

**BEFORE THE PUBLIC SERVICE COMMISSION OF UTAH**

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In the Matter of the Application of PacifiCorp            )  
and ScottishPower plc for an Order Approving        )       Docket No. 98-2035-04  
the Issuance of PacifiCorp Common Stock            )

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**PACIFICORP**

**REBUTTAL TESTIMONY OF RICHARD T. O'BRIEN**

**JULY 13, 1999**

**INTRODUCTION**

1     Q.     Please state your name.  
2     A.     My name is Richard T. O'Brien.  
3     Q.     Are you the same Richard T. O'Brien who submitted direct testimony in this proceeding?  
4     A.     Yes, I am.  
5     Q.     What is the purpose of your rebuttal testimony?  
6     A.     I provide testimony regarding the overall conclusions reached by the Division of Public  
7            Utilities (DPU). I address several issues raised by Large Customer Group (LCG) witness  
8            Richard M. Anderson and Utah Industrial Energy Consumers= (UIEC) witness Brubaker.  
9            These issues relate to ScottishPower=s suitability as a merger partner for PacifiCorp and  
10           PacifiCorp=s ability to achieve efficiencies and improvements on its own compared to its  
11           ability to achieve those efficiencies and improvements in combination with  
12           ScottishPower. My testimony also responds to a number of other issues raised by the

1 UIEC, the Committee of Consumer Services (CCS), Deseret Generation & Transmission  
2 (DG&T) and the Utah League of Cities and Towns (ULCT).

3 **BENEFITS OF THE TRANSACTION**

4 Q. What is Pacificorp's response to the overall conclusions articulated by the DPU?

5 A. We are very pleased that the DPU has recommended that the Commission approve the  
6 transaction. With respect to the concerns raised by the DPU in its direct testimony,  
7 PacifiCorp and ScottishPower have worked with the DPU to address and resolve these  
8 concerns and are committed to continue to do so throughout this process.

9 Q. LCG witness Anderson suggests that ScottishPower is not a very good merger  
10 candidate (LCG/Anderson, page 48) due to a lack of quantifiable synergies between  
11 ScottishPower and PacifiCorp. UIEC witness Brubaker also seems to suggest that  
12 PacifiCorp, on its own, could achieve the same degree of improvement in performance  
13 without the transaction (UIEC/Brubaker, page 14). Please respond.

14 A. I strongly disagree. ScottishPower is an excellent merger candidate for PacifiCorp. ScottishPower and  
15 PacifiCorp have complementary assets, views and objectives. As I noted in my direct testimony,  
16 ScottishPower's demonstrated commitment to its regulated utility business was one of the reasons we  
17 decided it was the right partner for us. The ScottishPower commitments to improve service will bring  
18 significant benefits to Utah customers. These are not commitments that PacifiCorp could, or was intending  
19 to make absent this merger. ScottishPower has a proven track record for improving customer service and  
20 reliability while achieving efficiencies in operations. ScottishPower will bring to PacifiCorp a unique set of  
21 experiences, skills and business practices such as benchmarking, best practice transfer,  
22 transition planning, and program management which could not easily be replicated. I do  
23 not believe PacifiCorp alone could achieve similar improvements as quickly, as fully or  
24 with the same high probability of success.

25 Q. LCG seems to suggest that the Commission should review this transaction in comparison  
26 with other recent merger proposals. Do you agree that this would be an appropriate  
27 approach?

A. 28 No. The Commission's task is to evaluate this transaction and determine whether it is in the  
29 public interest. The Commission should compare the benefits offered by combining the  
30 skills and effort of ScottishPower and PacifiCorp only to those that would be offered by  
31 PacifiCorp standing alone. It should not compare this transaction to some hypothetical  
32 deal or one involving different utilities. Moreover, the transactions mentioned by LCG  
33 may present risks not associated with this transaction, such as the potential for  
34 concentration of market power and a reduction in competition. It would be speculative  
35 and futile to attempt to compare the identifiable characteristics of this transaction with the  
36 unknown characteristics of a hypothetical transaction.

