ORIGINAL

Roger E. Clark, Esq.

Attorney for The Environmentalists

905 Denston Drive
Ambler, PA 19002-3901
phone: 215.643.2364
fax: 215.628.2630
e-mail: rclark@libertynet.org

February 12, 1998

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
P.O. Box 3265
Harrisburg, PA 17105-3265

KJR

Re: Application of Duquesne Light Company
for Approval of its Restructuring Plan,
Docket No. R-00974104

Dear Mr. McNulty:

As a favor to David Hughes, I agreed to file his brief in the above-captioned proceeding. Unfortunately, I sent the wrong number of copies of his brief for filing just as I did for the Environmentalists' briefs in the Duquesne and West Penn proceedings.

Enclosed are eight additional copies of David Hughes' brief in the Duquesne restructuring proceeding.

Sincerely,

DOCUMENT
FOLDER

Roger E. Clark
Attorney for the Environmentalists

Enclosures: Eight additional copies of the Duquesne Light brief of David Hughes

ORIGINAL

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Application of Duquesne Light Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code	} } }	Docket No. R-00974104

MAIN BRIEF OF DAVID HUGHES

FEBRUARY 10, 1998

INTRODUCTION AND SUMMARY OF ARGUMENT

I am David Hughes, a Duquesne Light Company ("Duquesne") rate payer. Once Duquesne implemented (in 1974) its ill-fated decision to build nuclear generation, its rates began an upward climb that has kept the cost of its electricity to residential customers significantly above the national average for over two decades. I believe the Commission should make a determination as to whether Duquesne's current rates are just and reasonable before it makes decisions with regard to prospective issues such as stranded cost recovery. Accordingly, I filed a Formal Complaint on June 14, 1994, requesting that the Pennsylvania Public Utility Commission ("Commission") conduct an investigation to determine whether Duquesne's current rates are just and reasonable. On September 19, 1996, the Commission granted a stay in that proceeding, stating that the instant restructuring proceeding would be the "appropriate forum" for the Commission to investigate my complaint issues. Accordingly, I have submitted Direct and Surrebuttal Testimony in this restructuring proceeding, and today present this Main Brief.

This Main Brief includes the following arguments:

- Duquesne's **current** rates are unjust and unreasonable, a situation that should be remedied **before** the onset of retail competition.
- Duquesne's nuclear units should not be included in the Commission's calculation of the Company's stranded cost.
- Duquesne's cold reserved units should not be included in the Commission's calculation of the Company's stranded costs.
- Duquesne has a poor stranded cost mitigation track record.
- The Commission should follow the law in determining just and reasonable stranded cost recovery.

ARGUMENT

1) Duquesne's current rates are unjust and unreasonable.

It is my contention that Duquesne's **current** rates are unjust and unreasonable as a result of the failure of the Perry 1 and Beaver Valley 2 (BV2)generating units to provide an economic benefit to rate payers. The high cost of these units has precluded Duquesne from giving its customers rate reductions. Perry 1 and BV2 fail to meet the useful side of the used and useful test.

Duquesne's rates were set by the Commission in March, 1988. In that rate base case, the Commission found that Duquesne had failed to meet its burden of proof that Perry 1 and BV2 did not represent economic excess capacity on the Company's system; and the Commission made a relatively small excess capacity adjustment for this at the time. Duquesne has admitted *(Clayton Rebuttal Testimony, p. 57) that these adjustments did not cost the Company.* However, the decision to rate base Perry 1 and BV2 has resulted in enormous costs to rate payers. The rate base decision was based on projections of how these units would perform. We now have 10 years of operation and it is clear that Perry 1 and BV2 have not provided, and most likely will never provide, an economic benefit (energy savings) to rate payers.

In my formal complaint testimony (Exhibit DH-4)), I detailed how the Perry Plant was particularly expensive and in Exhibit DH-5, how Duquesne itself admitted that this unit was a "financial drain" on the Company. Duquesne chose not to rebut my complaint testimony. Mr. Duckworth attempted to do that in the instant proceeding, but as I made clear in my surrebuttal

testimony (pp 6-8), there were serious flaws in his rebuttal. Mr. Duckworth chose not to offer a rejoinder to my surrebuttal and admitted (transcript p. 687:11) that Perry has "caused Duquesne to spend unanticipated expenditures". I focused on Perry only to show, as vividly as possible, how the investment in nuclear generation has failed. However, the Commission's Order in the complaint case stated (p.7) that rather than examining the economics of one generating unit, the Commission would prefer to evaluate all the units on the Duquesne system within the restructuring proceeding. Following the Commission's Order, I intervened in the instant proceeding and have presented testimony with regard to the units that make up the bulk of Duquesne's stranded costs, including Perry 1, BV2, Brunot and Phillips stations.

The questions that must be addressed in this proceeding are: Are these units used and useful? Do they provide an economic benefit to rate payers? Do Perry 1 and BV2 costs preclude Duquesne from giving rate reductions? The answer to all of these questions is yes. The Company has not rebutted my contention that Perry 1 and BV2 are uneconomical; that the units fail to provide an economic benefit to rate payers. Indeed, under cross examination, Mr. Marshall (see evidentiary hearing transcript pp 113-116) and Mr. Clayton (transcript pp. 287-293) have stated that Duquesne does not make an analysis of the economics of a generating unit based on whether the unit provides energy savings to rate payers, but rather on the basis of whether, on a "to go" basis, it would be cheaper to operate the unit or shut it down. This method of economic analysis ignores one important factor: sunk costs.

Mr. Biewald's surrebuttal testimony in this case included an economic analysis (Environmentalists Statement No. 2-S, exhibits 5, 6 and 7) of Duquesne's shares of Perry 1 and

BV2. Mr. Biewald concluded (page 4) that for Perry 1, the cumulative losses amount to approximately $2.0 billion (in 1997 present value dollars) and for BV2, the cumulative losses total approximately $1.0 billion (also in 1997 present value dollars).

There was only one challenge to Mr. Biewald's analysis in the entire record of this case, and that was by Mr. Schnitzer, in his oral rejoinder testimony. Mr. Schnitzer did not criticize any of Mr. Biewald's specific assumptions or calculations. Rather, Mr. Schnitzer merely pointed out that in his opinion, once a unit has already been constructed, an economic analysis of the unit should include only "avoidable costs" (transcript, page 386, lines 15 to 23). On cross-examination, Mr. Schnitzer explained that "the only way I know to reasonably interpret that question: 'Are Perry 1 and Beaver Valley 2 economically useful?', is to ask, given that the plants do exist, on an economic basis, does it make sense to continue to operate them or not" (transcript page 499). Mr. Schnitzer's lack of imagination would apparently rule construction costs out of any economic analysis.

For Perry 1 and BV2, the exorbitant construction costs were the root of the economic problem. If one is deciding whether or not a generating unit should continue to be operated, then it would be appropriate to exclude construction costs from the analysis, since they are "sunk" and therefore unavoidable. On the other hand, if one seeks to determine whether a generating unit is "economically useful", then it is important to include all of the costs. This latter question is the one that concerns us here. That is, "What are the economic costs and benefits associated with these units, and how do the costs and benefits compare?" Mr. Biewald's analysis speaks directly to these questions, and he finds that the costs greatly exceed the benefits, yielding net

losses of $2 billion and $1 billion for Perry 1 and BV2, respectively. Mr. Biewald did not conclude that the nuclear units should be shut down. He did not analyze that question. He did conclude that the Company's involvement in these units, including Duquesne's share of the construction costs, has been an economic disaster. In this situation, it is appropriate to protect customers from bearing the full burden of the economic losses. Indeed , the Commission has an obligation to share such losses between consumers and shareholders. Rates that put all of the economic losses upon customers are not just and reasonable.

If Duquesne volunteered to remove the construction costs from rates, then they could be excluded from the economic analysis. As long as the Company requests that customers pay the carrying costs or (in the case of BV2) lease payments associated with the construction costs, then these costs should, indeed must, be included in the economic analysis. This is what Mr. Biewald has done. Mr. Schnitzer's testimony (rejoinder and cross-examination) indicates that he fails to understand the purpose of Mr. Biewald's economic analysis. If Mr. Schnitzer's understanding of the purpose of the analysis were correct - that Mr. Biewald was attempting to determine whether the units should continue operating - then his criticism would be valid. In fact, this was not the purpose of Mr. Biewald's analysis, thus, Mr. Schnitzer's criticism is erroneous.

Mr. Schnitzer states in his Rebuttal Testimony (p. 37:3); "I fail to see how Duquesne's rates can be just and reasonable today based on prudently incurred costs and magically be unjust and unreasonable the next day based on the same prudently incurred costs". Obviously, Mr. Schnitzer does not understand Pennsylvania utility regulations. The Commission has the authority to make a determination, at any time, as to the just and reasonableness of a company's

rates.[1] This is particularly the case when new information is available and justifies a Commission investigation. A generating unit that is used and useful today, could become not used or not useful tomorrow. Indeed, that is the crux of my argument. The analysis Mr. Biewald has done is based on information the Commission did not have when it last looked (1987) at the economics of these units. We now have new information, i.e. 10 years of operation. Despite Messrs. Marshall's, Clayton's and Schnitzer's constant references to the prudence of these investments , these "prudently" incurred costs are not used and useful. The two standards are not related. Mr. Schnitzer does recognize, however, that these investments were "economically unsuccessful".[2]

Thus, my contention stands: Perry 1 and BV2 are uneconomical and have precluded Duquesne from giving customers rate relief. I contend that rate payers should be refunded for all the charges they have paid for these uneconomic plants since 1990. 66 Pa., Section 1312 gives the Commission "the power and authority to make an order requiring the public utility to refund the amount of excess paid...within four years prior to the date of the filing of the complaint, together with interest at the legal rate from the date of each such excessive payment".

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[1] ALJ Orders in Docket no. C-945953, 12/21/94, p.5 and 4/10/96 pp. 5&6; 66 Pa. PUC Sections 1311 & 1323(c); *PA PUC v. West Penn Power Co.* 63a PUC 295, 303 (1987); *PA PUC v. Philadelphia Electric Co.*, Docket No. M-880183 (1988).

[2] Schnitzer Rebuttal Testimony, p. 41.

2) Duquesne's nuclear units should not be included in the Commission's calculation of the Company's stranded costs. **[outline section IV F (4)]**

I suggest that the Commission's task in determining appropriate stranded cost recovery has two parts. First the Commission must calculate what it believes the Company's stranded costs to actually be. Then the Commission must decide how much of those stranded costs are just and reasonable to recover. As I have argued in my testimony, I do not believe the Commission should include the cost of Perry 1 and BV2 in its calculation of the Company's stranded costs. Section 2803 of The Electric Generation Customer Choice and Competition Act ("Act")states that stranded or transition costs are costs "which traditionally would be recoverable under a regulated environment". Had the Commission done as I requested, and investigated the just and reasonableness of Duguesne's rates in 1993 and 1994, the Commission would have found that the Company's rates were not just and reasonable as a result of the fact that Perry 1 and BV2 did not meet the "useful" part of the excess capacity standard. The cost of Perry 1 and BV2 would, then, not be recoverable under a regulated environment. This is what I asked the Commission to do in my complaint case and the Commission said the instant proceeding is the appropriate place to make this determination. So again, I request that the Commission make a determination in the instant proceeding as to whether Duquense's current rates are just and reasonable.

To summarize: the evidence submitted in this proceeding has shown that Perry 1 and BV2 are uneconomic; neither Perry 1 or BV2 provide energy savings for rate payers. Thus, these units are not useful. The Company has not successfully rebutted this evidence. Therefore, the

Commission should adjust Duquesne's current rates first, to provide the appropriate relief. Once that is done, and it should be done, these units, then, fail to meet the definition of recoverable stranded costs in the Act. The Commission must, then, disallow the cost of these units in its stranded cost calculation.

3) Duquesne's cold reserved units should not be included in the Commission's calculation of the Company's stranded costs. **[IV B 2(c)]**

Duquesne is seeking recovery of the costs associated with the Brunot and Phillips units that are in cold reserve. The Company freely chose to remove these units from service. By the company's own admission (Exhibit DH-6), Brunot and Phillips are efficient and reliable generators. The Company could have kept these units in rate base and cold reserved more uneconomic units (e.g. Perry 1 and BV2), but it chose not to do this. Cold reserved units are not recoverable under regulation or traditional rate making. Thus, these assets are not stranded costs by definition (Act section 2803). The Company has not offered a valid reason for recovery of these assets, and expressed no intention to return these units to rate base. Therefore, I support the OTS and HHS in requesting that the Commission not include the Brunot and Phillips cold reserved units in its stranded cost calculation.

4) Duquesne has a poor stranded cost mitigation track record. **[IV F 2 (a)]**

Section 2808(c)(4) of the Act requires the Commission to consider mitigation efforts undertaken by the Company in making a determination of stranded cost recovery. First, the Company's mitigation efforts have been poor at best. As Jonathan Muehl's Direct Testimony plainly shows, Duquesne has had sufficient resources to mitigate all of their stranded costs. Duquesne chose to be the number one utility in the U. S. in terms of shareholde return rather than mitigate its stranded costs. Duquesne has not rebutted Mr. Muehl's testimony.

Secondly, a close look at Duquesne's testimony regarding the Company's mitigation efforts discloses an inflated mitigation calculation that is embarrassingly transparent. Although Mr. Clayton attempted to obfuscate the issue in his cross (pp.278-285), both he and Mr. Marshall are quite clear in their Direct Testimony[3] that most of the dollar amount of mitigation comes from cancellation of planned capacity additions that have nothing to do with the transition to competition. The cancellation of the Erie 1 and 2 and Davis Besse 2 and 3 nuclear units in 1980, the cold reserving of Brunot Island and Phillips in 1985 and 1986, and the abandonment of Perry 2 in 1986, have nothing to do with mitigating stranded costs as called for in the Act. And to claim "avoided rate increases" as stranded cost mitigation is laughable. The only decision or action that Duquesne has taken that can even be considered as a mitigating factor in reducing potential stranded costs is the Fort Martin sale. Thus, the $130 million in savings from the Fort Martin sale is the extent of Duquesne's stranded cost mitigation. The truth is, Duquesne has done

[3] Marshall Direct Testimony, pp. 19 & 20; Clayton Direct Testimony, p. 24

very little in this regard and the Commission should seriously consider this fact in determining just and reasonable stranded cost recovery.

5) The Commission should follow the law in determining a just and reasonable stranded cost recovery. **[IV F 2 (b)]**

David Marshall would have us believe that "[T]he Act...makes no reference at all to a generic 'sharing' of stranded costs."[4] However, sections 2802(8) and 2804(14) are very clear in calling for a fair sharing of the burdens associated with the transition to competition. If mistakes are to be shared, the fairest method of sharing is, by definition, a 50/50 split of these costs. Accordingly, anything more than a 50% recovery of stranded costs is unjust and unreasonable. In addition, I ask that the Commission seriously consider that, up to now, only customers of Duquesne have borne the negative consequences of Duquesne's management decisions. As Mr. Muehl's testimony so graphically illustrates, Duquesne's shareholders have only reaped positive benefits from Duquense's nuclear investment saga. Is it not time to swing the pendulum back to the fairness range?

[4] *Marshal Rebuttal Testimony, p. 18.*

CONCLUSION

To conclude, first, rate payers are due a refund for the losses associated with the Perry 1 and BV2 nuclear units since 1990. Second, there is no justification for recovery of future costs associated with the Perry 1, BV 2, Brunot Island and the Phillips investments. Duquesne has failed to adequately mitigate its stranded costs as required by the Act and has not met its burden of proof in rebutting the arguments for disallowance. For the Company to request 100% stranded cost recovery, assumes that the current rates would remain in place for the life of the units in question. I submit that, had deregulation not occurred, it is extremely unlikely that Duquesne's current rates would have remained in place for long. The Commission would eventually do what I am asking it to do now: First, adjust Duquesne's current rates to a level that is just and reasonable, and make that adjustment retroactive, as per section 1312 of the Public Utility Code, to 1990. Second, disallow the cost of Perry 1, BV2, Brunot and Phillips stations from any stranded cost recovery.

Accordingly, I request that the Commission consider implementing one of the following three remedies (All figures in 1997 present value dollars):

1. Using Mr. Biewald's unrebutted calculations, and keeping in mind section 1312 of the code, issue a refund to rate payers of $2,209 million for Perry 1 and BV2 losses experienced from 1990 to 1998. Disallow the full value of Perry and BV2 from stranded cost recovery, or

2. Refund $2,209 million and disallow $451 million in stranded cost recovery for Perry I and BV2 losses for the years 1999 through 2026, or

3. In the spirit of compromise and sharing of the burden as required by the Act, the Commission should, at the very minimum, issue a refund to customers in the amount of $1,105 million and order a stranded cost recovery disallowance of $226 million.

These recommendations only deal with the costs addressed in this brief and are not to be considered as my proposal for total stranded cost disallowance/recovery.

Finally, I request that the Commission discount any stranded cost recovery in the amount that Duquesne received as part of its settlement with the General Electric Company relative to the GE Mark III reactor problems at the Perry Plant.

Respectfully Submitted,

David Hughes

February 10, 1998

DAVID HUGHES MAIN BRIEF

SUMMARY OF STRANDED COSTS
($000)

	Company Claim	Adjustments	Adjusted Amount
Nuclear			
Fossil			
Regulatory Assets			
Total Net Present Value (NPV) in 1999$		($226)*	
PUC Jurisdictional %			

STRANDED COST CALCULATION-NUCLEAR
($000)

	Company Claim	Adjustments	Adjusted Amount
Net Book Value			
(Market Value)			
PV of Nuclear Decommissioning			
PV of costs Independent of Operation			
Net Present Value (NPV) in 1999 $ (a+b+c+d)		($226)*	
Discount Rate			
PUC Jurisdictional %			

* Does not include refund for past losses, full Perry1, BV2 or Brunot & Phillips disallowance

February 9, 1998

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
North Office Building-Filing Room
P.O. Box 3265
Harrisburg, PA 17105-3265

Re: *Duquesne Light Company Application for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code, Docket No. R-00974104.*

Dear Mr. McNulty:

Enclosed, please find a copy of the Main Brief of David Hughes in the above-referenced matter. A true copy of this document has been served upon all parties of record.

Thank you for your attention to this matter.

Yours truly,

David Hughes
4037 Ludwick St.
Pittsburgh, PA 15217
(412) 421-4163

Enclosures

cc: Judge John H. Corbett, Jr.
All parties

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Application of Duquesne Light Company for Approval of its Restructuring Plan : Docket No. R-00974104

CERTIFICATE OF SERVICE

I hereby certify that I have, served the Brief of David Hughes in the above-referenced docket upon the following persons, in the manner specified and on the dates indicated:

Service by Federal Express Overnight Mail for Delivery on February 10, 1998:

The Hon. John Corbett
PA Public Utility Commission
1103 Pittsburgh State Ofc. Bldg.
Pittsburgh PA 15222

John S. Moot, Esq.
Skadden, Arps, Slate, Meagher & Flom, LLP
1440 New York Avenue, NW
Washington DC 20005

Larry R. Crayne, Esquire
Duquesne Light Company
411 Seventh Avenue
Pittsburgh PA 15219

Rodney R. Akers
Assistant City Solicitor
313 City-County Bldg.
414 Grant Street
Pittsburgh PA 15219

David Hughes, Esquire
4037 Ludwick Street
Pittsburgh PA 15217

Scott J. Rubin, Esquire
IBEW
3 Lost Creek Drive
Selinsgrove PA 17870

Stephen L. Feld, Esquire
Pennsylvania Power Company
1 East Washington Street
P.O. Box 891
New Castle PA 16103-0891

Steven Baicker-McKee, Esq.
Wanda Schiller, Esq.
Babst, Calland, Clements & Zomnir PC
8th Floor, Two Gateway Center
Pittsburgh,PA 16222

Mark F. Sundback, Esq.
Kenneth L. Wiseman, Esq.
Andrews & Kurth, LLP
1701 Pennsylvania Avenue
Washington DC 20006

Michael L. Kurtz, Esq.
David F. Boehm, Esq.
Boehm, Kurtz & Lowry
2110 Cbld Center
36 East Seventh Street
Cincinnati OH 45202

Howard M. Louik, Esq.
Allegheny County Law Dept.
300 Fort Pitt Commons
445 Fort Pitt Boulevard
Pittsburgh PA 15219

Robert J. Stefanko, Esq.
341 South Bellefield Avenue
Pittsburgh PA 151213

Margaret Peters, Esq.
The Peoples Natural Gas Company
625 Liberty Avenue
Pittsburgh PA 15222-3197

John Stember, Esq.
Low Income Advocate Parties
1705 Allegheny Bldg.
429 Forbes Avenue
Pittsburgh PA 15219

Mark J. McGuire, Esq.
Ronald N. Carroll, Esq.
Jenner & Block, Suite 1200
601 13th Street, Nw
Washington DC 20005

Paul E. Russell, Esq.
Penna. Power & Light Company
Two North 9th Street
Allentown PA 18101

Councilman Jim Ferlo
510 City Council Building
Pittsburgh, PA 15219

Tim Merrill, Esquire
Suite 200
4 Penn Center West
Pittsburgh, PA 15276

Douglas F. John, Esq.
John & Hengerer
Suite 600
1200 17th Street, NW
Washington, D.C. 20036

Gary Jeffries, Esquire
CNG Energy Services
One Parkridge Center
Pittsburgh, PA 15244-0746

David Cruthirds
Electric Clearinghouse
Suite 5800
1000 Louisiana
Houston, TX 77002-5050

Donald A. Kalpan, Esquire
Preston, Gates, Ellis & Rouvelas Meeds
1735 New York Ave, N.W. - Suite 500
Washongton, D.C. 20006-4759

In-Hand Service on February 10, 1998

Edmund Berger, Esquire
Office of Consumer Advocate
1425 Strawberry Square
Harrisburg, PA 17105

Kandace Melillo, Esquire
Wayne Scott, Esquire
Office of Trial Staff
PA Public Utility Commission
Pitnick Building
Harrisburg PA 17105

Karen Oill Moury, Esquire
Office of Small Business Adv.
Suite 1102, Commerce Bldg.
300 North Second Street
Harrisburg PA 17120

Robert Young, Esq.
Allegheny Electric Coop., Inc.
212 Locust Street
Harrisburg PA 17108-1266

Patricia Armstrong, Esquire
Thomas, Thomas, Armstrong &Niesen
212 Locust Street
Harrisburg PA 17108-9500

Robert A. Mills, Esq.
McNees, Wallace & Nurick
100 Pine Street
P.O. Box 1166
Harrisburg PA 17108-1166

Brian A. Rider, President
Pennsylvania Retailers' Association
224 Pine Street
Harrisburg PA 17101-1325

Deneice Covert Zeve, Esq.
Terry Lupia, Esq.
Office of Attorney General
14th Floor, Strawberry Square
Harrisburg, PA 17120

Kevin J. McKeon, Esq.
Malatesta, Hawke & McKeon
100 North 10th Street
Harrisburg PA 17105

William T. Hawke, Esq.
Malatesta, Hawke & McKeon
100 North 10th Street
Harrisburg PA 17105

John Wilson, Exec. Dir.
Community Action Assn. of PA
222 Pine St.
Harrisburg, PA 17101

Thomas P. Gadsden, Esquire
Morgan, Lewis & Bockius
2000 One Logan Square
Philadelphia PA 19103-6993

Mary McFall Hopper, Esquire
PECO Energy Company
2301 Market Street S23-1
Philadelphia PA 19103

James P. Dougherty, Esq.
Robert A. Weishaar, Jr., Esq.
100 Pine Street
Harrisburg PA 17108

Daniel Clearfield, Esquire
Robert Longwell, Esquire
Wolf Block Schorr &Solis-Cohen
212 Locust St., Ste. 300
Harrisburg PA 17101

Terrance J. Fitzpatrick, Esq.
Ryan, Russell , Ogden & Seltzer
Suite 101
800 North Third Street
Harrisburg PA 17102-2025

Kenneth Zielonis, Esq.
Stevens & Lee
Pennsylvania Retailers' Assoc
208 North Third St, Suite 310
Harrisburg PA 17101

David M. Boonin
New Energy Ventures East, LLC
Suite 800
200 South Broad Street
Philadelphia PA 19102

Joseph A. Dworetzky, Esq.
John P. Lavelle, Jr., Esq.
Hangley Aronchick, Segal & Pudlin
12th Floor, One Logan Square
Philadelphia PA 19103

Service by First Class Mail on February 9, 1998

Brian Kalcic
Excel Consulting
Suite 720-T
225 S. Meramec Avenue
St. Louis MO 63105

James D. Steffes
Enron Power Marketing Inc.
1400 Smith Street
Houston TX 77002

Vickiren S. Aeshleman
QST Energy Inc.
300 Hamilton Blvd. - Suite 300
Peoria Il 61602

Robert B. Weisenmiller
MRW & Associates, Inc.
Suite 1440
1999 Harrison Street
Oakland CA 94612-3517

Michael Reid, Director
Materials Management Services
Administrative Resources, Inc.
500 Commonwealth Drive
Warrendale PA 15086-7513

Thomas J. Augspurger, Esq.
MiDCon Corporation
Office of General Counsel
701 East 22nd Street
Lombard Il 60148

Donald R. Ayersman, Jr., Esq.
IBEW
1125 Denver Avenue
Morgantown WV 26505

Lawrence E. Moncrief, Esq.
NAACP
1364 Silverton Ave.
Pittsburgh PA 15206

Albert M. Benincasa, Esq.
Director, Regulatory Affairs
Skipping Stone
46 9th Avenue
Sea Cliff NY 11579

Stephen J. Baron
J. Kennedy and Associates, Inc.
Suite 475
35 Glenlake Parkway
Atlanta GA 30328

John O'Brien, Esq.
Wheeled Electric Power Co.
Suite 207
50 Charles Lindburgh Blvd.
Uniondale NY 11553

Cindy Datig
$1 Energy Fund
P.O. Box 42329
Pittsburgh, PA 15203

Craig Nifong
Midcon Corporation
3200 Southwest Freeway
Houston, TX 77027

Timothy Moran
986 Greentree Road
Pittsburgh, PA

Roger E. Clark
905 Denston Drive
Ambler, PA 19002

v. 215-643-2364 / f. 215-628-2630

February 9, 1998

ANDREWS & KURTH L.L.P.
A REGISTERED LIMITED LIABILITY PARTNERSHIP
ATTORNEYS
1701 PENNSYLVANIA AVENUE, N.W.
SUITE 200
WASHINGTON, D.C. 20006-5805

TELEPHONE:(202) 662-2700
TELECOPIER:(202) 662-2739
TELEX: 79-1208

OTHER OFFICES:
HOUSTON
DALLAS
LOS ANGELES
NEW YORK
THE WOODLANDS
LONDON

ROBERT M. LAMKIN
202-662-2779

KJR

DOCUMENT FOLDER

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FEB 16 1998

PA PUBLIC UTILITY COMMISSION
PROTHONOTARY'S OFFICE

February 16, 1998

VIA OVERNIGHT MAIL

James J. McNulty
Prothonotary
Pennsylvania Public Utility Commission
North Office Building
Commonwealth Avenue and North Street
Harrisburg, Pennsylvania 17120

Re: Duquesne Light Company Restructuring Proceeding,
Docket No. R-00974104

Dear Mr. McNulty:

Pursuant to Sections 1.4 and 5.502 of the Pennsylvania Public Utility Code, enclosed please accept for filing an original and nine (9) copies of the Reply Brief of Hospital Shared Services and Administrative Resources, Inc. in the above-captioned proceeding.

Also, please find an additional copy of the cover of the Reply Brief to be stamped and returned to me in the enclosed self-addressed postage prepaid envelope.

Sincerely,

Robert M. Lamkin
One of Counsel for Hospital Shared Services
and Administrative Resources, Inc.

Enclosures

cc: Judge Corbett (w/encl.
and computer diskette version)
All parties (w/ encl. via first-class
mail dated Feb. 17, 1998)

5

WAS01:48296.1

ORIGINAL

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission,	)	
	)	
v.	)	Docket No. R-00974104
	)	
Duquesne Light Company Application to approve restructuring plan pursuant to 66 Pa. C.S. § 2806(d)	)	

REPLY BRIEF OF HOSPITAL SHARED SERVICES AND ADMINISTRATIVE RESOURCES, INC.

February 17, 1998

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission,	)	
v.	)	Docket No. R-00974104
Duquesne Light Company Application to approve restructuring plan pursuant to 66 Pa. C.S. § 2806(d)	)	

REPLY BRIEF OF HOSPITAL SHARED SERVICES AND ADMINISTRATIVE RESOURCES, INC.

February 17, 1998

TABLE OF CONTENTS

TABLE OF AUTHORITIES

COURT CASES

ADMINISTRATIVE DECISIONS

STATUTES

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	)	
	)	
v.	)	
	)	Docket No. R-00974104
Duquesne Light Company Application to approve restructuring plan pursuant to 66 Pa. C.S. § 2806(d)	)	

To: The Honorable John H. Corbett, Jr.
Presiding Administrative Law Judge

REPLY BRIEF OF HOSPITAL SHARED SERVICES AND ADMINISTRATIVE RESOURCES, INC.

Pursuant to the interim orders of the Presiding Administrative Law Judge, Hospital Shared Services ("HSS") and Administrative Resources, Inc. ("ARI") hereby submit their Reply Brief in this proceeding.[1]

I. INTRODUCTION

Duquesne Light Company ("Duquesne") correctly recognizes in its main brief that the most divisive and significant issue in this case concerns Duquesne's generation-related stranded cost claim. Duquesne Main Brief at 1. The most significant issue in terms of resolving that claim is how to determine the market value of Duquesne's generating assets, *i.e.*, the benchmark against which Duquesne's embedded costs must be measured to determine the amount, if any, of Duquesne's

[1] The Roman numeral headings of this Reply Brief do not necessarily correspond to the Roman numerals in the main briefs. To assist the reader, to the extent possible, the relevant section of the main brief outline is listed following the heading in each section of this Reply Brief.

stranded costs. At the last tally, Duquesne has submitted to the Commission four proposals for establishing the market value of its generation assets: Option A would set the market value based upon the results of an immediate auction of all of Duquesne's generating assets; Option B would establish market value *via* an auction of all the Company's generating assets, but the auction would not occur until 2002 or 2003; Option C would establish market values in 2002 or 2003 based upon the recommendation of a panel of experts; and, Option D would establish the market value of Duquesne's generating assets based upon the computer-generated price forecasts of Duquesne's witness Schnitzer. Duquesne announces in its main brief that it formally is opting for Option A, *i.e.*, to sell immediately all its generation assets. Duquesne Main Brief at 1.

But Duquesne's ostensible election is not without consequences. Duquesne represents in its brief that most of the disputes in this proceeding have been eliminated by Duquesne's decision to opt for Option A. Duquesne Main Brief at 2. Duquesne further argues that "the Presiding Judge should make findings here regarding [that] stand-alone valuation proposal." *Id.* at 3. That is another way of saying that Duquesne would have the Presiding Judge issue a decision that ignores substantially all of the evidence in this case based upon the contingency that Duquesne, in fact, will offer to auction its facilities immediately as would occur under Option A.

But, Duquesne's offer to exercise Option A is illusory. Duquesne supports Option A, but with an enormous caveat -- only if the proposed merger between Duquesne and Allegheny Power Systems ("APS") is *not* approved. *Id.* at 3. But, in the merger proceeding, Duquesne actively is seeking approval of the merger, and it states in its brief that it "fully expects that the merger will be approved . . . ." Duquesne Main Brief at 3. Thus, while Duquesne essentially concedes that Option A is the best choice and feigns that the battle has been lost, Duquesne fights against Option A (and

Option B, as well) on another battlefield -- the merger proceeding. *See* Marshall, Tr. 179:6-12 (if the merger is approved, the combined companies would be willing to sell only 330MW of generation capacity).

Thus, the question: where does that leave Duquesne's ratepayers assuming Duquesne succeeds and the merger is approved? Option C remains under which Duquesne would defer to 2002 or 2003 resolution of the issue: does Duquesne have any stranded costs in the first place? But, all the while under Option C, Duquesne would accelerate amortization and depreciation by $1.7 billion and charge a Competitive Transition Charge ("CTC") until the panel of experts provides its estimate of the market value of Duquesne's assets. Option D also remains under which Duquesne also would accelerate amortization and depreciation by $1.7 billion and recover through a CTC $1.9 billion in alleged stranded costs. And what lies at the heart of Option C and D? As is stated in HSS/ARI's main brief, Option C relies upon Mr. Schnitzer's price forecasts that Duquesne claims show Duquesne may have some stranded costs remaining as of December 31, 2005. HSS/ARI Main Brief at 17-19. And, Option D, the $1.9 billion stranded costs claim, is a direct derivative of Schnitzer's price forecasts, as well. HSS/ARI Main Brief at 20. Thus, Duquesne's illusory offer resolves nothing. For all of Duquesne's "smoke and mirrors," as HSS/ARI states in its main brief (HSS/ARI Main Brief at 5-6), Mr. Schnitzer's price forecasts still lie at the heart of the issues that the Commission must resolve to determine whether Duquesne is entitled to any stranded cost recovery and to the specific rate proposals that Duquesne has placed before the Commission in this docket.

As a consequence, HSS/ARI submit that the Commission should not be swayed by Duquesne's acquiescence to Option A--the immediate auction. Such acquiescence is fleeting and will disappear if Duquesne has its way. And, Duquesne fully expects that it will, and it is promoting

that result. Duquesne Main Brief at 3, 38. Thus, notwithstanding Duquesne's attempt to avoid a decision here *via* its illusory offer to sell its generation assets, the Commission needs to resolve the basic issues in this case. As posed by Duquesne, those issues are: (1) the appropriate methodology for quantifying stranded costs; (2) in the event Duquesne is found to have established that it has any stranded costs, whether any such amounts should be disallowed, *e.g.*, for failure to mitigate adequately, and (3) if Duquesne is found to have established the right to recover any stranded costs, the appropriate rate methodology for such recovery. Duquesne Main Brief at 1. As will be demonstrated below, Duquesne's main brief fails to refute HSS/ARI's showings: (1) that Duquesne failed to carry its burden of proving that it has net known and measurable stranded costs, and (2) that there is substantial evidence in the record that shows that Duquesne, in fact, has no stranded costs at all because its generation assets have positive market value. As a result, the Commission should reject Duquesne's request to recover any stranded costs and issue additional orders granting the rate relief requested in HSS/ARI's Main Brief at 87-88.

In support thereof, HSS/ARI state as follows:[2]

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[2] HSS/ARI note that its main brief addresses numerous issues referred to in Duquesne's main brief. As an example, Duquesne raises the issue of whether its net book investment in the cold reserved capacity of Brunot Island and Phillips should be included for purposes of calculating Duquesne's stranded cost claim. *See* Duquesne Main Brief at 24-25. HSS/ARI discussed that issue at pages 25-27 of its main brief. Therefore, there is no reason to discuss the issue again here. Thus, HSS/ARI rely upon their main brief for their position on the Brunot Island/Phillips issues, and all other issues not discussed specifically in this Reply Brief.

II. DUQUESNE'S RATEPAYERS ARE ENTITLED TO AN IMMEDIATE RATE RETENTION (HSS/ARI MAIN BRIEF SECTIONS III AND IV.F.3(b))

At page 22 of its main brief, Duquesne contends that the rate reduction sought by HSS/ARI is proscribed by Section 2804(4)(v) of the Electric Generation Customer Choice and Competition Act (the "Act"). Duquesne claims the protection of Section 2804(4)(v) for the obvious reason that Section 2804(4)(v) specifies that a "utility shall not be required to reduce its capped rates below the capped level upon the complaint of any party if the Commission determines that any excess earnings achieved under the cap are being utilized to mitigate transition or stranded costs . . . ." Duquesne is wrong. The protection of Section 2804(4)(v) is not even available to Duquesne in this case.

Duquesne has placed the cart before the horse. Duquesne's reliance on Section 2804(4)(v) begs the question: has Duquesne satisfied its burden of proving that it has net known and measurable stranded costs in the first place. *See* HSS/ARI Main Brief at 16. The answer to that question is critical to the outcome of this proceeding because before Duquesne can be accorded the statutory protection of Section 2804(4)(v) that prohibits a rate reduction when a utility is using excess earnings to mitigate stranded costs, Duquesne has to prove that it has stranded costs to mitigate. Nonetheless, throughout this proceeding, Duquesne has attempted to claim the protection of Section 2804(4)(v): (1) without having proven that it has stranded costs, and (2) while all the time acknowledging that it cannot satisfy the known and measurable standard for demonstrating that it has stranded costs. *See* HSS/ARI Main Brief at 27-28.

As a consequence, the rate reduction sought by HSS/ARI is not proscribed as Duquesne claims. Rather, because HSS/ARI have demonstrated that Duquesne failed to prove that it has stranded costs, and because the record is replete with evidence that shows that Duquesne's facilities

have positive market value, the prohibition of Section 2804(4)(v) does not apply. Thus, as HSS/ARI showed in their main brief, Duquesne's request to accelerate amortization and depreciation by $1.7 billion does not constitute an instance in which a utility will be attempting to gain excess earnings to mitigate stranded costs. It represents an attempt by Duquesne to manufacture an inflated cost of service to attempt to justify maintenance of exorbitant rates and the collection of amounts far in excess of those to which Duquesne would be entitled to earn under traditional ratemaking methodologies. HSS/ARI Main Brief at 17. As a result, the protections of Section 2804(4)(v) are not available to Duquesne, and Duquesne's ratepayers are entitled to an immediate rate reduction. The rate reduction is required in view of the reduction to Duquesne's cost of service that results principally from reductions to Duquesne's distribution and generation rate bases that are appropriate to eliminate the effects of past and future inflated capital expenditures. HSS/ARI Main Brief at 10-15, 24-27, 60-63 and 81-82.

III. DUQUESNE'S FEIGNED FINANCIAL COLLAPSE IS EXAGGERATED AND IRRELEVANT (HSS/ARI MAIN BRIEF SECTION I)

As is evident from a review of Duquesne's main brief, Duquesne clearly is uncomfortable discussing the merits of its claim and the specific challenges to that claim. Thus, as part of its strategy to camouflage its presentation (*see* HSS/ARI Main Brief at 5), Duquesne seeks to shift the focus from the merits of the issues to claimed dire results that Duquesne alleges will occur if Duquesne's stranded costs claim is rejected. Duquesne Main Brief at 4. Duquesne attempts to shift the focus in that way by asserting that certain parties' proposals to disallow between $400 and $700 million would severely damage the Company's financial integrity. *Id.* Duquesne claims that such a result is proscribed by *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989) ("*Barasch*"). *Id.*

Duquesne's claim is legally wrong and factually misleading. With respect to the legal issue, *Barasch* is inapposite. *Barasch* holds that the impact of rate orders are important in the sense that a state commission cannot "arbitrarily switch back and forth between methodologies in a way which required investors to bear the risk of bad investments at some times while denying them the benefit of good investments at others . . . ." *Barasch*, 488 U.S. at 315. However, a rejection of Duquesne's stranded cost claim in this case will not result from the Commission switching rate methodologies. It will result only from a finding that Duquesne has not proven that it will have costs that it cannot recover in the future competitive market. Thus, a Commission order rejecting Duquesne's stranded cost claim has no impact on investors, except *vis-a-vis* the timing of the recoveries of their investments, *i.e.*, a rejection of Duquesne's stranded cost claim merely would provide a requirement that Duquesne, during the transition period, charge just and reasonable rates, and that it recover its remaining generation-related investments and returns on those investments in the future competitive market as do other competitive entities. Thus, *Barasch* has no relevance to this proceeding because an order rejecting Duquesne's stranded cost claim would not constitute a disallowance order in the traditional sense of that term.

Furthermore, Duquesne's factual representations have no more merit that its legal position on this issue. For one thing, the financial crisis Duquesne posits is inconsistent with the lofty financial results that Duquesne has forecast to the investment community. *See* HSS/ARI Main Brief at 14. Moreover, a Commission order denying Duquesne's stranded cost claim merely would put Duquesne in the position in which it should be in view of the actual market value of its assets. *Id.* at 4. Such an order, thus, would have no impact on Duquesne's actual financial integrity,

although it would extinguish Duquesne's quest for an almost $2 billion windfall at ratepayer expense.

