

BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH

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

SCOTTISH POWER

SUPPLEMENTAL TESTIMONY OF ALAN V. RICHARDSON

APRIL 16, 1999

INTRODUCTION

Q. Please state your name.

A. My name is Alan V. Richardson. I previously offered direct testimony in this proceeding.

Q. What is the purpose of your supplemental testimony?

A. This testimony responds to certain of the issues identified by parties in their March 31 issues list to the Commission.

Q. Please summarize your testimony.

A. My testimony responds to the requests of some parties that we be more specific about the benefits and costs associated with the transaction. My testimony shows:

We are committed to providing substantial, quantifiable benefits, monetary and otherwise, to the Utah customers of PacifiCorp.

We have already identified cost savings that flow from the transaction -- the net corporate cost reduction of \$10 million per year -- and have committed to flow it through to customers through the ratemaking process. These savings are recurring, and are worth about \$100 million on a net present value basis. This alone satisfies the requirement that we produce net positive benefits to customers from the transaction. Our proposals go far beyond this, however.

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. Thus the \$55 million cannot be viewed as an "offset" to the \$10 million of annual cost reductions described above.

We are committed to providing benefits to customers through improved quality of

service, with our unprecedented package of customer service standards. These service quality benefits are significant and real, and our success in achieving them can be tracked through commonly accepted measurement techniques. It is possible to place a dollar value on the benefits to customers from this improved quality of service. An approach described in my testimony suggests that the value of portions of these improvements is worth approximately \$60 million annually to customers.

We expect to achieve other significant cost savings in the future, which together with the corporate cost savings mentioned above will lead to rates lower than they would have been without the transaction. Our experience in transforming ScottishPower operations in Scotland, Manweb and Southern Water substantiates our ability to achieve efficiencies in utility operations.

Where there are perceived costs and risks associated with the transaction, we have addressed them through our proposed conditions.

Taken together, Utah customers would be overwhelmingly better off, and the public interest served, by approval of the transaction.

Finally, my testimony also addresses certain of the remaining issues raised by the parties.

BENEFITS TO CUSTOMERS FROM THE TRANSACTION

Q. What are the quantifiable benefits to customers flowing from the transaction?

A. Many of the benefits lend themselves to being measured by dollar figures, such as the \$10 million per annum in net reduction in corporate costs which will be reflected in cost of service by the end of the third year after the transaction closes. We also expect to achieve additional cost savings in the future. These savings will provide a real and tangible benefit to Utah customers. As discussed below in this testimony, ScottishPower has a demonstrated ability to achieve efficiencies in utility operations, as witnessed by our experience with transforming ScottishPower operations in Scotland, Manweb and

Southern Water. Another benefit which ultimately will be captured in dollar savings is the expected reduction in the borrowing costs that PacifiCorp will incur as it becomes integrated into a larger, financially stronger ScottishPower group, with a combined capitalization of over \$18 billion. Given the recent financial results reported by PacifiCorp -- a loss of 19 cents per share for calendar year 1998 -- the value of ScottishPower's financial strength standing behind PacifiCorp should not be underestimated.

Other benefits flowing to customers from the transaction, while capable of being quantified, do not lend themselves easily to being measured in dollar savings. However, these benefits are substantial and must be taken into account in any aggregation of customer benefits from the transaction. Exhibit __ (AVR-1) is a compilation of the benefits which will flow to customers from the transaction.

Q. Please describe some of the benefits that cannot be easily quantified into dollar savings.

A. With our network performance standards, we are committing to improve system availability and system reliability by 10% over the next five years, and to reduce momentary interruptions by 5% during the same period. Our commitment will be tracked by commonly used measurement techniques--SAIDI¹ in the case of system availability, SAIFI² in the case of system reliability, and MAIFI³ in the case of momentary

¹ System Average Interruption Duration Index.

² System Average Interruption Frequency Index.

