

BEFORE THE  
WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of The Application of

PacifiCorp and Scottish Power PLC

For an Order (1) Disclaiming jurisdiction or, in  
The Alternative, Authorizing the Acquisition of  
Control of PacifiCorp by Scottish Power and (2)  
Affirming Compliance with RCW 80.08.040 for  
PacifiCorp's Issuance of Stock in Connection  
with the Transaction

Docket No. UE-981627

DIRECT TESTIMONY OF BRUCE E. BIEWALD  
ON BEHALF OF THE PUBLIC COUNSEL SECTION  
OFFICE OF THE ATTORNEY GENERAL

JUNE 15, 1999

Regarding Cost Savings And Benchmarking

## Table of Contents

1. Qualifications .....	1
2. Summary and Recommendations .....	3
3. Scottish Power's Projection of Cost Savings .....	8
4. Scottish Power's Benchmarking Analysis .....	11
5. Scottish Power's Experience With Cost Reduction in the UK .....	16

Exhibit BEB-1	Resume of Bruce Edward Biewald
Exhibit BEB-2	US Electric Utilities Sorted by Average Residential Revenue per kWh
Exhibit BEB-3	Annual Bills Charged to Typical Standard Domestic Tariff Customers in Great Britain

1 **1. Qualifications**

2 **Q. State your name, occupation and business address.**

3 A. My name is Bruce Edward Biewald. My address is Synapse Energy  
4 Economics, Inc., 22 Crescent Street, Cambridge, Massachusetts, 02138.

5 **Q. Please describe your current employment.**

6 A. I am President of Synapse Energy Economics, Inc., a consulting company  
7 specializing in economic and policy analysis of electricity restructuring  
8 particularly issues of consumer protection, market power, stranded costs,  
9 renewable energy, efficiency, environmental quality, and nuclear power.

10 **Q. What are your qualifications with regard to energy policy?**

11 A. I graduated from the Massachusetts Institute of Technology in 1981,  
12 where I studied energy use in buildings. I was employed for fifteen years  
13 at the Tellus Institute where, as Manager of the Electricity Program, I was  
14 responsible for studies on a broad range of electric system regulatory and  
15 policy issues. I have provided testimony on energy issues in more than  
16 fifty cases in twenty states, two Canadian provinces, and before the  
17 Federal Energy Regulatory Commission. I have co-authored more than  
18 one hundred reports, including studies for the Electric Power Research  
19 Institute, the U.S. Department of Energy, U.S. Environmental Protection  
20 Agency, the Office of Technology Assessment, the New England  
21 Governors' Conference, the New England Conference of Public Utility

1           Commissioners, and the National Association of Regulatory Utility  
2           Commissioners. My papers have been published in the *Electricity*  
3           *Journal, Energy Journal, Energy Policy, Public Utilities Fortnightly* and  
4           numerous conference proceedings, and I have made presentations on the  
5           economic and environmental dimensions of energy throughout the U.S.  
6           and internationally. My resume is provided here as Exhibit BEB-1.

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21

## 2. Summary and Recommendations

**Q. What is the purpose of your testimony in this case?**

A. I have been asked to assist Public Counsel by reviewing and commenting upon the benchmarking analysis and projected savings filed by Scottish Power in this case. My testimony also summarizes the testimony of Paul Chernick and Neil Talbot, witnesses for Public Counsel, and presents our overall recommendations in this case.

**Q. Please provide an overview of your analysis and this testimony.**

A. I begin with a discussion of Scottish Power’s expectation of large cost savings potential at PacifiCorp and contrast this with the “commitment” to pass \$10 million per year in corporate cost reductions on to PacifiCorp customers. I then address the two key areas of support that Scottish Power offers for its expectation of cost savings – its benchmarking analysis and its experience with Manweb in the UK.

The benchmarking analysis is a very abstract and limited exercise that deals with only a relatively small portion of PacifiCorp’s costs in a rather superficial way. The analysis is not very useful. Scottish Power itself expresses a lack of faith in its benchmarking analysis and declines to make a specific projection of savings or to guarantee any such savings on the basis of the benchmarking analysis.