In any event, as HSS/ARI stated in its main brief, Duquesne's claim of dire financial results is irrelevant if it would require the Commission to grant Duquesne stranded cost recoveries that are not authorized by the Act. HSS/ARI Main Brief at 7. And, given that Duquesne has failed to establish that it has any stranded costs, the only appropriate course of action is to deny Duquesne's claim notwithstanding its claims of financial stress. *Id.* at 16.

IV. TRANSITION OR STRANDED COSTS (HSS/ARI MAIN BRIEF SECTION IV)

Duquesne essentially launches a two-prong attack on those that challenge its stranded costs calculations. With respect to the Office of Consumer Advocate ("OCA") and the Duquesne Industrial Intervenors ("DII"), Duquesne claims that their computer-generated price forecasts are inferior to Duquesne's computer-generated price forecast because Mr. Schnitzer's price forecasts, in part, were based upon alleged actual market results. *See, e.g.*, Duquesne Main Brief at 29. With respect to HSS/ARI, Duquesne's most prominent criticism appears to be a complaint that HSS/ARI's witness, Dr. Robert B. Weisenmiller, did not directly attack OCA's, as well as Duquesne's, computer-generated price forecasts. Duquesne Main Brief at 28 n.14 and 32. As will be demonstrated below, Duquesne's criticisms of OCA, DII and HSS/ARI ironically show that HSS/ARI's position is the position in this case that is most supported by the only actual objective, verifiable evidence.

A. Only HSS/ARI Rely On Real Market Evidence (HSS/ARI Main Brief Section IV.B.3(b)(ii) (page 30) and IV.B.3(c))

Duquesne states that the fundamental premise of its approach to stranded cost recovery is that the market, not forecasters should set the value of Duquesne's generating assets. Duquesne Main Brief at 18. Based upon that premise, Duquesne claims that its approach to the case is superior to OCA's and DII's approaches because Mr. Schnitzer's price projections allegedly are based upon real market evidence for the years 1999-2005, the real market evidence being the results of Duquesne's summer 1997 Request for Proposals ("RFP"). *Id.* at 29. Duquesne asserts that the RFP results are "the only market evidence of power prices during the period." *Id.* (emphasis in original).

HSS/ARI agree with Duquesne that it is far more objective, and thus appropriate, to determine the value of Duquesne's generation assets, and hence the merits of its stranded cost claim, based upon actual market evidence. Thus, as stated in HSS/ARI's main brief, HSS/ARI do not believe that OCA's and DII's computer-generated price forecasts are reliable tools for determining Duquesne's net known and measurable stranded costs. *See, e.g.*, HSS/ARI Main Brief at 49. Nonetheless, Duquesne's claim that Schnitzer's price forecasts in any way are based upon real market evidence is thoroughly misleading. Further, Duquesne clearly has chosen to ignore the real market evidence in this case that reveals that Duquesne has no stranded costs at all.

With respect to Duquesne's claim that Schnitzer's price forecasts are based upon real market evidence, the obvious question arises: are Duquesne's RFP results actually reflective of a retail price that might prevail in a competitive market? HSS/ARI will not repeat the substantial record evidence discussed in their main brief that shows that Duquesne's wholesale RFP results substantially understate the retail price that Duquesne likely could sell its power for in a competitive market.

HSS/ARI principally rely upon their main brief at 30-36 to show the many shortcomings that disqualify the RFP results from serving as a proxy for competitive retail market prices. Data that Duquesne relies upon its main brief to attempt to validate the RFP results do not even marginally refute the showing made by HSS/ARI.

In its main brief, Duquesne claims that the RFP results are corroborated by other sources of information: (1) FERC form 714 data; (2) prices from *Power Markets Week;* and (3) a prior Duquesne sale. Duquesne Main Brief at 70. None of those sources of information, however, in any way validate Duquesne's wholesale RFP results as a proxy for competitive retail prices.

For instance, the reference to FERC Form 714 data is a reference to system "lambda" data from 1995 and 1996, which Duquesne and other utilities are required to file with the Federal Energy Regulatory Commission ("FERC"). However, system lambda data are by no means indicators of the full cost of power in an open market.[3] System lambda data, as reported in FERC 714, include only a utility's own estimate of the incremental cost of production for its own system. It is flawed as a measure of full market prices for several reasons. First, it is not a price that reflects any sort of bona fide market transaction. As Dr. Weisenmiller explained, the "system lambda" reflects only the incremental cost to operate the marginal plant on Duquesne's system to produce a small quantity of additional power. HSS/ARI Statement No. 1 at 28:15-19. Thus, the "system lambda" is not even reflective of Duquesne's "going forward" costs that it incurs to continue operating its plants, *e.g.*, costs for fuel, labor, more capital additions, *etc. Id.* at 28:11-15. Thus, as Dr. Weisenmiller also

[3] *See also* HSS/ARI Main Brief at 32 n.8.

explained, the "system lambda" reported in FERC Form 714 cannot serve as a proxy for sustainable market prices. *Id.* at 29:20-30:3.

The price that Duquesne cites from a prior sale also does not reflect retail market values. Duquesne's witness Irvin referenced the sale in his direct testimony. Duquesne Statement No. 7 at 3. The sale occurred during the period 1994 to 1997 to an unnamed Duquesne customer in PJM. *Id.* The price, as Mr. Irvin admitted, did not include the cost of transmission. *Id.* at 5. The price also did not include the cost of ancillary services and losses.[4] *Id.* at 4. Thus, the sale price does not even reflect a delivered wholesale price during the historical period, let alone is it reflective of future retail prices.

Finally, Duquesne's reference to certain prices it obtained from *Power Markets Week* is irrelevant. There is nothing in the record that shows that those prices are indicative of future prices. *See* Duquesne Statement No. 5 at 7. That is particularly so because prices in PJM and ECAR will undergo changes in the upcoming years as more power moves in those markets. However, current prices in those markets represent wholesale transactions only, none of which are reflective of prices that utilities, including Duquesne, can obtain in future retail sales. Accordingly, Duquesne's new claim that its RFP results are corroborated by market evidence has no foundation in fact.

Aside from the numerous factors that disqualify the RFP results from serving as a proxy for retail prices, it is clear that Mr. Schnitzer's price forecasts, and Duquesne's claimed stranded cost quantifications that are based upon Schnitzer's forecasts, should be disregarded in any event because Schnitzer and Duquesne ignore substantial market evidence relevant to an assessment of the market

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[4] As recommended by Dr. Weisenmiller, market prices must reflect the costs of transmission, ancillary services and losses. HSS/ARI Statement No. 1 at 38:4-21.

value of Duquesne's generation facilities. In fact, despite Duquesne's lipservice to the superiority of actual market data over projections, Duquesne's evidentiary presentation, and Duquesne's main brief, completely ignore, or attempt to discount, real evidence of market value in the form of actual asset sales.

As HSS/ARI pointed out in their main brief, the first, albeit not necessarily the most current, evidence of the market value of Duquesne's generation assets is the market value established by Duquesne's own sale to APS of Duquesne's interest in the Ft. Martin plant. HSS/ARI Main Brief at 55. As HSS/ARI discussed in their main brief, that was a real market transaction, and Duquesne's President and CEO acknowledged that APS' purchase of that interest established the fair market value of the plant at the time of the sale. Marshall, Tr. 71:15-20. Duquesne sold its 50% interest in the plant for *four and a half times* Duquesne's net book value. HSS/ARI Statement No. 1 at 22:14-22. Thus, the transaction reflects actual market evidence of a buyer paying a substantial premium for one of Duquesne's own generation assets, an indisputable fact.

That being said, it would be an "over-statement" to assert that the Ft. Martin sale establishes the price per MW that Duquesne could obtain in sales of its assets, and HSS/ARI never have represented otherwise. In fact, Dr. Weisenmiller testified during his deposition that the sale of one generation unit does not necessarily establish the market value of a different generation unit. *See* Duquesne Statement No. 2-R at 55. Of course, Duquesne cites that deposition testimony to attempt to support a claim that Dr. Weisenmiller has made inconsistent statements in this case. Duquesne Main Brief at 33. However, Duquesne's claim of inconsistency merely reflects that Duquesne has chosen to ignore Dr. Weisenmiller's testimony concerning the import of the Ft. Martin transaction. As he explained in his surrebuttal testimony, the Ft. Martin sale constitutes significant evidence that

if Duquesne were to sell its generation assets, they could be sold at a multiple of net book value, thus negating any claim that the plants have negative market value that would produce stranded costs. HSS/ARI Statement No. 1-S at 31:7-32:2.

But just as Duquesne ignores that testimony, it also ignores the evidence reflecting its own internal assessment, the assessment of its consultant, Metzler & Associates ("Metzler") and of its merger adviser, CS First Boston, all three of which reflect consistent determinations that Duquesne's generation assets would attract premiums above net book value of hundreds of millions of dollars if Duquesne would put the assets up for sale. HSS/ARI Main Brief at 52-55. Duquesne also ignores the evidence of actual market transactions occurring throughout the country that show that large capacity generation units are being sold at multiples of net book value. *Id.* at 55-56. But Duquesne's decision to ignore that evidence, coupled with its criticisms of OCA, ironically demonstrate why HSS/ARI's position should be adopted by the Commission.

In criticizing OCA, Duquesne states in its main brief that:

> [t]he OCA has it backwards. The issue here is the soundness of the valuation methodology, not whether it "results" in any particular rate stream.

Duquesne Main Brief at 27 (footnote omitted). However, in making that criticism, Duquesne has said too much because HSS/ARI's case is not based upon the results of a particular rate stream. HSS/ARI's case is based upon the soundness of the valuation methodology. HSS/ARI's approach focuses on real market evidence (Duquesne's preferred methodology) that shows that Duquesne could sell its assets at a premium above net book value, thus establishing that Duquesne has no stranded costs. *See, e.g.,* HSS/ARI Main Brief at 63. And, contrary to a statement in Duquesne's brief, "HSS [does not] stand [ ] alone on *this issue* . . . ." Duquesne Main Brief at 27. Duquesne,

itself, in its internal study, and Metzler and CS First Boston all reached the same conclusion in their independent valuations of Duquesne's assets.

Thus, HSS/ARI ask the Commission to adopt Duquesne's position that real market evidence is superior to computer-generated price projections for determining stranded costs. By doing so, the Commission necessarily will rely upon the evidence presented by HSS/ARI. It is the *only* evidence of real market asset sales, and it is corroborated by Duquesne's internal study, as well as the studies by Metzler and CS First Boston. That real market evidence shows that Duquesne has no stranded costs.

B. HSS/ARI Do Not Support OCA's or DII's Computer-Generated Price Projections (HSS/ARI Main Brief Section IV.B.3(b)(ii) (page 49))

As previously indicated, Duquesne's principal criticism of HSS/ARI's position on market valuation is not a criticism of the evidence that HSS/ARI rely upon.[5] Rather, Duquesne criticizes HSS/ARI because Dr. Weisenmiller did not submit testimony criticizing the OCA's computer-generated price forecasts.[6] Duquesne Main Brief at 28 n.14 and 32.

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[5] In its main brief, Duquesne does criticize HSS/ARI's reliance on the Ft. Martin transaction. Duquesne Main Brief at 33. Nonetheless, even with his caveats, Duquesne's President and CEO, Mr. Marshall, agreed that in an administrative determination of stranded costs, it would be appropriate to consider Ft. Martin as one of many data points. Marshall, Tr. 80:1-81:15.

[6] Duquesne also criticizes HSS/ARI as allegedly taking an inconsistent position with respect to nuclear decommissioning. Duquesne's position is without foundation. HSS/ARI's position is that Duquesne has not established its nuclear decommissioning costs on a known and measurable basis. HSS/ARI Main Brief at 67. As an alternative to rejection of those claimed costs, HSS/ARI proposed an independent audit to serve as an objective assessment of a highly technical matter that obviously should be of significant concern to all parties. Further, the issue of cost projections related to nuclear decommissioning is far removed from the issue of the ability of any party to predict with accuracy future market prices.

Duquesne is correct in its general assessment that HSS/ARI, in fact, spent more time criticizing Duquesne's market valuation than those offered as alternatives by other parties in this case. HSS/ARI undertook that approach because Duquesne bears the burden of proving that it will have net known and measurable stranded costs. 66 Pa. C.S. § 2803; *see also* HSS/ARI Main Brief at 21. Accordingly, it is Duquesne's market price forecasts that are at issue, not those offered by other parties.

However, Duquesne is wrong in claiming that HSS/ARI have not criticized the market valuations of other parties. In their main brief, HSS/ARI demonstrated that both the OCA's and DII's market price forecasts suffer from many of the same deficiencies as Duquesne's price projections. HSS/ARI Main Brief at 49-52. Moreover, the evidentiary record fully establishes that there are additional reasons that show that OCA's and DII's price projections, like Duquesne's, result in unreasonable overstatements of Duquesne's stranded costs.

For example, there are shortcomings in Mr. Falkenberg's analysis for DII that are demonstrated by his testimony. For instance, Mr. Falkenberg admitted that in performing his model runs, he ignored transmission constraints. DII Statement No. 2 at 40. Of course, the removal of a constraint necessarily will lower a price projection because it will assume that buyers and sellers will be able to trade across the entire ECAR when, in fact, there may be limitations on such trading that, in fact, are caused by transmission constraints. Mr. Falkenberg's analysis also is flawed in that he made no explicit assumptions concerning unit retirement. However, if market prices fall, some units will be retired early for economic reasons. And as Mr. Smith's testimony shows, early economic retirement could produce higher prices than forecast. OCA Statement No. 2 at 14:14-21. However, that dynamic was not captured by Falkenberg's model because of his failure to analyze economic

retirements. Accordingly, in addition to the reasons for rejecting DII's price forecasts that are discussed in HSS/ARI's main brief, DII's market price projections should be rejected for the additional reasons discussed here. *See also* HSS/ARI Main Brief at 49 and 52.

OCA's model also fails to establish reliable future market prices for reasons in addition to those discussed in HSS/ARI's main brief. For instance, OCA's implementation of ENPRO suffers from a fundamental methodological flaw. OCA modeled only the combined APS/DQL system. OCA Statement No. 2 at 5:8. Thus, OCA's model did not capture the effect PJM prices may have on future market prices in Duquesne's market area. Mr. Smith, in fact, acknowledged this shortcoming in admitting that the upward price pressure exerted on ECAR prices by PJM is not captured by his model. OCA Statement No. 2 at 13:28-14:4. He also acknowledged that his model did not capture upward price pressure that would be caused by circumstances in NEPOOL. *Id.* at 14:5-12. Finally, like DII's witness Falkenberg's model, OCA's implementation of ENPRO also suffers because it did not explicitly retire units as market prices fall. And, in view of that failure to test the economic viability of existing units within ECAR, Mr. Smith explained that "economic retirement" would cause actual market prices to exceed his projections. *Id.* at 14:14-21.

Thus, it is clear that neither DII's nor OCA's model results are acceptable in that they understate retail market prices that likely will prevail in future competitive markets. As a result, the OCA and DII price forecasts place the risk of price projections on Duquesne's ratepayers, not its shareholders. That is not an acceptable result.

C. Regulatory Assets (HSS/ARI Main Brief Section IV.E)

In addition to the arguments Duquesne raised in its main brief related to the market valuation of its facilities, Duquesne also opposes HSS/ARI's position regarding Duquesne's right to recover

certain amounts that Duquesne claims qualify as regulatory assets. Duquesne opposes HSS/ARI's position claiming HSS/ARI applied the wrong test to determine whether a cost is recoverable as a regulatory asset. Duquesne Main Brief at 44 & n.35. Duquesne claims that the appropriate test of a regulatory asset is whether "its future recovery is *probable*, not certain pursuant to a 'specific' order." *Id.* at 44 n.35 (citations omitted) (emphasis in original).

Duquesne's argument fails to acknowledge the test that the Commission set forth concerning regulatory assets in the proceeding concerning PECO Energy Company's restructuring application. *Application of PECO Energy Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code*, Docket No. R-00973953 (December 11, 1997) (hereinafter "PECO Order"). As HSS/ARI showed in their main brief, the test established in the PECO Order permits the recovery of regulatory assets "that are presently not included in rates but which the utility is *already* entitled to recover through future adjustments." HSS/ARI Main Brief at 69 (citing PECO Order at 66 (emphasis added)). HSS/ARI rely upon their main brief to demonstrate that particular claims Duquesne has presented do not qualify for recovery under the test set forth in *PECO.*

V. HSS/ARI RECOMMEND THAT DUQUESNE'S STRANDED COST CLAIM SHOULD BE REJECTED IN ITS ENTIRETY (HSS/ARI MAIN BRIEF SECTION IV.B)

Duquesne claims that HSS/ARI seek an order in this case that the Commission require Duquesne to sell its generating assets. Duquesne asserts that such a requirement is proscribed by the Customer Choice Act. *Id.* Duquesne Main Brief at 28 n.15.

Duquesne has misstated HSS/ARI's position. As unequivocally is set forth in their main brief, HSS/ARI's position is that Duquesne did not carry its burden of proof and that, as a result, its stranded cost claim should be rejected in its entirety. That is not a new position, and HSS/ARI never

have sought an order from this Commission that Duquesne *must* submit to a forced divestiture of its assets.

HSS/ARI's position in this proceeding always has been that Duquesne has not set forth a stranded cost claim that meets the known and measurable standard of the Act. In view of that position, Dr. Weisenmiller testified that "one option for the Commission would be to deny Duquesne any recovery" of its stranded costs. HSS/ARI Statement No. 1 at 141:18-20. Dr. Weisenmiller further stated:

> [i]n lieu of that result, at *Duquesne's option*, the Commission could allow Duquesne to put its generation plants up for bid to quantify stranded costs based upon a value-maximizing sale.

Id. at 141:20-22 (emphasis added). Thus, HSS/ARI are not seeking the unlawful remedy claimed by Duquesne. Rather, HSS/ARI offered Duquesne an option for purposes of determining its stranded costs that Duquesne in essence claims to have accepted, as is reflected by its claim that Option A, an immediate sale of its generation assets, is its preferred option in this case. Of course, as previously discussed, Option A is illusory in that Duquesne has no true intention of selling its assets absent circumstances that Duquesne is quite sure will not occur.

However, in the event that the proposed merger of APS and Duquesne is *not* consummated, and Duquesne does in fact offer to auction its facilities immediately, it is necessary to address an argument set forth by the International Brotherhood of Electrical Workers ("IBEW").

In its main brief, the IBEW claims that it is not in the public interest for Duquesne to sell or close any of its power plants because of the potential affects on Duquesne's current plant employees and their communities. IBEW Main Brief at 6-7. However, Dr. Weisenmiller's testimony shows

that the IBEW's fears are not likely to be realized if Duquesne sells its generating assets. HSS/ARI Statement No. 1 at 57-60. As his testimony shows, purchasers of Duquesne's plants likely would retain plant employees because of their expertise. *Id.* at 57:5-13. Dr. Weisenmiller also produced evidence to show that actual sales of generation assets in California and Massachusetts provided continued employment for workers and/or for early retirement, special severance and re-training programs. *Id.* at 60:4-20; *see also* Exh. RBW-61.

Thus, the IBEW's concerns with respect to the displacement of Duquesne's employees are largely unwarranted as the experience of a plant's current employees makes them invaluable assets to the plant's new owners.

VI. TRANSMISSION AND DISTRIBUTION RATES; UNBUNDLING ISSUES (HSS/ARI MAIN BRIEF SECTION III)

A. 1996 Test Year Cost Of Service (HSS/ARI Main Brief Section III.B)

At page 9 of its main brief, Duquesne states that it "is not aware of any party that has questioned the test year cost of service study presented by Mr. O'Brien, including the *pro forma* adjustments to test year amounts." That is a remarkable position because just four pages before, at page 5 of its main brief, Duquesne notes HSS/ARI's request for an immediate rate reduction. And, as Duquesne presumably is aware because it apparently read Dr. Weisenmiller's testimony, HSS/ARI specifically raised the request for rate relief with respect both to the unbundled distribution and generation components of Duquesne's rates. HSS/ARI Statement No. 1 at 55 -57. Thus, HSS/ARI do not understand Duquesne's claim that its distribution-related cost of service study is unchallenged.

In any event, as is abundantly clear from HSS/ARI's main brief, HSS/ARI do, in fact, challenge the rate base assumption that underlies Duquesne's cost of service study, *i.e.*, the inclusion of $473 million in post-1986 distribution-related capital additions that never have been shown to be just and reasonable because of Duquesne's unilateral decisions: (1) not to file a rate case in over ten years, and (2) to sponsor no evidence in this case to support the alleged reasonableness of its past expenditures for capital additions. HSS/ARI Main Brief at 10-12. HSS/ARI also challenged Duquesne's distribution rates that implicitly assume $532 million in distribution-related capital expenditures between 1997 and 2005. *Id.* at 12-15.

HSS/ARI will not reargue the merits of these issues. HSS/ARI rely upon their main brief to support their position that Duquesne's distribution-related rate base: (1) should be reduced to eliminate 50% of the net book value associated with Duquesne's 1987-96 distribution-related capital expenditures of $473 million that never have been shown to be just and reasonable, and (2) Duquesne's 1996 test year **distribution-related** rate base should be reduced to reflect a declining rate base through the year 2005 consistent with the effect of straight line depreciation. HSS/ARI Main Brief at 9-15.

VII. CONCLUSION

WHEREFORE, for the foregoing reasons and those set forth in their main brief, HSS/ARI respectfully request that the Commission:

(1) deny Duquesne's stranded cost claim in its entirety;

(2) deny Duquesne's request to accelerate amortization and depreciation of its generation assets;

(3) deny Duquesne's request for authority to charge a CTC;

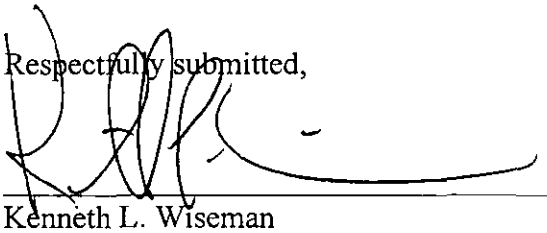
(4) order an immediate reduction in the unbundled generation component of Duquesne's rates;

(5) order an immediate reduction in the unbundled distribution component of Duquesne's rates;

(6) reject Duquesne's request to defer to a later date a final valuation of its generation assets for the purpose of establishing its stranded costs; and

(7) require that Duquesne offer the rates ordered herein to its Rule 4 customers to the extent the rates ordered herein are lower than the rates in a Rule 4 contract.

Respectfully submitted,



Kenneth L. Wiseman
Mark F. Sundback
Peter J. Thompson
Robert M. Lamkin
Andrews & Kurth L.L.P.
A Registered Limited Liability Partnership
1701 Pennsylvania Avenue, N.W.
Washington, D.C. 20006

ATTORNEYS FOR HOSPITAL SHARED SERVICES AND ADMINISTRATIVE RESOURCES, INC.

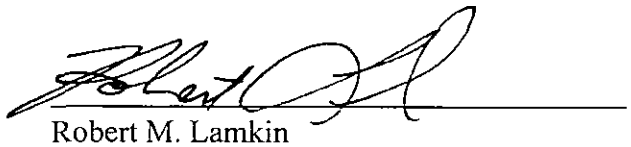
Dated: February 17, 1998

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the foregoing Reply Brief of Hospital Shared Services and Administrative Resources, Inc. on the Presiding Administrative Law Judge and Prothonotary via overnight mail (for delivery on February 17, 1998) and on the appropriate parties via first class mail (dated February 17, 1998) in accordance with Section 1.54 of the Commission's regulations.

Dated this 17th day of February, 1998.



Robert M. Lamkin
Andrews & Kurth L.L.P.
A Registered Limited Liability Partnership
1701 Pennsylvania Avenue, N.W.
Washington, D.C. 20006
TEL: (202) 662-2700
FAX: (202) 662-2739

An Attorney for Hospital Shared Services and Administrative Resources, Inc.

ORIGINAL

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY COMMISSION,	)	
v.	)	Docket No. R-00974104
DUQUESNE LIGHT COMPANY Application to Approve Restructuring Plan Pursuant to 66 Pa.C.S. §2806(d)	)	

REPLY BRIEF OF DUQUESNE LIGHT COMPANY

Larry R. Crayne
Assistant General Counsel
Richard S. Herskovitz
Corporate Attorney
Duquesne Light Company
411 Seventh Avenue
Pittsburgh, PA 15219
(412) 393-6049
(412) 393-6129

John S. Moot
Skadden, Arps, Slate, Meagher & Flom LLP
1440 New York Ave., N.W.
Washington, D.C. 20005
Counsel for Duquesne Light Company
(202) 371-7310
(202) 371-7939 (fax)

Dated: February 16, 1998

TABLE OF CONTENTS

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission,	)	
v.	)	**Docket No. R-00974104**
Duquesne Light Company	)	
Application to approve restructuring plan pursuant to 66 Pa. C.S. § 2806(d)	)	

REPLY BRIEF OF DUQUESNE LIGHT COMPANY

Pursuant to the Ninth Interim Order and 52 Pa. Code § 5.501 (1997), Duquesne Light Company ("Duquesne") hereby submits its Reply Brief. The purpose of this brief is not to address all the major intervenor arguments; that was the function of Duquesne's Main Brief. Instead, the reply brief addresses only assertions that are new or misleading regarding issues of critical importance.

1. Immediate Auction. The main briefs confirm that an auction is the best method for valuing Duquesne's generation plants. See, e.g., OCA Main Brief at 14 ("OCA agrees that a divestiture provides perhaps the best means of establishing the market value of plants"); DII Main Brief at 24. Only the IBEW opposes an auction, asserting that the Commission has no authority to order it. IBEW Main Br. at 4-7. Duquesne recognizes that the Commission does not have authority to compel Duquesne to sell its assets. 66 Pa.C.S. § 2804(5) ("[t]he Commission may permit,

but shall not require, an electric utility to divest itself of facilities . . ."). But that is not the issue presented here. Duquesne is proposing to exercise its right to auction its generating assets should the Commission find that a final stranded cost determination must be made today. DLC St. 1-Rej.; DLC St. 1-R at 11 ("Duquesne is willing to commit to such an auction to narrow or eliminate unproductive disputes in this case over market valuation."). To be sure, the auction would be precipitated by a Commission finding on a related issue (i.e., the permissibility of Duquesne's final valuation proposal); but the choice of whether to auction the assets in the face of such a finding is that of Duquesne alone, not the Commission. There is thus no conflict with Section 2804(5) or any other law. See IBEW Main Br. at 4-5.

OCA suggests that, while the auction is "perhaps the best means of establishing the market value of the plants," it is "impractical" to address it because the offer "is made only in the context of non-consummation of the merger." OCA Main Br. at 14. Duquesne and its customers do not have the luxury of side-stepping the issue, as the OCA seems to suggest. Rather, as explained in Duquesne's Main Brief,

> Duquesne fully expects that the merger will be approved by all necessary regulatory agencies, and that it will thereafter be consummated; however, it is critical that the Presiding Judge make findings here regarding Duquesne's stand alone proposal that would survive should the merger not occur. This will ensure that a customer choice plan is in place for Duquesne's customers under all circumstances.

DLC Main Brief at 3-4. This position is consistent with the OCA's own testimony that "the purpose of this proceeding [is] to resolve stranded costs and its recovery, not to defer it to a future proceeding." OCA St. 1 at 12. The Judge should therefore "resolve" the matter by finding that an auction provides, as all parties agree, the best valuation method.[1] Any necessary findings regarding competing valuation methods that have been presented in the merger case should be made in that case, not here.

2. Section 2804(4)(v). Several parties object to Duquesne's proposal to charge capped rates pursuant to Section 2804(4)(v),[2] but only the OCA contends that Duquesne's proposal rests on a mistaken "interpretation" of Section 2804(4)(v). According to the OCA, "Duquesne's proposal for continuation of the current level of rates until the final valuation is based on its interpretation of Section 2804(4)(v) of the Act, which it interprets as allowing electric utilities to charge rates up to current levels provided that 'any excess earnings achieved under the cap are being utilized to

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[1] DII mistakenly asserts that "the Company requests a rate cap waiver" as part of its auction proposal. DII Main Brief at 43 (citing Tr. 55). As Duquesne's testimony makes clear, however, the Company has not "requested a rate cap waiver"; rather, it has stated (i) a legitimate concern regarding the rate cap (DLC St. 1-R at 13-17); (ii) there are a range of methods for addressing that concern (id. at 16); (iii) that removing the rate cap is "one way" to do so (Tr. 56); and (iv) committed to file a proposal that addresses this concern should its auction proposal be adopted. DLC Main Brief at 21.

[2] Notably, however, neither the OTS nor DII object to the proposal to continue charging capped rates. OTS Main Br. at 49; DII Main Br. at 72.

mitigate transition or stranded costs for the benefit of ratepayers.'" OCA Main Br. at 14. But there is no "interpretation" at all in the passage quoted: OCA is quoting Section 2804(4)(v) itself, not Duquesne's words.[3] Undeterred, OCA plunges ahead with its own interpretation: "OCA submits that the intent of this section which is included in the rate cap provisions of the Act, was to preent [sic] complaints against current rates after the Company's restructuring had been completed, not to prevent rates from being lowered in the Company's restructuring case." OCA Main Br. at 16 (emphasis in original). The plain language of Section 2804(4)(v), however, does not permit such a distinction. The only "temporal" dimension of that section is the requirement that capped rates not exceed those "approved by the commission as of the effective date of this chapter." That, of course, is precisely Duquesne's proposal. DLC St. 2 at 35-36. The OCA interpretation, by contrast, rewrites the section to say: capped rates shall not exceed those "approved by the commission as of the effective date of the utility's restructuring plan."[4]

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[3] Assuming it were necessary (which it is not) to discern a legislative "intent" for Section 2804(4)(v), we think it quite obvious that the section mirrors Duquesne's "Ft. Martin plan" (which froze current rates while using excess earnings to accelerate the amortization of stranded costs) that was approved by the Commission shortly before passage of the Act. DLC St. 1 at 9.

[4] OCA's new interpretation even contradicts its own case. To explain, the OCA calculates a fixed CTC based on a one-time forecast of market prices and operating costs. OCA St. 4 at 15; OCA Ex. LS-4. Duquesne bears the risk that market prices (continued...)

3. Final Valuation. The OCA and DII contend that Duquesne's final valuation plan cannot be accepted because the Act requires that a final stranded cost determination be made today. OCA Main Br. at 15; DII Main Br. at 31-33.[5] Several supposed statutory barriers are raised, but only three merit a response. The first is the Act's reference to stranded costs as being stated on a "net present value" basis: 66 Pa.C.S. § 2803; see OCA Main Br. at 15. This, however, is a calculational issue, not a timing issue: whether stranded costs are determined today or in 2003, they can, and should, be calculated on a net present value basis.[6] The second is the Act's reference to stranded costs as being determined "as part of [the utility's] restructuring

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[4](...continued)
may turn out lower, or operating costs higher, than forecast by the OCA; however, Duquesne also has the theoretical opportunity, if the converse is true (i.e., market prices turn out higher or operating costs lower than forecast by the OCA) to earn higher returns. OCA St. 1 at 43. The OCA considers this a key aspect of its plan, providing Duquesne a purported opportunity to mitigate the severe impacts of the "sharing" disallowance. Id; OCA Main Br. at 60. Under the OCA's new-found interpretation of Section 2804(4)(v), however, this becomes an empty promise: if Duquesne achieves "excess earnings" (through, for example, more aggressive cost reductions), the OCA or any customer group could force Duquesne to reduce its rates even further by filing a complaint "after the Company's restructuring had been completed." OCA Main Br. at 16 (emphasis in original). Such a one-sided CTC recovery plan is punitive and we are frankly astonished the OCA would even suggest it.

[5] We note that the OTS and the Environmentalists, by contrast, support deferring a final valuation of Duquesne's generation. OTS Main Br. at 15; Environ. Main Br. at 14.

[6] For example, Mr. Clayton provides a net present value calculation of Duquesne's stranded costs as of December 31, 2005. DLC St. 2 at 30; DLC Ex. DJC-3.

plan." 66 Pa.C.S. § 2803; see DII Main Br. at 31. This, however, does not require that stranded costs be determined today; it requires that they be determined "as part of [Duquesne's] restructuring plan." They clearly will: Duquesne's plan is that market methods be used in a final valuation in 2001-2003. DLC St. 2 at 28, 40. The third is that Section 2808(f) requires an annual CTC true-up for changes in sales levels. DII Main Br. at 32-33. Duquesne's proposal, however, does this and more: Duquesne's ROE spillover provides a true-up for sales levels and for changes in other factors that affect earnings, such as operating costs. DLC St. 1 at 9; DLC St. 2 at 42-44; DLC St. 3 at 24. Moreover, given Duquesne's $1.7 billion minimum amortization commitment, there is no guarantee that Duquesne will even earn its required return. DLC St. 1 at 22. The ROE spillover proposal therefore adds to the consumer protections embodied in Section 2808(f). DLC St. 1 at 23.

In the end, the viability of Duquesne's final valuation proposal should not turn on such semantic debates, but rather its fidelity to the substantive requirement that it provide a "known and measurable" quantification of stranded costs. See OTS Main Br. at 15. There can be no honest debate that it does. Duquesne's final valuation plan gives the Commission the right to order an auction of all its generating assets (DLC St. 1-R at 2) and all parties, including the OCA and DII, agree that is the best valuation method. Id. at 10-11. It is thus not surprising the OCA and DII,

having no other lawful basis to oppose the plan, erect these supposed statutory impediments.

4. PECO Energy. The OCA, citing a laundry list of victories it purportedly achieved in PECO Energy (OCA Main Br. at 2-3), asserts that "[t]he Company's approach should be rejected in favor of a stranded cost determination as recommended by the OCA and as established in the PECO Order." OCA Main Br. at 3. The OCA's portrayal of PECO Energy is not at all fair or accurate. Two examples suffice. First, on the very same page that it makes the foregoing assertion, the OCA also contends that:

> [Duquesne] should not be permitted a return on the unamortized balance of its owned-generation stranded costs during this period. OCA submits that denial of a return on these assets during the recovery period provides an appropriate sharing of such costs.

OCA Main Br. at 3. While this sharing claim is not new, it is astonishing that the OCA continues to press it without acknowledging that the same sharing proposal was rejected in PECO Energy. PECO Energy, slip op. at 104-105. Equally remarkable, the OCA later cites numerous other precedents to support its sharing proposal, but again fails to mention PECO Energy as having any bearing on the matter. OCA Main Br. at 59.

Second, the OCA argues that Mr. Smith's market price projections are based on "the same . . . model utilized in the PECO case" and therefore, "to be

consistent with the approach taken in PECO," the Judge should "adopt OCA's analysis of the market value" of Duquesne's generation. OCA Main Br. at 29 (emphasis added). Aside from being improper,[7] this assertion is highly misleading because it attempts to blur the distinction between Mr. Smith's market price projections and Mr. Kahal's market value estimate. The two are not the same. As explained in Duquesne's Main Brief, there is no material dispute between Mr. Schnitzer and Mr. Smith regarding market price projections: Mr. Smith's projection is only $17 million higher than Mr. Schnitzer's "low case."[8] DLC Main Br. at 29; DLC St. 3-R at 24. The dispute between Duquesne and the OCA relates, instead, to Mr. Kahal's exogenous "adjustments" to those projections. For example, Mr. Kahal adds

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[7] Whether the OCA's testimony here is "the same" as that submitted in PECO Energy is a factual matter that cannot be resolved on the face of the PECO Energy Order. Indeed, as to Mr. Smith's "model," the Commission "emphasize[d] that we are not adopting each and every assumption and input" therefrom. PECO Energy, slip op. at 90. It is therefore improper for the OCA to make such factual allegations in its main brief. It also was improper for the OCA to submit a "Revised" Exhibit LS-7 to account for one, but not the other, mistakes identified by Duquesne in the dispute regarding the admission of Enron Cross-Examination Exhibits 6-10.

[8] OCA's brief also mixes apples and oranges by comparing Mr. Kahal's "market value" estimate to Mr. Schnitzer's high market price forecast, arguing that they are not "significantly" different. OCA Main Br. at 30. But, again, the correct comparison is between Mr. Smith's market price projection and Mr. Schnitzer's low price forecast. DLC St. 3-R at 23. (Mr. Schnitzer did not recommend the use of his high case. DLC St. 3 at 30-36.) To eliminate the potential confusion, we attach an excerpt from Mr. Schnitzer's rebuttal testimony that provides graphical depictions of the differences among Duquesne, OCA and DII regarding market price and market value projections. See Appendix C (DLC St. 3-R at 19-28).

nearly $200 million in market value to Duquesne's assets by "life-extending" those units (OCA Ex. MIK-1 at 3), but in PECO Energy no dispute regarding life extensions was raised or resolved by the Commission; rather, PECO's life extension studies were adopted, without change, by the OCA and the Commission. OCA Main Br. at 40. Equally weak is the suggestion that Mr. Kahal's "productivity enhancements" mirror those adopted in PECO Energy. OCA Main Br. at 2, 29. The productivity adjustment proposed by Mr. Kahal here is five times that proposed by the OCA in PECO Energy. Compare Direct Testimony of Richard LaCapra at 10 (OCA witness in PECO Energy proposing a 0.2% adjustment to inflation)[9] with OCA St. 1 at 34 (Mr. Kahal proposing a 1.0% adjustment to inflation). In sum, the adjustments of Mr. Kahal – who was not even a witness in PECO Energy – must stand or fall on their own merits, without any assumption that they were "adopted" in PECO Energy. OCA Main Br. at 2.

5. Sharing. The OCA and DII cite several cases in support of the contention that a sharing disallowance is "consistent with established ratemaking policy and practice in Pennsylvania." OCA Main Br. at 59; accord DII Main Br. at 69. None of these cases, however, addressed economic excess capacity, which is the

[9] Given that OCA has claimed that its evidence in both cases was essentially "the same" (OCA Main Br. at 29), Duquesne has no choice but to rebut that claim with the OCA's own testimony in PECO Energy. We understand that such testimony is not "evidence" and we do not recommend that it be used as such.

gravamen of the OCA and DII claim. OCA St. 1 at 41 (nuclear generation "would normally be considered 'economic excess capacity'"); DII St. 1-S at 9. Two of the cases involved disallowances for physical excess capacity,[10] while the other involved a plant (TMI) that was shut down and thus was not used and useful.[11] Moreover, neither party cites the most recent case on economic excess capacity, Pennsylvania Pub. Util. Comm'n et al. v. Pennsylvania Power & Light Co., 1995 Pa. PUC LEXIS 189 (Pa. P.U.C. 1995), aff'd sub nom., Popowsky v. Pennsylvania Public Util. Comm'n, 695 A.2d 448 (Pa. Commw. Ct. 1997), appeal denied, 702 A.2d 1062 (Pa. 1997). In PP&L, the Commission rejected the OCA's economic excess capacity adjustment (which was proposed by Mr. Kahal), "concur[ring]" that the "highly speculative nature of the OCA's market price projections" merited their rejection. 1995 Pa. PUC LEXIS 189, *19.[12]

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[10] Philadelphia Electric Co. v. Pennsylvania Pub. Util. Comm'n, 61 Pa. Commw. 325, 433 A.2d 620 (1980); Public Util. Comm'n v. Pennsylvania Power & Light Co., Docket No. R-842651, 59 Pa.P.U.C. 332, 67 PUR 4th 30 (1985), aff'd, 101 Pa. Commw. 370, 516 A.2d 426 (1986). "Physical excess capacity" means that the utility has constructed more capacity than is necessary to reliably serve customers. There is no claim here that Duquesne has "too much" capacity (DLC St. 9 at 9); the argument is that the capacity is "too expensive." OCA St. 1 at 41.

[11] Pennsylvania Elec. Co. v. Pennsylvania Pub. Util. Comm'n, 509 Pa. 324, 502 A.2d 130 (1985), appeal dismissed sub nom., Metropolitan Edison Co. v. Pennsylvania Pub. Util. Comm'n, 476 U.S. 1137 (1986).