³ Momentary Average Interruption Frequency Index.

interruptions. In consultation with the regulators, we will establish a benchmark as the starting point for this commitment, and our delivery on this commitment will be quantified by statistics gathered using these accepted indices. The benefits are quantifiable and real, and we have committed to pay penalties if we don't achieve them. The other network performance standards to which we are committed (improving the 5 worst performing circuits in Utah and prompt supply restoration) and the customer service performance standards (telephone service levels and complaint resolution) also provide real and quantifiable benefits. The service improvements which we achieve will be tracked according to identified and agreed upon measurement tools.

Q. What other benefits can you identify?

A. Our customer service guarantees are an undeniable benefit to customers. We are committing to specific standards in our dealing with customers, and backing that commitment up with payments when failures occur. This is clearly a measurable benefit. A customer will either experience specific improvements in certain performance measurements or receive \$50 (or \$100 for a commercial or industrial customer in the case of some of the standards) if we fail to meet our commitment. Such a program is not in place for Utah customers today. Indeed, we believe the program is unprecedented in the U.S. Our commitment to back up our guarantees with dollars is a benefit which we think customers will find to be very valuable. Customers also benefit from knowing exactly what to expect from their electric utility, and that our performance will be measured against specific standards with periodic reports to customers on our accomplishments.

Q. Are these benefits capable of being measured in dollars?

A. In some cases. For example, in the case of our promised improvement in system availability and momentary interruptions, there are techniques available which attempt to put dollar figures on the value to customers of not having their power interrupted. I have included as Exhibit ___ (AVR-2) one such study which attributes dollar values on these measures of improved service quality. That estimate, using a 1990 survey performed by the Bonneville Power Administration and the Electric Power Research Institute, suggests that the improvements to SAIDI and MAIFI to which we are committed produce approximately \$60 million annually in value to our customers, or about \$600 million on a net present value basis. While parties may debate the analytical techniques used in arriving at these figures, the estimates nonetheless demonstrate that our promised service quality improvements represent a substantial and quantifiable benefit to Utah customers. Whatever the precise numbers, it is clear that the reduced interruptions in service have an obvious and significant value.

Q. Are the benefits related to the remaining performance and customer guarantee standards also quantifiable in a similar manner?

A. No, they are not. While it is difficult to quantify the benefits of the other performance standards and the customer guarantee standards in a similar manner, intuitively customers do value these commitments. The benefits exist, whether or not a dollar value can easily be assigned to them. Some of the many examples that demonstrate a link between such service standards and value creation include the following:

Commercial establishments will be better able to schedule maintenance work or other downtime activity during periods of planned interruption.

Homeowners will be better able to plan their daily activities knowing there will be greater certainty on keeping appointments.

All customers will know that the telephone will be answered more promptly.

Customers will also know that complaints, bill inquiries, concerns about power quality and meter problems will be addressed more promptly and with a degree of certainty. This avoids the seemingly innumerable telephone calls that some customers experience to try to achieve resolution of a problem.

Power supply will be established for customers on a timely basis so that the other start-up activities for a new commercial establishment can proceed more smoothly.

With these improvements in service, customers will be able to rely upon the performance of their electric utility as they plan their daily activities, thereby reducing the loss in productivity that would otherwise occur.

Q. ScottishPower states that it will provide other benefits through its transformation of PacifiCorp. How can Utah customers be assured these benefits will be realized?

A. The simple answer is that we have done it before. The assurance that these benefits will be delivered is substantiated by our experience in transforming ScottishPower, Manweb, and Southern Water. A later section of my testimony describes our experience in transforming Manweb. While that experience does not exactly parallel the circumstances of this transaction, it does demonstrate our capability of achieving efficiencies by transforming utilities. It is this capability and experience which we intend to bring to bear upon PacifiCorp's operations.

COMPARISON OF BENEFITS AND COSTS OF THE TRANSACTION

Q. Has ScottishPower demonstrated that there is a net positive benefit to PacifiCorp's Utah customers if the transaction is approved?

A. We have clearly satisfied our burden to show net positive benefits to customers. The promised \$10 million annual net reduction in corporate costs in and of itself meets this standard. Our proposals extend far beyond just meeting this standard, as is apparent from reviewing the benefits itemized in Exhibit ___ (AVR-1).

Q. What about the costs associated with the additional investment which ScottishPower will undertake to achieve the improvements in system performance?