Mr. Richardson points to the experience with Manweb as support for his

1 confidence that Scottish Power “can achieve significant efficiencies in  
2 PacifiCorp’s operations, and the resulting cost reductions will be captured  
3 through the ratemaking process to produce rates for customers that are  
4 lower than had the transaction not occurred” (Richardson Supplemental  
5 Testimony, pages 16 and 17. Specifically, Mr. Richardson points to  
6 reductions in bills for residential customers over a recent five-year period  
7 since Scottish Power acquired Manweb. Scottish Power did reduce costs  
8 at Manweb, but the situation faced in the UK by Manweb differs in  
9 important ways from that faced by PacifiCorp, most notably that Manweb  
10 was a government owned and operated business in the process of being  
11 privatized. To the extent that Manweb may be relevant, it should be  
12 viewed in context. Based upon data from OFFER for bills to typical  
13 residential customers over the same five-year period used by Mr.  
14 Richardson, the reductions at Manweb (22% are not exceptional, or even  
15 above average. Most of the Public Electricity Suppliers in the Great  
16 Britain had even greater residential bill savings over this same 5 year  
17 period, and the average for England and Wales as a whole was 23%.

18 **Q. What do you recommend in this case with regard to Scottish Power’s**  
19 **savings projections?**

20 A. While \$10 million per year of corporate cost savings is not insignificant, it  
21 should be viewed in the context of PacifiCorp as a \$2 billion per year  
22 company, and in the context of the risks associated with the merger  
23 discussed in Mr. Talbot’s testimony on behalf of Public Counsel.  
24 Moreover, before the \$10 million amount represents any real benefit to  
25 PacifiCorp customers there would have to be a rate case, and even then

1 realization of the savings could be elusive, since additional costs could  
2 offset the savings.

3 As for any additional cost savings, Scottish Power makes positive but  
4 unsubstantiated and noncommittal claims. I recommend that the  
5 Commission take a skeptical view toward cost savings that are not backed  
6 upon by enforceable guarantees and specific mechanisms. I recommend  
7 that the Commission recognize the potential for PacifiCorp to reduce costs  
8 as a stand-alone company, without the merger with Scottish Power. I  
9 recommend that the Commission not approve the merger on the basis of  
10 Scottish Power's unsubstantiated and noncommittal claims.

11 **Q. Please summarize Mr. Chernick's Testimony.**

12 A. Mr. Chernick reviews the performance standards and customer  
13 guarantees offered by Scottish Power as a merger benefit. Mr. Chernick  
14 concludes that what is being offered by Scottish Power is vague and  
15 therefore of uncertain benefit; that the Company's baseline performance is  
16 not defined, in part as a result of data quality problems; and that  
17 PacifiCorp should be able to implement these performance standards and  
18 customer guarantees without merging with Scottish Power.

19 **Q. Please summarize Mr. Talbot's Testimony.**

20 A. Mr. Talbot addresses financial aspects of the proposed merger. Mr.  
21 Talbot concludes that PacifiCorp's current financial situation is  
22 fundamentally sound, and that there will be no improvement to

1 PacifiCorp's cost of capital as a result of the merger, as claimed by  
2 Scottish Power. Rather, the merger carries substantial financial risks for  
3 PacifiCorp and therefore its customers. Specifically, Scottish Power's  
4 strategy of expansion and diversification could lead to management  
5 distraction and operating cost increases for PacifiCorp, and if Scottish  
6 Power becomes overextended or otherwise errs in its acquisition strategy,  
7 PacifiCorp's cost of capital could increase.

8 **Q. Overall, is the proposed merger in the public interest?**

9 A. No. The merger, as proposed, is not in the public interest.

10 Scottish Power has not offered a meaningful proposal to assure that  
11 customers receive an appropriate portion of merger benefits. The \$10  
12 million per year offered by Scottish Power as a merger benefit is a vague  
13 commitment that customers will not see for many years, if at all. The  
14 amount is small compared with the size of PacifiCorp's operations, small  
15 compared with savings estimates for other mergers, and small compared  
16 with Scottish Power's stated expectations of savings for this merger.  
17 There is no compelling evidence that future cost savings and proposed  
18 improvements to PacifiCorp's system performance and customer service  
19 require a merger with Scottish Power, or any merger at all. There are  
20 costs and risks associated with the merger, described in the testimony of  
21 Mr. Talbot. In general, the benefits to shareholders from the merger are  
22 relatively immediate and certain while the claimed benefits for customers  
23 are relatively distant, speculative, and unverifiable.

1           The Commission should not find the proposed merger to be in the public  
2           interest until Scottish Power and PacifiCorp offer a meaningful and  
3           verifiable means to guarantee that customers are not harmed by the risks  
4           inherent in the transaction. Furthermore, the uncertainties of the proposed  
5           customer service and service quality elements should be addressed.