[12] The Commission also "concur[red]" that PP&L's "statutory obligation to serve would have precluded" it from relying solely on market purchases. PP&L, 1996 Pa.

(continued...)

6. Shopping Credits. Not surprisingly, Enron and MAPSA focus their briefs on the "shopping credits" produced by the competing stranded cost recovery proposals. With great passion, Enron asserts that the "linchpin" of Duquesne's proposal is to set an artificially "low" shopping credit (based on the RFP) that will "impede competitive development," allow Duquesne to build a "war chest," and impose "catastrophic" losses on its competitors. Enron Main Br. at 2-3, 25. This claim is devoid of any substance. The only thing that matters to Enron (and MAPSA) is a CTC calculation methodology that permits them to offer sufficient "savings" to induce customers to switch suppliers. See Enron Main Br. at 31; MAPSA Main Br. at 32. It does not matter to them whether that result is achieved through stranded cost disallowances, above market "shopping credits" or some other mechanism. That is verifiable on the record here, as the following example illustrates.

Enron now contends that the CTC methodology adopted in PECO Energy is "arguably the only methodology which fully complies with the Act." Enron Main Br. at 30. Yet that methodology is the exact opposite of (i) the method

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[12](...continued)
PUC LEXIS 189 *19. That is consistent with Duquesne's testimony here. DLC St. 1-R at 20.

Enron originally supported in this case,[13] and (ii) the method it proposed in PECO Energy. PECO Energy, slip op. at 35. In both cases, Enron proposed the same method as Duquesne here – i.e., calculating the CTC as the residual after deducting a CGC (shopping credit) from current rates. Id.[14] Tellingly, before flip-flopping to support a different method on brief (i.e., the PECO Energy method), Enron satisfied itself that, as applied to Duquesne,[15] it would still produce a shopping credit "sufficient to permit suppliers to offer sufficient savings." Enron Main Br. at 31. That, as indicated, is Enron's sole objective here. In sum, Enron's new-found embrace of PECO Energy should be seen for what it is: a vote for that (or any other) method, provided it results in a shopping credit substantially above current market prices.[16]

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[13] Enron supported the CGC proposal of MAPSA, which proposed to calculate the CTC as a residual after deducting a shopping credit from current rates. See Enron St. 5.0 at 13-15; MAPSA St. 1 at 29.

[14] To be sure, the CGC proposed by Enron/MAPSA was higher (and artificially so, DLC St. 1-R at 23), but the methodology was the same.

[15] Pushing the limits of ethical conduct, Enron bases this conclusion (albeit without citation) on the very calculations (Enron CX Ex. 6-10) the Judge rejected in the Seventh and Eighth Interim Orders. Enron Main Br. at 31.

[16] Also telling is the contradictory position taken by Enron's subsidiary, Portland General Electric Co. ("PGE"), an electric distribution company, in its transition to competition proceedings in Oregon. There, Enron proposed (i) to set the CTC as a residual after deducting a shopping credit (which conflicts with the PECO Energy method, but is consistent with the method originally supported by Enron here), and (ii) to set a shopping credit that closely tracked actual market prices, with only a de minimus incentive credit available for one year (which conflicts with the inflated

(continued...)

7. HSS. The entire thrust of HSS's case is that an auction is the best, and indeed only, known and measurable method for valuing Duquesne's generating assets. HSS St. 1 at 141. Given that Duquesne has now offered to do precisely that (DLC St. 1-R at 2; DLC St. 1-Rej.), we are mystified at the 90 pages of histrionics contained in the HSS Main Brief.[17] HSS attacks all three market price witnesses (including OCA and DII),[18] arguing that the Judge should reject their testimony and rely instead on "studies" obtained in discovery. HSS Main Br. at 6-7, 52-55. HSS claims that one of those studies included an "assumed power price" under which Duquesne would have $500 million in stranded benefits, not stranded costs. See HSS Main Br. at 54; Tables to HSS Main Brief. This claim is as odd as it is dishonest. It is odd because the study relies on the same "computer generated" projections that HSS argues are unreliable. HSS Main Br. at 3, 5, 22, 29, 57-58. It is dishonest

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[16](...continued)
shopping credit Enron seeks here, Enron Main Br. at 31). DLC St. 3-R at 54; Tr. 527-34. At hearing, it became obvious that Enron had not informed its counsel of the particulars of the PGE proposal (Tr. 532) and counsel was forced to request the documents from Duquesne (Tr. 531-32); after the documentation was provided (Tr. 532), nothing further was heard from Enron on this issue.

[17] We note that the 90-page brief is largely a regurgitation of Dr. Weisenmiller's testimony and, hence, no detailed rebuttal is necessary here.

[18] HSS has now recognized its tactical error in failing to contest the market price projections of Messrs. Smith and Falkenberg (DLC Main Br. at 28 n.14), which each shows stranded costs of $1 billion or more. HSS now seeks to impeach them with excerpts from their own testimony (HSS Main Br. at 49-51), but that effort, as one would expect, is quite weak.

because it fails to reveal that all these studies provided a range of estimates, including estimates showing that Duquesne's plants have no value at all. DLC St. 2-R at 54. For example, HSS claims that the "Metzler" study shows "sales of [Duquesne] generation assets could 'add $500-750 million in after tax cash for investing." HSS Main Br. at 6. But this statement conveniently omits to mention that Metzler later concluded that the "valuations likely to be more accurate" show negative values for Duquesne's units. HSS Ex. RBW-9 at 4 (emphasis added). In sum, HSS adds very little to this case because it is simply incapable of providing a credible analysis of Duquesne's stranded cost claim.[19]

8. Mr. Hughes. Mr. Hughes rests his claim for rate reductions (and refunds) on the surrebuttal testimony of Mr. Biewald, who purported to compare the costs of Duquesne's nuclear generation to the cost of market purchases over the past ten years, as well as for the remaining lives of the assets. Envir. St. 2-S. However,

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[19] Also typical of the HSS "approach" (HSS Main Br. at 21) is the request that 50% of all Duquesne's capital expenditures (transmission and distribution) - both past (since 1987) and projected - be disallowed. HSS Main Br. at 10-15. HSS claims that Duquesne did not rebut HSS "directly" on this request (id. at 11), but there was nothing whatsoever to rebut. Dr. Weisenmiller, HSS' witness, did not identify a single expenditure that was imprudent (HSS St. 1 at 54-56) and did not even compare these expenditures to the depreciation of those assets over the same time period. Id. Indeed, he appeared oblivious to the fact that transmission and distribution systems must be maintained and upgraded; they do not simply "depreciate" away. In short, HSS failed to meet its own test: that an intervenor must raise "credible issues" regarding an expenditure to overcome its "presumption of reasonableness." HSS Main Br. at 11 (citing Pennsylvania Pub. Util. Comm'n v. Equitable Gas Co., 57 PaPUC 423, 444 n.37 (1983)).

Mr. Biewald's analysis cannot be relied upon for four reasons. First, Mr. Biewald himself did not regard his calculations as a "rigorous, independent analysis"; rather, he characterized them as a "first cut" derived from "materials at hand, and a number of approximations." Environ. St. 2-S at 3-4. Second, he compared apples to oranges: the sunk costs of Duquesne's nuclear units to the (supposed) incremental cost of purchasing power from the market. Environ. Ex. BEB-5; Tr. 386-87. Third, Mr. Biewald's prices for the expected cost of alternatives were "seriously understated." Tr. 387.[20] Fourth, his analysis conflicted with PP&L, where the Commission found it inappropriate to base an economic excess capacity adjustment (which is essentially what Mr. Hughes seeks, Hughes St. 1-S) on the estimated cost of "market purchases." PP&L, 1995 Pa. PUC LEXIS 189, *19. For all these reasons, Mr. Biewald's analysis should be rejected as flawed, unreliable and in conflict with PP&L.[21]

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[20] It is thus not correct to assert that Mr. Schnitzer "did not criticize any of Mr. Biewald's specific assumptions or calculations." Hughes Main Br. at 4.

[21] Duquesne previously addressed (Main Br. at 58-59) Mr. Hughes' request for rate reductions. We add here that his new request for retroactive rate refunds to 1990 (Hughes Main Br. at 6) is barred because (i) it was never raised in testimony (rather, in testimony he only requested "a refund to customers retroactive to June 1994," Hughes St. 1 at 10), (ii) Section 2804(4)(v) does not permit rate reductions, much less retroactive rate refunds, and (iii) retroactive refunds would violate the Commission-made rate doctrine. Cheltenham & Abington Sewerage Co. v. Pennsylvania Pub. Util. Comm'n, 344 Pa. 366, 25 A.2d 334 (1942).

9. Misleading Factual Assertions. The briefs of the opposing parties include a significant number of misleading factual assertions. While it is not possible, within the time permitted, to respond to all of them, Duquesne addresses some of the most obvious and significant misstatements in Appendix A.

10. Reconciliation of Tables. Duquesne attached to its Main Brief a "Revised Exhibit DJC-10" for the purpose of stating the stranded cost claims of Duquesne, OCA, DII and OTS on a consistent basis. The tables attached to the main briefs of these parties do not, however, match Revised Exhibit DJC-10 precisely. Duquesne has therefore submitted a revised set of tables that compares Revised Exhibit DJC-10 to the actual numbers provided by these parties (restated in the right-hand "box"), with explanatory notes attached describing the reasons for the differences. These revised tables are as Appendix B.

WHEREFORE, the Judge should issue a Recommended Decision that is consistent with the Duquesne's Customer Choice Plan, as set forth in Duquesne's testimony and as described in Duquesne's Main and Reply Briefs.

Respectfully submitted,

Larry R. Crayne
Assistant General Counsel
Richard S. Herskovitz
Corporate Attorney
Duquesne Light Company
411 Seventh Avenue
Pittsburgh, PA 15219
(412) 393-6049

John S. Moot
Skadden, Arps, Slate,
Meagher & Flom LLP
1440 New York Ave., N.W.
Washington, D.C. 20005-2111
(202) 371-7310

Dated: February 16, 1998

APPENDIX A

APPENDIX A TO REPLY BRIEF
OF
DUQUESNE LIGHT COMPANY

The purpose of this Appendix is to respond to certain obvious and significant factual misstatements contained in the main briefs of the intervenors. The arguments of the intervenors are provided in the left column and Duquesne's response is provided in the right column.

Intervenor Argument	**Duquesne Response**
ECR Roll-In. OCA objects to a rolled-in ECR of 14.7 mills/kWh because "Duquesne's earnings are expected to be very strong." OCA Main Br. at 69.	As the OCA concedes, however, Duquesne is "entitled to [14.7 mills/kWh if] it is justified by higher actual fuel costs." OCA Main Br. at 69. Mr. Clayton has so justified that rate (DLC St. 2 at 35) and the OCA chose not to rebut that testimony. Compare OCA St. 1 at 12.
$5 Million BI Adjustment. The OCA claims $5 million should be deducted from net book value because, under the Ft. Martin agreement, that amount was "to be used to reduce the costs of returning [Brunot Island 2B and 3] to service." OCA Main Br. at 27.	This adjustment is punitive. The Ft. Martin order did not require Duquesne to spend the money to return those Brunot Island units to service (DLC St. 2-R at 35) and the OCA concedes that it was never spent. The reason was that it was more economic to purchase capacity in the market. DLC St. 7 at 5. There is simply no lawful basis for "crediting" that amount against net book value.

RFP Prices. The OCA contends that "[i]t is difficult to believe . . . that retail customers will be able to purchase electricity at the [RFP price]." OCA Main Br. at 17.

First, the RFP for calendar year 1998 specifically stated that "[t]he firm power may be used to serve eligible customers in Duquesne's retail access pilot program." DLC Ex. RAI-4 at 2. Second, the 1998 RFP price is virtually identical to the market price predicted by the OCA's Mr. Smith for 1999. Compare DLC St. 7 at 10 – ($18.16/MWH) with OCA Ex. DCS-4 ($18.83/MWH). It is only after Lee Smith "adjusts" Mr. Smith's price to reflect a cost-based "A&G" adder that the OCA's proposed shopping credit differs significantly from Duquesne's RFP. DLC St. 5-R at 23. But this adder has no place in a market-based shopping credit. Id.; DLC St. 5-Rej. at 22-25.

Rate Reductions. The OCA asserts that immediate rate reductions is "one of the primary goals of the Act." OCA Main Br. at 16.

This statement conflicts with (i) Section 2804(4)(v), which permits maintenance of current rate levels, and (ii) PECO Energy, which rejected similar proposals for "temporary rate cuts through tariffed generation rate reductions." PECO Energy, slip op. at 43.

Mr. Smith's Capacity Findings. The OCA asserts that "the Commission specifically endorsed Mr. Smith's capacity assumptions in its PECO Order" and the Judge should therefore accept Mr. Smith's assumption of an 8% reserve margin in this case. OCA Main Br. at 36.

First, the Commission held that "[i]n adopting witness Smith's proposals, we emphasize that we are not adopting each and every assumption and input, however." PECO Energy, slip op. at 90. Second, it is undisputed that PECO Energy concerned a power pool ("PJM") with set reliability margins, but that no such pool, and no such required reserve margins, exist in Duquesne's region. DLC St. 9-R at 2.

Windfall Profits. The OCA makes the highly misleading claim that Duquesne cannot satisfy Section 2804(4)(v) because the OCA's analysis shows that Duquesne will have "windfall profits" during the transition period. OCA Main Br. at 61.

Section 2804(4)(v) permits a utility to maintain capped rates even if there are "excess earnings," provided such earnings are used to accelerate the amortization of stranded costs. In any event, the OCA claim of windfall profits is based principally on its punitive sharing disallowance (in excess of $500 million).

Heightened Risk. DII claims, over and over, that Duquesne's customers have "heightened risk" under Duquesne's final valuation plan. DII Main Br. at 33, 40-41, 79.

This is a restatement of the theme that a one-time determination of stranded costs provides customers the benefits of "certainty." But no such certainty exists, as such market price projections will almost certainly be wrong (DLC Main Br. at 26-27). By contrast, a market-based plan actually reduces risk to both customers and shareholders. DLC St. 1 at 18.

T&D Rates. DII suggests, without citation to the record, that Duquesne's use of a required return for T&D rates will cause the "distribution rate [to] exceed the rate authorized as of January 1, 1997." DII Main Br. at 11.

As DII's lack of citation suggests, there is no evidence to support this statement. DLC Main Br. at 13.

Pre-2005 Market Prices. DII argues that "[i]n determining Duquesne's stranded generation cost, Duquesne acknowledges that the critical portion of the market price forecasts is the post-2005 portion." DII Main Br. at 38.

This statement is false and misleading. If the purpose of the forecast is to determine the amount of accelerated amortization that can be achieved for purposes of applying Section 2804(4)(v), market prices during the transition period have little impact. DLC St. 3-R at 47. However, if the purpose instead is to perform a one-time calculation of stranded costs – which is the point at issue – market prices during the transition period have the most impact because of their greater "net present value." DLC Main Br. at 30 n.21.

APPENDIX B

Notes on Office of Consumer Advocate Table 1 (Appendix A)

The Summary of OCA Recommended Stranded Costs has reflected the Nuclear, Fossil and Regulatory Asset recommendations on a NPV after-tax basis, consistent with the presentation in DLC Appendix A.

The attached table shows the Restated DJC-10 (from DLC Appendix A) comparison between DLC and OCA, and an additional comparison with the OCA Table 1.

The OCA Table 1 shows total after-tax Recommended Stranded Costs of:

$1,351,150,000

Notes:

OCA-1) The Market Value of $299.07 MM (OCA Table 1, at 2) reflects the revised market value for Cheswick (OCA Ex. MIK-1-Update at 2) and the revised productivity adjustment of $13.04 MM (OCA Ex. MIK-1-Update at 3). OCA Table 1, at 2, Footnote 3.

OCA-2) OCA has presented these Regulatory Assets on a NPV basis calculated at their recommended after-tax discount rate of 6.88 percent. OCA Table 1, at 5, Footnote 2.

OCA-3) OCA has presented these Regulatory Assets on an after-tax basis consistent with the Company claim based on ratio of DLC after-tax to DLC pre-tax (DLC Appendix A at 4). OCA Table 1, at 5, Footnote 2.

Restated Exhibit No. DJC-10
(w/ Gross and Def. Tax)
(All PV Amounts)

Duquesne Light Company

Summary of Stranded Cost Estimates
As of December 31, 1998
($ Millions)

		DLCo				OCA			
		Gross	Def. Tax	Net		Gross	Def. Tax	Net	
Generating Plant									
Net Book Value of Gen. Plant	*	$1,370.53	$462.92	$917.61		$1,365.94	$452.92	$913.02	
Working Capital		0.00	0.00	0.00		61.53	0.00	61.53	(5)
M&S and Fuel-Related Sunk Costs	*	41.11	0.00	41.11		0.00	0.00	0.00	
PV of BV2 Lease Expense (1)	*	475.57	197.33	278.24	(1)	513.36	213.01	300.35	(6)
Net Book Value		1,887.21	650.25	1,236.96		1,940.83	665.93	1,274.90	
P V of Decommissioning		123.90	0.00	123.90		44.47	0	44.47	
PV of Costs Independent of Operation	*	208.23	0.00	208.23		0	0	0.00	
Estimated Market Value	*	(46.83)	(19.43)	(27.40)		(670.10)	(278.05)	(392.05)	(10)
Stranded Generating Plant		2,172.51	630.82	1,541.69		1,316.20	387.88	927.32	
Regulatory Assets				(2)				(7)	
SFAS 109	*	$236.48	$57.48	$179.00		$236.48	$57.48	$179.00	
Post-2005 - Unamortized Debt Cost	*	29.92	10.88	19.04		29.34	10.67	18.67	
Pre-2006 - Unamortized Debt Cost	**	16.76	6.96	9.80		16.43	6.82	9.61	
Deferred Rate Sync. Costs		25.37	1.87	23.50	(3)	20.80	1.52	19.08	
Deferred Employee Costs		13.83	0.00	13.83		11.06	(3.18)	14.24	
Deferred Nuclear Maintenance	*	3.25	1.35	1.90		3.25	1.35	1.90	
DOE Decom and Decon.		5.58	2.33	3.25		4.46	1.86	2.60	
Deferred Coal Costs	*	13.50	0.00	13.50		0.00	0.00	0.00	
Deferred Caretaker Costs	*	6.77	2.85	3.92		0.00	0.00	0.00	
BV2 Training Costs	*	2.42	0.84	1.58		2.42	0.84	1.58	
Low Level Rad. Waste	*	2.27	0.00	2.27		2.27	0.00	2.27	
Coal Cost Equalization	*	0.12	0.00	0.12		0.12	0.00	0.12	
Other	*	0.53	0.00	0.53		0.53	0.00	0.53	
Pre-Accrue Nuclear Outages		17.60	7.31	10.29		0.00	0.00	0.00	
Gain on Sale/Leaseback	*	55.13	0.00	55.13		55.13	0.00	55.13	
Deferred Rate Sych. Costs (Tax)		0.21	0.00	0.21		0.17	0.00	0.17	
BV-2 (Tax)	*	0.17	0.00	0.17		0.17	0.00	0.17	
Deferred Fuel Cost		11.51	4.78	6.73		9.20	3.82	5.38	
Transition Costs	*	18.10	7.51	10.59		18.20	7.61	10.59	
SFAS 106		3.28	1.36	1.92		2.62	1.09	1.53	
SFAS 109 Plant	*	0.00	0.00	0.00	(4)	0.00	0.00	0.00	
Total Regulatory Assets		462.80	105.52	357.28		412.46	89.88	322.57	
Total Stranded Cost		$2,635.31	$736.34	1898.9700		$1,727.66	$477.77	$1,249.89	
Percent of Company Claim		100.00%	100.00%	100.00%		65.56%	64.88%	65.82%	

OCA TABLE 1				
Gross	Notes	Net	Nuclear	Fossil
		$913.02	$476.95	$436.07
		61.53	20.48	41.05
		0.00	0.00	0.00
		300.35	300.35	0.00
		1,274.91	797.78	477.13
		44.47	44.47	0.00
		0.00	0.00	0.00
	(OCA-1)	(299.07)	0.00	(299.07)
		1,020.31	842.25	178.06
$236.48		$179.00		
29.34		18.67		
16.43		9.61		
26.52	(OCA-2)	24.57		
14.24	(OCA-2)	14.24		
3.25		1.90		
5.74	(OCA-2)	3.35		
0.00		0.00		
0.00		0.00		
2.42		1.58		
2.27		2.27		
0.12		0.12		
0.53		0.53		
0.00		0.00		
55.13		55.13		
0.22	(OCA-2)	0.22		
0.17		0.17		
11.84	(OCA-2)	6.92		
18.10		10.59		
3.37	(OCA-2)	1.97		
0.00		0.00		
426.17	(OCA-3)	330.84		
		$1,351.15		

* Items included in rate base for stranded cost.
** Included in Interest Expense.

1) Includes premiums and unamortized debt costs.
2) Duquesne's Regulatory Assets are shown net of deferred taxes.
3) Reflects adjustment based on DII proposal.
4) Included in plant as of 12/31/98.
5) Item not claimed by the Company.
6) Net of tax amount based on OCA gross amount of $513.36 million.
7) Regulatory assets adjusted to reflect net of deferred tax amounts.
8) PV is based on OTS recommended cost of capital.
9) Not specifically addressed by HSS/ARI.
10) Includes OCA's proposed productivity ($25.32) and life extension benefits ($170.72).

Notes on Duquesne Industrial Intervenors Appendix A

The Summary of DII Recommended Stranded Costs has not reflected the DII Nuclear, Fossil and Regulatory Asset recommendations on a NPV after-tax basis, consistent with the presentation in DLC Appendix A.

The Summary of DII Recommended Stranded Costs (DII Appendix A, Table 1) shows a total of $1,623,641,000 of NPV 1999$ (of which $1,622,169,000 in PUC jurisdictional). Table 1 states that "All items are stated on a pre-tax basis." However, in fact, only the DII Regulatory Asset recommendation is stated on pre-tax basis. The DII Nuclear ($769,324,000) and Fossil ($269,507,000) recommendations are after-tax results based on book values net of deferred taxes and an after-tax margin analysis.

The attached table shows the Restated DJC-10 (from DLC Appendix A) comparison between DLC and DII, and an additional comparison with the DII Appendix A presentation.

When the pre-tax DII Regulatory Asset recommendation is stated on an after-tax basis, the total DII Recommended Stranded Costs are:

$1,454,420,000

Notes:

DII-1) The Net Book Value shown on DII Appendix A, Tables 2 and 3 sums to $917.61 MM. This is the after-tax Net Book Value (after netting out the deferred tax balances) as shown in DLC Appendix A, Footnote 1.

DII-2) DII presents the BV2 lease in two parts (DII Appendix A, Table 1, Footnote 1). The present value of BV2 lease payments (following the transition period) is shown as a regulatory asset (see note DII-6 below). The lease payments during the transition period (1999-2005) are included as an expense in Mr. Falkenberg's margin analysis (DII Ex. RJF-5b).

DII-3) Mr. Falkenberg calculates a "Net Margin After Tax" of negative $16.74 MM (DII Ex. RJF-5b). This is the after-tax Market Value obtained by summing negative $229.0 MM for Nuclear (DII Appendix A, Table 2) and positive $212.25 MM for Fossil (DII Appendix A, Table 3).

DII-4) Both the Net Book Value and the Market Value are after-tax, and thus the Nuclear ($769.32 MM) and Fossil ($269.51 MM) recommendations are necessarily after-tax.

DII-5) DII has presented these Regulatory Assets on a book basis (DII Appendix A, Table 4, Footnote 1) rather than a NPV basis (DLC Appendix A, General Note on Regulatory Assets).

DII-6) Other category includes the present value of the post-2005 BV2 lease payments of $227.78 MM as a Regulatory Asset. This is a pre-tax present value (DII St. 3 at 6, DLC Ex. DJC-4 at 2). The equivalent after-tax value is obtained by multiplying $227.78 MM by [1-tax rate] = $133.27 MM. The Other category also includes $0.7 MM of other regulatory assets (DII Appendix A, Table 4).

DII-7) DII has included this amount in Deferred Rate Sync. Costs (DII Appendix A, Table 4).

DII-8) DII has included this amount in Other (DII Appendix A, Table 4).

DII-9) After-tax values (*in italics*) are calculated based on ratio of DLC after-tax to DLC pre-tax (DLC Appendix A at 4) and as described in note DII-6 above.

Restated Exhibit No. DJC-10
(w/ Gross and Def. Tax)
(All PV Amounts)

Duquesne Light Company

Summary of Stranded Cost Estimates
As of December 31, 1998
($ Millions)

		DLCo				DII				DII Appendix A				
		Gross	Def. Tax	Net		Gross	Def. Tax	Net		Gross	Notes	Net	Nuclear	Fossil
Generating Plant														
Net Book Value of Gen. Plant	*	$1,370.53	$452.92	$917.61		$1,370.53	$452.92	$917.61			(DII-1)	$917.61	$476.95	$440.66
Working Capital		0.00	0.00	0.00		61.53	0.00	61.53				61.53	20.42	41.10
M&S and Fuel-Related Sunk Costs	*	41.11	0.00	41.11		0.00	0.00	0.00				0.00	0.00	0.00
PV of BV2 Lease Expense (1)	*	475.57	197.33	278.24	(1)	475.57	197.33	278.24			(DII-2)	0.00	0.00	0.00
Net Book Value		1,887.21	650.25	1,236.96		1,907.63	650.25	1,257.38				979.13	497.37	481.76
P V of Decommissioning		123.90	0.00	123.90		42.96	0.00	42.96				42.96	42.96	0.00
PV of Costs Independent of Operation	*	208.23	0.00	208.23		0.00	0.00	0.00						
Estimated Market Value	*	(46.83)	(19.43)	(27.40)		(219.17)	(90.94)	(128.23)			(DII-3)	16.74	229.00	(212.25)
Stranded Generating Plant		2,172.51	630.82	1,541.69		1,731.42	559.31	1,172.11			(DII-4)	1,038.84	769.32	269.51
Regulatory Assets				(2)				(7)						
SFAS 109	*	$236.48	$57.48	$179.00		$236.48	$57.48	$179.00		$236.48		*$179.00*		
Post-2005 - Unamortized Debt Cost	*	29.92	10.88	19.04		0.00	0.00	0.00		0.00		*0.00*		
Pre-2006 - Unamortized Debt Cost	**	16.76	6.96	9.80		0.00	0.00	0.00		0.00		*0.00*		
Deferred Rate Sync. Costs		25.37	1.87	23.50	(3)	24.60	1.81	22.79		24.87	(DII-5)	*23.04*		
Deferred Employee Costs		13.83	0.00	13.83		0.00	0.00	0.00		0.00		*0.00*		
Deferred Nuclear Maintenance	*	3.25	1.35	1.90		3.25	1.35	1.90		3.25		*1.90*		
DOE Decom and Decon.		6.58	2.33	3.25		5.58	2.33	3.25		7.18	(DII-5)	*4.18*		
Deferred Coal Costs	*	13.50	0.00	13.50		0.00	0.00	0.00		0.00		*0.00*		
Deferred Caretaker Costs	*	6.77	2.85	3.92		0.00	0.00	0.00		0.00		*0.00*		
BV2 Training Costs	*	2.42	0.84	1.58		2.42	0.84	1.58		2.42		*1.58*		
Low Level Rad. Waste	*	2.27	0.00	2.27		2.27	0.00	2.27		2.27		*2.27*		
Coal Cost Equalization	*	0.12	0.00	0.12		0.12	0.00	0.12		0.12		*0.12*		
Other	*	0.53	0.00	0.53		0.74	0.00	0.74		228.48	(DII-6)	*133.97*		
Pre-Accrue Nuclear Outages		17.60	7.31	10.29		0.00	0.00	0.00		0.00		*0.00*		
Gain on Sale/Leaseback	*	55.13	0.00	55.13		55.13	0.00	55.13		55.13		*55.13*		
Deferred Rate Sych. Costs (Tax)		0.21	0.00	0.21		0.21	0.00	0.21		0.00	(DII-7)	*0.00*		
BV-2 (Tax)	*	0.17	0.00	0.17		0.17	0.00	0.17		0.00	(DII-8)	*0.00*		
Deferred Fuel Cost		11.51	4.78	6.73		11.51	4.78	6.73		14.81	(DII-5)	*8.66*		
Transition Costs	*	18.10	7.51	10.59		9.80	4.07	5.73		9.80		*5.73*		
SFAS 106		3.28	1.36	1.92		0.00	0.00	0.00		0.00		*0.00*		
SFAS 109 Plant	*	0.00	0.00	0.00	(4)	0.00	0.00	0.00		0.00		*0.00*		
Total Regulatory Assets		462.80	105.52	357.28		352.28	72.66	279.62		584.81	(DII-9)	*415.58*		
Total Stranded Cost		$2,635.31	$736.34	1898.9700		$2,083.70	$631.97	$1,451.73				$1,454.42		
Percent of Company Claim		100.00%	100.00%	100.00%		79.07%	85.83%	76.45%						

* Items included in rate base for stranded cost.
** Included in Interest Expense.

1) Includes premiums and unamortized debt costs.
2) Duquesne's Regulatory Assets are shown net of deferred taxes.
3) Reflects adjustment based on DII proposal.
4) Included in plant as of 12/31/98.
5) Item not claimed by the Company.
6) Net of tax amount based on OCA gross amount of $513.36 million.
7) Regulatory assets adjusted to reflect net of deferred tax amounts.
8) PV is based on OTS recommended cost of capital.
9) Not specifically addressed by HSS/ARI.
10) Includes OCA's proposed productivity ($25.32) and life extension benefits ($170.72).

Notes on Office of Trial Staff Appendix

The Summary of OTS Recommended Stranded Costs has reflected the Nuclear, Fossil and Regulatory Asset recommendations on a NPV after-tax basis, consistent with the presentation in DLC Appendix A.

The attached table shows the Restated DJC-10 (from DLC Appendix A) comparison between DLC and OTS, and an additional comparison with the OTS Appendix.

The OTS Appendix shows total after-tax Recommended Stranded Costs of:

$1,378,680,000

Notes:

OTS-1) The Market Values of $81.10 MM for Nuclear (OTS Appendix, Table 2) and $ 77.90 MM for Fossil (OTS Appendix, Table 3) reflect the revised market values in OTS Ex. 4-SR.

Restated Exhibit No. DJC-10
(w/ Gross and Def. Tax)
(All PV Amounts)

Duquesne Light Company

Summary of Stranded Cost Estimates
As of December 31, 1998
($ Millions)

		DLCo			OTS			
Generating Plant		Gross	Def. Tax	Net	Gross	Def. Tax	Net	
Net Book Value of Gen. Plant	*	$1,370.53	$452.92	$917.61	$1,263.37	$411.34	$852.03	
Working Capital		0.00	0.00	0.00	0.00	0.00	0.00	
M&S and Fuel-Related Sunk Costs	*	41.11	0.00	41.11	0.00	0.00	0.00	
PV of BV2 Lease Expense (1)	*	475.57	197.33	278.24 (1)	490.87	203.68	287.19	(6)
Net Book Value		1,887.21	650.25	1,236.96	1,754.24	615.02	1,139.22	
P V of Decommissioning		123.90	0.00	123.90	45.10	0.00	45.10	
PV of Costs Independent of Operation	*	208.23	0.00	208.23	N/A	N/A	N/A	
Estimated Market Value	*	(46.83)	(19.43)	(27.40)	N/A	N/A	N/A	
Stranded Generating Plant		2,172.51	630.82	1,541.69	N/A	N/A	N/A	
Regulatory Assets				(2)			(7)	
SFAS 109	*	$236.48	$57.48	$179.00	$236.48	$57.48	$179.00	
Post-2005 - Unamortized Debt Cost	*	29.92	10.88	19.04	29.92	10.88	19.04	
Pre-2006 - Unamortized Debt Cost	**	16.76	6.96	9.80	16.76	6.96	9.80	
Deferred Rate Sync. Costs		25.37	1.87	23.50 (3)	25.37	1.87	23.50	
Deferred Employee Costs		13.83	0.00	13.83	13.83	0.00	13.83	
Deferred Nuclear Maintenance	*	3.25	1.35	1.90	3.25	1.35	1.90	
DOE Decom and Decon.		5.58	2.33	3.25	5.58	2.33	3.25	
Deferred Coal Costs	*	13.50	0.00	13.50	13.50	0.00	13.50	
Deferred Caretaker Costs	*	6.77	2.85	3.92	0.00	0.00	0.00	
BV2 Training Costs	*	2.42	0.84	1.58	2.42	0.84	1.58	
Low Level Rad. Waste	*	2.27	0.00	2.27	2.27	0.00	2.27	
Coal Cost Equalization	*	0.12	0.00	0.12	0.12	0.00	0.12	
Other	*	0.53	0.00	0.53	0.53	0.00	0.53	
Pre-Accrue Nuclear Outages		17.60	7.31	10.29	17.60	7.31	10.29	
Gain on Sale/Leaseback	*	55.13	0.00	55.13	55.13	0.00	55.13	
Deferred Rate Sych. Costs (Tax)		0.21	0.00	0.21	0.21	0.00	0.21	
BV-2 (Tax)	*	0.17	0.00	0.17	0.17	0.00	0.17	
Deferred Fuel Cost		11.51	4.78	6.73	11.51	4.78	6.73	
Transition Costs	*	18.10	7.51	10.59	18.10	7.51	10.59	
SFAS 106		3.28	1.36	1.92	3.28	1.36	1.92	
SFAS 109 Plant	*	0.00	0.00	0.00 (4)	0.00	0.00	0.00	
Total Regulatory Assets		462.80	105.52	357.28	456.03	102.67	353.36	
Total Stranded Cost		$2,635.31	$736.34	1898.9700	N/A	N/A	N/A	
Percent of Company Claim		100.00%	100.00%	100.00%	N/A	N/A	N/A	

* Items included in rate base for stranded cost.
** Included in Interest Expense.

1) Includes premiums and unamortized debt costs.
2) Duquesne's Regulatory Assets are shown net of deferred taxes.
3) Reflects adjustment based on DII proposal.
4) Included in plant as of 12/31/98.
5) Item not claimed by the Company.
6) Net of tax amount based on OCA gross amount of $513.36 million.
7) Regulatory assets adjusted to reflect net of deferred tax amounts.
8) PV is based on OTS recommended cost of capital.
9) Not specifically addressed by HSS/ARI.
10) Includes OCA's proposed productivity ($25.32) and life extension benefits ($170.72).

OTS APPENDIX				
Gross	Notes	Net	Nuclear	Fossil
		$852.03	$476.95	$375.08
		0.00	0.00	0.00
		0.00	0.00	0.00
		287.19	287.19	0.00
		1,139.22	764.14	375.08
		45.10	3.50	41.60
		0.00	0.00	0.00
	(OTS-1)	(159.00)	(81.10)	(77.90)
		1,025.32	686.54	338.78
		$179.00		
		19.04		
		9.80		
		23.50		
		13.83		
		1.90		
		3.25		
		13.50		
		0.00		
		1.58		
		2.27		
		0.12		
		0.53		
		10.29		
		55.13		
		0.21		
		0.17		
		6.73		
		10.59		
		1.92		
		0.00		
		353.36		
		$1,378.68		

APPENDIX C

Duquesne Statement No. 3-R

BEFORE THE

PENNSYLVANIA PUBLIC UTILITY COMMISSION

DUQUESNE LIGHT COMPANY
DOCKET NO. R-00974104

Rebuttal Testimony
of
Michael M. Schnitzer

Contents:

Response to Intervenor Testimony Regarding Stranded Cost Calculation and Recovery, and Determination of the CGC for Retail Customers

Generation Stranded Costs Not Over Estimated

Q. Which parties present alternate views of the value of the Company's generating assets?

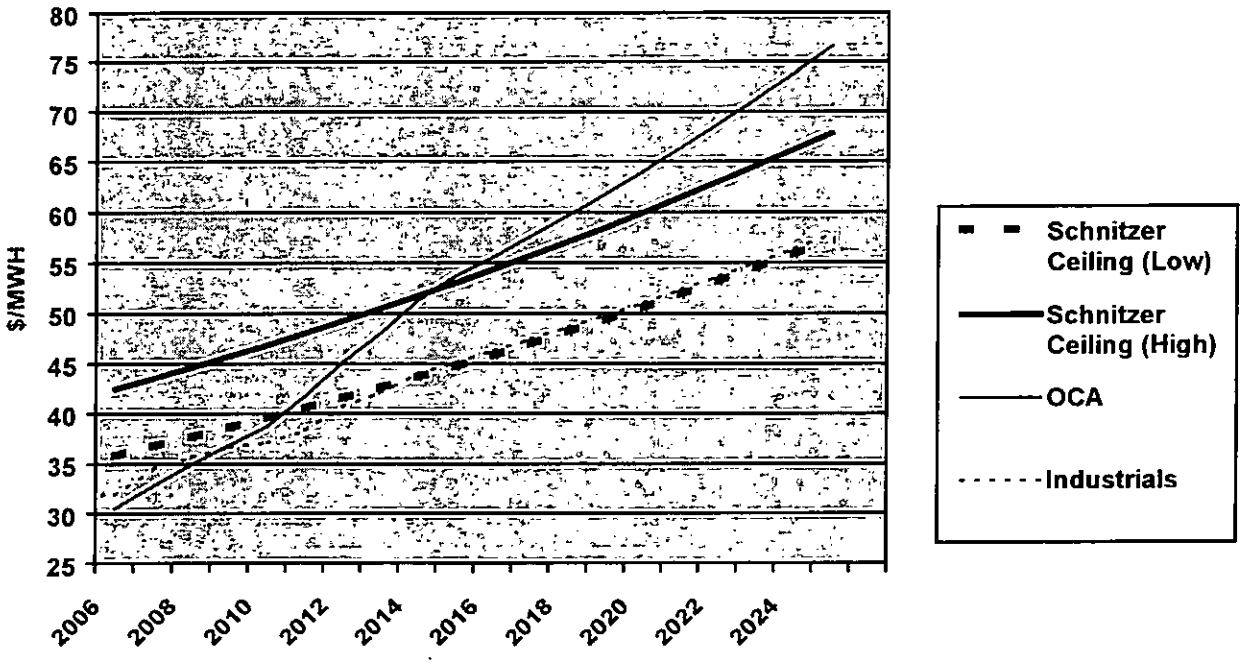
A. The OCA and the Industrials each present estimates of generation value which are significantly higher than the Company estimates as shown in the table below.

	Duquesne	OCA	Industrials
Generation Operating Value	($181 million)	$392 million	$128 million
Difference from Duquesne	--	$573 million	$309 million

Q. The OCA and the Industrials have been quite critical of your ceiling market price estimates on which the Company relied to estimate generation market value. I take it that your ceiling price range is much lower than the market price forecasts of OCA and the Industrials?

A. Actually, and surprisingly given their rhetoric, the answer is no. The figure below illustrates my ceiling market price range from 2006 on, together with the market price assumptions relied on by OCA and the Industrials.

As the figure shows, through the year 2010 both parties forecast market prices lower than the low end of my ceiling price range, indeed the Industrial forecast is lower through the year 2013. Over the remaining forecast period, the Industrial forecast lies nearly on top of the low end of my ceiling price range, while the OCA forecast escalates more sharply to a point just above the high end of the range in the year 2015, and diverges further from that point.



Q. On average, how do the OCA and Industrial market price estimates compare to your ceiling price range over the 2006 to 2025 time period?

A. My ceiling market price ranges from $36 per MWh to $43 per MWh in 2006, on a real levelized (that is, escalating at inflation) basis. The comparable number for the OCA is $39 per MWh, and for the Industrials $35 per MWh. Thus, the Industrial market price forecast for 2006 and beyond is actually below the low end of my ceiling price range, while the OCA's figure is well within my range.

Q. Given all of the criticisms of your approach, why isn't there more of a difference between your ceiling price range and the market price forecasts of OCA and the Industrials?