A. As stated in Mr. Moir's testimony, ScottishPower estimates that it will spend \$55 million, or about \$11 million annually, during the five-year implementation period to put the proposed service standards package into place. About \$32 million of this expenditure is capital investment to be made over the five-year implementation period (\$31.1 million for the performance standards and \$0.9 million for the customer guarantees). The remaining \$23 million are operating expenses. PacifiCorp's overall capital and revenue budgets will not increase as a result of these expenditures, however. This is because, first, ScottishPower will seek to make performance-improving investments which also lead to operational efficiencies. Second, a portion of the committed expenditure will come from modifying or accelerating existing projects contained within PacifiCorp's budget (e.g., capital projects to improve worst performing circuits). Third, ScottishPower will, in parallel, be seeking other efficiencies in both the

capital expenditure program (while delivering the same or improved outputs) and operating expenditures (while delivering improved reliability and service). Thus the \$55 million expenditure will not have an impact on the rates of Utah customers. Indeed it will help to mitigate upward cost pressures rather than adding to them.

Q. In the Statement of Additional Issues submitted by the Committee of Consumer Services, the \$55 million cost for implementing the system improvements is placed alongside the \$10 million in net corporate cost reductions to which ScottishPower has committed. Is this an appropriate analysis?

A. Not at all. The \$55 million expenditure is not really a "cost" of the transaction and should not be considered as an "offset" to the benefits identified earlier in my testimony. As noted above, this investment is not over and above PacifiCorp's existing capital plans, but represents a refocusing of those plans. In any event, the magnitudes are far different, as the \$10 million in net corporate cost reductions is an annual figure which can be expected to recur in future years, and has a net present value of about \$100 million. The \$55 million expenditure, on the other hand, is primarily capital spending that would not have the same sort of impact on revenue requirement. Apart from the corporate cost reductions, we are confident that we will achieve additional significant cost savings in the future, although their magnitude cannot be quantified.

Q. What are some other potential costs or risks associated with the transaction?

A. One obvious expense item is the cost ScottishPower and PacifiCorp will incur to complete the transaction, which we have promised to exclude from our books for

ratemaking purposes. Customers are therefore unaffected by that cost. In other cases, we have attempted to identify costs and risks that could be associated with the transaction, and to address them through conditions that we propose to attach to approval of the transaction. For example, risks associated with a feared loss of regulatory oversight or access to PacifiCorp's books and records are addressed through specific commitments which we are making in these areas. These are presented in Mr. Green's testimony at pages 13 to 15.

**ASSURANCE OF FUTURE COST SAVINGS, AS SUBSTANTIATED BY
MANWEB EXPERIENCE**

Q. Why does ScottishPower's experience with Manweb demonstrate an ability to achieve efficiencies in utility operations?

A. In 1995, ScottishPower successfully acquired Manweb, a regional electricity company serving 1.3 million customers in the northwest of England and north Wales. In the three plus years since that acquisition, we have been successful in reducing operating costs, while at the same time achieving substantial improvements in customer service. We have therefore shown it is possible to do both, by refocusing the utility's efforts on providing excellent service to customers. The Manweb experience provides a proven track record that substantiates our commitment here to produce cost savings.

Q. Please describe ScottishPower's experience with Manweb.

A. At its core, the ScottishPower experience with Manweb serves as a testament to our ability to transform utility businesses to the benefit of our customers, employees and

shareholders. The approach we followed to transform Manweb was applied in the transformation of our ScottishPower operations in Scotland and to Southern Water. This same approach, which is unique in the industry and one that delivers on promised results, will be applied to PacifiCorp as well.

Q. What is unique about the ScottishPower approach to transforming utility businesses?

A. ScottishPower's capability is unique in that it relies upon a complex mix of skills, experiences, knowledge, processes, systems and people that deliver the results, as described in Mr. MacRitchie's direct testimony.

Q. Please describe the various actions that ScottishPower implemented to achieve efficiencies and cost savings at Manweb.

A. The actions included the following:

Changes to organizational accountabilities to provide greater alignment of responsibilities with service delivery.

Changes to planning, budgeting and reporting systems to focus on efficiency and customer service.