37 Q. LCG witness Anderson contends that in identifying merger savings, ScottishPower has  
38 failed to consider the cost cutting and performance enhancements that PacifiCorp has  
39 undertaken in its 1998 ARefocus program and other re-engineering efforts.  
40 (LCG/Anderson, pages 34-37). Is this a valid criticism?

41 A. No. It has always been our intention that merger-related savings will be incremental to  
42 those that have been realized through PacifiCorp's ARefocus program and other re-engineering  
43 efforts. As stated in Mr. MacRitchie's rebuttal testimony, ScottishPower's transition plan filing  
44 will take into consideration any PacifiCorp-initiated cost savings to ensure that no double-

1 counting takes place. For example, in the third quarter of 1998, PacifiCorp announced a cost  
2 reduction program to achieve \$30 million of savings to 1999 budgets. This initiative is described  
3 in Chairman Keith McKennon=s March 31, 1999 press release included in the LCG testimony as  
4 RMA \_\_\_\_ Exhibit 7. These cost-saving measures are reflected in PacifiCorp=s 1999 budget  
5 and will be reflected in 1999

6 results of operations before ScottishPower=s post-merger initiatives are identified.

7 PacifiCorp has no specific plans for achieving cost savings in addition to the \$30 million reduction to 1999  
8 budgets.

9 The significance of these ARefocus@ cost savings measures should not be understated. I am  
10 convinced, however, that ScottishPower=s proven capability for transforming utility  
11 businesses in the U.K. will allow PacifiCorp to achieve further efficiencies while at the  
12 same time improving customer service and system reliability.

13 Q. CCS witness Talbot asserts that PacifiCorp is in a strong financial position and that the  
14 proposed transaction would not enhance PacifiCorp=s financial strength. Please  
15 comment.

16 A. While I would agree with Mr. Talbot that PacifiCorp=s return to its core business is likely  
17 to improve PacifiCorp=s financial strength over time, I do not agree that it is appropriate  
18 to conclude that PacifiCorp is in a strong financial position that would be worsened  
19 through the proposed transaction with ScottishPower. For example, one measure of  
20 financial strength is the amount of earnings that are used to meet dividend payments to  
21 shareholders. On average, U.S. electric utilities have a dividend payout ratio - - the ratio  
22 of dividends to earnings on a per share of common stock basis - - of between 60% to  
23 70%. In 1998, PacifiCorp=s earnings were insufficient to cover dividends to  
24 shareholders; the payout ratio exceeded 100%. For 1999, the expectation on Wall Street  
25 is that this payout ratio will continue to be over 100%, significantly exceeding the  
26 industry average. By contrast, we expect that post-transaction, the combined company=s  
27 payout ratio will be lower than the industry average. PacifiCorp=s ability to attract capital  
28 will not be diminished. Indeed, PacifiCorp was placed on “credit watch positive” after the  
29 transaction was announced. Overall, I believe that the proposed transaction will result in  
30 a financially stronger company than PacifiCorp on a stand-alone basis.

31 Q. CCS witness Chernick suggests that, as a result of the annual Oregon performance  
32 review and the Utah Commission reliability docket, PacifiCorp=s service quality will  
33 improve over the next few years without this transaction. Please respond.

34 A. This is possible, although not assured. The Oregon performance standards are designed to prevent a  
35 deterioration of service, and the outcome of the Utah docket is not yet known. I recognize that the  
36 Commission has broad authority over its jurisdictional utilities, but this should not detract from the  
37 significance of what ScottishPower is proposing. I believe a voluntary and well-communicated commitment  
38 to customers backed by proven experience will deliver results to customers that PacifiCorp and the  
39 Commission could not achieve otherwise.