A. While it is true that some of my assumptions, capital cost and heat rate in particular, are lower than those of these other parties, other of my assumptions, notably cost of capital and capital recovery period, are higher. Thus, to some extent the differences in assumptions offset each other. In addition, my ceiling price range assumes that market prices will have risen to the combined cycle new entry level by 2006,

although I acknowledge the possibility that with all the excess baseload generation in ECAR, prices may not in fact rise to that level until after 2006. Industrials and OCA conclude that combined cycle capacity will not be economic under their assumptions until well after 2006, again with the result that the market price estimates are closer together rather than further apart. But underlying the apparent numerical similarity, there are significant differences of opinion over the usefulness of such forecasts.

Q. What do you mean?

A. Both the OCA and the Industrials are willing to rely on these forecasts as the basis of a one time stranded cost valuation, hedging their bet on market prices through their sharing proposals, which would impose significant costs on shareholders. The Company, on the other hand, believes these forecasts are useful only for the purpose of establishing the likely magnitude of stranded costs so as to determine the appropriate timing for the proposed second stage market valuation.

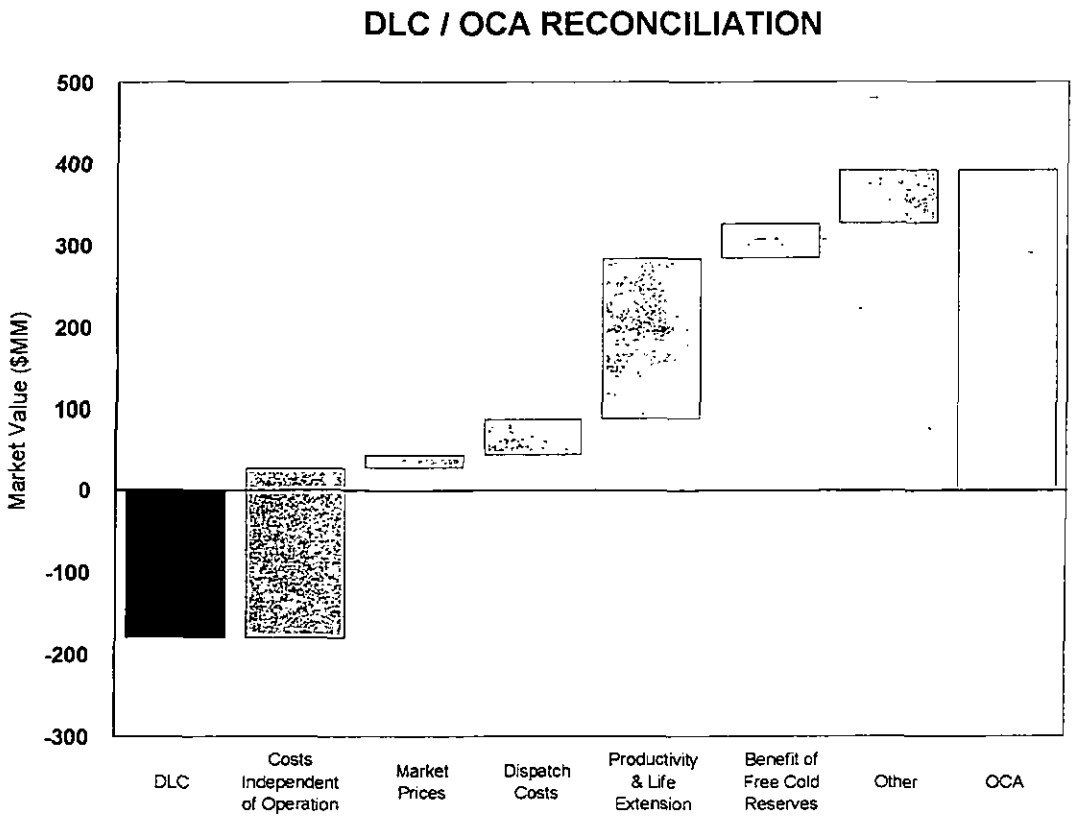
Q. To what do you attribute this difference of opinion?

A. I attribute it to a fundamentally different view of how competitive markets work. The specific criticisms of my approach are very revealing in this regard. The core criticism of the other parties is that I have assumed lower capital costs and higher efficiencies than any combined cycle unit currently operating, or than any unit currently available for construction. The first contention is true, the second arguable, but both miss the point. The critical question that OCA and the Industrials never even bother to ask is: has administrative determination based on current technology cost been an accurate predictor of market prices 10 to 20 years hence? The answer is no. In my experience the administrative approach based on a fixed technology view of

the world has been high nearly every time, and three specific examples are summarized in Exhibit MMS-6. Yet, for instance, OCA has the temerity to value life extensions 29 to 37 years hence based on such a fixed technology forecast. In light of the documented failures of accurately predicting market prices even five years in the future, OCA's position is somewhere between silly and reckless. Technological progress in electricity production is a fact. Gas combined cycle costs have fallen dramatically in nominal dollars over the last several years. Indeed, a review of Gas Turbine World, one of the sources cited by Mr. Falkenberg, indicates that in the just the last year, turnkey cost estimates for some combined cycle technologies have fallen by 17 to 33 percent (even more in real terms), and installed costs are now quoted as low as $318 to $380 per kW. In a similar vein, the Energy Information Administration, citing improved efficiency and lower costs of generation has reduced its forecast of long term electricity prices by 13 percent relative to a similar forecast made only one year ago. Given these trends, given the prospect of new technologies displacing combined cycle, and given the experience of the last 15 years, it is only reasonable to acknowledge the real possibility that future market prices could be lower than the ceiling price range, and lower than the OCA and Industrial forecasts.

Q. Well, if differences in long term market price assumptions are not that significant, why are the Company's estimates of generation value lower than the other parties?

A. The specific reasons vary for each party. Let me start with a discussion of the OCA analysis. The figure below illustrates the major sources of the $573 million difference between the Company's $(181) million estimate of net generation value and OCA's $392 million estimate.



Q. Please explain the $208 million of difference attributable to costs independent of operation.

A. Under Mr. Kahal's cost and market price assumptions, several of Duquesne's generating plants have a negative margin over their remaining lives – that is, the present value of costs exceeds the present value of revenues. For stranded cost quantification purposes, Mr. Kahal does not use this negative margin figure, but instead uses a value of zero. Implicit in his choice to use zero rather than the projected negative margin is the assumption that the operating costs which produce the negative margin are all avoidable if the unit is shut down or placed in cold

reserve. Unfortunately, as Mr. O'Brien, Mr. Duckworth and Mr. Nelson testify, this is not the case. Certain operating costs are not avoidable, and cannot be saved. Mr. Kahal's incorrect assumption that these costs are avoidable causes him to overstate net generation value by over $200 million.

Q. What about the $17 million difference attributable to market prices.

A. The OCA market prices are virtually identical to the prices derived from Duquesne's recent auction through 2002, but escalate more quickly thereafter, and thus are above the low end of the ceiling price range, on average, over the forecast period. But the net effect of these market price differences is only $17 million, as the figure illustrates.

Q. Please explain the difference in value attributable to dispatch costs.

A. The Company and OCA use different assumptions with respect to fuel and variable O&M costs. The effect of using OCA's assumptions, rather than the Company's, is to increase net generation value by $44 million.

Q. What about the $196 million in the figure above attributable to life extensions and productivity improvement?

A. A more significant source of difference involves life extension and productivity assumptions. The Company believes that future life extension economics are speculative, and will hinge both on future market prices and environmental requirements for coal generation. OCA has assumed that life extension will be economic, particularly at the higher long-term price levels they project. In addition, OCA has assumed further, unspecified improvement in generation productivity above and beyond the Company's projections. As shown above, these speculative life

extension assumptions together with their unspecified productivity improvements increase net generation value by $196 million.

Q. What is the next item, the benefit of free cold reserves?

A. Mr. Kahal's analysis suggests that the Cheswick unit has negative margins on an annual basis until 2006, at which time the annual margin turns positive. For valuation purposes, Mr. Kahal assumes that the Cheswick unit can be placed in reserve for free until 2006, at which point it can be reactivated at no cost. Unfortunately, as Mr. Nelson describes, this is not technically or economically feasible. The "free cold reserve" error causes generation value to be overstated by $42 million.

Q. What is in the "Other" category?

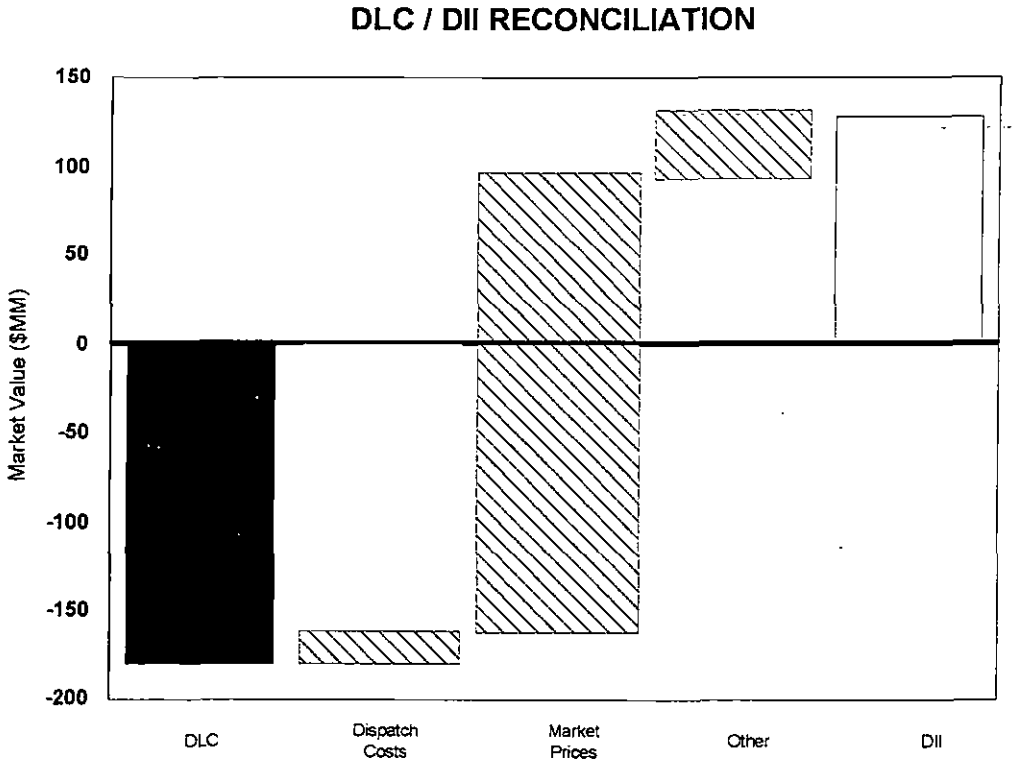
A. There are several other differences in assumptions between OCA and the Company, including inflation and discount rates. As the figure illustrates, these other differences account for $66 million of the difference in net generation value.

Q. What do you conclude from this analysis of differences between the Company and OCA net generation plant valuations?

A. The difference in values of nearly $600 million is clearly a significant difference. Much of it is attributable to errors in the OCA's analysis. The assumption that all costs are immediately avoidable, and that there are no costs independent of operation is just wrong. Likewise the assumption that a unit can be placed in cold reserve for a number of years and then reactivated for free is also incorrect. The life extension benefits are possible, but extremely speculative, and the productivity improvement assumption is unsupported. On balance, the Company's valuation is more reasonable than the OCA valuation.

Q. What about the DII analysis of net generation plant value?

A. The figure below summarizes the major sources of the $309 million difference in net



generation value between the Company and DII. As the figure illustrates, the major source of difference -- $255 million – is market price assumptions. Different fuels price assumptions account for a very small part of the difference, and all other sources account for about $35 million of the difference.

Q. Why is the market price difference so significant? From 2006 on, isn't DII's market price forecast actually a little lower than the Company's?

A. In the long term DII's market price projection is just below the Company's ceiling price range, but during the transition period DII's market price is well above the projection based on RFP results and well above OCA's projection as well.

Q. Why is that?

A. On an energy basis, all the forecasts are quite comparable during the transition period. The difference is entirely attributable to Mr. Falkenberg's capacity price assumption. Based on his reserve margin analysis, he assumes that the market will support a capacity price equal to the economic costs of a new combustion turbine starting in 1999. Neither the results of Duquesne's RFP nor the Company's experience in the market as a purchaser of capacity (as described by Mr. Lahtinen and Mr. Irvin in their direct testimony) are consistent with this assumption, but Mr. Falkenberg is apparently undeterred. With no market evidence to support the DII assumption, and ample market evidence to support the Company's position (plus, in this regard, the analysis of OCA), the Company's net generation value is much more reasonable than DII's.

Q. What about HSS's contention that there are no generation stranded costs?

A. Mr. Clayton discusses Mr. Weisenmiller's valuation contentions in more detail, but I have two observations. First, to the extent Mr. Weisenmiller is relying on the Fort Martin transaction to support his valuation, his valuation should be rejected. Relying on a single, old transaction to value all of Duquesne's generating assets is simply not credible. Mr. Weisenmiller offers no evidence that similar transactions could be achieved today, or that such a transaction can reasonably be generalized to all of the Company's generation. Second, while he references selected values from past assessments of the market value of the Company's assets performed by Duquesne and others, he offers no evidence that the market price assumptions underlying the valuations he cites are in fact reflective of current power markets. The Company's

RFP_results indicate that they are not. To the extent his valuation relies on these selective citations, it should be rejected.

No Opportunity for Over Recovery

Q. Opposing parties have made the claim that Duquesne's rate cap and market valuation proposal may result in over recovery of stranded costs. Why do they believe this will be the case?

A. For the most part, this concern stems from a belief that the Company has overestimated its stranded costs, and that allowing recovery of the amount requested would translate to over recovery. There are also secondary issues concerning the ROE spillover mechanism; particularly whether the Company could game that mechanism to achieve over recovery, or would have insufficient incentives to mitigate stranded costs to the detriment of customers.

Q. How do you respond?

A. Duquesne's proposal will not result in over recovery of its stranded costs because the proposal is premised on a market valuation of its generation assets, not on a one time administrative valuation. If the market valuation indicates that stranded costs are lower than what the Company now believes, and maintaining the rate cap through the end of 2005 is not necessary, then the recovery period can be shortened. That is why the Company is proposing that the valuation be completed in 2003 so that any required adjustments to the rate cap could be made in 2004 and 2005. As shown in Mr. Clayton's Exhibit DJC-21 (Revised Exhibit DJC-3, p.2) over 600 million of the Company's minimum amortization commitment is not funded until 2004 and 2005, so

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	)	
	)	
v.	)	**Docket No. R-00974104**
	)	
Duquesne Light Company Application for Approval of a Restructuring Plan Pursuant to 66 Pa. C.S. § 2806(d)	)	

CERTIFICATE OF SERVICE

I hereby certify that I have this day served two copies of Duquesne Light Company's Reply Brief, by first-class mail, upon the participants on the attached service list in accordance with Section 1.54 of the Commission's regulations.

Dated this 16th day of February, 1998.

John S. Moot
Skadden, Arps, Slate,
Meagher & Flom LLP
1440 New York Ave., N.W.
Washington, D.C. 20005
(202) 371-7310

Counsel to
Duquesne Light Company

Kenneth Zielonis
(Pa. Retailers Assn.)
Stevens & Lee
208 North Third St., Ste. 310
P. O. Box 12090
Harrisburg, PA 17108-2090

Brian A. Rider
President
Pennsylvania Retailers' Assn.
224 Pine Street
Harrisburg, PA 17101-1325

James P. Dougherty
David M. Kleppinger
Robert A. Weishaar
Pamela C. Polacek
McNees, Wallace & Nurick
100 Pine Street
P. O. Box 1166
Harrisburg, PA 17108

Kandace F. Melillo
Wayne T. Scott
PA Public Utility Commission
Office of Trial Staff
901 N. 7th Street, Rear
Third Floor, Pitnick Bldg.
Harrisburg, PA 17105-3265

Jacqueline R. Morrow
Rodney R. Akers
Assistant City Solicitor
City of Pittsburgh
313 City County Building
414 Grant Street
Pittsburgh, PA 15219

Stephen J. Baron
J. Kennedy & Associates, Inc.
Suite 475
35 Glenlake Parkway
Atlanta, GA 30328

Angela T. Jones
Office of Small Business Advocate
Suite 1102
300 North 2nd Street
Harrisburg, PA 17101

Howard M. Louik
Allegheny County Law Dept.
300 Fort Pitt Commons
445 Fort Pitt Blvd.
Pittsburgh, PA 15219

Marisa A. Sifontes
Irwin A. Popowsky
Steven K. Steinmetz
Office of Consumer Advocate
1425 Strawberry Square
Harrisburg, PA 17120

Wanda Schiller
Steven Baicker-McKee
Babst, Calland, Clements & Zomnir PC
8th Floor, Two Gateway Center
Pittsburgh, PA 15222

Kenneth L. Wiseman
Robert M. Lamkin
Andrews & Kurth, LLP
1701 Pennsylvania Ave., N.W.
Washington, D.C. 20006

Mark F. Sundback
Robert M. Lamkin
Andrews & Kurth, LLP
1701 Pennsylvania Ave., N.W.
Washington, D.C. 20006

Matthew Kahal
Exeter Associates, Inc.
Suite 350
12510 Prosperity Drive
Silver Spring, MD 20904

David F. Boehm
Michael I. Kurtz
Boehm, Kurtz & Lowry
2110 CBLD Center
36 East Seventh Street
Cincinnati, OH 45202

Terrance J. Fitzpatrick
David M. DeSalle
Ryan, Russell, Ogden & Seltzer, LLP
Suite 101
800 North Third Street
Harrisburg, PA 17102-2025

Robert B. Weisenmiller
MRW & Associates, Inc.
Suite 1440
1999 Harrison Street
Oakland, CA 94612-3517

Michael Reid, Director
Materials Management Services
Administrative Resources, Inc.
500 Commonwealth Drive
Warrendale, PA 15086-7513

Robert J. Stefanko
341 South Bellefield Avenue
Pittsburgh, PA 15213

Margaret Peters
The Peoples Natural Gas Co.
625 Liberty Avenue
Pittsburgh, PA 15222-3197

John Stember
Low Income Advocate Parties
1705 Allegheny Building
429 Forbes Avenue
Pittsburgh, PA 15219

Stephen I. Feld
Pennsylvania Power Company
1 East Washington Street
P. O. Box 891
New Castle, PA 16103-0891

Donald R. Ayersman, Jr.
1125 Denver Avenue
Morgantown, WV 26505

Mark J. McGuire
Ronald N. Carroll
Jenner & Block
Suite 1200
601 13th Street, N.W.
Washington, D.C. 20005

Tim Merrill
Suite 200
4 Penn Center West
Pittsburgh, PA 15276

Kevin J. McKeon
Malatesta, Hawke & McKeon, LLP
P. O. Box 1778
Harrisburg, PA 17101

Thomas P. Gadsden
Morgan, Lewis & Bockius
2000 One Logan Square
Philadelphia, PA 19103

David Hughes
4037 Ludwick Street
Pittsburgh, PA 15217

Thomas J. Augspurger
Midcon Corporation
Office of General Counsel
701 East 22nd Street
Lombard, IL 60148

William T. Hawke
Janet L. Miller
Todd S. Stewart
Malatesta, Hawke & McKeon, LLP
P. O. Box 1778
Harrisburg, PA 17101

Joseph A. Dworetzky
Luke E. Dembosky
John P. Lavelle, Jr.
Hangley, Aronchick, Segal & Pudlin
One Logan Square, 12th Floor
Philadelphia, PA 19103

Roger E. Clark
The Environmentalists
905 Denston Drive
Andler, PA 19002-3901

Attorney of Record
Environmental Energy Project
3700 Vartan Way
Harrisburg, PA 17110

Scott J. Rubin
3 Lost Creek Drive
Selinsgrove, PA 17870-9357

Patricia Armstrong
Thomas, Thomas, Armstrong & Niesen
212 Locust Street, Suite 500
P. O. Box 9500
Harrisburg, PA 17106-9500

Paul E. Russell
Pennsylvania Power & Light Co.
2 North 9th Street
Allentown, PA 18101

David M. Boonin
New Energy Ventures East, LLC
1845 Walnut Street
Ste. 2525
Philadelphia, PA 19103

John O'Brien
Wheeled Electric Power Co.
Suite 207
50 Charles Lindburgh Blvd.
Uniondale, NY 11553

Daniel Clearfield
Gerald Gornish
Alan Kohler
Robert J. Longwell
Wolf, Block, Schorr &
Solis-Cohen, LLP
212 Locust St., Suite 300
Harrisburg, PA 17101

James D. Steffes
Enron Power Marketing, Inc.
1400 Smith Street
P. O. Box 4428
Houston, TX 77002

Brian Kalcic
Excel Consulting
Suite 720-T
225 S. Meramec Avenue
St. Louis, MO 63105

Albert M. Benincasa
Director, Regulatory Affairs
Skipping Stone
46 9th Avenue
Sea Cliff, NY 11579

Douglas F. John
Gordon J. Smith
John & Hengerer
1200 17th Street, N.W.
Suite 600
Washington, D.C. 20036

Larry R. Crayne
Richard S. Herskovitz
Duquesne Light Company
411 Seventh Avenue, 15th Floor
Pittsburgh, PA 15219

Vickiren S. Aeschleman
Director, Regulatory Policy
QST Energy, Inc.
300 Hamilton Blvd., Suite 300
Peoria, IL 61602

Mary Ann Ralls
Duane, Morris & Heckscher LLP
1667 K Street, N.W., Suite 700
Washington, D.C. 20006

Mary McFall Hopper
PECO Energy Company
2301 Market Street
P. O. Box 8699
Philadelphia, PA 19101

Craig R. Kuennen, Ph.D.
904 Melaleuca Avenue, #N
Carlsbad, CA 92009

John Wilson
Executive Director
Community Action Association
of Pennsylvania
222 Pine Street
Harrisburg, PA 17101

Samuel W. Braver
Bruce A. Americus
Buchanan Ingersoll, P.C.
One Oxford Centre, 20th Floor
301 Grant Street
Pittsburgh, PA 15219-1410

Donald A. Kaplan
Lisa M. Helpert
Preston, Gates, Ellis & Rouvelas
Meeds LLP
1735 New York Ave., N.W., Ste. 500
Washington, D.C. 20006-4759

Gary A. Jeffries
CNG Energy Services Corporation
One Park Ridge Center
P. O. Box 15746
Pittsburgh, PA 15244-0746

Keith M. Sappenfield, II
Director of Marketing Support
NorAm Energy Management, Inc.
P. O. Box 2628
Houston, TX 77252-2628

John R. Orr
Duke Energy Trading & Marketing LLC
One Westchester Center
10777 Westheimer, Suite 650
Houston, TX 77042

David Cruthirds
Electric Clearinghouse, Inc.
100 Louisiana, Suite 5800
Houston, TX 77002-5050

Lawrence E. Moncrief
1364 Silverton Avenue
Pittsburgh, PA 15206

THE LAW FIRM OF

MALATESTA HAWKE & McKEON LLP

HARRISBURG ENERGY CENTER
100 NORTH TENTH STREET
HARRISBURG, PENNSYLVANIA 17101
(717) 236-1300
FAX (717) 236-4841

http: //www.MHM-LAW.com

MAILING ADDRESS:
P.O. BOX 1778
HARRISBURG, PA 17105

JOSEPH J. MALATESTA, JR.
WILLIAM T. HAWKE
KEVIN J. McKEON
LOUISE A. KNIGHT
THOMAS J. SNISCAK
NORMAN JAMES KENNARD
LILLIAN SMITH HARRIS
SCOTT T. WYLAND
JANET L. MILLER
SUSAN J. SMITH
TODD S. STEWART
THOMAS S. PEDERSEN

February 16, 1998

Via Hand Delivery

James J. McNulty, Secretary/Prothonotary
Pennsylvania Public Utility Commission
North Office Building - Filing Room
PO Box 3265
Harrisburg, PA 17105-3265

RE: Pennsylvania Public Utility Commission v. Duquesne Light Company; Application for Approval of Restructuring Plan Under Section 2806 of the Public Utility Code; Docket No. R-00974104; REPLY BRIEF OF THE MID-ATLANTIC POWER SUPPLY ASSOCIATION

Dear Mr. McNulty:

Enclosed, for filing with the Commission, please find an original and **nine (9)** copies of the Reply Brief of the Mid-Atlantic Power Supply Association ("MAPSA") in the above-referenced matter.

All parties to this proceeding have been served in accordance with the attached Certificate of Service. If you have any questions concerning the enclosed documents, please direct them to me. Thank you for your attention to this matter.

Very truly yours,

Todd S. Stewart

TSS/bes
Enclosures
cc: Attached Certificate of Service
Honorable John H. Corbett, Jr., ALJ (via Federal Express) (2 copies and diskette)

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Duquesne Light Company - Application for Approval of Restructuring Plan Under Section 2806 of the Public Utility Code	:	Docket No. R-00974104

ORIGINAL

REPLY BRIEF OF THE MID-ATLANTIC POWER SUPPLY ASSOCIATION ("MAPSA")

William T. Hawke
Janet L. Miller
Todd S. Stewart
Malatesta Hawke & McKeon LLP
100 North Tenth Street
P.O. Box 1778
Harrisburg, PA 17105
717-236-1300

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Regulations

I. INTRODUCTION AND SUMMARY OF THE ARGUMENT[1]

On page 1 of its Main Brief, Duquesne Light Company ("Duquesne") characterizes the most significant issue in this case as being generation-related stranded costs. Duquesne breaks this issue into three categories, those being: the appropriate methodology for quantifying generation-related stranded costs; proposals for disallowance of a portion of those costs; and, the appropriate rate methodology for recovering such costs. Duquesne argues that its offer to auction its generation assets will eliminate most disputes regarding the quantification of stranded costs and the appropriate rate methodology for recovering stranded costs. MAPSA disputes Duquesne's assumption that the auction of generation assets will resolve any issues regarding the appropriate methodology for recovering stranded costs in rates. While MAPSA whole-heartedly supports Duquesne's offer to auction its generation assets (if indeed that auction ever is to occur), it is the appropriate ratemaking methodology for the recovery of those stranded costs which drives the issue of foremost concern to MAPSA in this proceeding, namely, the level of the competitive generation credit ('CGC"). It is remarkable that Duquesne has failed even to address MAPSA's position on this latter issue.

On page 2 of its Main Brief, Duquesne states that it has agreed to auction all of its generation assets today, if the Commission finds that the Competition Act[2] requires the evaluation of stranded costs be made today. Because of the likelihood that a decision in the "stand-alone" restructuring case will not be left in tact, nothing short of an unqualified waiver on the part of Duquesne to allow the Commission to order it to auction its generation assets

[1] MAPSA's Argument headings follow the agreed-upon common Brief outline; where MAPSA has taken no position on an issue, no Argument heading appears. This format also was used in MAPSA's Main Brief.

[2] Electricity Generation Customer Choice and Competition act, 66 Pa. C.S. §2801, et seq. ("Competition Act" or "Act").

immediately is satisfactory. Otherwise, Duquesne's offer is merely illusory. This point is illustrated by Duquesne's argument in its Main Brief that the auction proposal applies only to its "stand-alone" case.

On page 5 of its Main Brief, Duquesne argues that 66 Pa. C.S. §2804(4)(v) gives it an absolute right to continue to collect its fully-capped rate if it applies any excess earnings under the cap toward the mitigation of stranded costs. Duquesne appears to believe that this section of the Competition Act eliminates the requirement that it actually determine a specific competitive transition charge ("CTC") in this proceeding, which CTC is to be designed to recover a "known and measurable" level of stranded costs. 66 Pa. C.S. §2803. In short, the Statutory Construction Act is quite clear; namely, where a specific provision applies, a general provision or a provision which is not specific to that requirement, must be disregarded. 1 Pa. C.S. §1921, et seq. In this particular case, the Competition Act is specific about the requirement that a utility first determine an appropriate level of stranded costs for recovery in this proceeding, and then develop a CTC designed to recover that level of stranded costs. 66 Pa. C.S. §2803; §2808. The statutory requirement is specific and applies to all utilities. If the Competition Act is read to give effect to all of its provisions, the absurdity of Duquesne's argument becomes readily apparent. Why would the Legislature require, in one provision, the specific present value enumeration of stranded costs, and in a separate unrelated provision, give a utility a huge loophole allowing it to avoid that requirement? The answer is simple; that is not what the Legislature intended. Duquesne's attempt to justify its failure to develop a known and measurable level of stranded costs and to design a CTC to recover those costs in this proceeding, is a violation of the statute and must be rejected.

The Office of Consumer Advocate ("OCA") argues in its Main Brief that the decision of this Commission in PECO[3] should be modified, that Duquesne's rates should be unbundled, and that a CTC and CGC be calculated in such a way that all customers will achieve immediate rate reductions of approximately 16.9%. (OCA Main Brief, p. 4). The OCA's argument that an immediate rate decrease should be adopted in lieu of a CGC which would allow for vibrant competition, specifically was rejected by the Commission in PECO and should, likewise, be disregarded in this case. What was stated by the Commission in PECO is equally applicable here: "Our general concern is that the Partial Settlement trades temporary, inadequate rate cuts and other concessions for a delay in competition and de facto monopoly status for PECO Energy." PECO, p. 14. While implementing the OCA proposal would achieve immediate rate reductions, competition in the long-term would be damaged irreparably.

A. Overview of MAPSA's Reply Brief

As argued by MAPSA in its Main Brief, MAPSA believes that the most significant issue, among the many significant issues that will be resolved in this case, is whether or not Duquesne's Restructuring Plan, as proposed and amended, will allow for the development of a robust competitive market for retail sales of electric energy in the Commonwealth of Pennsylvania. The key question is: whether the competitive generation credit or "shopping credit" proposed by Duquesne is sufficient to allow competitive suppliers to compete in Duquesne's service territory? The Commission's decision in PECO specified a process for answering that question. Specifically: Duquesne's total level of stranded costs must be determined in this proceeding in accordance with the Competition Act's "known and

[3] Application of PECO Energy Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code, R-00973953, (Order entered December 23, 1997) ("PECO").

measurable" standard; a competitive transition charge must be designed to recover those stranded costs in this proceeding; and, the resulting shopping credit or CGC -- produced by adding the CTC to Duquesne's unbundled transmission and distribution charges, with the sum of that calculation subtracted from Duquesne's current bundled rate -- must be examined to determine whether or not it will allow for competition. Once it has been determined (as MAPSA submits this Commission must find) that Duquesne's shopping credit is wholly inadequate to allow for the development of a truly competitive market in Duquesne's service territory, this Commission has the option either to extend the recovery period for stranded costs, or, to levelize the recovery of those stranded costs. Duquesne's Main Brief completely fails to address this methodology or its relevance; in fact, Duquesne's Main Brief fails to acknowledge the absolute necessity that Duquesne's Restructuring Plan must allow for the development of a competitive market. Therefore, Duquesne's Restructuring Plan should be rejected.

As will be noted throughout this Reply Brief, Duquesne's Main Brief has failed to address specific evidentiary points raised on the record by MAPSA; therefore, Duquesne has failed to meet its burden of proof and persuasion on these issues. The Commission's regulations at 52 Pa. Code §5.501(a)(3), specifically require that "the party with the burden of proof shall, in its main or initial brief, completely address, to the extent possible, every issue raised by the relief sought and the evidence adduced at hearing." It is clear from even the most liberal reading of Duquesne's Main Brief, that it not only has failed to address several key evidentiary issues raised by MAPSA in this proceeding, it simply has failed to acknowledge their existence. While it might be true that parties, even those with the burden of proof, are not required to anticipate every possible argument that an opponent might raise, they are, at a minimum, required to address substantive issues adduced on the evidentiary record by opposing parties.

Specifically, Duquesne has failed to address the following issues raised in the testimony of MAPSA:

1. The appropriate level of the CGC or "shopping credit" (MAPSA St. No. 1, pp. 29-37; MAPSA Exhibit No. 1);

2. The appropriateness of Duquesne's $100.00 scheduling charge, and the fact that it is not cost justified (MAPSA St. No. 1, pp. 41-42); and,

3. The fact that Duquesne's proposed Imbalance Charges are not cost justified and are unreasonable (MAPSA St. No. 1, pp. 55-59).

In the alternative, and at the very least, Duquesne's failure even to acknowledge MAPSA's substantial evidentiary positions should disqualify Duquesne from arguing against MAPSA's positions in its Reply Brief. If Duquesne were allowed to do so, it would leave MAPSA no practical means of defending its positions. In other words, this Commission should not countenance Duquesne's obvious attempt to "sandbag" on critical positions.

Duquesne's Main Brief does acknowledge, in certain parts, the potential for the Commission decision in PECO to control the implementation of the Competition Act as it relates to Duquesne.[4] However, in the most important sections of its Main Brief, Duquesne fails to acknowledge that the PECO decision applies with equal force. Particularly, in the area of stranded cost quantification and in the determination of an appropriate level of shopping credit, Duquesne ignores the mandate of PECO and attempts to set a shopping credit based on a wholesale market price. Duquesne's "pick and choose" application of the PECO Opinion and

[4] See, e.g. Duquesne Main Brief, p. 9.

Order renders much of its argument quite inconsequential in that Duquesne ignores the only relevant precedent in this area. Therefore, Duquesne's arguments which disregard the specifically applicable PECO outcomes must be disregarded.

II. PHASE-IN OF CUSTOMER CHOICE

A. Method of Customer Selection

On pages 6-7 of its Main Brief, Duquesne argues that its first-come, first-served methodology is superior to any methodology offered by any Intervenor. Duquesne ignores the fact that its selection process gives Duquesne ultimate control over what geographic areas and what industrial and commercial segments are allowed to have choice. The Competition Act clearly recognized the potential for abuse in this process, and thus specified first-come, first-served as the method of choice. 66 Pa. C.S. §2806(b)(4). Duquesne's unsubstantiated attempt to justify its proposal on the basis that it will eliminate competitive disadvantage falls short of the mark. Indeed, Duquesne's proposal still allows for competitive disadvantage, but simply gives Duquesne control over which segment of the population is disadvantaged. Likewise, Duquesne's arguments regarding building on experience gained from the Pilot Program are irrelevant. During the Pilot Program, Duquesne did not employ the process it proposes to employ following restructuring. Therefore, no party has experience with the methodology proposed by Duquesne. Rather, the parties have had experience with the first-come, first-served methodology and are more likely to be better prepared to deal with that methodology than with Duquesne's arbitrary and anticompetitive proposal. Duquesne's enrollment methodology must be rejected.

III. TRANSMISSION AND DISTRIBUTION RATES: UNBUNDLING ISSUES

E. Ancillary Services

On pages 15 and 16 of its Main Brief, Duquesne asserts that it is not the fault of Duquesne that it is not able to provide all of the *pro forma* ancillary services to competitive suppliers at this time. Duquesne relies upon the testimony of Mr. Lahtinen for the proposition that it is ECAR, not Duquesne, which has prevented Duquesne from offering these services on a competitive, unbundled basis. However, Mr. Lahtinen admitted that this may not be the case:

> Q: Is it your understanding of these ECAR rules, as Mr. Irvin has described them to you, that ECAR would currently not permit Duquesne to unbundle any other ancillary services?
>
> A: No, no. I think I can answer the question. I don't think ECAR has got anything to do with unbundling the services.

Tr. 772.

Statements such as the one quoted above clearly undercut Duquesne's credibility and destroy the only argument that it has presented on this issue. Consequently, its position must be rejected and it should be required to unbundle all ancillary services, and provide an appropriate, fully-allocated credit to the CGC of customers who purchase these services from Duquesne's competitors.

IV. TRANSITION OR STRANDED COSTS

B. Generation-Related Stranded Costs

3. Market Value.

On page 27 of its Main Brief, Duquesne argues that 66 Pa. C.S. §2804(4)(v) suggests a Legislative preference for accelerating stranded cost amortization. MAPSA disagrees with

Duquesne's suggestion that lengthening the CTC recovery period is not allowed by the Competition Act, if that is what Duquesne intends to imply. Rather, the Competition Act expressly allows for the extension of the CTC recovery period if it is necessary to promote competition. 66 Pa. C.S. §2808(b).

F. Recovery of Stranded Costs

On page 56 of its Main Brief, Duquesne again restates its argument that 66 Pa. C.S. §2804(4)(v) relieves it of the responsibility to propose a "known and measurable" CTC. Obviously, Duquesne has misread the statute, because §2804(4)(v) has nothing to do with setting a CTC. Rather, it is a "rate cap" provision intended to be effective after the Commission reviews this Restructuring Plan. Duquesne should be required to determine an actual level of stranded costs (preferably through an immediate auction process, which Duquesne appears to have adopted) and develop a CTC designed to recover those stranded costs while still allowing for the development of competition. Duquesne's proposal likewise ignores the Commission's requirement that the CTC be collected on a per kWh basis rather than on a fixed charge, customer-specific or, more accurately, a "premise-specific" basis, as proposed by Duquesne. PECO. Duquesne's proposal should be modified to collect the CTC on a per kWh basis alone.

V. THE COMPETITIVE TRANSITION CHARGE

A. Conceptual Disputes Regarding Calculation

On page 62 of its Main Brief, Duquesne addresses the methodology adopted by this Commission in PECO, as being the appropriate methodology for setting a CGC. Duquesne's characterization is wholly inaccurate, and completely self-serving. Duquesne appears to believe that the shopping credit that it proposes is intended to reflect current market prices. While

Duquesne conveniently ignores the fact that its "market price" is a wholesale market price, which obviously will not allow for competition, the record evidence is clear on this point. Duquesne ignores the fact that the shopping credit is the price against which competitors will have to compete and, if the shopping credit is not sufficient to allow for competition, there will be no competition and, therefore, no stranded costs. The guarantee in question is not that the shopping credit will reflect current market prices (or Duquesne's distorted view of market prices) but, rather, whether the shopping credit will guarantee the development of a robust competitive market. Duquesne continues to mistakenly rely upon 66 Pa. C.S. §2804(4)(v) for the proposition that it has the continuing statutory right to collect its current bundled rate. Duquesne's analysis must be rejected in favor of the correct application of the mandates of the PECO decision and the Competition Act.

At page 62 and continuing onto page 64 of its Main Brief, Duquesne attempts to justify its annual adjustment of the CGC based on the results of its RFP. For all the reasons stated in MAPSA's Main Brief, Duquesne's RFP is a flawed mechanism for predicting a wholesale market price and has no chance of ever producing a result that would reflect a fully-delivered price of energy which is required of a shopping credit.[5] Because Duquesne's proposed adjustment methodology relies upon its RFP, which is incapable of producing an accurate result, its proposal must be rejected. It also is quite apparent that Duquesne ignores the methodology for calculating a CGC set forth in the PECO decision as being the appropriate methodology. Duquesne's proposal should be rejected on that basis alone.

[5] See, MAPSA St. No. 1, pp. 25-27; MAPSA; Main Brief, pp. 22-24.

Duquesne's proposal in its Main Brief, page 65, ignores the fact that there is the potential cost-shifting within customer classes if it is allowed to implement a customer-specific or premise-specific CTC. Duquesne's position ignores the Order of the Commission in PECO, that the CTC be collected on a per kWh basis in order to send the appropriate price signals to customers. Duquesne's arguments to the contrary - merely stating that MAPSA's position is "intellectually indefensible" - ignore the fact that Duquesne's proposal is legally indefensible and must be rejected.

On page 68 of its Main Brief, Duquesne argues that, while MAPSA criticizes its RFP proposal, MAPSA fails to offer any alternative to the RFP. Duquesne asserts that MAPSA's failure to offer an alternative is fatal to its criticism. Attempting to fix Duquesne's RFP proposal is akin to attempting to repair a car which has been put through a car shredder. "What's the point?" The fact that the criticisms offer no alternative fails to address the merits of the perfectly valid criticism, namely, that the RFP process if fatally flawed.