Greater use of technology to improve productivity and respond better to customer requirements.

Development of working practices at all levels in the organization to more closely match the operating priorities of the different parts of the business.

Simplified business processes around service delivery.

Integration of common functions while retaining local accountabilities.

Implementation of best practices in procurement to leverage greater purchasing power

and supplier relationships.

Rationalization of operations to achieve efficiencies.

Development of performance management techniques to drive productivity improvements.

Q. What cost savings was ScottishPower able to achieve in its transformation of Manweb?

A. Since 1993-94, the year before we acquired Manweb, its business operating costs have been reduced by over 55%, from £176 million to £78 million in 1997-98. This dramatic reduction in business operating costs is shown in Figure 1 below.

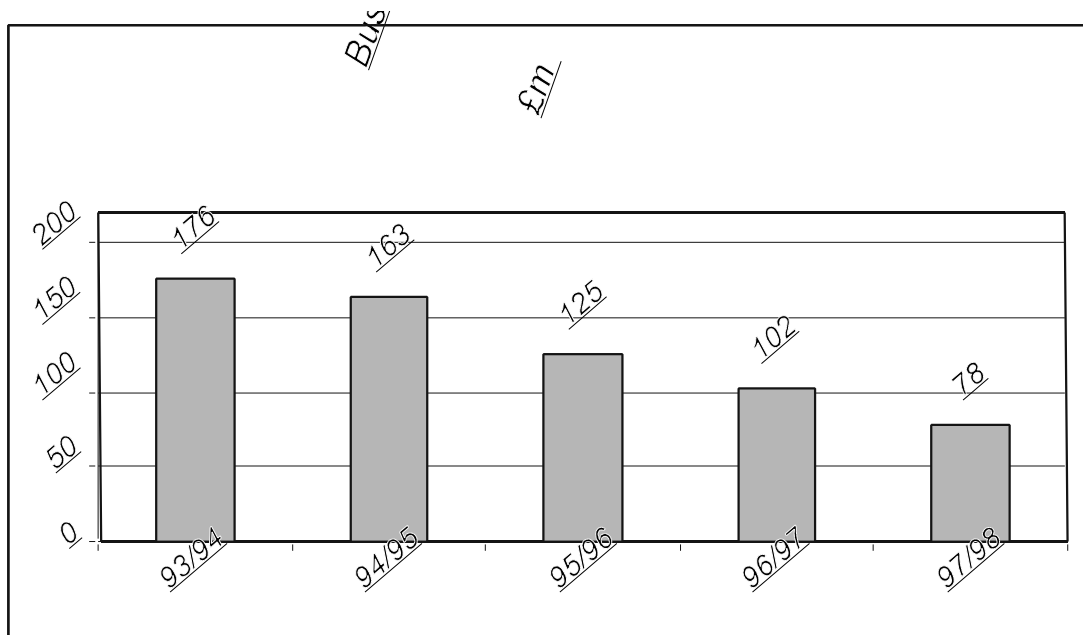


FIGURE 1

Q. What other conclusions can be drawn from the Manweb experience?

A. The Manweb experience confirms another point made in Mr. MacRitchie's testimony regarding the time required to transform the business. The ScottishPower experience is that the proper way to transform businesses requires sufficient time to introduce the types of investments in information technology, people and systems that will provide sustainable improvements in the business. This was undertaken in Manweb and the results of this effort are apparent from Figure 1. Another point on timing is that in the case of Manweb, it was several months after we received regulatory approval of the acquisition before we could make precise commitments as to cost reductions.

Q. Were the cost savings at Manweb achieved through reductions in capital spending?

A. No. As shown in Figure 2, the level of capital expenditures at Manweb remained relatively unchanged during the transformation at Manweb, meaning we were able to achieve these efficiencies by investing more smartly. This was attributable to the application of the investment strategy that emphasizes value rather than mere asset replacement as described in both Mr. MacRitchie's and my earlier testimony.