### 3. Scottish Power's Projection of Cost Savings

1  
2 **Q. What level of cost savings does Scottish Power expect to achieve in**  
3 **operating PacifiCorp?**

4 A. Scottish Power's objective is that "PacifiCorp should be within the top ten  
5 major U.S. electric utilities with respect to non-generation operating costs  
6 as soon as possible" (MacRitchie Direct Testimony, page 4 and that the  
7 "current estimate is that it will take up to five years..." (MacRitchie Direct  
8 testimony, page 13. In round numbers, it would appear that this would  
9 require a reduction in PacifiCorp's non-production operating cost of about  
10 \$100 per customer, yielding a total savings of \$140 million per year (see  
11 Scottish Power response to Utah CCS data request 9.19.

12 Scottish Power also expects to realize savings in production costs, but it  
13 has not estimated these or set specific goals. Scottish Power has  
14 indicated savings of \$200 million. When asked about the basis for this  
15 figure, Scottish Power pointed to the \$140 million in potential cost savings  
16 identified in the benchmarking analysis of one category of costs, and  
17 stated that "It is not therefore unreasonable for Scottish Power to  
18 speculate that if it was to look across the whole company, to also include  
19 all the previously excluded costs, then there could indeed be the potential  
20 to save up to \$200 million." (Response to Utah CCS data request 9.19.

21 There is also an expectation of a net savings of \$10 million in corporate  
22 costs.

1 **Q. What amount of savings has Scottish Power offered as a benefit of**  
2 **the merger?**

3 A. Scottish Power has offered only the \$10 million savings in corporate costs.  
4 The Company states that it “will commit to reflecting this reduction in  
5 PacifiCorp’s results of operations filed with the Commission” (Richardson  
6 Supplemental, Ex. SP\_\_\_\_(AVR-1, page 6 and that this amount “will be  
7 reflected in cost of service by the end of the third year after the transition  
8 closes” (Richardson Supplemental Testimony, page 2.

9 **Q. How does the \$10 million figure compare with the size of PacifiCorp?**

10 A. The \$10 million amount is very small in the context of a Company the size  
11 of PacifiCorp, with annual revenues of about \$2 billion.

12 **Q. Is it assured that the \$10 million savings will be reflected in**  
13 **electricity prices?**

14 A. No. The treatment of the \$10 million savings that is committed is not  
15 clear. According to Mr. Richardson’s Supplemental Testimony (May 14,  
16 1999 Scottish Power has “committed to flow it through to customers  
17 through the ratemaking process” (page 1, line 13. This would require a  
18 rate case. It would also require that the net \$10 million reduction in  
19 corporate costs be achieved without shifting, or increasing other  
20 categories of costs offsetting the \$10 million reduction. Scottish Power  
21 has not offered to pass the \$10 million savings to customers in a merger-  
22 related rate reduction, but merely to recognize such savings in a rate case

1 filing, if such a filing occurs and is far enough into the future to include  
2 savings that are not expected until “the end of the third year following the  
3 closing of the transaction” (Mr. Green’s Direct Testimony, page 9.

4 In Washington, this would require a test year no earlier than 2002 for a  
5 filing no sooner than 2003. Given a typical rate proceeding, Washington  
6 consumers might see their share of the \$10 million from a 1999  
7 transaction reflected in rates in 2004. However, given the relatively small  
8 and uncertain size of any Washington share of the proposed benefits, it is  
9 also possible that rates would increase if any of the risks described by Mr.  
10 Talbot come to pass or if PacifiCorp alleged underearnings.

11 **Q. What evidence does Scottish Power offer in support of its**  
12 **expectation that it will be able to significantly cut costs in**  
13 **PacifiCorp’s operation?**

14 A. The two areas of support offered by Scottish Power are its benchmarking  
15 analysis and its experience with transforming Manweb. I will address each  
16 of these in turn.

1                                   **4. Scottish Power’s Benchmarking Analysis**

2   **Q.    Please describe the benchmarking analysis offered by Scottish**  
3   **Power in this case.**

4   A.    Mr. MacRitchie has presented Scottish Power’s “high-level preliminary  
5       estimates of the potential for operating cost savings” in PacifiCorp. The  
6       benchmarking analysis involved comparing 1996 cost data – excluding  
7       production, customer service and informational expenses and  
8       uncollectables – across roughly 144 U.S. companies. The comparison  
9       showed that “PacifiCorp’s operating costs per customer were higher than  
10      those experienced by many other utilities both in the Pacific Northwest  
11      and across the rest of the U.S.” and led Scottish Power to believe that  
12      “there is potential for reducing operating costs at PacifiCorp” (MacRitchie  
13      Direct Testimony, page 2.