B. Other Disputes Regarding Specific Proposals

Duquesne's argument on page 69 of its Main Brief that fails to acknowledge the fact that the RFP was designed to produce a wholesale market price and not to reflect the fully-delivered cost of power at retail, as admitted by Duquesne's witnesses. Tr. 763. Duquesne's attempt to set the "shopping credit" based on this wholesale price is contrary to the intent of the Competition Act and the clearly-expressed intent of this Commission in PECO. Arguing that MAPSA has no interest in the "constructive debate" regarding a shopping credit is simply a smokescreen. MAPSA has stated a specific proposal for the development of a shopping credit sufficient to allow for competition - an evidentiary point which Duquesne has completely ignored. (MAPSA

St. No. 1, pp. 29-37). The PECO Order clearly requires: the present-day evaluation of Duquesne's stranded generation assets (which MAPSA asserts is best accomplished by an immediate auction); the setting of an appropriate CTC designed to recover those stranded costs; and, the derivation of a "fallout" shopping credit. The analysis then examines that shopping credit to determine whether it is sufficient to allow for the development of a robust competitive market. If not, the CTC recovery should be extended or levelized. Duquesne's failure to even recognize the existence of the precedent indicates Duquesne's unwillingness to engage in a productive discussion and defies the reality of the Commission's intentions. PECO.

MAPSA does not dispute that the RFP produces prices that are reflective of the discrete product offered for sale in the RFP. However, MAPSA does take issue with the product itself. Namely, MAPSA argues that the product offered in the RFP was a wholesale power product which would be only a single component of the portfolio of supply requirements necessary for a competitive supplier to provide service to retail customers. Also, as MAPSA witness Whitfield Russell testified, Duquesne's RFP result did not reflect all of the ancillary or additional services that would be required of a supplier. (MAPSA St. No. 1, pp. 32-33). This was admitted by Duquesne's witness. Tr. 136. The reason that MAPSA opposes using the low prices produced by the RFP is that these prices are reflective of a discreet wholesale transaction, not a fully-delivered retail price. As discussed at pages 22-24 of MAPSA's Main Brief, Duquesne's RFP results must be rejected as an indication of a "market price," for the purposes of setting a CGC or CTC.

VIII. COMPETITIVE SAFEGUARDS

A. Code of Conduct

On page 79 of Duquesne's Main Brief, Duquesne argues that an appropriate Code of Conduct is a generic issue and that it must not be resolved in this proceeding. However, Duquesne's argument denies the practical reality that it is unlikely that a final rulemaking will be in place in time for the January 1, 1999 transition to competition. Duquesne's proposed Code of Conduct is wholly inadequate, as evidenced by the Intervenors' testimony. Therefore, Duquesne's Code of Conduct proposal must be rejected and one of the Intervenors' Codes of Conduct, (e.g. MAPSA St. No. 1, Attachment II) should be adopted as an Interim Code, until final regulations are enacted.

IX. DUTY TO SERVE

C. Electric Transmission and Distribution Service

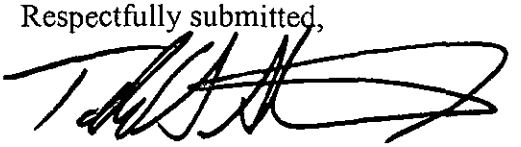
1. Unbundling Other Customer Services.

On pages 81 and 82 of its Main Brief, Duquesne argues its position on the unbundling of revenue-cycle services, namely, that those services should be unbundled, if at all, pursuant to a generic rulemaking proceeding and that the Commission need not address unbundling here. Indeed, it is Duquesne which makes the most compelling argument for the unbundling of the metering and billing functions. Duquesne's new, real-time metering system (CARS) will make unbundling far less complicated than it would be with other utilities. (Tr. 858-873). Duquesne has no technical reason not to unbundle these services, except that it desires not to have competitors engaging in the functions of metering and billing. Duquesne simply would prefer to maintain its monopoly position. Duquesne should be required to unbundle these services now.

XIII. CONCLUSION

In summary, Duquesne's Restructuring Plan fails to guarantee the development of a robust competitive market for retail sales of electric generation. Duquesne's proposal is anti-competitive and, if adopted, would allow Duquesne to maintain its near monopoly status in this marketplace until well into the future. Therefore, this Commission should reject those provisions of Duquesne's Restructuring Plan as set forth in the Main Brief of MAPSA and in this Reply Brief, and should require that Duquesne modify its Restructuring Plan in accordance with the recommendations contained herein. As before, where the Commission found that a Restructuring Plan was inadequate, the Commission should, in this case, re-emphasize the fact that: the Competition Act requires competition as a means of regulating rates; it is by reason of competition that Duquesne will have any stranded costs at all; and, without competition, the future benefits envisioned by the Competition Act will not be realized. For these reasons, MAPSA recommends the Commission adopt its position in this proceeding.

Respectfully submitted,



William T. Hawke
Janet L. Miller
Todd S. Stewart
Malatesta Hawke & McKeon LLP
100 North Tenth Street
P.O. Box 1778
Harrisburg, PA 17105
717-236-1300

Counsel for The Mid-Atlantic
Power Supply Association

Dated: February 16, 1998

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Reply Brief of the Mid-Atlantic Power Supply Association has been served upon the persons and in the manner indicated below.

Service by First Class Mail:

John Moot, Esquire
Skadden, Arps, Slate Meagher & Flom
1440 New York Avenue N.W.
Washington D.C. 20005

James P. Dougherty, Esquire
Robert A. Weishaar, Jr., Esquire
Pamela C. Polacek, Esquire
McNees, Wallace & Nurick
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108

Kandace F. Melillo, Esquire
Wayne T. Scott, Esquire
Pennsylvania Public Utility Commission
Office of Trial Staff
P.O. Box 3265
Harrisburg, PA 17105-3265

Jacqueline R. Morrow, Esquire
Rodney R. Akers, Esquire
Assistant City Solicitor
313 City County Building
414 Grant Street
Pittsburgh, PA 15219

Stephen J. Baron
J. Kennedy and Associates, Inc.
Suite 475 - 35 Glenlake Parkway
Atlanta, GA 30328

Larry P. Crayne, Esquire
Richard S. Herskovitz, Esquire
Duquesne Light Company
411 Seventh Avenue
Pittsburgh, PA 15219

Angela T. Jones, Esquire
Karen Oill Moury, Esquire
Office of Small Business Advocate
Suite 1102 - Commerce Building
300 North 2nd Street
Harrisburg, PA 17101

Howard M. Louik, Esquire
Allegheny County Law Department
300 Fort Pitt Commons
445 Fort Pitt Boulevard
Pittsburgh, PA 15219

Irwin A. Popowsky, Esquire
Marisa A. Sifontes, Esquire
Steven K. Steinmetz, Esquire
Office of Consumer Advocate
1425 Strawberry Square
Harrisburg, PA 17120

Michael L. Kurtz, Esquire
David F. Boehm, Esquire
Boehm, Kurtz & Lowry
2110 CBLD Center
36 E. Seventh Street
Cincinnati, OH 45202

Samuel W. Braver, Esquire
Bruce A. Americus, Esquire
Buchanan Ingersoll, P.C.
20th Fl., One Oxford Centre
301 Grant Street
Pittsburgh, PA 15219-1410

Terrance J. Fitzpatrick, Esquire
Ryan, Russell, Ogden & Seltzer, LLP
Suite 101 - 800 North Third Street
Harrisburg, PA 17102-2025

Stephen L. Feld, Esquire
Pennsylvania Power Company
1 East Washington Street
P.O. Box 891
New Castle, PA 16103-0891

Matthew Kahal
Exeter Associates
Suite 350
12510 Prosperity Drive
Silver Spring, MD 20904

Wanda Schiller, Esquire
Steven F. Baicker-McKee, Esquire
Babst, Calland, Clements & Zomnir, P.C.
Two Gateway Center, 8th Floor
Pittsburgh, PA 15222

Margaret Peters, Esquire
The Peoples Natural Gas Company
625 Liberty Avenue
Pittsburgh, PA 15222-3197

Thomas Gadsen, Esquire
Morgan, Lewis & Bockius
2000 One Logan Square
Philadelphia, PA 19103

Thomas J. Augspurger, Esquire
MidCon Corporation
Office of General Counsel
701 East 22nd Street
Lombard, IL 60148

Mark J. McGuire, Esquire
Ronald N. Carroll, Esquire
Jenner & Block
Suite 1200 - 601 13th Street, N.W.
Washington, DC 20005

Paul E. Russell, Esquire
Pennsylvania Power & Light Company
2 North Ninth Street
Allentown, PA 18101

Mary McFall Hopper, Esquire
PECO Energy Company
S23-1
2301 Market Street
Philadelphia, PA 19103

Joseph A. Dworetzky, Esquire
John P. Lavelle, Jr., Esquire
Hangley, Aronchick, Segal & Pudlin
12th Floor - One Logan Square
Philadelphia, PA 19103

Albert M. Benincasa
Director, Regulatory Affair
Skipping Stone
46 9th Avenue
Sea Cliff, NY 11579

Donald A. Kaplan, Esquire
Lisa M. Helpert, Esquire
Preston Gates Ellis & Rouvelas Meeds LLP
Suite 500 - 1735 New York Avenue, N.W.
Washington, D.C. 20006-4759

David M. Boonin
New Energy Ventures East, LLC
Suite 2525 - 1845 Walnut Street
Philadelphia, PA 19103

Patricia Armstrong, Esquire
Thomas, Thomas, Armstrong & Niesen
212 Locust Street - Suite 500
P.O. Box 9500
Harrisburg, PA 17108-9500

John O'Brien, Esquire
Wheeled Electric Power Company
Suite 207 - 50 Charles Lindburgh Blvd.
Uniondale, NY 11553

Vickiren S. Aeshleman
Director, Regulatory Affairs
QST Energy, Inc.
Suite 300 - 300 Hamilton Boulevard
Peoria, IL 61602

Gary A. Jeffries, Esquire
CNG Energy Services Corporation
One Park Ridge Center
P.O. Box 15746
Pittsburgh, PA 15244-0746

David Cruthirds, Esquire
Electric Clearinghouse, Inc.
Suite 5800 - 100 Louisiana
Houston, TX 77002-5050

Douglas F. John, Esquire
Gordon J. Smith, Esquire
John & Hengerer
Suite 600 - 1200 17th Street, N.W.
Washington, DC 20036-3006

Mary Ann Ralls, Esquire
Duane, Morris & Hechscher LLP
Suite 700 - 1667 K Street, N.W.
Washington, D.C. 20006-1608

Keith M. Sappenfield, II
Director of Marketing Support
NorAm Energy Management, Inc.
P.O. Box 2628
Houston, TX 77252-2628

John R. Orr, Esquire
Duke Energy Trading & Marketing, LLC
One Westchester Center
Suite 650
10777 Westheimer
Houston, TX 77042

Lawrence E. Moncrief, Esquire
1364 Silverton Avenue
Pittsburgh, PA 15206

Daniel Clearfield, Esquire
Gerald Gornish, Esquire
Alan Kohler, Esqire
Robert J. Longwell, Esquire
Wolf, Block, Schorr & Solis-Cohen, LLP
Suite 300, 212 Locust Street
Harrisburg, PA 17101-1236

James D. Steffes
Enron Power Marketing, Inc.
1400 Smith Street
P.O. Box 4428
Houston, TX 77002

John Stember, Esquire
Low Income Advocate Parties
1705 Allegheny Building
429 Forbes Avenue
Pittsburgh, PA 15219

Kenneth L. Wiseman, Esquire
Robert M. Lamkin, Esquire
Andrews & Kurth, LLP
Suite 200
1701 Pennsylvania Avenue, N.W.
Washington, DC 20006

Alan Barak
Environmental Energy Project
1417 Blue Mountain Parkway
Harrisburg, PA 17112

Mark F. Sundback, Esquire
Robert M. Lamkin, Esquire
Andrews & Kurth, LLP
Suite 200
1701 Pennsylvania Avenue, N.W.
Washington, DC 20006

Robert J. Stefanko, Esquire
341 South Bellefield Avenue
Pittsburgh, PA 15213

Tim Merrill, Esquire
Suite 200 - 4 Penn Center West
Pittsburgh, PA 15276

Robert B. Weisnemiller
MRW & Associates, Inc.
Suite 1440 - 1999 Harrison Street
Oakland, CA 94612-3517

Michael Reid, Director
Materials Management Services
Administrative Resources, Inc.
500 Commonwealth Drive
Warrendale, PA 15086-7513

Brian Kalcic
Excel Consulting
Suite 720-T
225 S. Meramec Avenue
St. Louis, MO 63105

Brian A. Rider, President
Pennsylvania Retailers' Association
224 Pine Street
Harrisburg, PA 17101-1325

Scott J. Rubin, Esquire
3 Lost Creek Drive
Selinsgrove, PA 17870-9357

Cindy Datig, Esquire
Dollar Energy Fund
P.O. Box 42329
Pittsburgh, PA 15203

Kenneth Zielonis, Esquire
Stevens & Lee
Suite 310 - 208 North Third Street
P.O. Box 12090
Harrisburg, PA 17108-2090

Donald R. Ayersman, Jr., Esquire
IBEW Local 2357
1125 Denver Avenue
Morgantown, WV 26505

Roger Clark, Esquire
The Environmentalists
905 Denston Drive
Andler, PA 19002-3901

David Hughes
4037 Ludwick Street
Pittsburgh, PA 15217

Kevin J. McKeon
Malatesta Hawke & McKeon LLP
P.O. Box 1778
Harrisburg, PA 17105

John Wilson, Executive Director
Community Action Association of PA
222 Pine Street
Harrisburg, PA 17101

Todd S. Stewart

DATED: February 16, 1998

LAW OFFICES
WOLF, BLOCK, SCHORR AND SOLIS-COHEN LLP
212 LOCUST STREET
SUITE 300
HARRISBURG, PA 17101-0213
(717) 237-7160
FACSIMILE: (717) 237-7161

DOCUMENT FOLDER

ORIGINAL

ROBERT J. LONGWELL
DIRECT DIAL: (717) 237-7173
E-MAIL: RLONGWELL@WOLFBLOCK.COM

February 17, 1998

VIA HAND DELIVERY
James McNulty, Secretary
Pennsylvania Public Utility Commission
P.O. Box 3265
Harrisburg, PA 17105-3265

RE: Duquesne Light Company Application to Approve Restructuring Plan Pursuant to 66 Pa. C.S. §2806(d)
Docket No. R-00974104

Dear Mr. McNulty:

Enclosed for filing please find an original and nine copies of the Reply Brief of Enron Power Marketing, Inc. As indicated on the attached Certificate of Service, copies of this document are being served this day on the parties in the manner indicated.

Please contact me if you have any questions with respect to the enclosed.

Very truly yours,

Robert J. Longwell
For WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP

DC/lww
Enclosure

cc: Hon. John Corbett, Jr. (w/enc.) (via hand delivery)
All Parties of Record (w/enc.)

DSH:11126.1

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
	:	Docket No. R-00974104
v.	:	
	:	
Duquesne Light Company Application to approve Restructuring Plan pursuant to 66 Pa. C.S. §2806(d)	:	

REPLY BRIEF OF ENRON POWER MARKETING, INC.

Daniel Clearfield
Gerald Gornish
Robert J. Longwell
WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP
212 Locust Street, Suite 300
Harrisburg, PA 17101

Dated: February 17, 1998

TABLE OF CONTENTS

STATEMENT OF CASE

I. INTRODUCTION AND SUMMARY OF ARGUMENT

Enron Power Marketing Inc. ("Enron") hereby submits its response to the Main Briefs of Duquesne Light Co. ("Duquesne") and several of the parties submitted in Duquesne's restructuring proceeding.

As an overall observation, Enron notes that on a variety of issues some parties, and particularly Duquesne, have urged the Commission to depart from the policy pronouncements made just a few months ago in its PECO[1] decision. But as many others have stated, such a departure would create confusion and inequities that would add to the cost and complexities of an already arduous process.[2] Indeed a failure to adhere to the affirmative policy rules established in PECO could create unfair competitive burdens or advantages between Pennsylvania's EDCs. On this point, Enron agrees with PECO itself whose position in this case essentially is that, whatever the merit of the Commission's rules for PECO, the same standards and policies should be applied uniformly. As PECO stated, "[w]hatever rules are applied to PECO must be imposed on other utilities as well. Otherwise the playing field will be anything but 'level' and PECO's ability to compete will be severely hampered."[3] Enron is happy to join

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1 Application of PECO Energy Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code, R-00973953 (December 23, 1997), Reconsideration Order (January 16, 1998) and Order on Compliance Filing (February 5, 1998) (referred to respectively as "PECO Restructuring Order," "PECO Reconsideration Order" and "PECO Compliance Filing Order").

2 Accord, OCA Main Brief at 2 ("[T]he PECO Order provides a foundation that, in large part, provides an appropriate and reasonable resolution of many of the difficult issues presented to the Commission that should be followed in this case.")

3 PECO Main Brief at 6. This uniformity goal clearly would not prevent the PUC from (continued...)

with PECO in this call for the uniform application of the PECO decision, especially its seminal aspects, such as:

- The PUC's landmark decision to adopt a pro-competition paradigm that rejects one time, limited rate decreases in favor of a residual shopping credit which will produce far greater benefits and savings both in the short and longer term;

- A calculation of a levelized CTC based upon a stranded cost recovery allowance that permits 100% of the utility's known and definite non-mitigatable stranded costs plus a return on the unamortized balance at a rate which accurately reflects associated market risk;

- The expedited phase-in of customer choice, using a process that complies with first-come-first-serve and promotes maximum participation; and

- The establishment of appropriate rules on universal services and consumer education that promotes consumer welfare and education on a state-wide basis.

Accordingly, Enron respectfully requests that the ALJ and the Commission issue an order for Duquesne which is consistent with these precepts and which facilitates the development of a robust competitive market and maximum consumer benefits.

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[3](...continued)
going farther to allow greater competitive choice as part of the Duquesne restructuring, especially on issue, such as the unbundling and competitive provisioning of metering and billing or permitting agency, where the Commission deferred ruling on the position.

II. PHASE-IN OF CUSTOMER CHOICE

A. Method of Customer Selection

1. Duquesne

Duquesne continues to argue that its "grouping" method, which, in the case of residential and industrial customers, would require customers to be phased into customer choice based on geographic location or industry grouping is superior to the method mandated by the Commission in the PECO Restructuring Order because it allegedly prevents competitive disadvantages among similarly situated customers and "builds on the experience gained from the pilot program . . . rather than establishing a selection process that ignores those results."[4] The fact that the two most active groups of customers participating in this proceeding (the Duquesne Industrial Intervenors ["DII"] and the Pennsylvania Retailers Association ["PRA"]) both oppose the Duquesne "market segment" methodology for selecting customers to participate in the first phases of direct access[5] clearly puts to the lie the notion that Duquesne's proposal will be more likely to avoid creating competitive disadvantages among Duquesne's commercial and industrial customers. Moreover, most groups commenting on the Duquesne proposal pointed out that the fundamental premise of Duquesne's approach — i.e., that the selection process should mirror the degree to which a geographic area or industrial commercial market segment responded to the opportunity to participate in the pilot because this response somehow created an appropriate priority for participation in the phase-in of direct access — is illogical and

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4 Duquesne Main Brief at 7. Duquesne also pointed out that its proposed approach was not considered in the PECO Restructuring Order. See, PECO Restructuring Order at 47.

5 See DII Main Brief at 5-6; PRA Main Brief at 8.

irrelevant. Indeed, as most of the parties pointed out, participation of customer segments or geographic areas in the pilot may have little to do with their present interest, desire or level of information about participation in direct access.[6]

The overriding concern about the Duquesne proposal is that it increases the chances that less than the permitted amount of customers will actually participate in direct access when they have the opportunity to do so. While this might be to the advantage of Duquesne, it is neither consistent with the desires of customers or suppliers, nor the Commission's determination in the PECO proceeding. Duquesne's position should be rejected.

B. Timetable for Phase-In

The Commission's PECO Restructuring Order, sets the precedent for design of the transition to direct access for all Pennsylvanians by accelerating the phase-in to enable all customers to choose by January 2, 2000. Enron asserted in its Main Brief that it would cause unnecessary customer confusion to allow the duration of the phase-in period to vary from service territory to service territory and that the consumer benefits which justified acceleration of the phase-in the PECO Restructuring Order are also present in the instant case.[7]

In its Initial Brief, GPU, joined by PECO, that acceleration of the phase-in is "contrary to the plain language of Section 2806(b) of the Competition Act" and should not be

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6 See, OCA Main Brief at 5; DII Main Brief at 7.

7 Enron Main Brief at 8-9.

applied to the case at hand.[8] Duquesne appears to join in these arguments.[9] All of these parties are wrong.

While Section 2806(b) certainly restricts the Commission's implementation of direct access, the plain language of the subsection provides the Commission with discretion to both accelerate the phase-in or extend the phase-in under certain circumstances. As to acceleration of the phase-in, Section 2806(b), by its express terms, establishes the maximum "peak load of each customer class" which can be provided the opportunity for direct access "**as of**"[10] or, in other words, not later than January 1, 2001. Despite GPU's claim, the plain meaning of the statutory language does not state that 33% of the peak load of each customer class be provided the opportunity for direct access beginning on, or "no sooner than" January 1, 1999 or 66% beginning on January 1, 2000.[11] Instead, the plain language states that "as of" a date certain, the maximum penetration of direct access shall not exceed a certain level. It follows that by any reasonably reading, at any time after that date certain, the Commission has discretion to increase the penetration as long as it does not exceed the next cap.

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8 GPU's's Initial Brief, p. 7, PECO Main Brief at 2. GPU and PECO apparently accept Enron's assertion that the duration of the phase-in period should not vary between service territories since they do not assert that a longer phase-in is appropriate in service territories other than PECO's. (See, e.g., PECO Main Brief at 2.) Instead, they simply argue that this aspect of the PECO Restructuring Order is illegal and should be reversed through the Commission's decision in this proceeding.

9 Duquesne Main Brief at 8-9.

10 Emphasis added.

11 If the General Assembly had intended to preclude Commission discretion to accelerate the phase-in, it could have easily adopted language for Section 2807(c) that "Beginning on January 1, 1999, 33% of the peak load of each customer class shall be provided the opportunity for direct access," or "Beginning on January 1, 2000, 66% of the peak load of each customer class shall be provided the opportunity for direct access."

GPU's claim that the phrase "as of" should be interpreted as meaning "beginning on" is completely inconsistent with the plain language of the Act as the phrase "as of" is normally understood.[12] Furthermore, GPU's claim that Section 2807(c) establishes the implementation date for direct access as January 1, 1999 and precludes the Commission from advancing the January 1, 1999 date reads meaning into Section 2807(c) which is not supported by the statutory language. Section 2807(c) is the subsection which allows the Commission to extend the initiation date for customer choice and has no bearing on the clear language of Section 2807(a) which provides the Commission with clear discretion to accelerate the January 1, 1999 date.[13] Section 2807(c)(1) merely requires that the first phase of direct access be implemented by January 1, 1999 unless the Commission extends that date for a "six month transition period" for the reasons set forth in the subsection.[14]

Additionally, GPU's statement that, "[t]here is no dispute over this point. No one in this proceeding or elsewhere has advocated that the phase-in to direct access may begin before

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[12] *Webster's II New College Dictionary* defines the term "as of" as "on" not as "beginning on." Accordingly, the plain language of Section 2807(a) establishes the maximum penetration for direct access "**on**" January 1, 1999 and does not affect the Commission's discretion to advance the initiation of direct access or to accelerate the phase-in.

[13] Interpretation of the phrase "as of January 1, 1999" contained in Section 2807(a)(1) as meaning "beginning on January 1, 1999" is critical to its argument since its argument its based on the premise that the term "as of" should be interpreted consistently. While Enron agrees the term should be interpreted consistently, it is clear that GPU consistently and completely misinterprets the term.

[14] Postponement of the implementation of direct access until after January 1, 1999 can only occur if the Commission makes such a determination by no later than November 16, 1998. Technically, the Commission could still postpone the date for implementation of the phase-in if circumstances so dictate.

January 1, 1999"[15] is blatantly false. On October 6, 1997, Enron Energy Services Power, Inc. ("EESPI") filed a petition with the Commission requesting approval of its Choice Plan for the restructuring of PECO.[16] As part of the Choice Plan, Enron proposed not only to accelerate the phase-in but also to advance the initiation of direct access to September 1, 1998.[17] GPU and PECO participated actively in the PECO proceedings and each filed a comprehensive brief which identified areas where each believed the Choice Plan was in violation of the Act. Neither PECO nor GPU raised a legal objection to Enron's proposal to advance the initiation of direct access in their respective briefs. Furthermore, while the Commission did not adopt the Choice Plan, the Commission declined to accept the Choice Plan on other grounds.[18] Overall, despite the contentions of GPU, the legality of advancement of the January 1, 1999 direct access date is disputed, was raised by Enron in the PECO proceeding and was litigated by Enron and the other parties to that proceeding, including GPU and PECO. The fact that the Commission did not

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15 GPU Main Brief at 5-6.

16 Petition of Enron Energy Services Power, Inc. for Approval of an Electric Competition and Choice Plan and for Authority Pursuant to Section 2887(E)(3) of the Public Utility Code to Serve as the Provider of Last Resort in the Service Territory of PECO Energy Company, P-00971265. Shortly after filing, EESPI's petition was consolidated by the Commission with the PECO restructuring proceedings for litigation and decision making purposes.

17 As paragraph 23(f) of EESPI's Choice Plan Petition stated:

> (f) The phase-in of direct access to competitive generation services will be accelerated as follows:
>
> 9/1/1998 - 33% of load per class is eligible.
> 1/2/1999 - 66% of load per class is eligible.
> 1/2/2000 - 100% of load is eligible.

18 PECO Restructuring Order at 36-38.

comment on the legality of advancement has no bearing on whether such advancement is permitted by the Act. In fact, given the common language between the subsections of Section 2807(a), and the plain meaning of the term "as is" used in each subsection, one can just as easily presume that the Commission accepted the legality of advancement but determined that it was not necessary or appropriate given the applicable time constraints in the PECO and other restructuring proceedings.

The legality of the Commission's accelerated phase-in contained in its PECO Restructuring Order is further supported by the fact that the exact accelerated phase-in was included in PECO's Partial Settlement. Since it is beyond reasonable dispute that entering into a partial settlement does not excuse the settlement parties from complying with applicable law in all respects, every provision of the Act, including Section 2807(a), had to be complied with and could not be evaded by its signatories.[19] As a result, PECO, through its participation in the Partial Settlement, has accepted the Commission's authority to order an accelerated phase-in. Furthermore, GPU filed a brief in the PECO proceeding which raised various concerns with the Partial Settlement but did not raise one word of protest regarding the accelerated phase-in.[20]

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19 The Commission agreed with the applicability of the Act to the Partial Settlement in its PECO Restructuring Order, pp. 26-29. The statement of GPU on pages 8-9 of its Main Brief that "an EDC may agree to an expedited phase-in pursuant to settlement with its customers" is simply unsupportable unless the Act permits acceleration of such a phase-in. Nothing in the Act can be interpreted to provide the EDC authority to accelerate the phase-in which is not provided to the Commission.

20 Amazingly, on page 8, fn. 5, of GPU's Main Brief, they claim that the accelerated phase-in statutory construction issue was not briefed in the PECO proceeding. Given the fact that an accelerated phase-in was a component of both the Choice Plan and the Partial Settlement, the only reason the issue was not briefed in that case was because PECO and GPU chose not to brief the issue.

Finally, no party has suggested that the Commission's acceleration of the phase-in is not in the public interest. It is undisputed that the sooner customers have the opportunity to shop, the sooner they will receive the far-reaching benefits provided by the competitive market. Overall, the Act authorizes the Commission to accelerate the phase-in as provided for in the PECO Restructuring Order and the Commission should expand its phase-in policy to all EDC service territories since such a policy is undeniably in the best interests of Pennsylvania's consumers and businesses.

III. TRANSMISSION AND DISTRIBUTION RATES; UNBUNDLING ISSUES

B. 1996 Test Year Cost of Service

1. Duquesne

Duquesne's main response to the testimony of Enron witness Reising that several costs were incorrectly allocated 100% to the transmission and distribution portion of the rates was to state that this allocation methodology was necessary because Duquesne allegedly will continue to engage in these functions after restructuring.[21] Duquesne's argument entirely misses the point. The question is not whether Duquesne will have to continue to engage in such functions as sales and customer assistance, but whether some portions of these costs should be reallocated so that they are attributed to the "generation" portion of Duquesne's rates. As Duquesne has totally failed to provide any rebuttal to Enron's arguments, Enron's testimony

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21 Duquesne Main Brief at 10. Duquesne also pointed out that the PECO Restructuring Order does not adopt these adjustments. However, that decision was based upon the record developed in that proceeding and evidence that has not been presented here. See PECO Restructuring Order at 53-63.

should be accepted as an admission by Duquesne and the adjustments proposed by Enron should be adopted.

C. Required v. Realized Rates of Return

1. Duquesne

Duquesne's arguments as to why it should be permitted to utilize a "required" rate of return, as opposed to the return it actually earned on the transmission and distribution portion of its rates actually proves why Duquesne's position violates the Act and is unsupported by the record.

Duquesne frankly admits that its calculation method, unique among utilities submitting restructuring plans,[22] restates the T&D portion of its rates at levels higher than those that were in place as of January 1, 1997, because as of that date, Duquesne was obviously earning its realized as opposed to the return claimed to be "required" here. In effect, Duquesne has awarded itself a rate increase for the Transmission and Distribution portion of its business. Unfortunately, Duquesne failed to file for a rate increase, and has therefore failed to comply with any of the requirements in Chapter 13 of the Public Utility Code associated with such a hike. Moreover, Duquesne's methodology must be rejected as violative of the requirements of the rate cap provisions of the Act which require that T&D rates be held to their January 1, 1997 levels.[23]

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22 Duquesne claims that its "required" rate of return methodology is appropriate notwithstanding the fact that no other electric utility adopted it, because of the time that has passed since Duquesne's last base rate proceeding in 1987. But PECO's last base rate proceeding had been in 1990 (PECO Restructuring Order at 60), and, notwithstanding, utilized their actual rate of return in calculating T&D rates.

23 See Enron Main Brief at 17-19.

Ironically, Duquesne actually asserts that it is the rate cap that justifies its approach. It claims, essentially, that it has restated all of the various portions of its rates to reflect its claimed "required" rate of return. The T&D rates that it proposes, however, are the only rates that it proposes to establish using this required rate of return because, as it admits, if it restated all of its rates, including the generation portions of its rates, at the higher "rate increase" levels, its rates would exceed its rate cap.[24] Duquesne's methodology in effect allocates its claimed higher cost of capital (i.e., its required verses realized rate of return) to each of the three functional parts of its rates, but in recognition of the restraints of the Act's rate cap, allocates the decrease necessary to comply with the cap only to the generation portion of its total rate. This is obviously inappropriate and, as the Duquesne Industrial Intervenors point out, shifts costs between customer classes and functions from the way in which they are recovered prior to restructuring, thus violating the Act's prohibition against inter class costs shifts.[25] Duquesne's T&D rate increase attempt should be rejected.

F. Voltage-Differentiated Rates

1. Duquesne

Duquesne argues against Enron's proposal to establish voltage-differentiated rates as part of a comprehensive delivery service tariff by stating that Enron's proposal "shifts costs between classes" and that Enron "does not dispute" this contention.[26] This is a gross distortion of the testimony submitted by Enron. In fact, Enron witness Reising refuted Duquesne's arguments

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24 Duquesne Main Brief at 12-13.

25 66 P. C.S.§2808(a); DII Main Brief at 11.

26 Duquesne Main Brief at 17.

on this point by indicating that the examples presented by Duquesne witness Lahtinen purporting to show that the voltage-differentiated rate proposal would cause cost shifting presumed that Duquesne's present rates by customer class already allocated costs to certain classes for which they were not responsible and for which they should not bear responsibility.[27] Mr. Reising's testimony pointed out that if customers *who only* took service at the transmission level were today being allocated costs for secondary and primary voltage, such an allocation was a cross-subsidy already built into rates. Mr. Reising suggested that either that kind of cross-subsidy was unlikely to exist in Duquesne's rates (since unreasonable cross-subsidies have always been violative of the Public Utility Code)[28] or, if they existed, would not cause a cost shifting but eliminate one.[29] Enron's proposal would not create illegal cost shifting but, if anything, relieve it.

IV. TRANSITION OR STRANDED COSTS

A. Overview of Stranded Cost Valuation and Recovery Approaches

1. Duquesne

Enron strongly endorses Duquesne's proposal that its level of stranded costs be determined by auctioning all of its generating assets and that such an auction take place "today."[30] Duquesne's "immediate auction" alternative is consistent with the Electric Competition Act because it allows the market to provide the evidence of the value of Duquesne's

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27 Enron St. 2.1 at 5.

28 See 66 Pa. C.S. §1304.

29 Enron St. 2.1 at 5.

30 Duquesne Main Brief at 18.

generating assets in a competitive retail marketplace. While no one, including Enron or Duquesne, can be certain of the result, if an auction is conducted appropriately, it should produce accurate indications of the value of Duquesne's generating assets and, in turn, an accurate determination of the portion of its net investment, which should be considered "stranded" in accordance with the definition in the Electric Competition Act.[31]

Enron's main concern, however, is that the proposal for an immediate auction not be superseded by other proposals that might be put forward in an extraneous proceeding involving the APS/Duquesne merger. It is Enron's position that Duquesne's offer to be subjected to an immediate auction should be accepted unconditionally and that this offer should be final and not subject to any modification as a result of the merger proceeding. Indeed, based on a careful reading of the Electric Competition Act, such an unconditional acceptance is mandated by the required procedures set forth in the Act,[32] which appears to require a "once and done" determination.

Assuming that the immediate auction proposal is accepted as final regardless of the outcome in the merger, Enron welcomes the opportunity to work with Duquesne and the Commission to establish the appropriate procedures and other criteria to carry out an immediate auction process. Enron suggests that the Commission convene a task force to make recommendations to the Commission which would then be the basis for the auction.

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31 66 Pa.C.S. §2803(14).

32 See 66 Pa. C.S. §2806(f) ("The commission shall . . . issue an order accepting, modifying or rejecting [a restructuring] plan.").

In the meantime, as the restructuring process goes forward, Enron agrees that some interim CTC mechanism needs to be established. Enron submits that, in accordance with the PECO ruling, it would make most sense to establish the CTC based on the "model based" approach recommended by the OCA. Of course, the PECO decision mandates that the CTC established by use of the OCA formula be subtracted from current rates and, along with the subtraction for appropriately calculated T&D rates, the remaining portion of Duquesne's rates be established as a generation credit. Future adjustments once the auction takes place could be made to that CTC to appropriately phase in recovery of any stranded costs determined as a result of the auction.

V. COMPETITIVE TRANSITION CHARGE

A. Conceptual Disputes Regarding Calculation of CTC/CGC

1. Differences and overall approach (e.g., CTC or CGC as residual; OCA proposal)

Duquesne's brief spends a good bit of time attempting to make arguments in support of its "market price" based proposal for calculating a CGC. Quoting testimony by its witness Mr. Marshall, it claims that a "calculation" is necessary because of the "rate cap," and that it has a right to a "calculated" CGC approach using its market evidence because it has invoked the provisions of the Electric Competition Act which, it claims, permits it to utilize any revenues that otherwise would be reflected as rate decreases to mitigate stranded costs.[33] It even claims that, because it has asserted a claim under this particular provision of the Electric Competition Act its position is somehow different than that presented to the Commission in

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[33] Duquesne Main Brief at 60-65; 66 Pa.C.S. § 2804(4)(v).

PECO and that a different result (from that in PECO) should obtain.[34] Duquesne's insistence on a "calculated" generation credit is to further its claim that the CTC should be established as the residual of its entire generation related rate. Not only does Duquesne's proposal turn the PECO Order on its head, such an approach would simultaneously allow Duquesne to recover stranded costs at a maximum level and, at the same time, assure that competitors have no hope of winning customers in its service territory.

Duquesne's position is, of course, incorrect. As was set forth carefully in Enron's Main Brief, the PECO paradigm does not "calculate" a "CGC" using any projections, guesses or assumptions about market prices. As the Commission determined in PECO, the CGC is a residual number which is not calculated but produced after determinations of the portions of Duquesne's rates which were associated with transmission and distribution and CTC. When those elements are determined and removed from Duquesne's current rates, the remainder — whatever that may be — is the customer generation credit. The Commission stated as follows:

> The shopping credit is not a selected number. It is the number that results from the difference between a particular customer's total rate as of January 1, 997 and the sum of T&D and CTC rates established pursuant to this order." PECO Restructuring Order at 42. The residual establishment of a shopping credit does not purport to track a market price for generation but is the Commission's determination of what is necessary to create incentives for customers to want to shop and for sellers to be able to offer savings, therefore building the foundation for a competitive market. Nothing in the Act explicitly or implicitly links the unbundling of rates and the design of the shopping credit to market price.[35]

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34 Id.

35 PECO Restructuring Order at 42; Enron Main Brief at 29.

While, as MAPSA and Enron have pointed out, it may be necessary in some cases to review that resulting level to make sure that a competitive market can continue to develop, that step is an incidental one after the initial calculations are made. In this respect, Duquesne cannot complain about the level of CGC because it is entirely its responsibility; it alone is responsible for the level of generation rates that it has required and charged to customers over the years. It alone could have filed for a voluntary rate decrease if it found these levels too high (and still can). The PECO paradigm merely recognizes that fact and also recognizes the obvious principle that whatever is not declared to be uneconomic as a result of the advent of competitive market — that is that portion that is not a stranded cost — is the generation revenue requirement associated with Duquesne's generation business that will continue after restructuring.

Moreover, the PECO paradigm is completely consistent with the section of the Act that gives an EDC the ability to maintain rates at existing levels after its restructuring. Indeed, the PECO paradigm works from the basic proposition that the development of competition should respond to the rates being charged for the product, e.g., the utility's present rates.

In addition to Duquesne, the OCA and Duquesne Industrial Intervenors have advocated that the CGC be "calculated" based upon market prices. Both of these customer representatives also argue that the "generation credit," should be a calculated number based upon some determined "market price."[36] Duquesne and OCA/DII quickly diverge with Duquesne, of course, after this point, arguing that the annual CTC should be determined using their respective "margin" models and that, after subtracting: (1) the resulting CTC; (2) the market based CGC;

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[36] See, OCA Main Brief at 57-58, 62-63, 64-65; DII Main Brief at 75-76.

and (3) the determined Transmission and Distribution rates, the "residual" should be transformed into rate decreases for customers.[37] Both claim that achieving rate decreases for customers was a principal goal of the Electric Competition Act and is necessary once the PUC determines the CTC and the "market based" CGC.[38]

But the "rate reductions as residual" argument suffers from a number of infirmities. Most importantly, both the OCA and DII (and, as noted, Duquesne for that matter) assume incorrectly that the "shopping credit" should be or is "calculated and that it should equate to some version of the delivered market price for power. As the Commission established in PECO (and as referenced above) this is incorrect. The Electric Competition Act does not support the position that the CGC should be a "calculation" or that it should equate to some "estimation of the market generation price."

First, there is nothing in the Act that supports a calculated CGC. Indeed, the Act's principal goal to establish a competitive retail electric market would be completely frustrated by a market calculated CGC. Moreover, the record does not support the OCA/DII position. The OCA/Duquesne II approach would, in effect, require a one-time rate decrease to all customers based upon a predetermined market price based upon a government imposed determination of the record. But market prices are really determined by the market — many suppliers selling electricity to many customers. To achieve a competitive market, regulation must not be used to control price. It is for this reason that all suppliers[39] and some customer

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37 Id.

38 Id.

39 E.g., MAPSA Main Brief at 28-29.

representatives[40] have advocated that rate reductions should come from a vigorous market and that the PECO paradigm should be applied to Duquesne.

Further, to effectuate regulated rate decreases, the PUC would need to make a finding that the portion of Duquesne's rate which is associated with generation but not identified as stranded is unjust and unreasonable. While such evidence might well have been submitted (and presumable still could be in some future proceeding)[41] it has not been put forward.

In addition, the OCA/DII approach suffers from the fact that they require accurate calculations not just of the generation market price but a host of "adders" to reflect such items as retail costs, line losses, load factor, etc. The Commission implicitly rejected this exercise in PECO.