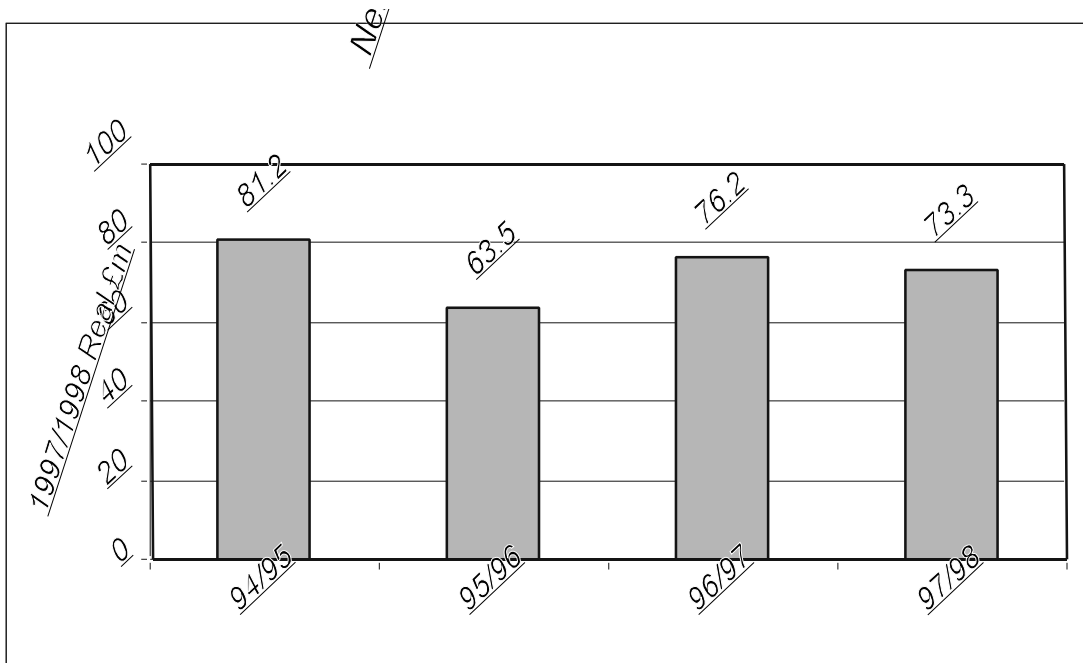


FIGURE 2

Q. How can you show that ScottishPower was able to achieve greater workforce productivity at Manweb?

A. Following the transformation at Manweb, we were able to do a better job with fewer people. Figure 3 below shows the manpower levels during the period from 1994 through 1998.