14   **Q.    Is the Scottish Power benchmarking analysis a reasonable basis to**  
15   **predict savings in PacifiCorp’s operations?**

16   A.    It may have some value, but only in a very limited sense. It is a very  
17       superficial comparison – presented in a simple two-page table sponsored  
18       by Mr. MacRitchie. It excludes production costs and several categories of  
19       non-production costs (customer service, informational, and uncollectables.  
20       This leaves only about \$415 million to be included in the analysis, less  
21       than one fifth of PacifiCorp’s annual retail operating revenues.

22       The benchmarking analysis involves almost no effort to account for

1 differences in the conditions of the different companies. For example,  
2 companies of widely different sizes are compared, ranging from 6  
3 thousand customers to 4.6 million customers. Companies in the  
4 benchmarking analysis also have very different amounts of distribution  
5 lines, one of the primary factors driving distribution system maintenance  
6 costs. The benchmarking analysis is done by expressing costs per  
7 customer – making no effort to account for the fact that industrial  
8 customers are larger and impose greater costs than residential customers.  
9 Companies in the benchmarking analysis have significantly different  
10 mixes of high and low usage customers.

11 Also, PacifiCorp has an extensive transmission system and mine-mouth  
12 coal generation, so one might reasonably expect its generation costs to be  
13 low and its transmission costs to be high, relative to a more typical  
14 company. Benchmarking comparisons, such as Scottish Power's that  
15 focus exclusively upon non-production operating costs could thereby tend  
16 to overstate the potential for cost reduction in that area for PacifiCorp.

17 **Q. How do PacifiCorp's total residential prices compare with other**  
18 **companies in the U.S.?**

19 A. I have listed residential prices for 177 U.S. companies in Exhibit\_\_\_BEB-2,  
20 with PacifiCorp's state-specific prices indicated. The data source is the  
21 Edison Electric Institute's Typical Bills database for Winter 1998.  
22 PacifiCorp's prices are among the lowest, particularly for its sales in the  
23 Washington (#10, Wyoming (#14, and Oregon (#27 areas.

1 **Q. Does the price data presented in Exhibit\_\_\_(BEB-2 have the same**  
2 **problem of comparing companies in different situations?**

3 A. Yes. It is a simple comparison of simple revenue per unit of sales, and  
4 does not involve any adjustments to account for differing conditions in  
5 which various companies operate. I offer these price data in order to  
6 show how PacifiCorp compares with other U.S. companies when all of the  
7 cost categories are included. These residential price data suggest that  
8 PacifiCorp is among the lower cost companies overall. This is similar to  
9 the conclusion reached by Mr. MacRitchie in his examination of non-  
10 production costs – but indicates that perhaps there is somewhat less room  
11 for cost reduction in the production area, at least on a percentage basis.

12 **Q. Are there other assessments that indicate that PacifiCorp is doing**  
13 **reasonably well on its own?**

14 A. Yes. A recent article in Public Utilities Fortnightly analyzed data for one  
15 hundred U.S. utilities and identified PacifiCorp as one of nineteen  
16 “efficient” utilities (“The Fortnightly 100: Which Utility Ranks the Highest,”  
17 by Forrester, Khawaja, Haeri, and Carter, September 1, 1998.

18 **Q. Does the benchmarking analysis account for PacifiCorp’s ability to**  
19 **realize cost savings on its own?**

20 A. No. The benchmarking simply compares PacifiCorp with other companies  
21 and indicates that there may be some room for improvement in reducing  
22 costs per customer. It makes no attempt to account for savings that

1 PacifiCorp could achieve without the merger. PacifiCorp has already  
2 made some substantial employment reductions over the past few years,  
3 and with its renewed focus upon its core electric utility business can be  
4 expected to make gradual efficiency improvements in the future. A true  
5 analysis of the “benefits of the merger” would compare scenarios with and  
6 without the proposed merger.

7 **Q. Does Scottish Power disagree with your view of the adequacy of the**  
8 **benchmarking analysis?**

9 A. I expect that Scottish Power would generally agree with my view that the  
10 benchmarking analysis is not adequate as a reliable estimate of future  
11 cost savings. Scottish Power has been careful to state that the  
12 benchmarking is “preliminary” and was used only to determine that “there  
13 is potential to reduce operating costs in PacifiCorp” (MacRitchie Direct  
14 Testimony, page 2. Mr. MacRitchie has stated that Scottish Power would  
15 conduct more detailed benchmarking as part of its overall process of  
16 “transforming the business” after the closing date of the merger  
17 (MacRitchie Rebuttal Testimony before the Public Utility Commission of  
18 Oregon, June 2, 1999 in UM 918.