OCA contends that the Commission should reverse course from its PECO approach because mandated rate decreases will benefit all customers, not just those who shop.[42] But the PECO Order determined that establishing the generation credit as the residual would produce the necessary "headroom" to assure that savings would be forthcoming from the competitive market itself. This is far preferable than government imposed, once and done, rate reductions because the former course not only delivers rate reductions to customers in the near term it simultaneously allows the development of a robust competitive market. This, in turn provides the potential for even greater savings and benefits to customers, in the form of new

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40 Environmentalists Main Brief at 29-30.

41 The Act establishes January 1, 1997 rates as caps not floors; Duquesne's rates will continue to be subject to Chapter 13 of the Public Utility Code and could be reduced if a case was made that they were unjust and unreasonable. PECO Reconsideration Order at 21.

42 OCA Main Brief at 62.

products and offers, better service and greater efficiencies overall. The potential for benefits from this competition enhancing strategy is thus unbounded.

In contrast, establishing the shopping credit at the market means no or virtually no competition developing. As noted, a competitor has little chance to attract customers away from the incumbent if the utility is permitted to provide a credit that reflects the same (or lower) price that suppliers are required to offer in order to recover their costs. How can there be competition, one must ask, if the incumbent's price and the new entrant's price are mandated to be the same? Indeed, since even Duquesne acknowledges that suppliers have to be able to offer 10-20% savings if they have any hope of attracting customers,[43] establishing the CGC at the retail "market price" means competitive markets simply will not develop and customers will likely never see the additional benefits that vigorously competitive markets bring.

Moreover, OCA's fundamental premise — that savings produced from the competitive market will not benefit all customers — is not based upon any empirical evidence. Indeed, it is only common sense that if Duquesne's present customers are offered 10-15% savings, all those who wish to benefit from such discounts will exercise their right to choose. Those who wish to achieve savings but who want to stay with their traditional supplier can do so — simply by arranging for service with a Duquesne competitive affiliate or division. The notion that, once direct access is available to them, any customer who wants savings will be denied them under the PECO approach simply is not supportable.[44]

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43 Tr. 1056-61..

44 The OCA's other argument for diverging from the PECO approach is that after the phase-in period (January 1, 2001), "customers who do not choose are to be served by the utility (continued...)

Enron submits that both Commission precedent, the requirements of the Act and the need to take steps to create a competitive market all mandate that the Commission follow the PECO paradigm and unbundle Duquesne's rates by (1) establishing T&D rates for each class; (2) establishing a CTC and recovery period for each class; and (3) removing items 1 and 2 above from the total rates and establishing the remainder as the generation credit (unless changed pursuant to Public Utility Code Chapter B).

Pursuant to PECO, this generation credit will apply to all customers and be the generation charge for all customers who: cannot choose, do not choose or who choose and then return to Duquesne unless and until (a) Duquesne voluntarily changes those rates pursuant to Chapter 13 of the Code; or (b) the rate for such "Provider of Last Resort" customers is changed pursuant to a formula established by the PUC pursuant to regulations. See, discussion of Provider of Last Resort, Section IX, B, infra.

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[44](...continued)

or a commission-approved alternative supplier at 'prevailing market prices', subject to the rate cap . . . ." Certainly the Commission should not provide an incentive to competition which will suddenly disappear two years after the beginning of competition." OCA Main Brief at 62-63. But OCA's argument suffers from a misunderstanding of the provision establishing rates for "default" customers. As Enron explained in its Main Brief, that section on its face simply does not mandate that the rate for such service will be "prevailing market prices," but that power will be acquired at "prevailing market prices" and sold at a rate that recovers that price "together with all reasonable costs." 66 Pa. C.S. § 2807(e)(3). That total rate presently equates to Duquesne's residual generation credit since that is the only rate that recovers all of Duquesne's non-stranded generation costs. See Enron Main Brief at 48.

IX. DUTY TO SERVE

B. Provider of Last Resort

The OCA's Main Brief presents somewhat conflicting views of the approach that should be used to establish the rates applicable to "Provider of Last Resort" customers. As OCA notes, these include customers who: (1) choose not to shop; (2) cannot find a supplier (presumably including those who legally are not yet permitted to shop); and (3) those who may return to Duquesne for service for various reasons.[45] As OCA states in its "Provider of Last Resort" discussion, the rates for such customers — which includes all but pilot customers prior to January 1, 1999 — should be established in accordance with procedures that the Commission establish in a "POLR" rulemaking.[46] Enron agrees with this approach but would note that the rulemaking-derived generation rates that would have to be established pursuant to the Act, would not reflect simply some derived market price for generation as OCA implies in a different section of its brief.[47] The Act requires that POLR customers (which as noted above would include customers who legally cannot choose) would be charged either Duquesne's generation charge or a rate that reflects prevailing rates for power but which recovers all associated costs.[48] That rate may well be Duquesne's present generation credit since presumably that rate was established to recovery Duquesne's price for power (its prevailing market prices) plus all reasonable associated

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45 OCA Main Brief at 72.

46 Id.

47 OCA Main Brief at 57-58, 62.

48 Enron Main Brief at 48.

costs.[49] At any rate, as the OCA has agreed here the determination of precisely what rate is applicable to such customers should be made in the context of the contemplated rulemaking.

C. Electric Transmission and Distribution Service

1. Unbundling other customer services

(a) Introduction

Both Duquesne and System Council U-IO, International Brotherhood of Electrical Workers ("IBEW") oppose the proposal of Enron and other parties, including OTS[50] and OCA,[51] to unbundle non-wire or revenue cycle services, especially billing and metering. Duquesne's and IBEW's arguments misinterpret the Act, are not supported by the record in this proceeding and are inconsistent with the best interests of consumers as both the OCA and OTS have pointed out.[52]

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49 Id.

50 OTS Main Brief at 81-85; OTS concludes: "Billing and metering costs should also be specified on the customers' bills so that they can make informed decisions as to their choices for the provision of these services. If a less expensive supplier can provide those services at a lower cost, the customer should have the right to know this and act accordingly." Id. at 85 (emphasis added).

51 OCA Main Brief at 72-76. OCA points out that Duquesne's CARS automatic metering system should make it easier to interface with EGSs to allow the supplier total bill option; that Duquesne should unbundle the current costs of some features associated with metering and provide a credit to any customer who obtains an alternative meter or whose meter is electronically read by an EGS; and that Duquesne should be prepared for installation of and billing for alternative meters by suppliers. OCA expressed some concerns with Enron's agency proposal in connection with the supplier complete bill option, especially with regard to consumer protection issues. OCA Main Brief at 76; OCA St. 5R at 7-9. Enron believes that it has addressed these issues. See Enron Main Brief at 64, 68-71; 72-73.

52 See Enron Main Brief at 49-68. Enron comprehensively presented its legal, factual and policy arguments in support of the unbundling of and competitive entry into revenue

(continued...)

(i) Duquesne's Position

In its Main Brief, Duquesne suggests that resolution of these issues should be handled generically,[53] relying principally on the Commission's rulemaking orders, such as the Customer Services Order[54] and Advanced Meter Order.[55] Duquesne also relies on the PECO Restructuring Order,[56] where the Commission determined not to require PECO to unbundle those services at this time based on the record before it.[57] In its Main Brief, Enron addressed in detail the Commission's treatment of revenue cycle services in the PECO Restructuring Order and demonstrated why revenue cycle services should now be unbundled in Duquesne's service territory based on the record of this proceeding.[58]

The fact of the matter is that the Commission has expressly determined that the appropriateness of unbundling and competitive entry into revenue cycle services should be

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[52](...continued)
cycle services in its Main Brief and will not repeat those arguments here except as necessary to respond to specific arguments raised by either Duquesne or IBEW.

[53] Duquesne Main Brief at 81-82.

[54] Final Order re: Guidelines for Maintaining Customer Services at the Same Level of Quality Pursuant to 66 Pa. C.S. §2807(D) and Assuring Conformance with 52 Pa. Code Chapter 56 Pursuant to 66 Pa. C.S. §2809(E) and (F), M-00960890F.0011 (July 11, 1997) ("Customer Services Order").

[55] Rulemaking re: Advanced Meter Deployment for Electricity Providers; 52 Pa.C.S. §57.250-57.257, L-00970128 (Nov. 24, 1997) ("Advanced Meter Order").

[56] Duquesne Main Brief at 81-83.

[57] PECO Restructuring Order at 138-40.

[58] See Enron Main Brief at 53-58, 61-62, 67.

decided on the record of each restructuring proceeding. In the Commission's Customer Services Order, the Commission stated just that:[59]

> Utility restructuring plans should provide for the contingency of allowing suppliers to (1) render at the customer's request a consolidated bill that includes both EDC and supplier charges, and (2) engage in complaint handling.

And again, as the Commission specifically concluded pertaining to supplier billing:[60]

> We will not repeat our prior comments in their entirety, but we will reiterate some of the key points which we believe make it appropriate, both legally and as a matter of policy, to sustain this guideline so that parties may continue to explore in the Restructuring Filing of each utility the contingency of allowing a supplier single bill.[61]

Notwithstanding Duquesne's assertions to the contrary, the Commission's firm determinations not only support, but require, that revenue cycle service issues be addressed in each EDC restructuring filing and in each litigated restructuring proceeding. Duquesne cannot be permitted to avoid these issues in this case and the Commission's determinations must be based on the specific record of this proceeding.

Duquesne's position regarding metering is particularly hard to accept given the fact that it is phasing itself out of the provision of metering services and has contracted out a substantial portion to Itron, a third party provider, which will own and operate meters in

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59 Customer Services Order, Appendix B, Section II.B.

60 Customer Services Order at 30.

61 See also Customer Services Order at 10, 11, 30, Appendix B, Section II.B. and II.H.I. and OCA Main Brief at 73-74. In its Customer Services Order, the Commission further stated that provision of these services by EGSs would be dependent on their conformance with Commission regulations and guidelines applicable to these customer service functions and expressed its intent that the EGS's performance of these services must maintain the same level of quality. Id. at 7-8.

Duquesne's service territory.[62] Duquesne has admitted that such third party participation is not compliant with the Advanced Meter Order, which required the EDC to own and operate all meters.[63] Duquesne believes this inadequacy can be cured by obtaining an exemption if the Advanced Meter Order becomes the final rule.[64] However, Duquesne does not believe the Commission need be concerned with system reliability, because although Itron is not subject to the Commission's jurisdiction, it is bound to comply with metering standards "by contract."[65]

Enron agrees with many of Duquesne's assertions regarding metering. For example, Enron agrees that third parties other than the EDCs can provide safe and reliable metering services compliant with the Commission's metering standards.[66] Enron also agrees that these metering services have the potential to be more advanced and efficient than the EDC's traditional "one size fits all" approach. However, Enron does not agree that only an EDC-selected vendor is qualified to provide metering services, or that such restricted third-party metering is either fair or nondiscriminatory. While Duquesne has no choice but to agree that the Act permits the provision of metering services by entities other than the EDC,[67] its view that

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62 Tr. 856-57.

63 Tr. 858-59.

64 Tr. 859.

65 Tr. 859-60.

66 In fact, the Commission is in a better position to regulate EGS metering services than Itron's metering services, since although EGSs are not "public utilities" they are at least subject to the Commission's jurisdiction.

67 If IBEW's legal interpretation of the Act — that unbundling of and non-EDC provision of metering services is illegal — is accepted, then the provision of metering services by Itron would be illegal since Duquesne can not be exempted from a statutory requirement.

only EDCs' selected third-party vendors should be exempted from a requirement that EDCs provide metering services, is absurd on its face. In light of the fact that Duquesne has been able to use outside contractors to take substantial advantage of advanced metering technology to achieve cost savings and increase revenues, fairness requires the unbundling of and competitive entry into metering services in Duquesne's service territory now, and the Commission should take the appropriate steps to do so in its decision in this proceeding.

(ii) IBEW'S Position

IBEW, on the other hand, presents a frontal attack on the Commission's legal authority to require the unbundling and competitive provisioning of non-wire services. Notwithstanding the fact that the Commission has already determined these legal issues adversely to IBEW's position in the Customer Services Order.[68] The Commission's determination regarding legality is consistent with the Act and should be affirmed here.

(iii) Impact of Electric Competition Act on Public Utility Code

In order to understand the legality of the Commission's authority to unbundle and competitive entry into non-wire services, it is necessary to consider the impact of the Electric Competition Act on pre-existing provisions of the Public Utility Code. So long as the furnishing of electricity was entirely a regulated utility service, no fine lines were necessary regarding the classification of those services. Admittedly, the Public Utility Code was drafted with the presumption that all electric service, and related services, would be provided by the franchised monopoly. Indeed, as IBEW asserts, the terms "services" and "facilities" were defined broadly

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[68] See Enron Main Brief at 59-67.

in the Public Utility Code to include the vast majority of activities conducted by public utilities, including EDCs.[69]

However, the "competition" overlay that was introduced by the Electric Competition Act — which requires a comprehensive restructuring of the electric industry — has completely revamped the statutory rules under which the restructured industry will operate. To make a competitive retail electric market a reality, as required by that Act, competition must be permitted in every aspect of the retail electric business that is not a natural monopoly in order to maximize value to consumers.[70] Only transmission and distribution service — the wires service — are required to be maintained as EDC monopoly services. Accordingly, all pre-existing provisions of the Public Utility Code, as applied to the electric industry, must be understood and interpreted in light of the newly enacted amendments to the Code embodied in the Electric Competition Act. From this perspective, billing and metering are clearly not part of the monopoly utility service because they have nothing to do with physical distribution of electricity.[71] Instead, they are service functions, which are essential components of both the

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69 66 Pa. C.S. § 102; see IBEW Main Brief at 9. The fact that the statutory term "services" is defined broadly in 66 Pa. C.S. §102 is irrelevant to interpretation of the statutory phrase "transmission and distribution of electricity" in 66 Pa. C.S. §§ 2802 and 2803 which the General Assembly has found should remain subject to regulation as a "natural monopoly." The record in this proceeding is undisputed that revenue cycle services are not "natural monopolies" and are provided by a wide variety of entities in other industries. Enron St. 2.0 at 27; Enron St. 3.0 at 10-11; Enron Exh. 3, JAB-1 and JAB-2. In fact, as IBEW acknowledges (IBEW Main Brief at 14-15), the Act expressly authorizes suppliers to provide billing services. Furthermore, Duquesne has already phased itself out of the provision of metering and has contracted out the provision of metering services to Itron — which is not a public utility.

70 Enron St. 1.0 at 5-6; Enron St. 4.0 at 5-6.

71 Enron St. 2.0 at 27.

delivery and sale of the commodity and fully associated with and support the distribution, transmission and generation supply service categories.

Consistent with the avowed purposes of the Electric Competition Act, to develop retail electric competition to the greatest extent possible,[72] only those services or facilities which remain natural monopolies and for which unbundling is not technically feasible or for which it is shown that competition will sacrifice system safety and reliability should be permitted to justify the continuance of the utility's monopoly status.[73] The only utility service that meets this standard is the actual "wire" distribution network of each utility. All other services and service functions should be unbundled to the extent technically feasible so that competitive alternatives can become available.

IBEW's arguments interpret the pro-competitive provisions of the Act as if they are restricted by the traditional view that utility services are subject to a monopoly, and attempt to apply pre-existing provisions of the Code in a manner which would defeat the Act's intent. Instead, these statutory provisions must not be read in isolation but must be interpreted consistent with the General Assembly's overriding objective to restructure the electric industry in a manner which brings the full benefits of retail competition to Pennsylvania's consumers and businesses.

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72 See 66 Pa. C.S. §§ 2802(5), (7), (8), (12), (14) and (15).

73 The Commission can obtain policy guidance by following the policies reflected in the federal law governing the development of telecommunications competition, which recognizes that marketplace development cannot occur unless the monopoly is required to unbundle its services to the greatest extent that is technically feasible. Section 251(c)(3) of the Telecommunications Act of 1996, 47 U.S.C. § 251(c)(3).

(iv) Authority to Unbundle "Other Services"

The second gross error in IBEW's rationale is its failure to consider § 2804(3) of the Act. Indeed, it is not surprising that reference to this important subsection is noticeably absent from IBEW's brief. Section 2804 of the Act delegates responsibility to the Commission to define standards and assure compliance with a utility's unbundling obligation in the context of its review of each utility's restructuring plan. This Section then provides as follows in relevant part:

> The following interdependent standards shall govern the Commission's assessment and approval of each public utility's restructuring plan, oversight of the transition process and regulation of the restructured electric utility industry:
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> * * *
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> (3) The Commission shall require the unbundling of electric utility services, tariffs and customer bills to separate the charges for generation transmission and distribution. The Commission may require the unbundling of other services. (Emphasis added.)

The General Assembly's delegation of discretionary authority to unbundle "other" services in addition to the three primary service categories clearly establishes that there must be services other than the three types mentioned that can be unbundled. Furthermore, this clause provides ample authority for the Commission to establish standards requiring and implementing the unbundling of non-wire services. In fact, the statutory reference to "the unbundling of other services" is almost certainly a direct reference to such services.[74] Furthermore, § 2804(3) makes

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[74] The declaration of policy found at 66 Pa.C.S. § 2802(14) creates two distinct mandatory obligations on the part of EDCs: "to unbundle their rates and services and to provide open access over their distribution and transmission systems." (Emphasis added.)

(continued...)

it clear that required unbundling should extend not only to services,[75] but also to "tariffs" and "bills." IBEW completely ignores this important provision and the authority it confers on the Commission. The truth of the matter is that the General Assembly has expressly provided the Commission with discretionary authority to unbundle revenue cycle services. None of IBEW's creative, but unreasonable, arguments can change this simple fact.

(v) IBEW Overstates the Effect of EDC's Requirement to Provide Customer Services

IBEW improperly relies upon and misreads § 2807(d) of the Act — which requires that each utility continue to provide customer services to its customers at the same level of quality as it does now — to assert that only an EDC may legally provide those services. But this provision does not prohibit the unbundling or the competitive provision of these services (any more than it precludes the competitive provision of electric generation, or other services "traditionally provided by EDCs") by those same suppliers. Nothing in the language of § 2807(d) can reasonably be interpreted to establish the EDC as the exclusive provider of non-

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[74](...continued)
Compliance with both obligations is absolutely necessary for compliance with the Act and the meaningful development of retail competition. Moreover, while costs of non-wire services and service functions are presently included in Duquesne's rates, those services and functions themselves are not part of Duquesne's energy delivery system. Enron St. 2.0 at 27. Accordingly they are subject to the unbundling requirement of "other services" imposed by the General Assembly.

[75] The only conceivable purpose of unbundling services is to allow the competitive provisioning of those services subject to unbundling. The only exception to this general rule is the unbundling of services like distribution and transmission which is necessary to define jurisdictional lines (i.e., distribution services are regulated by state and a transmission services are regulated by the FERC).

wire services or restrict the Commission's express authority under § 2804(3) to establish standards for the unbundling and competitive entry of such services.

This statutory language, as noted in the Customer Services Order, "is merely a reflection that the EDC must stand ready to provide these customer service functions"[76] if requested to do so. But, it obviously does not establish the EDC as the exclusive provider. In fact, in the billing area under Section 2807(c), as IBEW itself notes,[77] the Act continues to impose quality of service requirements on EDCs while at the same time expressly providing that EGSs can also provide billing services to customers. Furthermore, in Duquesne's case, it has turned over ownership and operation of many of its meters to Itron, subject only to a contract between the two companies. IBEW has unsuccessfully argued its interpretation of Section 2807(d) to the Commission in other dockets and its arguments are no more convincing here.

(vi) The Commission's Legal Rulings in the Customer Services Order

In the Customer Services Order, the Commission, upon careful consideration of the legal issues that had been raised, ruled that it does indeed have the legal authority to require the unbundling and competitive provisioning of non-wire services.[78] The Commission also

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76 Customer Service Order at 10.

77 IBEW Main Brief at 14-15.

78 See Customer Services Order at 10-11, 29 (quoted, in part, in Enron Main Brief at 59-60). The Commission cited as the statutory basis for this option, 66 Pa. C.S. § 2803 (which defines Electric Generation Supplier to include brokers, marketers, and aggregators and recognizes that suppliers may engage in "related services"), 66 Pa. C.S. § 2804(3) (which authorize the Commission to unbundle "other services"), and 66 Pa. C.S. § 2809(e) (relating to regulation of EGSs).

issued guidelines for maintaining "customer services" at the same level of quality under retail competition[79] and to assure conformance with Chapter 56 of the Commission's regulations.[80] It also required that these guidelines be addressed in each of the various restructuring proceedings.[81]

Significantly, in requiring that the unbundling and competitive provisioning of these non-wire services be considered in each restructuring, the Commission also required the assurance that any EGS providing those services maintain the same quality of service as provided by regulated utilities.[82] This is a short and complete answer to IBEW's completely speculative contention that competitive provisioning will lead to a decline in service quality.[83]

(vii) Refutation of IBEW's Arguments

IBEW parses the provisions of the Electric Competition Act and the other provisions of the Public Utility Code in such a way — reading them in isolation — to fabricate an argument that the unbundling and competitive provision of non-wire services is unlawful. As demonstrated above, IBEW's arguments have no merit and are no more than an attempt to revisit issues the Commission has already conclusively decided. Its newly developed arguments, as

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79 As required by 66 Pa. C.S. § 2807(d).

80 As required by 66 Pa. C.S. §§ 2809(e) and (f).

81 Customer Services Order at 11, 29, Appendix B, Sections II.B and II.H.

82 Customer Services Order at 7-8

83 IBEW's views regarding service reliability in a competitive environment are not only completely speculative but are inconsistent with the experience in other industries in which the service quality billing services has increased through the introduction of competition. Enron St. 3.0 at 10-11.

explained below, are no more convincing than previous arguments already raised before and correctly rejected by the Commission.

1. IBEW asserts that EGSs are not public utilities, but that only public utilities can provide non-wire services.[84] IBEW is *half right*. It is true that EGSs are not "public utilities" except for the limited purposes described in §§ 2809 and 2810.[85] However IBEW's contention that only a "public utility" can provide non-wire services, because those services were traditionally provided by public utilities prior to the enactment of the Electric Competition Act, is simply concocted from whole cloth. Such a view completely ignores the requirements of § 2802(14), which requires electric utilities to unbundle their rates and services and to provide open access, as well as § 2804(3), which explicitly delegates to the Commission the authority to require the unbundling of services other than generation, distribution and transmission service, which would include non-wire services.[86] If this argument were true, suppliers wouldn't be able to provide generation services or anything else "traditionally" provided by "public utilities."

2. IBEW also overlooks the fact that while the definition of an EDC is narrowly constructed in the Act as "providing facilities for the jurisdictional transmission and

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84 IBEW Brief at 9-11.

85 66 Pa. C.S. § 102 defines "public utility" in part as follows:

> "(2) The term [public utility] does not include:
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> (vi) Electric generation supplier companies except for the limited purposes as described in sections 2809 . . . and 2810 . . . ."

86 As indicated previously, acceptance of IBEW's view would render illegal the metering services presently provided by Duquesne via Itron.

distribution of electricity to retail customers," an EGS is defined with a broader scope as one that sells "electricity or related services" to end-use customers.[87] By definition, therefore, an EGS may additionally provide retail customers with "related" services, which clearly includes and was specifically intended to reference non-wire services. While IBEW may be correct that jurisdictional T&D services must be provided by an EDC,[88] that begs the question as to non-wire services, because they are not T&D services but are "other services" under § 2804(3).[89]

3. IBEW ignores the objectives and definitions contained in the Electric Competition Act, and relies instead on a misreading of 66 Pa. C.S. §102 which contains the broad definition of "service" and "facilities."[90] As noted above, the scope of these terms must be interpreted within the context of the overlay of the Electric Competition Act, and any restrictions on unbundling or competitive entry are expressly limited to services involving the transmission and distribution of electricity; they do not apply to all EDC services and facilities as IBEW argues.

4. IBEW likewise ignores the provisions of the Electric Competition Act to argue that an electric meter must be considered utility property because it is used or supplied by public utilities, or that a bill rendered for distributing electricity is an "act done" in providing

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87 66 Pa. C.S. § 2803 (emphasis added).

88 IBEW Main Brief at 10.

89 The fact that the term "facilities" is defined broadly in § 102 also has no bearing on interpretation of the definition of "electric distribution company" in § 2803 since under § 2803 only those facilities which pertain directly to the "transmission and distribution" or delivery function are within the scope of the definition.

90 IBEW Main Brief at 10.

regulated distribution services.[91] The fact of the matter is that non-wire services are not delivery services and do not involve the physical distribution and transmission of electricity, but are service functions which not only support distribution and transmission services, but are integral components of generation supply. There is simply no basis, as this Commission has already held,[92] to require these services to be provided only by an EDC.

5. IBEW contends that § 2807(c), which specifically recognizes the right of an EGS to render a separate bill to a customer, thereby precludes the EGS from rendering a single bill.[93] IBEW claims that since the provisions of that section otherwise apply specifically to EDCs, this somehow precludes EGSs from performing the same functions.[94] Of course, as the PUC has established, this provision only requires the non-exclusive continuation of such services by the EDC to customers who need or desire such services from the EDC, and the Commission has so ruled:[95]

> Although §2807(C) recognizes that the EDC "may be" responsible for the billing of all electric services, there is nothing in this passive provision or anywhere else in the Act that makes the EDCs the exclusive provider of this customer service function.

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91 IBEW Main Brief at 10-11. Each of these argument can just as easily be characterized as a generation function since a meter and a bill are necessary to provide generation service. The term "generation service" is not defined in the Act and could easily be construed to include these items, which the Act clearly does subject to competition.

92 Customer Services Order at 10-11.

93 IBEW Main Brief at 13-14.

94 IBEW Main Brief at 14.

95 Customer Services Order at 29 (emphasis added). Although, the Commission has interpreted the language of Section 2807(c) as providing discretionary authority to allow EGSs to provide a single supplier bill, in Enron's view, Section 2807(c) mandates that the EGS provide a single supplier bill if a single supplier bill is requested by a customer.

Moreover, to the extent that an EGS provides those functions, the Commission can and should require that the EGS be required to do so subject to all the applicable requirements of the Public Utility Code, not only § 2807(c).[96]

6. IBEW points to a number of sections of the Public Utility Code[97] that it claims require public utilities only to bill and meter utility services.[98] These provisions, however, merely contain certain billing, collection, termination and metering procedures that must be met by public utilities for service to customers (except for bills for installation charges). However, none of these sections specifically direct that only "public utilities" may provide any of these functions, nor do they preclude EGSs from doing so subject to similar regulations by the Commission.[99] Moreover, certain of the provisions, 66 Pa. C.S. § 1521-33, apply to the rights of tenants where a utility proposes to terminate electrical service to a landlord. This would have nothing at all to do with an EGS, which cannot terminate service.[100]

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96 The Commission has in fact done so in the guidelines in Customer Services Order at 7-8.

97 66 Pa. C.S. §§ 317(b), 1504, 1507, 1509, and 1521-33.

98 IBEW Main Brief at 11-13.

99 In fact, virtually all of the requirements in the provisions of the Code identified by IBEW are repeated in Chapter 56, which as IBEW points out already govern suppliers. For example, the statutory due date for payments provided for in 66 Pa.C.S. §1509 is codified by regulation at 52 Pa. Code §56.21; and the landlord-tenant provisions of 66 Pa.C.S. §§1521-1523 are codified almost verbatim at 52 Pa. Code §§56.121 et seq.

100 To the extent that an EGS cancels its own electricity supply service under any circumstances, the EDC or some other Commission designated supplier would still be required to provide such service as the provider of last resort. To the extent consumer protections in addition to those currently included in Chapter 56 are required to assure the continuous flow of electricity, those protections should be implemented as soon as possible. Neither the Customer Services Order nor Enron's position in this case in any

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7. IBEW also incorrectly states that allowing the unbundling of non-wire services would remove the protections provided by relevant Commission regulations,[101] especially Chapters 57 and 58, because they are not specifically required to be applicable to EGSs under the Electric Competition Act, as is Chapter 56.[102] This argument is ludicrous. There is nothing to preclude the Commission — which, after all, promulgated all those requirements — from imposing all necessary standards on EGSs as a condition of unbundling.[103] In fact, Enron consistently has advocated, and continues to agree, that the relevant portions of Chapters 57 and 58 of the Commission's regulations should be applied to generation suppliers that wish to provide metering services. This could be accomplished as part of the Commission's final order in this case as well as in its metering docket.

8. IBEW relies on various "purpose" provisions of § 2802 of the Act to argue that EGSs should not be permitted to provide billing and metering services.[104] However, IBEW misapprehends these provisions. As demonstrated above, their primary purpose of the Act is to create a competitive retail electricity market. While this is accomplished primarily by unbundling and introducing competition into the generation supply market, the General

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[100](...continued)
way remove termination and reconnection authority from the EDC; indeed, paragraph L of the Customer Services Order confirms such authority.

[101] IBEW Main Brief at 14-15.

[102] See 66 Pa. C.S. §§ 2809(e),(f).

[103] The record reflects that Itron, not Duquesne, is providing metering services to approximately 50% of Duquesne's customers and that while Commission quality of services regulations are not directly applicable to Itron, such standards are imposed on Itron through its contract with Duquesne. Tr. 859 (December 18, 1997).

[104] IBEW Main Brief at 15-16.

Assembly empowered the Commission with discretion to unbundle (and introduce competition) *in other services* consistent with the public interest. In addition to that explicit statutory language, the Commission has implicit authority to carry out its statutory duties.[105] Under its implicit authority, the Commission is authorized to act in furtherance of the statutory objectives identified in the Electric Competition Act.[106] For all the reasons set forth herein, and in the Customer Services Order, such unbundling is necessary and should be permitted.

(b) Resolution in Generic Proceedings

IBEW next claims that the Commission has resolved these issues in the PECO Restructuring Order and the Advanced Meter Rulemaking. But, neither of these decisions is dispositive here. In the PECO proceeding, the Commission relied *specifically on the record* in that case and has recently indicated a continuing interest in the supplier complete bill option.[107] As for metering, IBEW's citation is to a proposed rulemaking which can be accorded no legal

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105 As an agency of delegated powers, the Commission has both those powers explicit in its enabling statute and implicit as necessary to exercise of those express powers. Pennsylvania Public Utility Commission v. Philadelphia Electric Company, 460 A.2d 734 (Pa. 1984); Metropolitan Edison Co. v. Pennsylvania Public Utility Commission, 437 A.2d 76 (Pa. Cmwlth. 1981).

106 The fact that an administrative agency or other governmental unit is a creature of statute does not mean that *all details* of its scope of delegated authority must be expressly or separately enumerated in the enabling statute, but only that the basic policy choices must be made by the Legislature which guides and restrains the exercise of administrative functions. Gilligan v. Pennsylvania Horse Racing Commission, 422 A.2d 487 (Pa. 1980); Hospital Association v. MacLeod, 410 A.2d 731 (Pa. 1980); William Penn Parking Garage, Inc. v. City of Pittsburgh, 346 A.2d 69 (Pa. 1975); Charters Valley Joint School District v. County Board of School Directors, 211 A.2d 487 (Pa. 1965); Pennsylvania Builders Association v. Pennsylvania Public Utility Commission, 483 A.2d 1025 (Pa. Cmwlth. 1984); Western Pennsylvania Water Company v. Pennsylvania Public Utility Commission, 311 A.2d 370 (Pa. Cmwlth. 1973).

107 See, PECO Compliance Filing Order at 22.

weight until finalized. As indicated previously, the Commission has unequivocally declared the legality of the unbundling of and competitive entry into non-wire services and has indicated that the timing of such unbundling should be considered within the context of these restructuring proceedings. As the Commission stated in its Advanced Meter Order:[108]

> The Act does not require unbundling of metering at this time, but certainly anticipates that unbundling may occur in the future.

While the Act does not require immediate unbundling, the record of this proceeding does, and the Commission should act accordingly.

(d) Specific Services

IBEW's policy arguments against unbundling metering and billing should also be rejected. Its first assertion — that current EDC provision of non-wire services is accurate and prompt[109] — totally disregards the premise underlying the Act that competition will improve, not deteriorate service to customers. IBEW's argument could also be made —and was implicitly rejected by the Commission — with respect to retaining generation as a monopoly-EDC function. IBEW's contention demonstrates only that it does not share the General Assembly's confidence that competition, not regulation, is the best and most efficient method for bringing lower-priced, higher quality service to consumers.[110] Moreover, the Commission makes administrative notice of the thousands of complaint it receives each year from consumers alleging billing errors, slow (or fast) meters, meter reading errors, collection and termination transgressions and numerous other violations of Chapter 56. Clearly, the evidence submitted by

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108 Advanced Meter Order at 13.

109 IBEW Main Brief at 20.

110 66 Pa.C.S. § 2802(5).

Enron demonstrates, given the experience of other industries, that competition improves, not detracts from, the quality of billing and customer services.

IBEW next argues that Enron's proposal would eliminate customer choice in violation of § 2807(c), because the EGS would determine who does the billing and metering.[111] But, as Enron has demonstrated, ultimately it is the end-users who will determine their preferred service provider through their determination and selection of an EGS.[112] If the end-user does not choose to have the EGS do billing and metering, it can select an EGS — including even an EGS affiliated with the EDC (Duquesne) — who will utilize the EDC to provide such services. IBEW argues that it is possible that all EGS will provide only the same choice.[113] While improbable, if it did occur it would be because that is what customers want; and if it were a feature not desired by end-user customers, it is virtually certain either that many competitors would offer the choices customers desire. What IBEW fails to recognize is that in a competitive market, customer preferences will determine what choices are available. Such a premise is not only consistent with § 2807(c), but is the underlying premise of a competitive market.

IBEW also sets up a straw man, claiming that EGSs would be able to charge any price they want for non-wire services, while EDCs would be required to charge for these services under their tariffed rates.[114] Aside from the fact that this is practically an admission that utilities

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111 IBEW Main Brief at 20-23. Again, this is as silly as arguing that consumers will not have "customer choice" because they won't be able to dictate where a particular supplier procures its generation.

112 Enron St. 4.1 at 7-8; Enron St. 5.1 at 3.

113 IBEW Main Brief at 22.

114 IBEW Main Brief at 23-24.

are overcharging for these services, IBEW ignores the fact that, once unbundled, these services would become competitive, and could be provided competitively by Duquesne or suppliers or even Duquesne's affiliates. Customers would always be able to use utility provided meters, if they wished. IBEW's arguments merely demonstrate its protectionist view of the EDC's business, regardless of whether the approach it advocates is consistent with the Act or beneficial to consumers.

IBEW next throws out safety and reliability warnings if metering becomes competitive.[115] However, Duquesne has already that non-EDC metering does not adversely impact the safety and reliability by contracting out much of its metering services to Itron under which the only protections for maintaining safety and reliability result from a contract between Duquesne and Itron.[116] IBEW's alleged concerns with safety and reliability are no more than a red herring, as Enron's testimony demonstrates.[117] In any event, the General Assembly has spoken otherwise.

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115 IBEW Main Brief at 21-25.

116 Tr. 859-60 (December 18, 1997). Nowhere in its papers has IBEW identified any concerns with the provision of metering services by Itron — a third party provider which is not even subject to the Commission's jurisdiction as a generation supplier.

117 See Enron St. 2.1 at 6-7; Enron St. 3.1 at 10-13; Enron St. 4.1 at 3-4, 9; Enron St. 5.1 at 3-4. Enron has consistently urged the Commission to maintain existing industry-wide standards for meter and meter reading safety, accuracy, installation, and performance. The introduction of competition will require the Commission to develop additional standards with respect to meter reading including minimum data elements, timely data access, open architecture storage and communications, security, and enforcement procedures. Enron continues to endorse the working group format as the appropriate venue to develop these additional guidelines.

Finally, IBEW has the temerity to challenge unbundling by claiming that the only reason Enron and other suppliers are for it is because it hopes to make money.[118] However, IBEW ignores the fact that no competitive market for any service is possible without a profit motive. The unbundling of and competitive entry into non-wire services will not only provide EGSs with more opportunity to be profitable but will also provide EGSs with more opportunities to add value for consumers. If consumers do not find added value, they will simply go elsewhere for their service or will remain with the EDC. Once its veil is dropped, IBEW's arguments represent nothing more than an attempt to impede competitive development and to protect the EDC from customer choice.[119]

2. Agency

As discussed in Enron's Main Brief,[120] there is no legal impediment which would prevent the Commission from approving the agency relationship between supplier and customer proposed by Enron. If allowed to occur, agency holds the possibility of many benefits for both consumers and for the competitive market.

Duquesne contends first that the Act does not authorize agency and that the Customer Services Order would appear to prohibit it.[121] Duquesne provides no citation for either

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118 IBEW Main Brief at 26-27.

119 Moreover, Enron believes the competitive provisioning of non-wire services is likely to create many more jobs as utilities and others expand to attempt to provide such services.

120 Enron Main Brief at 68-71.

121 Duquesne Main Brief at 84.

of these propositions, because there are none. To the contrary, the Commission explicitly acknowledged the right of an EGS to act as agent for an end use customer in the PECO case.[122]

Duquesne further argues, incorrectly, that, as an agent, the EGS would have to provide metering and disconnection, which only an EDC may do. Again, the Commission specifically recognized the right of an EGS to act as the agent on behalf of its customer to have an advanced meter installed and meter reading services provided.[123] Finally, Duquesne contends that agency and the unbundling of billing, specifically the supplier single bill option, are inextricably linked, but that that option has not been approved. Duquesne is wrong again. Agency is a viable and necessary option whether or not the supplier itself performs any of these functions, so long as it is authorized by the customer to arrange for them. The Commission has not only permitted such an agency function under the Act, it has also recognized the likelihood that it will permit the supplier single bill option.[124]

Accordingly, whether or not the Commission chooses to unbundle non-wire services at this time, it should allow agency arrangements to begin immediately. This will enable suppliers and customers to benefit from having the service in place now, and will also more easily accommodate future billing and unbundling changes.

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122 PECO Compliance Filing Order at 12-13, where the Commission required PECO to add to its tariff a requirement that, unless elsewhere prohibited, "an EGS may act as agent for an end user customer upon written authorization to PECO which may be part of the notice of EGS selection."

123 PECO Compliance Filing Order at 18-21.

124 PECO Compliance Filing Order at 22.

XIII. CONCLUSION

For all of the foregoing reasons, Enron Power Marketing, Inc. respectfully requests the Honorable Commission to implement the recommendations as set forth in its Main and Reply Briefs.

Respectfully submitted,

Daniel Clearfield
Gerald Gornish
Robert Longwell
Wolf, Block, Schorr and Solis-Cohen LLP
212 Locust Street, Suite 300
Harrisburg, PA 17101

Dated: February 17, 1998

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the foregoing document via Hand Delivery, Federal Express, facsimile or first class mail, postage pre-paid upon the participants, listed below, in accordance with the requirements of 52 Pa. Code § 1.54.