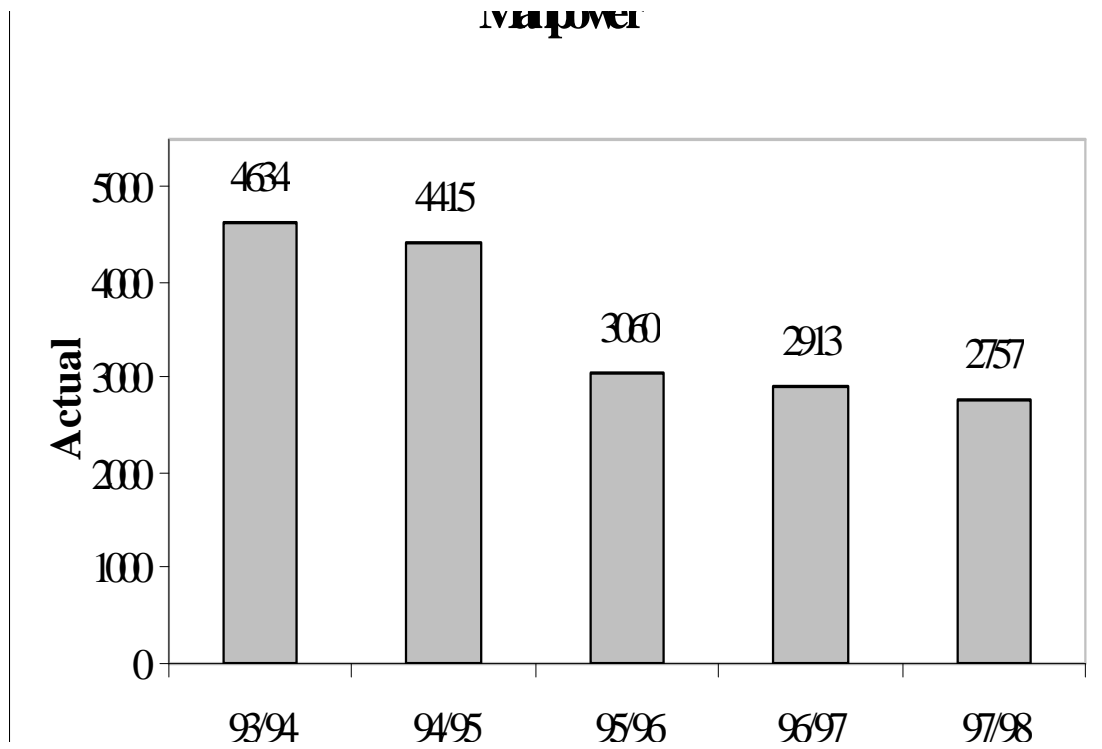


FIGURE 3

- Q. Did these reductions in manpower levels have any adverse impact on safety?
- A. No. Manweb's reportable accident rate declined from 2.41 reportable accidents per 100 employees in 1994/95 to 1.84 in 1997/98. This was attributable in large measure to the adoption of ScottishPower best practices and a management focus on safety.
- Q. Has ScottishPower also been able to deliver increased system performance as a results of efforts to transform Manweb?