19 **Q. What is your conclusion regarding the benchmarking analysis?**

20 A. I conclude that savings may be somewhat more difficult to achieve at  
21 PacifiCorp than would be suggested by Scottish Power’s preliminary  
22 benchmarking analysis, and that there has been no analysis whatsoever  
23 of incremental savings attributable to the merger, other than the claimed

1 net savings of \$10 million in corporate costs discussed above.

1       **5. Scottish Power’s Experience With Cost Reduction in the UK**

2       **Q.     What evidence from the UK does Scottish Power point to in support**  
3       **of its expectation that it can reduce costs in PacifiCorp’s operations?**

4       A.     The primary example put forward by Scottish Power in support of its ability  
5       to transform a regulated electric utility business is Manweb, which Scottish  
6       Power acquired in 1995 (see MacRitchie direct testimony, page 6 and 8.  
7       Mr. Richardson provides a specific example of the average residential  
8       customer’s bill in the Manweb service territory, which he points out  
9       declined by 25% in real terms between 1993/94 and 1998/99 (Richardson  
10      supplemental testimony, page 15.

11      **Q.     Please comment on the relevance of the Manweb experience to**  
12      **PacifiCorp.**

13      A.     The situation at Manweb in 1995 was quite different from that currently  
14      faced by PacifiCorp. The distribution companies in the UK had been  
15      government organizations with well known inefficiencies, and were in the  
16      process of being privatized. In contrast, PacifiCorp has been a privately  
17      owned company subject to state price regulation and some degree of  
18      competition – and has already made substantial employment reductions  
19      over the past few years. Also, the geographic differences between  
20      Manweb and PacifiCorp are considerable. Manweb serves a fairly small  
21      and densely populated area in England while PacifiCorp serves a  
22      sprawling area including portions of five Western states that in total is  
23      larger than the entire UK. While the experience with Manweb has some  
24      relevance to what Scottish Power may do with PacifiCorp, the applicability

1 is limited.

2 **Q. Is the 25% reduction in residential bills at Manweb an accurate**  
3 **figure?**

4 A. I am not certain. It does not agree with data from OFFER which shows a  
5 reduction of only 22% for Manweb between 1993/94 and 1998/99. I have  
6 not been able to establish the reason for this difference.

7 **Q. How does the amount of residential bill reduction for Manweb over**  
8 **this period compare with that experienced by customers of other**  
9 **electricity suppliers in the UK?**

10 A. The data published by OFFER showing a bill reduction for Manweb  
11 customers of 22% has analogous data for the other systems in the UK.  
12 These prices are summarized in Exhibit\_\_\_(BEB-3. They show that most  
13 of the Public Electricity Suppliers in the Great Britain had even greater  
14 average residential bill savings over this same 5 year period, and that the  
15 average for England and Wales as a whole was 23%.

16 The Manweb experience is not exceptional, at least insofar as savings to  
17 residential customers is concerned.

18 **Q. Have you reviewed data on cost trends at Manweb and other**  
19 **systems in the UK?**

20 A. As far as I am aware, cost data analogous to the data on bill trends

1 discussed above is not available. However, as discussed in Mr. Talbot's  
2 testimony, the trend in Manweb's returns on capital employed has been  
3 similar to the trend for other Public Electricity Suppliers, supporting the  
4 idea that Manweb's costs have followed a trend similar to the other Public  
5 Electricity Suppliers as well.

6 **Q. What has the trend been in Scottish Power's own residential prices**  
7 **in recent years?**

8 A. The data in Exhibit\_\_\_(BEB-3 indicate that Scottish Power's current prices  
9 are among the highest in the UK, well above average – and that the bill  
10 reductions for residential customers have been lagging behind other  
11 companies. Scottish Power's typical residential bill decreased by only  
12 18% over the recent five-year period during which the average decline for  
13 residential customers in Great Britain was 22%.

14 Similar data for the four year period just prior to this (1989/90 to 1993/94  
15 show that Scottish Power's average residential bill actually increased  
16 slightly in real terms (by 1% while the general trend in Great Britain was  
17 downward (by 3%.

18 **Q. What do you conclude about Scottish Power's UK performance and**  
19 **its ability to transfer that performance to PacifiCorp?**

20 A. Scottish Power's performance, based upon the information described  
21 above, is adequate but not spectacular. Price reductions appear to be in  
22 line with what other UK providers have achieved. This does not indicate

1           that the Commission and consumers in the U.S. should expect results that  
2           PacifiCorp could not achieve on its own.

3   **Q.    Does this conclude your testimony?**

4   **A.    Yes.**