems*, 11 (1994), pp. 481-495.
- "An Economic Interpretation of Stranded Costs in a Restructured Electric Utility Industry."
- "Information Versus Market Power: The Effect of Advertising on market Share Instability."
- Information and Competition: Their Role in a Restructured Electric Utility Industry."
- "An Empirical Comment on the Regional Distribution of Bank Closings in the United States From 1982 to 1988."

PRESENTATIONS

- "Stranded Costs," Electric Deregulation and Customer Choice Task Force, Utah State Legislature, Spring/Summer 1997

- "Retail Access Electric Pilot Programs," Utah Public Service Commission, Fall 1996.
- "Free Enterprise and the Entrepreneur," Gatlin Center for Free Enterprise, University of Mississippi, Fall 1995.
- "Simultaneous Equations Systems Forecasting with Neural Networks," with Lou Caporaletti, Bob Dorsey, and John Johnson, Combined Meetings of Operations research Society of America and The Information and Management Systems Society, May 1991.
- "Adaptive Behavior and Coordination Failure," with John VanHuyck, Joseph Cook, and Raymond Battalio, Economic Science Association Meetings, October 1990 and 1991.

CIVIC ACTIVITIES

- Participant, Utah Economic Forum
- Member, Huntsville Town Boosters Club
- Member, Huntsville Town Parks Committee
- Little League Baseball Coach, Weber County
- Trustee, Ogden Valley TV Translator District

HONORS

- Outstanding teacher of the Year, Nominee (by student vote), School of business Administration, University of Mississippi, 1994-1995
- Outstanding Graduate Teaching Award, Department of Economics, Texas A&M University, 1988-1989
- Senate Banking Committee Summer Intern, 1982