Kandace Melillo, Esq.
Office of Trial Staff
PA Public Utility Commission
Pitnick Bldg., 3rd Fl.
901 North 7th St, Rear
Harrisburg, PA 17102

John S. Moot, Esq.
Kurt W. Bilas, Esq.
Skadden, Arps, Slate, Meagher & Flom, LLP
1440 New York Ave., NW
Washington, DC 20005

Larry R. Crayne, Esquire
Duquesne Light Company
411 Seventh Ave.
P.O. Box 1930
Pittsburgh, PA 15230-1930

Angela T. Jones, Esquire
Office of Small Business Adv.
Suite 1102, Commerce Bldg.
300 North Second Street
Harrisburg, PA 17120

Brian Kalcic
Excel Consulting
Suite 720-T
225 S. Meramec Ave.
St. Louis, MO 63105

Mary Ann Ralls, Esquire
Duane, Morris & Heckscher LLP
Suite 700
1667 K Street, NW
Washington, DC 20006-1608

Scott J. Rubin, Esquire
3 Lost Creek
Selinsgrove, PA 17870

Mary McFall Hooper, Esq.
PECO Energy Company
2301 Market Street S23-1
Philadelphia, PA 19103

Vickiren S. Aeshleman
QST Energy Inc.
Suite 300
300 Hamilton Blvd.
Peoria, IL 61602

David Hughes
4037 Ludwick Street
Pittsburgh, PA 15217

Brian A. Rider, President
Pennsylvania Retailers' Assoc.
224 Pine Street
Harrisburg, Pa 17101-1325

Patricia Armstrong, Esquire
Thomas, Thomas, Armstrong & Niesen
212 Locust Street
P.O. Box 9500
Harrisburg, PA 17108-9500

Steven Baicker-McKeen, Esq.
Wanda Schiller, Esq.
Babst, Calland, Clements & Zomnir, PC
8th Floor, Two Gateway Center
Pittsburgh, PA 16222

Kenneth L. Wiseman, Esq.
Mark F. Sundback, Esq.
Andrews & Kurth, LLP
1701 Pennsylvania Ave., NW
Washington, DC 20006

Michael L. Kurtz, Esq.
David F. Boehm, Esq.
Boehm, Kurtz & Lowry
2110 CBLD Center
36 East Seventh Street
Cincinnati, OH 45202

Thomas P. Gadsden, Esq.
Morgan, Lewis & Bockius
2000 One Logan Square
Philadelphia, PA 19103-6993

David M. DeSalle, Esq.
Terrance J. Fitzpatrick, Esq.
Ryan, Russell, Ogden & Seltzer, LLP
800 N. Third St., Suite 101
Harrisburg, PA 17102-2025

Robert B. Weisenmiller
MRW& Associates, Inc.
1999 Harrison St., Suite 1440
Oakland, CA 94612-3517

Michael Reid, Director
Materials Management Services
Administrative Resources, Inc.
500 Commonwealth Drive
Warrendale, PA 15086-7513

Thomas J. Augspurger, Esq.
Midcon Corporation
Office of General Counsel
701 East 22nd St.
Lombard, IL 60148

William T. Hawke, Esq.
Kevin J. McKeon, Esq.
Malatesta, Hawke & McKeon
100 North 10th St.
P.O. Box 1778
Harrisburg, PA 17108

Joseph A. Dworetzky, Esq.
John P. Lavell, Jr., Esq.
Hangley, Aronchick, Segal & Pudlin
12th Fl., One Logan Square
Philadelphia, PA 19103

Alan J. Barak, Esq.
Environmentalists
1417 Blue Mountain Parkway
Harrisburg, PA 17112

Donald R. Ayersman, Jr., Esq.
1125 Denver Avenue
Morgantown, PA 26505

Mark J. McGuire, Esq.
Ronald N. Carroll, Esq.
Jenner & Block, Suite 1200
601 13th St., NW
Washington, DC 20005

Tim Merrill, Esq.
4 Penn Center West, Suite 200
Pittsburgh, PA 15276

Cindy Datig, Esq.
$1 Energy Fund
P.O. Box 42329
Pittsburgh, PA 15203

Paul E. Russell, Esq.

Pennsylvania Power and Light Company
2 North 9th Street
Allentown, PA 18101

David M. Boonin
New Energy Ventures East, LLC
1845 Walnut Street, Suite 2525
Philadelphia, PA 19103

Roger Clark, Esq.
The Environmentalists
905 Denston Drive
Andler, PA 19002-3901

Albert M. Benincasa, Esq.
Director, Regulatory Affairs
Skipping Stone
46 9th Ave.
Sea Cliff, NY 11579

Douglas F. John, Esq.
John & Hengerer
1200 17th St., NW, Suite 600
Washington, DC 20036

John O'Brien, Esq.
Wheeled Electric Power Company
50 Charles Lindburgh, Blvd., Suite 207
Uniondale, NY 11553

Rodney R. Akers, Esq.
Assistant City Solicitor
313 City-County Building
414 Grant Street
Pittsburgh, PA 15219

James P. Dougherty, Esq.
Robert A. Weishaar, Esq.
McNees, Wallace & Nurick
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108

Stephen J. Baron
J. Kennedy & Assoc. Inc.
Suite 475
35 Glenlake Parkway
Atlanta, GA 30328

Howard M. Louik, Esq.
Allegheny County Law Dept.
300 Fort Pitt Commons
445 Fort Pitt Blvd.
Pittsburgh, PA 15219

Robert J. Stefanko, Esq.
341 South Bellefield Ave.
Pittsburgh, PA 15213

Margaret Peters, Esq.
The Peoples Natural Gas Co.
625 Liberty Ave.
Pittsburgh, PA 15222-3197

John Stember, Esq.
Low Income Advocate Parties
1705 Allegheny Bldg.
429 Forbes Ave.
Pittsburgh, PA 15219

Kenneth Zielonis, Esq.
Stevens & Lee
Suite 310
208 North Third Street
Harrisburg, PA 17108-2090

Stephen L. Feld, Esq.
Pennsylvania Power Co.
1 East Washington Street
P.O. Box 891
New Castle, PA 16103-0891

Exeter Associates, Inc.
Suite 350
12510 Prosperity Drive
Silver Springs, MD 20904

Donald A. Kaplan, Esq.
Lisa M. Helpert, Esq.
Preston, Gates, Ellis & Rouvelas,

Meeds, LLP
Suite 500
1735 New York Ave., NW
Washington, DC 20006-4759

Gary A. Jeffries, Esq.
CNG Energy Services Corp.
One Park Ridge Center
P.O. Box 15746
Pittsburgh, PA 15244-0746

David Cruthirds, Esq.
Electric Clearinghouse, Ins.
Suite 5800
100 Louisiana
Houston, TX 77002-5050

Keith M. Sappenfield, II
Director of Marketing Support
NorAm Energy Management Inc.
P.O. Box 2628
Houston, TX 77252-2628

John R. Orr, Esq.
Duke Energy Trading & Marketing, LLC
One Westchester Center
Suite 650
10777 Wesheimer
Houston, TX 77042

Lawrence E. Moncrief, Esq.
1364 Silverton Ave
Pittsburgh, PA 15206

Samuel W. Braver, Esq.
Bruce A. Americus, Esq.
BUCHANAN INGERSOLL P.C.
One Oxford Centre, 20th Floor
301 Grant Street
Pittsburgh, PA 15219-1410

Irwin A. Popowsky, Esquire
Marisa A. Sifontes, Esquire
Office of Consumer Advocate
1425 Strawberry Square
Harrisburg, PA 17120

John Wilson, Executive Director
Community Action Assoc. of PA
222 Pine Street
Harrisburg, PA 17101

Robert Longwell

Date: February 17, 1998

DSH:10096.1

McNEES, WALLACE & NURICK
ATTORNEYS AT LAW

100 PINE STREET
P. O. BOX 1166
HARRISBURG, PA 17108-1166
TELEPHONE (717) 232-8000
FAX (717) 237-5300

http://www.mwn.com

PAMELA C. POLACEK
DIRECT DIAL: (717) 237-5368
E-MAIL ADDRESS: PPOLACEK@MWN.COM

DOCUMENT FOLDER

February 17, 1998

VIA HAND DELIVERY

James J. McNulty, Secretary
Pennsylvania Public Utility Commission
Room B-20, North Office Building
Harrisburg, PA 17120

Re: Application of Duquesne Light Company for approval of Restructuring Plan Under Section 2806 of the Public Utility Code; Docket No. R-00974104

Dear Secretary McNulty:

Enclosed for filing are the original and nine (9) copies of the Reply Brief of the Duquesne Industrial Intervenors ("DII") in the above-referenced proceeding.

As evidenced by the attached Certificate of Service, all parties are being duly served with the brief. Please date stamp the extra copy of this letter and return it for our filing purposes.

Very truly yours,

McNEES, WALLACE & NURICK

Pamela C. Polacek

By
Pamela C. Polacek

Counsel to the Duquesne Industrial Intervenors

PCP/clc
Enclosures
c: Administrative Law Judge John H. Corbett, Jr. (w/ diskette) (via hand delivery)
Certificate of Service

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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY COMMISSION, ET. AL.	:	
v.	:	
	:	DOCKET NO. R-00974104
DUQUESNE LIGHT COMPANY FOR APPROVAL OF ITS RESTRUCTURING PLAN UNDER SECTION 2806 OF THE PUBLIC UTILITY CODE	:	

REPLY BRIEF OF THE DUQUESNE INDUSTRIAL INTERVENORS

BOC Gases
General Motors Corp.
J&L Specialty Steel, Inc.
LTV Steel Company, Inc.
Nabisco Inc.
Nova Chemicals, Inc.
USX Corporation - US Steel Group

David M. Kleppinger
James P. Dougherty
Pamela C. Polacek
McNEES, WALLACE & NURICK
100 Pine Street
P.O. Box 1166
Harrisburg, PA 17108-1166
(717) 232-8000

Counsel to the Duquesne Industrial Intervenors

Dated: February 17, 1998

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Statutes and Rules: Page

I. INTRODUCTION AND SUMMARY OF ARGUMENT

On February 10, 1998, the parties filed Main Briefs pursuant to the procedural schedule in this proceeding. The Duquesne Industrial Intervenors ("DII") filed a Main Brief addressing the following general issues: phase-in; transmission and distribution rate unbundling; stranded cost; the competitive transition charge ("CTC"); universal service; and, tariff related issues. DII received briefs from the following Parties:

- Duquesne Light Company ("DLC," "Duquesne," or "Company");
- The Office of Trial Staff ("OTS");
- The Office of Consumer Advocate ("OCA");
- The Office of Small Business Advocate ("OSBA");
- PECO Energy Company ("PECO");
- The Environmentalists and the Low-Income Advocates (collectively, "Environmentalists");
- Enron Power Marketing, Inc. ("Enron");
- Mid-Atlantic Power Supply Association ("MAPSA");
- The City of Pittsburgh;
- The Community Action Association of Pennsylvania;
- NEV East, LLC;
- Pennsylvania Retailers' Association ("PRA");
- David Hughes;
- System Council U-IO, International Brotherhood of Electrical Workers; and
- Hospital Shared Services and Administrative Resource, Inc. ("HSS/ARI")

DII hereby responds to those Main Briefs. DII reiterates and endorses all arguments contained in its Main Brief, except to the limited extent modified below. In addition, the choice of DII not to respond to another Party's arguments or criticisms should not be construed as acquiescence to those arguments or criticisms.

II. PHASE-IN OF CUSTOMER CHOICE

A. Method of Customer Selection

DII proposes to select commercial and industrial customers for the first segments of phase-in

based on a "first-come, first-served" approach.[1] DII Main Brief, pp. 5-8; DII Statement No. 1, pp. 60-61. However, if any customer class is over-subscribed in any phase, all customers signing up to participate will experience a pro-rata reduction in their load for that phase. Id. As DII explains in its Main Brief, this approach has two distinct advantages. See DII Main Brief, pp. 5-8. First, it maximizes the number of customers permitted to participate in the first two stages of the phase-in of direct access. Id. Second, it eliminates competitive disadvantage claims because all customers that want to participate will be permitted to do so to a certain extent of their load. Id. The Commission adopted an identical approach in the PECO restructuring proceeding. Application of PECO Energy Company for Approval of Its Restructuring Plan Under Section 2806 of the Public Utility Code and Joint Petition for Partial Settlement & Petition of Enron Energy Services Power, Inc., for Approval of an Electricity Competition and Choice Plan and for Authority Pursuant to Section 2807(E)(c) at the Public Utility Code to Serve as the Provider of Last Resort in the Service Territory of PECO Energy Company, Docket Nos. R-00973953 & P-00971265, Order on Reconsideration entered on January 16, 1998, slip op. at 22 ("PECO Reconsideration Order"). The DII phase-in approach is clearly reasonable and should be endorsed by the Commission.

Duquesne describes its approach as being based on "first-come, first-served principles." DLC Main Brief, p. 6 (emphasis in original). As DII explains in its Main Brief, however, the DLC proposal is based only on first-come, first-served for pilot enrollment. DII Main Brief, pp. 6-7. A true first-come, first-served methodology would permit the willingness to participate in the first (or second) phase of direct access to determine participation, not the willingness of a percentage of customers in a SIC code segment to participate in the pilot to determine participation. Id. Duquesne has not shown sufficient support for deviating from the Act's default position that phase-in be "first-come, first-served." 66 Pa. C.S. § 2806(b)(4).

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[1]OSBA in its Main Brief misunderstands the DII proposal. OSBA Main Brief, p. 10. The DII proposal does not apply "for the industrial customer class only." Id.

Furthermore, the Duquesne methodology does not prevent competitive disadvantage situations. See DLC Main Brief, p. 7. To the contrary, the DLC proposal may create more disadvantages than it prevents. SIC market segments that compete against each other will be permitted access in different stages of the phase-in, thus producing competitive disadvantages. Tr. at 1039-41. Adoption of the DLC methodology with such potential to create competitive disadvantages is unnecessary and unwarranted because an alternative exists that both uses the first-come, first-serve methodology (not "principles") and eliminates competitive disadvantage situations (i.e., the DII first-come, first-served approach with a pro rata reduction in load for commercial and industrial customers if a class is over-subscribed). See DII Main Brief, pp. 5-8. Furthermore, the DLC proposal inappropriately merges consideration of the commercial and industrial customer classes and inappropriately uses response to the pilot solicitation as a proxy for interest in receiving competitive supply. See DII Main Brief, pp. 6-7. The DLC proposal must be rejected.

In its Main Brief, Duquesne describes the PRA pro-rata selection approach as "a special 'deal' to large commercial customers that is incompatible with the Act." DLC Main Brief, p. 7. Duquesne attempts to distinguish the Commission's adoption of an identical approach in the PECO proceeding. DLC Main Brief, p. 7, n. 1. Contrary to Company assertions, a proposal similar to the DII first-come, first-served approach with a pro rata reduction for over-subscribed commercial and industrial classes was proposed and adopted in the PECO proceeding. PECO Reconsideration Order, slip op. at 22. This approach is clearly appropriate under the Electricity Generation Customer Choice and Competition ("Act"), which provides that "as of January 1, 1999, a maximum of 33% of the peak load of each customer class shall have the opportunity to direct access." 66 Pa. C.S. § 2806(b)(1) (emphasis added). The Act does not specify that this 33% must be filled customer by customer; rather, as long as only 33% of the class peak load has direct access on that date, the dictates of the Act are satisfied regardless of how many customers within that class are provided direct access.

Duquesne also faults the PRA proposal (and by extension the DII proposal) by stating that it presents administrative and billing complexity. DLC Main Brief, pp. 7-8. The Company misperceives its actual administrative responsibilities. The limitations on individual customer load in the pilot program already result in customer loads supplied both competitively and non-competitively. In addition, PECO will face the same situation. With respect to the inconvenience of customers, DII submits that the commercial and industrial customers involved in the instant proceeding have made it abundantly clear that the pro rata approach is worth any purported inconvenience. See DII Main Brief, pp. 5-8; PRA Main Brief, pp. 6-12. Duquesne itself states that it will introduce the pro-rata approach if sufficient customer interest is expressed. Tr. at 1049-50.

The pro-rata phase-in proposal is proper under the Act, maximizes the number of customers able to participate in the first two stages of direct access, and minimizes (if not eliminates) competitive disadvantages. See DII Main Brief, pp. 5-8. The DII proposal should be accepted.

B. Timetable for Phase-in

DII proposes an accelerated timetable for customer choice whereby 33% of customers receive choice on January 1, 1999, an additional 33% of customers receive choice on January 2, 1999, and all customers receive choice on January 2, 2000. See DII Main Brief, pp. 8-9; DII Statement No. 1, p. 61. An identical accelerated phase-in schedule was adopted by the Commission in the PECO Restructuring proceeding. Application of PECO Energy Company for Approval of Its Restructuring Plan Under Section 2806 of the Public Utility Code and Joint Petition for Partial Settlement & Petition of Enron Energy Services Power, Inc., for Approval of an Electricity Competition and Choice Plan and for Authority Pursuant to Section 2807(E)(c) at the Public Utility Code to Serve as the Provider of Last Resort in the Service Territory of PECO Energy Company, Docket Nos. R-00973953 & P-00971265, Opinion and Order entered on December 23, 1997, slip op. at 48 ("PECO Restructuring Order"). Duquesne maintains that the accelerated phase-in is a distorted interpretation of the Act, but

appropriately recognizes that the PECO precedent should control this issue. See DLC Main Brief, pp. 8-9.

DII agrees that the PECO precedent controls. It is illogical and unfair to allow ratepayers in the PECO service territory to take advantage of an accelerated timetable without allowing all other ratepayers in the Commonwealth to do the same. DII respectfully requests that the Commission adopt the accelerated phase-in approach as detailed in the DII Main Brief. See DII Main Brief, pp. 8-9.

III. TRANSMISSION AND DISTRIBUTION RATES; UNBUNDLING ISSUES

A. Introduction

DII submits that Duquesne inappropriately inflates its transmission and distribution rates by using a "required" rate of return, including the cost of "distribution losses" in distribution rates and including the cost of certain generation-related ancillary services in transmission rates. See DII Main Brief, p. 10. Duquesne's attempts must be rejected.

B. 1996 Test Year Cost of Service

DII provisionally accepts the Company's 1996 test year Cost of Service, with the adjustments discussed below and in the DII Main Brief, as the rate unbundling starting point. DII Main Brief, p. 10.

C. Required v. Realized Rates of Return

DLC proposes to unbundle its transmission and distribution rates on the basis of a "required" rate of return. DLC Main Brief, pp. 11-14. DII objects to the use of the required rate of return and instead proposes that the Company use the "realized" rate of return that is presently earned from each rate class. DII Main Brief, pp. 10-12.

In support of its use of the required rate of return, Duquesne advances the following argument:

> These proposals (to use realized rate of return) must fail because this is not how regulated rates are set. They are set to recover the required rate of return.

DLC Main Brief, p. 13. DLC is misguided. Although, in a general ratemaking proceeding, it would be appropriate to move all classes towards a system-wide average rate of return, it is not appropriate in this

proceeding.

> Although such an approach might be appropriate in a rate proceeding in which class rates are going to be adjusted towards cost of service, it is not appropriate to use these results in this proceeding, since the current bundled rates reflect the earned rate of return produced by the rate class, and not DLC's desired rate of return. As such, I have utilized the earned rate of return for each rate class to compute the distribution revenue requirements for each rate schedule in my unbundling analysis. This is consistent with the approach that other electric utilities in Pennsylvania have used. In general, I support the concept that rates should be based on costs and that each customer class (and therefore cost function within the class) should pay a rate of return based on the system average rate of return. However, since this is not a rate case and rates cannot actually be adjusted, the Company's proposal is not appropriate. In fact, it effectively results in a cost-shifting in violation of the Competition Act since the generation component of the unbundled rate for each rate schedule is computed as a residual.

DII Statement No. 1, pp. 41-42.

The purpose of this proceeding is not to set new transmission and distribution rates for Duquesne; *the purpose of this proceeding is to unbundle the existing rates and to do so in a manner that* does not shift costs or violate the rate caps. See 66 Pa. C.S. §§ 2802(14), 2804(3), 2804(7) & 2808(a). Duquesne will have an opportunity to adjust its rates (and possibly move the class rate of return towards system average) after the transmission and distribution rate cap mandated in Section 2804(4)(i), 66 Pa. C.S. § 2804(4)(i), expires. Duquesne's use of the required rate of return in unbundling its transmission and distribution rates is inconsistent with this purpose.

Duquesne also claims that the use of the required rate of return does not shift costs because total unbundled charges exactly equal bundled charges at current rates. DLC Main Brief, pp. 13-14. The objective of Duquesne's proposal is to shift costs between functions and ensure that it is able to continue to recover as much revenue as possible through its regulated monopoly service rates. As DII amply illustrates, the use of the required rate of return shifts costs between the generation function and the transmission and distribution functions. DII Main Brief, pp. 10-12. The result of this cost shift between functions is to inflate unreasonably Duquesne's monopoly transmission and distribution rates. Id. The Act clearly requires that the rates for non-generation services (e.g., transmission and distribution) be

capped at the January 1, 1997, levels for 54 months. 66 Pa. C.S. § 2804(4)(i). In addition, the use of the required rate of return changes the generation component of rates and results in a shifting of stranded cost liability between classes, which is prohibited by the Act. See 66 Pa. C.S. § 2808(a); DII Main Brief, pp. 10-12.

DII demonstrates that the Company's use of the required rate of return in unbundling its transmission and distribution rates results in prohibited cost shifting under the Act. Duquesne clearly attempts to inflate non-generation rates above January 1, 1997 levels. DII respectfully submits that the Commission reject the Company's proposal to use the required rate of return, as opposed to the realized rate of return, in unbundling its transmission and distribution rates.[2]

D. Distribution Losses

Duquesne states that no dispute exists regarding that treatment of distribution losses. DLC Main Brief, p. 14. DII agrees and expects that DLC will rectify the error in its compliance filing. See DII Main Brief, pp. 12-14.

E. Ancillary Services

Duquesne proposes to remove from its transmission and distribution rates costs associated with generation-related ancillary services that can currently be competitively procured. DLC Main Brief, pp. 15-17. DII objects to this approach and instead proposes that all costs of generation-related ancillary services (competitive and non-competitive) be removed from the Company's transmission and distribution rates. DII Main Brief, pp. 14-17 Any ancillary service that can be competitively procured should be made available from alternative suppliers. Any ancillary service that cannot be competitively

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[2]Duquesne also notes that it should be treated differently from other companies on this issue because it has not had a base rate proceeding since 1987. DLC Main Brief, p. 14, n. 3. The timing of Duquesne's last base rate proceeding is irrelevant. The Act requires that Duquesne's rates in effect as of January 1, 1997, are capped and must be unbundled according to those capped rates. The Act creates no special exceptions according to the timing of a company's last base rate proceeding. Duquesne will have the opportunity after the transmission and distribution rate cap expires to request that any rate of return allocation be changed.

procured should still be provided by the Company. Id.

Duquesne confuses the issue of proper allocation of costs to the transmission and distribution function with whether the Commission should, in this proceeding, afford customers the opportunity to procure all generation-related ancillary services from competitive suppliers. DLC Main Brief, pp. 15-16. Whether all ancillary services should be competitively available is not the issue in this proceeding; rather, the issue in this proceeding is the proper unbundling and functionalization of Duquesne's current rates. Duquesne inappropriately states that the treatment of generation-related ancillary services should vary based on whether the particular service can presently be competitively procured. DLC Main Brief, pp. 16-17. As DII shows, generation-related ancillary services should be functionalized as part of generation rates, even if the Company continues to provide those services because ECAR or FERC does not permit competitive procurement. DII Main Brief, pp. 14-17. The Duquesne piecemeal approach to removing generation-related ancillary services from transmission and distribution rates as those services become authorized to be procured competitively is unnecessary and inappropriate. DII submits that the Commission should require Duquesne to remove all such costs from its transmission and distribution rates in this proceeding.

F. Voltage-Differentiated Rates

Enron proposes a rate re-design based on customers' service voltage levels. See Enron Main Brief, pp. 21-23. The Act prohibits cost shifting in the unbundling process and institutes a rate cap on non-generation rates through mid-2001. See 66 Pa. C.S. §§ 2804(4)(i) & 2804(7). The Company objects to the proposal as an inappropriate cost shift. DLC Main Brief, p. 17. DII respectfully submits that the Enron proposal must be rejected because Enron has not shown sufficiently that implementation of voltage differentiated rates will not shift costs between classes.

G. Other Issues

None.

H. Conclusion

DII submits that Duquesne inappropriately unbundles transmission and distribution rates. The rates submitted with the DLC filing are inflated because: (1) DLC uses the required rate of return rather than the realized rate of return; (2) DLC includes the costs of distribution losses in distribution rates; and, (3) DLC includes costs of generation-related ancillary service in transmission rates. See DII Main Brief, pp. 10-18. The DII unbundling recommendations based on the realized rate of return, including the cost of distribution losses and the costs of all generation-related ancillary services in the generation component are reasonable and should be accepted. Id. In addition, Enron's proposed redesign of transmission and distribution rates must be rejected.

IV. TRANSITION OR STRANDED COSTS

A. Overview of Stranded Cost Valuation and Recovery Approaches

1. Introduction

DII sets forth a detailed explanation of the mechanics of the stranded cost calculation in its Main Brief. See DII Main Brief, pp. 18-23. Generally, DII advocates a three step approach:

(1) The cost must be properly claimed under the definition in the Act, 66 Pa. C.S. § 2803,

(2) The cost must be properly quantified (i.e., "known and measurable," and calculated on net present value basis at 12/31/98),

(3) The cost must be just and reasonable to recover from ratepayers (i.e., mitigated, and stranded generation costs shared between shareholders and ratepayers).

Id. The burden of proof is on Duquesne to establish the proper level of recoverable stranded costs. See PECO Restructuring Order, slip op. at 68. DII submits that Duquesne fails to meet this burden.

2. Duquesne's Approach

Duquesne goes to great length to categorize its various approaches to stranded cost quantification as "market-based evaluations." "The fundamental premise of Duquesne's approach to stranded cost recovery is that the market, not career forecasters should set the value of Duquesne's generating assets."

DLC Main Brief, p. 18. The Company's approach, however, is not necessarily market-based. Unless the Commission takes advantage of Duquesne's offer to auction all of its generating assets to determine the market value of those assets, a market-based valuation will not occur. If any assets are valued based on the judgment of an arbitration panel, then such approach is not market-based, but rather properly classified as an administrative determination. DII Main Brief, pp. 41-42. In addition, use of an arbitration panel to value any portion of the Company's generating assets raises significant due process concerns. Id. As such, Duquesne's characterization of its preferred approach to stranded cost quantification is inapt and inappropriate.

DII believes that use of a market price forecast and the "asset value methodology" to determine asset market value provides an accurate proxy to the results of any auction. Id. at 34.[3] The use of the market price forecast is sufficient to satisfy the Act's "known and measurable" requirement and should be accepted by the Commission. The Company itself admits that methods other than an auction can meet the known and measurable standard. DLC Main Brief, p. 20, n. 8. DII submits that use of a market price forecast meets the Act's known and measurable standard and appropriately provides a one-time definitive determination of Duquesne's stranded generation costs.

The Company's Main Brief also discusses various "auction implementation issues." DLC Main Brief, pp. 20-21. The first issue is the process by which the auction will be conducted. DII takes no position on this issue.

The second issue is the establishment of an interim CTC prior to commencement of the auction. Id. DII recognizes that it may not be possible for the auction of Duquesne's assets to occur prior to January 1, 1999. In such event, DII agrees that continuation of the rates and credits in the pilot program

[3]Duquesne notes DII's statement that market price simulations are not completely certain. DLC Main Brief, p. 19, n. 7. Absent a full and immediate auction, however, the Company provides no way to perform the definitive stranded cost valuation necessary under the Act. See DII Main Brief, pp. 30-35. The balancing of the known and measurable standard with the Act's mandate that stranded cost be determined definitively in this proceeding militate in favor of use of a market price projection (absent an immediate and full auction by DLC).

may be acceptable. However, if the Commission accepts Duquesne's offer to conduct an immediate and full auction of its assets, this auction should occur as soon as possible and not be unreasonably delayed.[4]

The third issue the Company discusses is the calculation of a permanent CTC using the market value produced by the auction. Id. The Company states that it is willing to adopt the approach used in PECO, which provided an allocated levelized CTC, provided that two conditions are met. DLC Main Brief, p. 21. Both of the Company's "conditions" are clearly contrary to the requirements of the Act.

The first condition that the Company places on its offer is that DLC must be permitted to recover fully its stranded costs with no sharing of those costs between shareholders and ratepayers. Id. As DII fully explains in its Main Brief, the Commission has a duty to use its regulatory discretion to determine whether *sharing* is appropriate in this proceeding. See DII Main Brief, pp. 18-22, 27-28 & 69-70. The Commission cannot shirk this responsibility based on the proposed interim compromise by Duquesne.

The second condition that the Company places on its offer to accept the PECO methodology is that the Commission must address the Company's concerns regarding its obligation to serve at capped rates during the transition period. DLC Main Brief, p. 21. In rejoinder testimony, the Company states that such a solution could be the following:

> It could involve an agreement to remove the cap or an arrangement with the purchaser of the assets to sell Duquesne power at a fixed price (a "call option").

Duquesne Statement No. 1R, p. 16. The Company confirmed during cross-examination that it desires to restrict ratepayers' statutory right to return to service from the utility at capped rates during the transition period while the Company is recovering stranded costs from that ratepayer. Tr. at 55. This condition on Duquesne's proposal is clearly unlawful. Ratepayers have a statutory right to return to service at capped levels during the transition period. 66 Pa. C.S. § 2804(4). As DII explains fully in

[4]DII emphasizes that an interim CTC is appropriate only if the Commission orders the immediate and full auction as offered by Duquesne in its rejoinder testimony. The DII comments in this section do not apply if the Commission employs any other valuation methodology (such as delaying divestiture until 2003 or requesting Duquesne to divest only a portion of its assets). In such event, DII would object to the use of the methodology. See DII Main Brief, pp. 30-33 & 39-45.

Main Brief, this right is a quid pro quo for the recovery of stranded costs by the utility. See DII Main Brief, pp. 43-44. Such statutory protection cannot be waived.

Duquesne's choice to auction generating assets is its own; the Act states the Commission cannot require Duquesne to divest assets. 66 Pa. C.S. § 2804(5). It is only the Company's offer that presents the Commission with this option to request divestiture. The Commission cannot eviscerate one of the central consumer protections contained in the Act based on the Company's offer to voluntarily divest itself of its generating units. Any Duquesne "compromise" that involves a waiver of the rate cap must be rejected.

Moreover, as DII explains in its Main Brief, the appropriate methodology for setting the CTC is the CTC residual methodology based on an expected market price. See DII Main Brief, pp. 75-83.

3. Intervenor Approaches

The Company explains that another approach to calculation of stranded cost is the DII and OCA calculations based on market price forecasts. DLC Main Brief, pp. 21-22. The Company objects to the use of market price forecast, or in the alternative, asserts that its own forecast performed by Mr. Schnitzer should be relied upon. Id. As explained fully in the DII Main Brief, the DII market price forecast is a reasonable basis upon which to determine Duquesne's stranded generation cost. See DII Main Brief, pp. 30-45. In addition, the Duquesne range of market prices submitted by Mr. Schnitzer is not appropriate for use in this proceeding. This issue will be discussed in more detail infra.

4. Conclusion

In Main Brief, Duquesne modifies its stranded cost request regarding several regulatory assets.[5] As discussed fully below, these adjustments change the DII stranded cost recommendation. Charts

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[5]DII bases the DLC claims as stated in Main Brief on the record evidence submitted as of February 10, 1998. See Duquesne Statement No. 2-R, Exhibits DJC-10 & DJC-15. Duquesne revises the following regulatory asset claims in its Main Brief: post-2005 unamortized debt costs, deferred rate synchronization costs, deferred employee costs, DOE decommissioning expenses, pre-accrued nuclear outage costs, FAS 106 deferral and deferred fuel costs. See DLC Main Brief, Regulatory Asset Table.

summarizing the revised DII recommendation (with and without the equity return disallowance) are contained in Appendix A, B & C, infra.

DII agrees, however, that the immediate, total and unconditional auction of Duquesne's generating assets is an acceptable way to value properly Duquesne's stranded generation cost. If this proposal is accepted, DII respectfully requests the Commission to continue to evaluate the DII recommendations regarding regulatory assets, nuclear decommissioning and fossil decommissioning, as well as the other DII proposals.

B. Generation Related Stranded Costs (Recovery Pursuant to Section 2808(3))

1. Introduction

DII includes an explanation of the standards for recovery of stranded generation costs in its Main Brief at pages 27-28. As DII explains, absent an immediate, total, and unconditional auction of DLC's generating assets, the proper valuation is obtained by application of the asset value methodology to DII's projection of market prices for the competitive ECAR region. See DII Main Brief, pp. 27-28. Further, the DII equity return disallowance must subsequently be employed to arrive at the just and reasonable level of stranded generation costs to recover from ratepayers. Id.

2. Net Book Value

(a) Total Net Book Value

For purposes of calculating DLC's stranded generation costs, DII uses the DLC net generating plant and CWIP balance at December 31, 1998. DII Main Brief, p. 29.

(b) Treatment of Beaver Valley 2 Lease Costs

DII agrees that Duquesne should be permitted to recover the Beaver Valley 2 lease costs. DII Main Brief, pp. 29-30. DII seeks to ensure, however, that the Company does not recover the costs in two portions of its stranded cost calculation. Id. The DII treatment of these costs ensures no double recovery.

DII agrees with the Company's statement in its Main Brief that Exhibit DJC-10 illustrates the OCA, DLC and DII proposals on a consistent basis. See DLC Main Brief, pp. 23-24. Furthermore, DII accepts the Company's explanation of the PECO Order in footnote 11 on page 24 of its Main Brief. As DII states in its Main Brief, DII does not conceptually disagree with the Company's approach, but prefers utilization of the DII approach. See DII Main Brief, pp. 29-30.

(c) Recovery of Phillips and Brunot Island Costs

Duquesne recovery of any costs associated with Phillips and Brunot Island has not been addressed by DII.

(d) Conclusion

As DII fully explains in its Main Brief, the DII recommendation for stranded generation costs uses the Duquesne quantification of its net book value of its assets at December 31, 1998, and appropriately treats the Beaver Valley 2 lease costs. See DII Main Brief, p. 30.

3. Market Value

(a) Introduction

According to Duquesne's Main Brief, the Commission should consider the Company's various positions regarding asset market value in the following order:

(1) The Company's offer to divest itself immediately of all generating assets to determine the market value;

(2) The Company's proposal to conduct a "final valuation" in 2001-2003 using market evidence, which could include an auction if ordered by the Commission; and

(3) The Company's stranded cost recommendation based on the range of market prices submitted by Mr. Schnitzer.

See DLC Main Brief, pp. 18, 22, & 28.

The only Company-sponsored option that is appropriate for the Commission's use is to accept Duquesne's offer to auction immediately all of the Company's generating assets. DII Main Brief, pp. 39-45. This option, however, must not eliminate customers' statutory right to return to service at capped

rates. Id.

Duquesne gives four reasons in support of its second option to conduct the final asset valuation in 2001-2003:

(1) Computer forecast of market prices are inherently unreliable;

(2) The market valuation in 2001-2003 will be superior because better market evidence will be available as electric markets mature;

(3) Evaluation today is not necessary given that Duquesne cannot fully recover its stranded costs until at least 2003; and,

(4) Duquesne's obligations under the rate cap militate in favor of a final valuation later in the transition period.

DLC Main Brief, p. 26. The Company's purported foundation for the delayed valuation is baseless and must be rejected.

First, although computer forecasts of market prices are not completely accurate, computer forecasts are the best evidence that the Commission has to fulfill its duty under the Act to value Duquesne's stranded costs (absent an immediate and full auction).

> DLC attempts to justify this omission on the basis that market prices are too uncertain to be forecasted. I agree that there are certain difficulties in forecasting market electricity prices. However, as economist William Baumol once stated, "The only thing worse than forecasting the future is not forecasting the future!" DLC appears to prefer the "head in the sand" approach to dealing with change. Based on DLC's comments, the Company apparently has no idea of what its assets are worth. One wonders how DLC was able to decide that the sale of its share of Fort Martin Unit 2 to APS (at a high multiple of book value) was a "good deal."

DII Statement No. 2, p. 13. Contrary to the Company's assertion that DII does not "rebut" its evidence of the past inaccuracy of market price forecasts (DLC Main Brief, p. 27), DII clearly asserts that market price forecasts are the best evidence in this proceeding to balance the need for a definitive determination of asset market value against the Act's known and measurable standards. See DII Main Brief, pp. 30-35; DII Statement No. 2, p. 13.[6] The Commission relied on a market price forecast to determine PECO's

[6]It is no more certain that the DII market price forecast will "inaccurately forecast future market (continued...)

stranded generation cost. PECO Restructuring Order, slip op. at 82-91. Certainly, reliance on a market price forecast is appropriate to determine Duquesne's stranded generation costs.

Second, delaying the market valuation will not necessarily produce better market evidence upon which to base the valuation in 2003. Under Duquesne's delayed valuation proposal, unless an auction is ordered, an arbitration panel will determine the value of Duquesne's assets. Duquesne Statement No. 2R, pp. 3-4. An arbitration panel must look at evidence such as market price forecasts. The arbitration panel must also review other market price indicia such as comparable sales of generating units. An arbitration panel will not be able to determine administratively, with certainty, the market value of Duquesne's generating assets in 2003. OCA Statement No. 1, p. 12. Any level of uncertainty inherent in DII's recommendation will also exist in the arbitration panel's decision in 2003. DII's market price forecasts provide the Commission with information to perform the definitive stranded cost valuation necessitated by the Act (See 66 Pa. C.S. §§ 2803, 2802(8) & 2808(f)); delaying valuation deprives the Commission of this ability.

Third, the length of time required for Company recovery of any authorized stranded cost is irrelevant to whether a definitive level of stranded costs must be determined in this proceeding. As DII fully explains in its Main Brief, the Act clearly contemplates a one-time assessment of the utility's stranded cost as part of this proceeding. See DII Main Brief, pp. 30-33. The following reasons support DII's assessment of the Act:

- The definition of stranded cost requires generation-related costs to be netted in determining stranded costs. 66 Pa. C.S. § 2803. It is impossible to net Duquesne's potential stranded costs if one component of stranded costs is not quantified.
- The definition of stranded cost states that such costs are to be determined "as part of the restructuring plan." Id. The Commission will not be reviewing Duquesne's restructuring plan in 2001-2003.

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[6](...continued)
prices" (DLC Main Brief, p. 27) than it is certain that the DLC proposals will result in an accurate market valuation by an arbitration panel in 2003.

- The definition of stranded cost requires that such cost be mitigated. Id. The Commission is required to look at both retrospective and prospective mitigation by the Company. Id. §§ 2808(4) & (5). The Commission cannot fulfill its duty to ensure that such costs are mitigated in order to produce a just and reasonable level to recover from ratepayers unless a definitive level of stranded cost is determined as part of this proceeding.

- The Commission cannot perform its duty to ensure that stranded cost recovery is "just and reasonable" unless a definitive determination of total stranded costs is made as part of the restructuring proceeding. See id. §§ 1301, 2802(15), 2804(13), 2804(14) & 2808(c)(3).

- The Commission cannot fulfill its duty under the Act to perform a yearly reconciliation of the CTC revenues (Id. § 2808(f)) unless a definitive level of stranded cost is established as part of this proceeding.

- Delaying determination of stranded costs does not adequately balance the interests of ratepayers and the Company, in violation of Section 2802(8). Id. § 2802(8).

- Delaying determination of a definitive level of stranded cost is unfair and equitable to Duquesne's ratepayers because other ratepayers in the Commonwealth have been granted such certainty as to stranded cost responsibility. Id. § 2802(8).

- Delaying determination of Duquesne's stranded cost will hinder the development of the competitive market, in contravention of the goals of the Act. Id. §§ 2802(4)-(7).

See DII Main Brief, pp. 31-33. As DII illustrates, regardless of how long it will take Duquesne to recover its allowed stranded costs, it is imperative that a definitive level of stranded costs be determined as part of this proceeding.

Fourth, Duquesne's concerns about the rate cap are insufficient to deviate from the Act's clear mandate that a definitive level of stranded cost be determined in this proceeding. The Act represents a balancing of ratepayers, shareholders, utilities, and competitors interests during the transition period. 66 Pa. C.S. § 2802(8). Although the Company repeatedly asserts its aversion to rate cap legislation (See Duquesne Statement No. 1R, pp. 13-16; Tr. at 137 & 163-64), this aversion is irrelevant; the Act requires a rate cap as a necessary consumer protection. Rate cap elimination eviscerates the balancing implicit in the Act. The Company cannot arbitrarily select which portions of the Act it will abide.

Finally, the Commission must reject any reliance on Duquesne's range of market prices and

stranded costs. DII Main Brief, p. 24. The Duquesne range developed by Duquesne witness Schnitzer does not address a number of relevant factors that must be considered in a market price forecast, including the following:

- The relevant market for the forecast (DII Statement No. 2, p. 15);
- An accurate assessment of fuel prices (Id. at 16);
- Consideration of information about the regional fleet of generation resources such as generator capacities, heat rates, availability statistics, and maintenance requirements (Id. at 16);
- Customer demands (average energy and usage patterns) (Id.);
- Sufficient future capacity additions (Id.); and,
- A realistic assessment of the cost and efficiency of new capacity (Id. at 17-18 & 24-33).