#### 40 **RESTRUCTURING CONDITIONS**

41 Q. UIEC witness Brubaker argues that the Commission should take the opportunity to extract from  
42 ScottishPower/PacifiCorp definitive restructuring commitments (UIEC/Brubaker, pages 42-47). Would you  
43 please respond?

44 Q.

45 A. Mr. Brubaker suggests two restructuring commitments. The first is that PacifiCorp should be  
46 required to place its transmission assets into a Regional Transmission Organization (ARTO@)  
47 that meets criteria to be established by the Federal Energy Regulatory Commission  
48 (“FERC”). The second is that ScottishPower/PacifiCorp should be required to Aagree not  
49 to make any claim for stranded cost recovery.@ These proposals are not appropriate for  
50 this docket. RTO=s, stranded costs and other restructuring issues involve policy and  
51 factual considerations that go beyond the scope of a merger proceeding. The Utah  
52 legislature has already established a Task Force to examine restructuring issues for the  
53 state of Utah. Similarly, FERC has already opened a docket to look at RTO issues.

1 Restructuring issues should be addressed and resolved in those forums. In addition, even  
2 if restructuring were an appropriate issue for this case, the Commission would require an  
3 adequate record, especially in the absence of any direction from the legislature, to impose  
4 restructuring requirements on PacifiCorp. That record certainly doesn't exist in this  
5 case.

#### 6 **SPECIAL CONTRACT CONDITIONS**

7 Q. UIEC witness Brubaker makes several recommendations with regard to special contract  
8 customers. Would you please address these recommendations?

9 A. Mr. Brubaker suggests that PacifiCorp be required to renew existing special contracts, or  
10 allow special contract customers to purchase electricity competitively on the open  
11 market.

12 In Docket No. 87-035-27 (the Utah Power/PacifiCorp merger proceeding) special  
13 contract customers sought a number of merger conditions, including contract  
14 amendments and retail wheeling. The Commission rejected those proposed conditions,  
15 stating:

16 AThe Commission will not alter the contracts for interruptible customers as a  
17 condition of the merger by providing a higher priority than was originally  
18 negotiated, signed by the parties, and approved by the Commission. We will  
19 provide the opportunity for this issue to be addressed in future proceedings,  
20 including any proceeding resulting from the cost-of-service filing in this case. We  
21 note, as a general observation, that in this era of increased competition and low  
22 energy prices the industrial customers have other options for power supply such as  
23 co- and self-generation which they have been able to use to some advantage in  
24 negotiating power contracts with the Company. It is therefore unlikely that these  
25 customers will be left holding the bag after the merger is consummated. In  
26 addition, the Commission has another proceeding in which a task force has been  
27 looking at the general issue of incentive rates. Whether or not the merger is  
28 consummated, the Commission intends to press forward with this proceeding and  
29 the interruptible industrial customers will be given full opportunity to present their  
30 case as to the value of incentive rates to Utah and Utah customers. The  
31 Commission further acknowledges the responsibility to determine just,  
32 reasonable, fair and equitable rates for and among the industrial and all customers.  
33 One customer should not get preferential treatment over others.

34 The Commission's reasoning in our prior merger case is equally applicable to the special  
35 contract customer demands in this case. The Commission has established a task force to  
36 review and make recommendations regarding the appropriate criteria for evaluating  
37 special incentive contracts. The task force report should be available by the end of the  
38 year and presumably Commission action on the report will not occur until next year. As  
39 DPU witness Ken Powell notes in his testimony, the existing contracts need no special  
40 protection and it would not be "prudent to require future special incentive contracts  
41 unless they pass whatever screens the task force recommends and are approved by the  
42 PSC."

#### 43 **DG&T CONDITIONS**

1 Q. DG&T witnesses Albrecht, Bowler and Stover allege that PacifiCorp's service to its  
2 wholesale and wheeling customers has deteriorated. (DG&T/Albrecht, pages 2-3;  
3 DG&T/Bowler, pages 2-3; DG&T/Stover pages 8-11) Would you please respond?