- A. Yes. We have been able to achieve substantial improvements in customer service, as evidenced by a 74% reduction in the number of Manweb failures of Guaranteed Standards -- as shown in Figure 4 below -- and a 38% reduction in complaints to OFFER, the U.K. electricity regulator, as shown in Figure 5 below. Another measure of the improved customer service is the 28% reduction in underlying customer minutes lost, from 75 minutes in 1995-96 to 54 minutes in 1997-98.

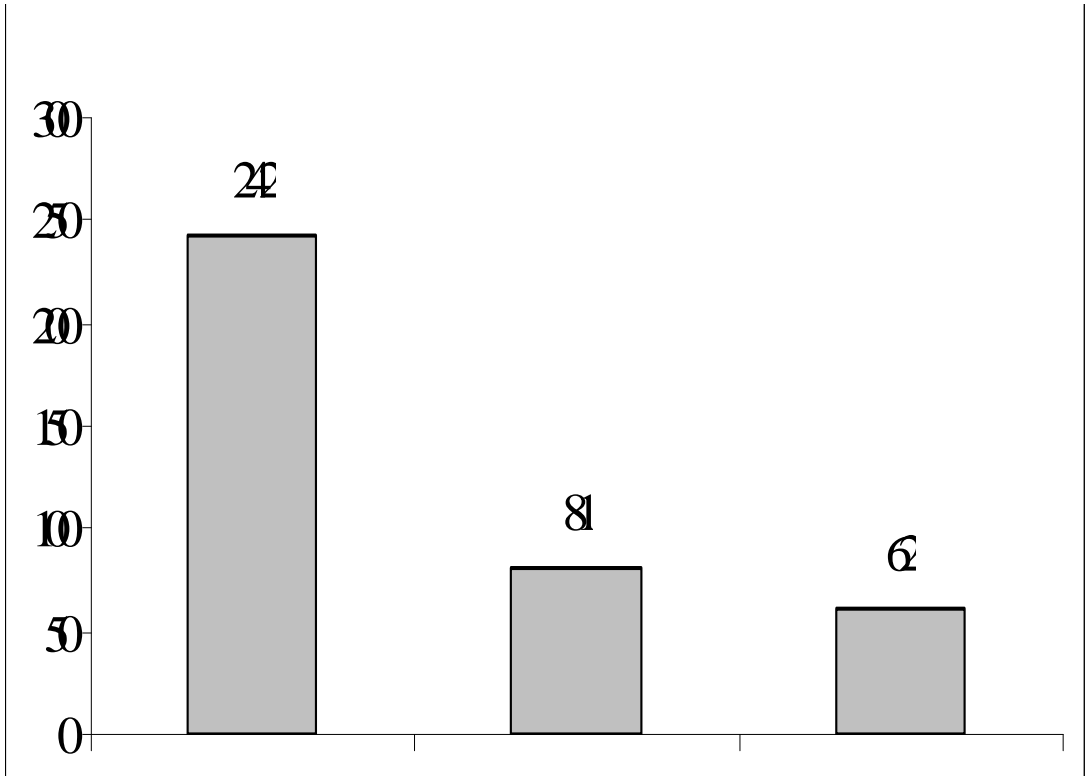
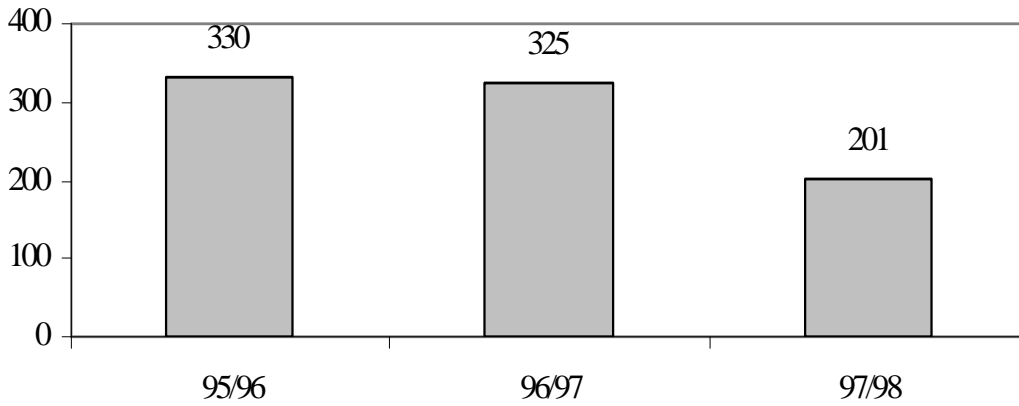


FIGURE 4

FIGURE 5

Complaints to OFFER



Q. Have rates been reduced for Manweb's customers since the transformation of the company?

A. Yes. The average residential customer's bill in the Manweb service territory (3,300 kWh annual usage) has declined from £357.69 in 1993/94 -- the year before the acquisition -- to £267.78 in 1998-99 (measured in constant May 1998 prices), which represents a 25% reduction. Figure 6 below shows these price reductions.

Average Residential Customer Bill

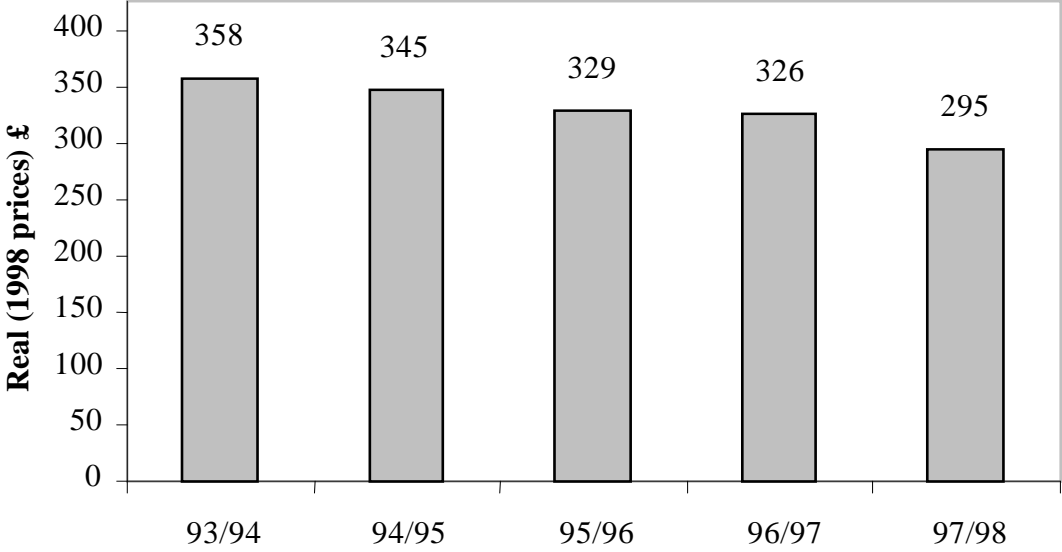


FIGURE 6

Q. Can Utah customers expect similar impacts on their rates if this transaction is approved?

A. The opportunities for cost reductions are different in Utah, but definitely real. The Manweb situation involved the combination of two electric utilities operating in nearby geographic areas, and thus presented greater opportunities for cost savings by eliminating duplicative functions and combining electric operations. This transaction presents limited opportunity for savings achieved in this manner. At the same time, however, the reduction in business operating costs shown in Figure 1 included savings which went beyond those attributable to elimination of duplicate functions. We are confident we can achieve significant efficiencies in PacifiCorp's operations, and the resulting cost reductions will be captured through the ratemaking process to produce rates for customers that are lower than had the transaction not occurred. We are confident as well that we can achieve measurable improvements in the quality of service while at the same time reducing costs, as we did in the case of Manweb.

USE OF SPECIAL CONTRACTS

Q. The LCG and UIEC issues list refers to the question of ScottishPower's approach with respect to special contracts. How will ScottishPower handle economic, non-tariff or special contracts?

A. As we have stated previously, after the transaction, PacifiCorp will honor all of its contractual obligations. We value our relationship with all our customer classes, and it

may be appropriate to evaluate the issue of special contracts following completion of the transaction. This evaluation must be done in parallel with the work of the task force recently appointed by the Commission to examine this issue. The Public Service Commission of Utah issued a Report and Order on March 4, 1999 in Docket No. 97-035-01 establishing a task force to study the standards the Commission should employ in approving special contracts and the regulatory treatment of all special contracts stating that:

We conclude that the Task Force desired by the Company and the Division, which we herein establish, should re-examine the previous Task Force guidelines and definitions for regulatory treatment of special incentive contracts, with particular emphasis on how risk should be shared between the Company and its customers. We also want an evaluation of the appropriateness of the confidential treatment customarily given to the rates and terms of service in Utah special contracts in an increasingly competitive environment.

The Commission has therefore established a procedure to examine the issue of special incentive contracts. PacifiCorp will participate in this process and add its resources to the task force. Prior to completion of the transaction and until the Commission's task force has finished its work, however, the discussion regarding special contracts is premature and should not be an issue in this docket.

THE "PREFERENCE SHARE" HELD BY THE U.K. GOVERNMENT

- Q. What is the "preference share" or "special share" referred to in the issues list of LCG and UIEC?
- A. I presume the reference is to the "special share" which was retained by the U.K.

government when ScottishPower was privatized. This special share has a nominal value of £1, and prevents a person (or persons acting in concert) from owning or controlling more than 15% of the voting rights of ScottishPower without the U.K. government's consent. The practical effect of the "special share" is to require government approval before control of ScottishPower may be transferred, much like the regulatory statutes in many of the states which require utility commission approval before control of a regulated utility passes to another. It comes into play only if a transfer of ownership of ScottishPower is involved, and does not in any way impose any restrictions on the actions which ScottishPower may take with respect to its own businesses or PacifiCorp.

SUMMARY

Q. Could you please summarize your supplemental testimony, Mr. Richardson?

A. Yes. The proposals we have put forth in Utah overwhelmingly satisfy any requirement to demonstrate net positive benefits to customers from the transaction. Our proposals, taken together, will provide substantial benefits to Utah customers which are quantifiable, monetarily and otherwise. We are committing to immediate cost savings through a \$10 million reduction in corporate costs annually -- which is equivalent to about \$100 million on a net present value basis -- and our proposed network system improvements will produce benefits to customers which, if quantified in the manner suggested in my testimony, are in the range of \$60 million annually. Beyond these immediate commitments, we are confident that we will achieve other significant cost savings in the future, building upon our successes in transforming ScottishPower, Manweb and Southern Water. Given this compelling demonstration of benefits, the public interest would be well served by approval of the transaction.

Q. Does this conclude your supplemental testimony?

A. Yes, it does.