4 Q.  
5 A. As Mr. Stover notes in his testimony, those allegations have already been raised in Docket No. 99-2035-01.  
6 That docket was opened by the Commission to investigate quality of service and reliability issues and that is  
7 also the docket in which PacifiCorp will have an opportunity to address the merits of the DG&T allegations  
8 in detail. However, I would like to make several general points. The first is that PacifiCorp takes its  
9 responsibilities to its FERC jurisdiction customers seriously and it has not and will not compromise its  
10 service to those customers through staff reductions, office closings or otherwise. For example, the staff  
11 reductions and office closings cited by Mr. Albrecht as a cause of Dixie's service problems involved the  
12 consolidation of business offices. PacifiCorp's operation centers, which are responsible for the actual  
13 maintenance and operation of the system, were not part of that consolidation. Another important point to  
14 consider is that DG&T, its members and PacifiCorp are all utilities which share, in varying degrees,  
15 responsibility for the safe and reliable operation of their interconnected systems, including the responsibility  
16 to pay their share of the costs of system improvements. As a result, system planning decisions, including  
17 those involving the "Middleton delivery point", are more complicated than DG&T suggests.

18 Q. DG&T witness Stover has suggested five conditions for approval of this transaction. Mr. Stover's condition  
19 number 3 would require PacifiCorp to make specified system changes to "improve service reliability at the  
20 Middleton delivery point." (DG&T/Stover, Exhibit \_\_\_ (CNS-4)). Do you agree with this condition?

21 A. No. My engineering staff has informed me that the DG&T proposal is not the best approach for all the  
22 affected utilities and their customers, specifically including PacifiCorp's retail customers. To the extent that  
23 the Commission wants to explore the merits of various solutions to system problems, it should require  
24 DG&T to provide, in an appropriate proceeding, the detailed engineering and cost support documentation  
25 which could provide a basis for a decision. This is not the appropriate proceeding for that engineering  
26 analysis and DG&T has not provided the information required to make any decisions regarding the  
27 problem, much less the solution.

28 Q. Mr. Stover's condition number 4 would require PacifiCorp to enter into discussions with DG&T regarding  
29 the transfer of service territories from PacifiCorp to DG&T. Is this an appropriate condition for this  
30 transaction?

31 A. It is not. Several months ago DG&T suggested that, if PacifiCorp were willing to transfer service territory to  
32 DG&T's members, DG&T would support the transaction. PacifiCorp/ Scottish Power rejected DG&T's  
33 proposal and we continue to believe that service territory transfers are simply irrelevant to the  
34 Commission's analysis of this transaction. If DG&T believes that particular service territory transfers could  
35 provide benefits to customers, it already has the option, outside of this proceeding, to bring its proposals to  
36 PacifiCorp and the Commission for review.

37 Q. Mr. Stover's condition number 5 would "establish a fixed A&G allocation factor applicable to the Hunter II  
38 ownership and management agreement." (DG&T/Stover, Exhibit \_\_\_\_ (CNS-4)) Would you please  
39 address that condition.

40 A. As I noted earlier, the Commission has previously rejected suggestions to provide similar relief to retail  
41 customers as a condition of merger approval. It should also reject this attempt by DG&T to unilaterally  
42 amend an agreement that was the product of lengthy negotiations between the two utilities as a condition of  
43 approval for an unrelated transaction.

#### 44 ULCT CONDITION

45 Q. ULCT witness Dolan suggests that the Commission condition the approval of the transaction on the  
46 reopening of PacifiCorp's current franchise agreements. Please respond to that proposed condition.

47 A. The abrogation of existing agreements, including agreements between PacifiCorp and  
48 the municipalities in which it serves, is not an appropriate condition of this  
49 transaction.

50 Q. Does this conclude your rebuttal testimony?

51 A. Yes.