The Schnitzer analysis simply lacks the level of detail necessary for the Commission to determine this important component of the restructuring filing.

> Mr. Schnitzer's approach is unrealistic. Mr. Schnitzer nominates a range of capacity prices, heat rates, carrying costs, and etc. He then selects the low and high end of each variable to derive his low and high prices. There is no reason to assume, however, that there is any realistic chance that all of the "low" or "high" variables will occur simultaneously. For example, it is quite unlikely that both the low heat rate and low capital cost estimates would occur in tandem. In fact, . . . capital costs are inversely related to heat rates: the more efficient plants cost more to build. Thus, the simultaneous selection of all "low" or "high" values is unrealistic. Arbitrarily combining the extreme values of all variables does nothing but produce a meaningless analysis. The wide range of possible prices that Mr. Schnitzer laments stem mostly from the fact that he has "manufactured" much of the claimed uncertainty by his combination of extreme values. In addition, even his so called "high" prices reflect heat rates and capacity cost forecasts that are more properly characterized as "low," "optimistic," or even "wildly optimistic" estimates. In other words, even Mr. Schnitzer's "high" prices reflect unreasonably low capacity costs and exceptionally high efficiency rates for new units.
>
> * * *
>
> Mr. Schnitzer shows no evidence to support his conclusion that new combined cycle plants will be the most economic capacity addition. He does not determine where such units will fall into the regional dispatch. He performs no detailed examination of the need for capacity in the region. He assumes all generators will be paid the same market prices, regardless of where they appear in the regional dispatch. All of these factors

influence market prices and where possible, should be considered in a more detailed analysis.

DII Statement No. 2, pp. 22-23.

Furthermore, the Company's assertion that the Schnitzer forecast is based on market evidence is misleading. DLC Main Brief, p. 29. The Schnitzer analysis for 1997-2005 is based on the results of Duquesne's offer to sell a firm block of power for an eight year period. Id. The results of that reverse-RFP, and the single year reverse-RFP, have been widely criticized in this proceeding as understating the retail price of electricity. See, e.g., HSS/ARI Main Brief, pp. 30-36. "Market evidence," such as Duquesne's sale of the Fort Martin Unit 2 for a substantial gain, clearly suggests that Duquesne overstates its stranded costs. DII Statement No. 2, p. 14.

All of the Company's options for asset valuation contain significant flaws. DII respectfully submits that the DII asset valuation is the most reasonable and accurate assessment of the value of Duquesne's generating assets in the competitive market. DII respectfully urges the PUC to accept the DII calculation.

(b) Market Price Projections

Duquesne states that examination of market price projections is necessary only if the Commission determines a definitive stranded cost total in this proceeding. DLC Main Brief, p. 16. As DII explains, such definitive determination must be made under the Act. DII Main Brief, pp. 30-35. Consequently, if an immediate, total and unconditional auction of DLC's assets does not occur, the Commission must address and adopt the DII or OCA stranded generation cost calculation based on a market price forecast. In its Main Brief, DII explains and supports the reasonableness of its market price projection provided in this proceeding. See DII Main Brief, pp. 35-39. The arguments raised by other parties do not undercut the validity of that analysis.

The OCA asserts that Mr. Smith's market price forecast should be used in this proceeding because it was used by the Commission in the PECO proceeding. OCA Main Brief, pp. 2 & 28-29.

Although DII believes that many issues must be addressed consistently on a state-wide basis, the use of one forecaster's market price analysis of two different markets is not one of those issues. Many of the inputs to the forecast logically should be consistent (such as the cost of new capacity). However, ECAR and PJM are different regional energy markets. In addition, the Commission specifically stated in the PECO decision that by adopting Mr. Smith's analysis, the Commission was not adopting "each and every input and assumption." PECO Restructuring Order, slip op. at 90. The Commission focused on the overall balance in Mr. Smith's market price projection for PJM. Id. Furthermore, the Commission found "substantial merit" in several of Mr. Falkenberg's recommendations. Id. Consequently, OCA places too much emphasis on the PECO precedent. DII asserts that Mr. Falkenberg presents a reasonable and reliable projection of market prices for the ECAR region that should be accepted by the Commission.[7]

(i) Forecasting Methodology

As DII explains fully in its Main Brief, the DII market price projection is based on a model designed to predict prices in a competitive market (i.e., the "KPC Model"). See DII Main Brief, pp. 35-36. Although the Company offers conclusory statements regarding the reputed superiority of its forecasts, it does not criticize the KPC Model in this proceeding. Moreover, the Company's general aversion to all computer models is both baseless and unrealistic because, as DII shows, the DII model and recommendation are the best evidence of asset market value submitted in this proceeding (absent immediate, full and unconditional auction of DLC's assets). See DII Main Brief, pp. 30-39.

(ii) Input Assumptions

Market price forecasts were submitted in this proceeding by OCA, DII, and Duquesne. In its Main Brief, Duquesne criticizes one of the inputs used by DII. DLC Main Brief, pp. 30-31. Specifically, Duquesne criticizes DII's use of a 15% reserve margin. As DII explains in its Main Brief,

[7]For these reasons, DII agrees that the same market price forecast should be used for both the DLC and the West Penn Power (Allegheny Power System) proceedings.

the 15% reserve margin is clearly a reasonable input to its forecast. See DII Main Brief, p. 37. Duquesne currently uses a 12% reserve margin for its planning purposes. Duquesne Statement No. 9, p. 9. It is axiomatic that customers in the competitive market will desire at least the same level of reliable service that they receive in the regulated market. The Act suggests that system reliability, including adequate generation, may need to be coordinated in the competitive market (e.g., through an independent system operator). 66 Pa. C.S. §§ 2802(20) & 2804(14). DII Main Brief, p. 37. Consequently, it is reasonable to assume that the market (as dictated by customer demand) will fall at equilibrium based on a 15% reserve margin requirement.[8]

Duquesne also attempts to address DII's criticism of Mr. Schnitzer's cost of a new combined cycle unit. DLC Main Brief, p. 32. The DLC argument in this regard is moot. Under the DII forecast, capacity additions are based on new combustion turbine (CT) units being the most economic capacity choice in ECAR, unless in a certain instance the incremental capital cost of the combined cycle plant over a combustion turbine is profitable. DII Statement No. 2, p. 43. DII's market price forecast supports adequate addition of cheaper CT units, not Duquesne's inflated price of adding new combined cycle units.

Duquesne also cryptically and selectively quotes DII witness Falkenberg. See DLC Main Brief, p. 31, n. 24. The correct and complete testimony on the cited page is as follows.

> **Q. Mr. Schnitzer testifies that a true "market" based evaluation would be superior to an administratively determined estimate of stranded costs. Do you agree?**
>
> A. Perhaps Mr. Schnitzer has a point. However, current electricity markets are too immature to provide a realistic assessment of market prices needed for this type of analysis. A reasonable solution would be for DLC to offer its assets for sale. GPU has recently decided to do just that. DLC's proposal to use short term contract prices is really not a reasonable approach because it does not derive a true market value or stranded cost. It would be equivalent to Mr. Schnitzer determining the "stranded cost" of his car by running an ad in the classifieds to

[8]Because Duquesne performs no complete analysis of future capacity additions, the reserve margin requirement is tangential to the DLC market price forecast. See DII Statement No. 2, p. 21.

> *rent* it for a few months and then comparing the best offer to his monthly car payments. In contrast to the low market prices suggested by recent solicitations (comparable to the above-referenced amateurish automobile rental scenario), recent asset sales have produced exceptionally good results. Until DLC is willing to actually put its assets on the block, the claim that market prices are now low is completely irrelevant. Indeed, the Commission should well recall that Duquesne sold its share of Fort Martin Unit 2 to APS for a substantial gain. Thus, the actual market data currently available suggests that Duquesne has not realistically assessed its stranded costs. In short, DLC has not met anything close to a reasonable burden of proof.

DII Statement No. 2, pp. 13-14. No inconsistency exists when DII testimony is considered in its entirety.

(iii) Results

As DII explains in Main Brief, the results of DII's market price projection are reasonable. See DII Main Brief, pp. 38-39. The DII results ensure sufficient capacity additions to provide for continued reliability. In addition, because the DII market prices beyond 2005 are low, relative to the other forecasts, any alleged inaccuracy serves only to increase the DII stranded cost recommendation. Id. The DII market price projection is reasonable and should be accepted by the PUC.

(c) Other Evidence of Market Value

DII addresses the various Duquesne market valuation proposals in this portion of its Main Brief. See DII Main Brief, pp. 39-44. As DII explains, all the Company's valuation options contain inherent flaws. The immediate divestiture offer, if accepted by the Commission, must involve the immediate, full and unconditional auction of DLC's assets. Id. The delayed valuation proposals do not satisfy the Act's requirement that a definitive level of stranded cost be determined in this proceeding. Id. Finally, the Schnitzer range of market prices lacks the specificity necessary in this proceeding. Id. All Company proposals, except the immediate, full and unconditional auction of its assets, must be rejected.

(d) Conclusion

The PUC should find that DII's market price projection is the most reliable because: (1) it is based on a model designed to simulate a competitive market; (2) it uses reliable and publicly available

sources for its inputs; and (3) it produces results that ensure the continued reliability of the system. See DII Main Brief, pp. 44-45. DLC's projection, contrary to the Company's claims, is not based on actual market data for a retail, competitive market. Based on the DII projection, Duquesne's generating units have a market value of negative $16.742 million in the competitive market. See DII Main Brief, pp. 44-45; DII Statement No. 2, Exh. No. RJF-5a.

4. Other Factors Affecting Market Value/Stranded Costs

(a) Life Extension

DII takes no position on whether life extensions should be considered in calculating DLC's stranded generating cost.

(b) Plant Shutdowns

DII takes no position on whether plant shutdowns should be considered in calculating DLC's stranded generation cost.

(c) Productivity Gains

DII takes no position on whether productivity gains should be considered in calculating DLC's stranded generation cost.

(d) Costs Independent of Operation

Duquesne's Main Brief contains a discussion of "Costs Independent of Operation," which purportedly represent costs that are unavoidable if a generating unit is shut down. DLC Main Brief, pp. 38-39. DLC first claims and quantifies these costs in rebuttal testimony. See Duquesne Statement No. 10R, p. 5. DII takes no position on the propriety of Duquesne's costs independent of operation. See DII Main Brief, pp. 45-46. Duquesne states, however, that "if an administrative determination of stranded costs is made, Duquesne's projection of these costs should be included." DLC Main Brief, p. 39. According to Duquesne's witness, the DII market price forecast covers these purported costs independent of operation; therefore, if the DII market price forecast is accepted, no adjustments for these

costs needs to be made. Tr. at 547-551; DII Main Brief, pp. 45-46. Furthermore, if the costs are already included in DII's recommendation, it is incorrect to conclude that "there is no real dispute that a significant level of these costs is unavoidable." DLC Main Brief, p. 39. The Company seems unable or unwilling to determine whether any level is "unavoidable" in the DII recommendation.

(e) Projected Capital Additions and O&M Expense

DII takes no position on whether projected capital additions and O&M expense should be considered in DLC's stranded generation cost.

(f) Environmental Regulations

DLC claims that recent environmental proposals will, if implemented, add significant costs to operating Duquesne's generation. DLC Main Brief, pp. 39-40. Specifically, the Company refers to the EPA State Implementation Plan ("SIP") and the CO_2 emission reductions in the Kyoto Accords. Id. The Company's statements in this regard are misleading. First, the Company never challenged DII's market price projection on this point. See Duquesne Statement No. 10R, pp. 7-10. Because of this failure, it is misleading to assume the DII projection does not address environmental regulations. Second, the Kyoto Accords on CO_2 emissions must be adopted by the U.S. Senate to become effective. Duquesne's witness expresses doubt that the treaty will be passed. Tr. at 940. Even if it were passed, Duquesne suggests that "at this point, it is impossible to say what those impacts will be." Tr. at 940.

(g) Other

None.

5. Conclusion

The reliable market price projection submitted by DII satisfies the Act's requirement of a one-time determination. Neither ratepayer nor shareholder interests are served by unreasonably delaying the uncertainty of stranded cost recovery during the transition period. As DII explains fully in its Main Brief, the DII stranded generation cost calculation of $994.969 million (jurisdictional) is clearly the most

reasonable and should be accepted by the Commission. See DII Main Brief, pp. 46-47.

C. Merger Savings

Duquesne is adamant that all discussion regarding the proposed merger between Duquesne and West Penn Power (Allegheny Power System) be addressed in the Commission's merger docket and not in this proceeding. DLC Main Brief, p. 41. Although DII recognizes that a separate docket has been convened for this purpose, DII notes that the Company is the Party that interjects the topic of merger savings into this docket by submitting Direct Testimony claiming "synergistic savings" will be achieved. See Duquesne Statement No. 1, p. 6. As DII notes in its Main Brief, it is only fair and equitable that any merger-related savings be credited against quantified stranded costs. DII Main Brief, p. 47.

D. Decommissioning

1. Nuclear Decommissioning

In the tables accompanying its Main Brief, Duquesne claims a net present value of $57.4 million in nuclear decommissioning costs. DLC Main Brief, Stranded Nuclear Cost Calculation Table.[9] The Company in its Main Brief neither acknowledges nor addresses DII's concern with respect to the claim being overstated, because it does not net any possible benefits of the nuclear decommissioning trust funds.

> DLC's claim is further inflated because it fails to incorporate net trust funds earnings on amounts collected through 2005 or subsequent to 2005 under the Duquesne CTC proposal. DII Statement No. 3, pp. 31-32. Amounts collected from ratepayers to fund future nuclear decommissioning expenses are put into an external trust fund that earns a rate of return. This rate of return increases amounts in that trust fund. In order to meet the Act standard that stranded costs represents the net portion of generation-related costs, the calculation of Duquesne's nuclear decommissioning claim must recognize an offset for the trust fund earnings. 66 Pa. C.S. § 2803; PECO Restructuring Order, slip op. at 79; DII Statement No. 3, pp. 31-32.

DII Main Brief, p. 48. Duquesne neither rebuts this argument, nor explains how the Company's

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[9]In its Main Brief, DII states that the Company's claim is $281.0 million for nuclear decommissioning costs. DII Main Brief, p. 47. This figure came directly from the Company's testimony. See Duquesne Statement No. 4, p. 8.

proposed quantification offsets decommissioning costs with trust fund earnings. The DII recommended adjustment that DLC recover $42.959 million in nuclear decommissioning expenses should be accepted. DII Main Brief, p. 49.

2. Fossil Decommissioning

DLC properly recognizes that the Commission rejected a claim for future fossil decommissioning costs in the PECO restructuring proceeding. DLC Main Brief, pp. 42-43. DII argues that the Commission should follow this precedent with respect to Duquesne's claim for future decommissioning costs. DII Main Brief, pp. 49-50.

DLC inappropriately attempts to extend the reach of the Commission's PECO decision to state that all costs and market forecasts presented in this proceeding must also be rejected because they do not meet the "known and measurable" standard. DLC Main Brief, p. 43. Duquesne's argument by extension is inherently flawed and must be rejected. Commission's decision in the PECO proceeding rests on two bases. DII Main Brief, pp. 49-50. First, the Commission's decision rests on the fact that future fossil decommissioning costs do not satisfy the Act's "known and measurable" requirement. Id. (citing PECO Restructuring Order, slip op. at 91-92 & Penn Sheraton Hotel v. Pennsylvania Public Utility Comm'n, 198 Pa. Super. 618 (1962)). Second, future fossil decommissioning costs are not recoverable under applicable PUC and appellate court precedent. Id. (citing Penn Sheraton). The cost must be both "known and measurable" and "traditionally . . . recoverable under a regulated environment" to qualify as a stranded cost under the Act. 66 Pa. C.S. § 2803. Because future fossil decommissioning expenses are not traditionally recoverable in a regulated environment, fossil decommissioning expense should be excluded from recovery as a stranded cost. The Company's claim for future fossil decommissioning expenses must be rejected.

E. Regulatory Assets and Liabilities

1. Introduction

In Main Brief, Duquesne modifies several of its regulatory asset claims. See DLC Main Brief, Regulatory Asset Table. These claims are modified from the Company's Exhibit DJC-10, the record evidence upon which DII relied in preparing the tables submitted with the DII Main Brief. Specifically, DLC's total regulatory asset claim changed from $489.82 million (pre-tax) to $462.8 million (pre-tax). See Appendix A, B & C, infra. As noted below, some of Duquesne's changes affect DII's recommendation. DII submits revised summary tables in Appendix A, B & C, infra, to reflect those changes.

2. Disputes Regarding Specific Claims

(a) SFAS 109 Deferred Taxes

As DII explains in its Main Brief, Duquesne appears to double count the SFAS 109 net plant regulatory asset in its original exhibits. See DII Main Brief, pp. 51-52. DLC does not address this issue in Main Brief. See DLC Main Brief, p. 45. Although it appears the Company eliminates the double recovery in Exhibit DJC-10, the Commission must ensure this actually occurs. DII Main Brief, p. 52.

(b) Unamortized Debt Costs

In its Main Brief, Duquesne re-quantifies the "pre-2005" portion of unamortized debt costs. See DLC Main Brief, Regulatory Asset Table. DII recommends complete denial of recovery for this claimed regulatory asset. DII Main Brief, pp. 53-55. The DII recommendation is not altered by the Company's re-quantification of its claim.

The Company states that the DII approach is inconsistent with the PECO decision and should be rejected. DLC Main Brief, p. 46. Interestingly, the Company cites to is own testimony, submitted prior to the issuance of the PECO decision, to support that claim. Id. Even the Company's citation to the PECO decision contained earlier in same paragraph (PECO Restructuring Order, slip op. at 76) does

not address the DII arguments against Duquesne's recovery of the unamortized debt costs (i.e., the cost is not "net" because the cost continues to be included in Duquesne's cost of debt). See DII Main Brief, pp. 53-55. The DII recommendation is reasonable and should be accepted.

(c) Unamortized Sale/Leaseback Premiums

Duquesne states that no party opposes recovery of the unamortized sale/leaseback premium associated with Beaver Valley No. 2. DLC Main Brief, p. 46. Although DII does not oppose recovery, the Company's original filing provides double recovery for these costs. See DII Main Brief, pp. 55-57. DII opposes the Company's double recovery of these costs. The revised exhibits appear to eliminate this possibility; however, the Commission must ensure that such double recovery does not occur. Id. at 56-57.

(d) Deferred Rate Synchronization Costs

Duquesne revises it claim for deferred rate synchronization costs to $25.37 million. See DLC Main Brief, Regulatory Asset Table. Duquesne's original claim was $33.43 million. See Duquesne Statement No. 2R, Exhibit DJC-10. DII recommends that the correct quantification, on a net present value basis, is $24.87 million. See DII Main Brief, pp. 57-58. Based on the information submitted with DLC's Main Brief, DII believes the difference between the DII recommendation and the DLC revised request is based on using a different amortization period. Because the Company's revised calculation is closer to the DII recommendation, DII accepts the Company's regulatory asset claim as recalculated in its Main Brief.[10]

(e) Deferred Employee Costs

DLC recalculates its claim for this regulatory asset in its Main Brief. See DLC Main Brief, Regulatory Asset Table. The new claim is $13.8 million. Id. This change is reflected on DII's revised summary tables in Appendix A, B & C, infra. As DII explains in its Main Brief, however, the

[10]The DII Regulatory Asset Table includes $210 thousand in deferred rate synchronization tax effect, for a total recommendation of $25.58 million. See Appendix A, B & C, infra.

Company's claimed stranded costs associated with deferred employee costs, valued at $17.8 million (or $13.8 million), should be disallowed. DII Main Brief, pp. 58-60. DLC objects to the proposed disallowance, but misstates DII's rationale. DLC Main Brief, p. 47.

The Company simplistically attributes DII's criticism of the regulatory asset claim to a "timing difference." DLC Main Brief, p. 47. The DII criticism is more detailed. Recovery should not be allowed because the Company will be compensated for the full value of this regulatory asset at a later date when the accounting reversal switches. DII Main Brief, p. 59. Consequently, the regulatory asset is not "stranded" as defined by the Competition Act, because the Company has not shown that the deferred employee costs will be unrecoverable in the competitive environment. 66 Pa. C.S. § 2803. In addition, deferred employee costs on an accrual basis have been inflated each year into the future and included as part of the Company's stranded generation cost quantification. DII Main Brief, p. 59-60. Because Duquesne will recover these costs as part of that stranded generation cost quantification, the regulatory asset is not a "net" electric cost and does not fulfill the statutory definition of a "stranded cost." 66 Pa. C.S. § 2803.

The Company's assertion in its Main Brief that all regulatory assets simply represent timing differences between accrual and cash recognition of expenses is inapt and fails to refute DII's comprehensive explanation of why these costs are neither "stranded" nor "net" costs consistent with the definition of stranded costs in the Act. See DLC Main Brief, p. 47. The Duquesne revised claim for recovery as a stranded cost of $13.8 million in deferred employee costs must be rejected.

(f) Deferred Coal Costs

DII recommends that the Company's claim for deferred coal costs be denied because the Company has not made the requisite showing that the future coal costs will be below market price. DII Main Brief, pp. 60-61. The Company attempts to refute this by claiming that the costs must fall below certain cost-based caps, not market-based caps. DLC Main Brief, p. 47. The Company submits no

additional evidence supporting its "interpretation" of the settlement document. DII submits that its recommendation to disallow recovery is correct and should be adopted.

(g) Deferred Caretaker Costs

As DII explained in its Main Brief, the Company claims recovery for $6.77 million (pre-tax) of deferred caretaker costs associated with the Bruno Island and Phillip plants. DII Main Brief, pp. 61-62. The Company claims that these costs are properly recoverable in this proceeding because the units are uneconomic and will not be returned to service. DLC Main Brief, p. 48.

However, the question of whether these costs are recoverable in this proceeding does not turn on whether operation of those units have become uneconomic; rather, Duquesne fails to satisfy its burden of proving that the costs qualify under another part of the definition of "stranded cost" (i.e., Duquesne has not shown that the costs are traditionally recoverable in the regulated environment). DII Main Brief, pp. 61-62. In order for caretaker costs to be recoverable in the regulated environment, the Company must show that it will return these units to operation as it was required to show under the Commission's Order at Docket No. P-900485. Id. It has not done so. Consequently, the deferred caretaker costs do not qualify as stranded regulatory assets for recovery in this proceeding. 66 Pa. C.S. § 2803.

(h) Pre-Accrual of Nuclear Outages

Duquesne revises its claim for pre-accrued nuclear outage costs from $13.5 million to $17.6 million. See DLC Main Brief, Regulatory Asset Table. DII continues to recommend complete disallowance of this claim; however, the DII summary tables have been modified to reflect the Company's change.

Duquesne should be denied recovery of its claimed regulatory asset of $13.5 million (or $17.6 million) in pre-accrued nuclear outages resulting from the Company's unilateral accounting change for nuclear outage costs. DII Main Brief, p. 63. Recovery must be denied because no part of the deferral

is made unrecoverable because of the transition to a competitive market. Id. DLC fails to address the DII criticism in its Main Brief. DLC Main Brief, pp. 48-49. This regulatory asset claim should be denied.

(i) Transition Costs

Duquesne alleges that its transition cost claim relates only to restructuring proceeding and pilot program deferrals. See DLC Main Brief, p. 49. As DII explains, however, a portion of the transition cost claim relates to the Company's implementation of the CARS meter reading system. DII Main Brief, pp. 64-65. This claim is inappropriate because the Company also claims that the CARS system pays for itself with savings in other areas such as base operations and meter reading. Id. The portion of the Company claim associated with CARS must therefore be denied.

(j) SFAS 106 Deferred Costs

The Company revises its regulatory asset claim for SFAS 106 deferred costs from $2.47 million to $3.28 million. See DLC Main Brief, Regulatory Asset Table. DII continues to recommend complete disallowance of this claim. DII Main Brief, pp. 65-67.

First, because the accounting treatment will reverse in the future and cash outlays for post-retirement benefits will exceed the accrual amount reflected on the Company's books, the stranded regulatory asset is not a "net" cost that is properly claimable as a stranded regulatory asset under the Act. Id. at 65-66. In addition, the cost is not a "net" cost because it is included elsewhere in the DLC stranded cost claim (i.e., the excessive level of ratepayer recovery necessitated under the accrual method of accounting is embedded in Duquesne's stranded generation cost claims). Id. at 66 (citing DII Statement No. 3, p. 21.) Furthermore, because the accounting treatment will reverse in the future, the Company will be able to recover the claimed regulatory asset in the competitive market; consequently, the claim does not satisfy the Act's requirement that a stranded cost be one that will not be recoverable in the competitive environment. 66 Pa. C.S. § 2803. Contrary to the Company's assertion, DII does not

"misunderstand the nature of these expenses" (DLC Main Brief, p. 50); DII completely understands the nature of these expenses and recognizes that the costs do not qualify as stranded under the Act.

DII submits recovery for the SFAS 106 regulatory asset must be denied.

(k) Warwick Mine Costs

DII takes no position.

(l) Pilot Program/Customer Education Expense

DII takes no position.

(m) Compensated Absences

See "Deferred Employee Costs," supra.

(n) Injuries/Damages

See "Deferred Employee Costs," supra.

(o) Other

In its Main Brief, the Company also revises its regulatory asset claims for DOE decommissioning expense and deferred fuel costs. See DLC Main Brief, Regulatory Asset Table. Because DII does not challenge recovery for those regulatory assets, the DII summary tables have been modified to reflect the Company's new calculation.

3. Conclusion

Based on the arguments in the DII briefs and the adjustments made by the Company in its Main Brief, DII recommends recovery by Duquesne of $580.62 million (NPV at 12/31/98) in stranded regulatory assets. See DII Regulatory Asset Summary Table, Appendix A, infra. DII emphasizes, however, that the change in its recommendation is necessitated only by the Company's revision of its claims included in its Main Brief.

F. Recovery of Stranded Costs

1. Introduction

As DII explains fully in its Main Brief, only a just and reasonable level of stranded costs can be recovered from ratepayers. DII Main Brief, p. 68. To arrive at that just and reasonable level, Duquesne's mitigation efforts (including possible securitization) and a sharing of stranded costs between ratepayers and shareholders (through an equity return disallowance) must be considered. Id.

2. Proposals To Adjust the Level of Stranded Cost Recovery

(a) Mitigation

DII takes no position on Duquesne's claimed mitigation efforts except to the extent those efforts are incomplete because the Company has not studied the possible benefits to ratepayers of securitization of the Company's stranded costs. DII Main Brief, pp. 68-69.

(b) Sharing of Stranded Costs (OCA and DII)

DII recommends that an "equity return disallowance" be applied to Duquesne's generation-related stranded costs in order to arrive at a level that is just and reasonable to recover from ratepayers. DII Main Brief, pp. 69-70. The Company advances four arguments against the application of any type of sharing of stranded costs. DLC Main Brief, pp. 52-55. Each argument is baseless.

First, the Company claims that there is no support in the Act for any type of sharing of stranded cost. Id. at 53. The Company claims that the sole consideration set forth in the Act regarding the level of stranded cost recovery is mitigation. Id. As DII explains, the Act clearly states that only a just and reasonable level of stranded generation-related costs are recoverable from ratepayers to the CTC. See DII Main Brief, pp. 27-28. Although mitigation is one element that the Commission is required by the Act to consider, the Commission has specifically recognized that it has the "discretion under Sections 2804(13) and (14) to disallow recovery of a portion of accurately quantified 2803(c)(3) stranded costs." PECO Restructuring Order, slip op. at 100. In addition, the Company admits that additional factors can

be analyzed in establishing stranded cost levels. Tr. at 57-58. DII submits that the Commission should use its discretion to disallow a portion of Duquesne's stranded generation-related costs.

Second, DLC claims that the DII proposal is not consistent with historic regulation for excess capacity in Pennsylvania. DLC claims that its witnesses' testimony on this point is unrebutted. DLC Main Brief, p. 53. DLC is mistaken. DII specifically addresses Mr. Marshall's assertion:

> **Q: Mr. Marshall indicates that he is unaware of any instance in past Pennsylvania proceedings where an economic excess capacity adjustment has been made based on a comparison between embedded cost and market prices. Do you believe that this is a valid criticism of your proposed sharing adjustment to arrive at a just and reasonable level of generation stranded cost for recovery form ratepayers?**
>
> A. No. The used and useful concept that I have discussed in my direct testimony is based on the ratemaking concept of economic excess capacity. Historically, in rate proceedings in which economic excess capacity has been an issue, the analysis compared embedded cost to the opportunity cost associated with a more economic alternative. For example, the life cycle cost of a nuclear unit would be compared to the life cycle cost of a combustion turbine to determine the present value "excess" costs associated with the investment in the nuclear unit. An economic excess capacity adjustment would then be based on the disallowance of all or a portion of the uneconomic amount of the investment being considered for ratemaking.
>
> **Q. Is a stranded cost analysis similar to an analysis of economic excess capacity?**
>
> A. Yes. The main difference in the stranded cost analysis is that the opportunity cost is the market price. In other words, a comparison is made between the cost of an investment (including operating cost) and the alternative or opportunity cost associated with market based pricing. In this manner, a stranded cost analysis is similar to an economic excess capacity analysis. DII's proposed sharing mechanism recognizes this underlying similarity and has relied on the used and useful standard as well as the Competition Act to arrive at a reasonable basis for sharing the stranded cost associated with DLC's generating units. The fact that the Commission has not disallowed a utility's investment or a cost based on a comparison of embedded cost to market prices does not change the fundamental nature of the used and useful principle, nor does it change the concept of an economic excess capacity evaluation based on opportunity cost.

DII Statement No. 1S, pp. 8-10. This situation is clearly analogous to the excess capacity situations in which an equity return disallowance has been used in the past. See, e.g., Pennsylvania Public Utility

Comm'n v. Pennsylvania Power & Light Co., Docket No. R-842651, Order entered on April 26, 1985, 59 Pa. P.U.C. 332, affirmed 101 Pa. Commw. 370 (1986) (disallowing return on common equity associated with Susquehanna Unit 2 because the unit was excess capacity). Therefore, the DII proposal is entirely consistent with historic regulation in Pennsylvania, notwithstanding DLC's claims to the contrary.

Third, the Company faults the DII sharing proposal as being "arbitrary." DLC Main Brief, p. 53. The DII proposal is not arbitrary because it does consider Duquesne's particular circumstances (i.e., Duquesne's debt structure). DII Statement No. 1, p. 19. Duquesne's debt structure is not an arbitrary rationale to strike the mandated sharing between ratepayers and shareholders. Instead of an equitable sharing the stranded costs, Duquesne would have ratepayers bear the full burden of the transition to a competitive market.

Fourth, the Company claims that the DII proposal violates state and federal law because it fails to maintain the financial health of the Company and because it represents an "opportunistic switching" in ratemaking standards. DLC Main Brief, pp. 54-55 (citing Duquesne Light Company v. Barasch, 488 U.S. 299 (1989)). DLC is misguided.

With respect to the financial impact on the Company, the Company admits that, in the end, the entire decision with respect to the stranded costs must be examined as a whole in order to determine its impact on the Company and on ratepayers. Tr. at 57-58. Ratemaking decisions traditionally have been reviewed with respect to the entire decision and not individual component parts. Barasch 488 U.S. at 310. In addition, the equity return disallowance does not represent opportunistic switching of ratemaking because the Commission's treatment of the Fort Martin sale came in the context of a settlement and not in the context of a litigated, Commission-decided proceeding. DII submits that the Company's arguments in this regard must be denied.

As DII explains, the Commission should employ the equity return disallowance as a reasonable

method to share stranded costs between shareholders and ratepayers. See DII Main Brief, pp. 69-70. Contrary to Company claims, a fair basis exists in law and fact to employ DII's sharing proposals.

(c) Securitization (DII Proposal)

DLC takes issue with the DII proposal that the Company use securitization as a final mitigation effort to minimize the stranded costs to be recovered from ratepayers. DLC Main Brief, pp. 55-56. Although DII acknowledges that the statute does not permit the Commission to force Duquesne to securitize debt, a consideration of securitization by the Commission is clearly part of its duty to ensure just and reasonable rates under the Act. 66 Pa. C.S. §§ 1301, 2804(13) & 2804(14). During the transition period, Duquesne has the duty to mitigate generation-related stranded costs to the extent practicable. 66 Pa. C.S. § 2808(4). The Act specifically recognizes the issuance of securitized debt as a possible avenue of mitigation of those generation-related stranded costs. Id. § 2808(4)(vi). Securitization reduces the amount that ratepayers must compensate Duquesne for its proven stranded costs. DII Main Brief, pp. 70-71. DLC admits that no detailed studies exist regarding the viability or necessity of securitizing its debt. Tr. at 242; Exhibit No. DJC-26. DLC should perform such studies to ensure that stranded cost recovery from ratepayers is minimized. DII respectfully requests that the PUC encourage DLC to securitize all or a portion of its stranded costs to fully mitigate stranded costs. See DII Main Brief, pp. 70-71.

3. Methods of Stranded Cost Recovery

(a) Accelerated Amortization Under Section 2804(4)(v) (Duquesne's ROE Spillover Proposal)

DII takes no position on Duquesne's accelerated amortization under Section 804(4)(v), 66 Pa. C.S. § 2804(4)(v), or the proposed ROE spillover mechanism.

(b) Immediate Rate Reductions (OCA Proposal)

DII urges the Commission to reject the OCA proposal for immediate rate reductions because it unreasonably extends the transition period and delays attainment of full competition. As discussed in

Section V.A.2.b, infra, the goal of the Act is to transition as quickly as possible. In addition, the OCA proposal is predicted on a CTC methodology that violates the rate cap for some customers (e.g., Interruptible Customers) in order to give reductions to other customers (e.g., Residual Customers). See DII Main Brief, pp. 75-78 & 80-83. This result is clearly not intended by the Act. 66 Pa. C.S. § 2802(7).

(c) Rate Cap/CTC Extension

The Company does not address rate cap or CTC extension in its Main Brief. See DLC Main Brief, p. 58. Apparently, the Company no longer requests extension of the CTC recovery period. See Duquesne Statement No. 2, p. 41. In the event that DLC still seeks such an extension, that extension must not be automatic and must be accompanied by a corresponding extension of the rate cap. DII Main Brief, pp. 72-73.

(d) Other Proposals

None.

4. Other Arguments Regarding Recovery of Stranded Costs

None.

5. Conclusion

In establishing DLC's level of recoverable stranded cost, the Commission must address securitization by the Company and the sharing of stranded costs between ratepayers and shareholders through a mechanism such as the DII equity return disallowance. See DII Main Brief, p. 74.

G. Conclusion

DII submits that its stranded cost recommendation is the most reasonable proffered by the Parties and should be accepted. The Commission must establish a definitive level of stranded costs in this proceeding. DII's use of asset value methodology to compute DLC's stranded generation costs is appropriate. In addition, DII's regulatory asset recommendation adheres to the dictates of the Act.

Based on these methodologies, DII calculates DLC's total stranded generation cost to be $1.618 billion (jurisdictional). See Appendix A, infra. A just and reasonable portion of that amount to recover from ratepayers is $1.386 billion. Id. See Appendix B & C, infra.

V. THE COMPETITIVE TRANSITION CHARGE

A. Conceptual Disputes Regarding Calculation of CTC/CGC

1. Differences in Overall Approach (e.g., CTC or CGC as Residual; OCA Proposal)

The Company claims that Section 2804(4)(v) of the Act requires that both the CTC residual methodology and the Company's variable CTC charge be adopted by the Commission. DLC Main Brief, pp. 60-62. Although DII agrees with the Company's use of the CTC residual methodology (the Company refers to this as the "top down" approach), DII submits that Section 2804(4)(v) does not mandate acceptance of the Company's variable CTC methodology.

Section 2804(4)(v) states as follows:

> If an electric distribution utility rolls its energy cost rate into base rates at a combined level that does not exceed its combined level of such rates which have been approved by the Commission as of the effective date of this chapter, the utility shall not be required to reduce its capped rates below the capped level upon the complaint of any party if the Commission determines that any excess earnings achieved under the cap are being utilized to mitigate transition or stranded costs for the benefit of ratepayers or to offset other known and measurable cost increases that would be recoverable under traditional ratemaking but are not included within the capped rates.

66 Pa. C.S. § 2808(4)(v). This Section does not require, as Duquesne suggests, that the Company be guaranteed recovery of its full capped rate level throughout the transition period. Instead, the provision simply requires that once Duquesne's rates are set in this proceeding, a complaint cannot be successfully sustained against the capped rates unless certain circumstances occur. Specifically, the complainant must show that any excess earnings achieved under the cap are not being utilized to mitigate transition or stranded cost, or, to offset other known and measurable cost increases. The Company misconstrues this Section of the Act.

DII addresses the OCA and OSBA proposals, infra.

2. Other Conceptual Disputes

(a) CGC Calculation: Annual Adjustments v. Fixed Schedule

The Company proposes to determine the yearly CTC based on an annual reverse-RFP for the sale of a block of firm power. DLC Main Brief, pp. 62-64. The Company's proposal is inappropriate because it will hinder development of a competitive market and because it is inconsistent with the Commission precedent in the PECO proceeding. DII Main Brief, pp. 78-80. The Company's apprehensions regarding the fair establishment of CTC customer class responsibility are misguided. The Company's proposal must be rejected. DII submits that a fixed schedule of CTC charges must be established in this proceeding. Id.

(b) Determination of Class Responsibility for Stranded Costs

The OCA and OSBA object to DII's proposal to determine class responsibility for stranded costs via use of the CTC residual methodology. OSBA Main Brief, pp. 17-21; OCA Main Brief, pp. 66-67.

The OCA and OSBA object to the DII proposal on two general bases. First, they object to the DII proposal on the basis that it represents an interclass cost shift. OSBA Main Brief, p. 18; OCA Main Brief, p. 66. Second, OSBA objects to the DII proposal because it accelerates recovery of stranded costs rather than providing for immediate rate reductions. OSBA Main Brief, pp. 17-19. Both of these arguments are misguided.

The DII proposal does not shift interclass cost responsibility. DII proposes to allocate stranded cost recovery to classes based on a CTC residual methodology. DII Main Brief, pp. 80-82 & 87. The CTC residual methodology subtracts an expected market price from the capped generation component of current rates to determine CTC responsibility. Id. The OSBA objects to the DII proposal using the following argument:

> This method is inappropriate since the available margin that a class exhibits under the generation rate cap is the function of its current rates. Those classes which implicitly

> pay larger "premiums" for generation should receive greater benefits from direct retail access. This follows from the premise that competition will eliminate all generation premiums paid by ratepayers. If, however, generation premiums are used to amortize Duquesne's stranded costs as quickly as possible (as is the case in the DII proposal), an interclass shift of CTC cost responsibility from low premium to high premium classes would result, effectively denying the latter classes their proportionate share of the benefits during the period of stranded cost recovery.

OSBA Main Brief, p. 18 (citations omitted). OSBA's argument is flawed in two respects.

First, the OSBA (and OCA) are incorrect that so-called lower premium rate classes should face a lower CTC responsibility. If regulation continued, Duquesne would collect less revenue per kWh from lower premium rates than from higher premium rates. In some cases, this lower premium is because alternative supply possibilities exist, such as a customer switching to fuel oil. In other cases, the lower premium exists because of a specified usage constraint in the rates (such as interruptible service) or because of a higher load factor usage by customers on that rate schedule. By permitting the lower premium classes to access the competitive market, Duquesne loses the revenue difference between the current capped generation component of those class rates and whatever price Duquesne can obtain for the sale of the same amount of load that the former low premium customers used. Under the DII proposal, each customer class is responsible for this difference between the current capped rate and the price that Duquesne can obtain on the open market for sale of the same electricity, which Duquesne's true "stranded cost" caused by that class's access to competitive supply. DII Main Brief, pp. 80-82.

Second, although OSBA is correct that competition is expected to eliminate some of the differences in class premiums, this will occur only after the CTC is eliminated and all customers can purchase electricity freely on the market. After these premiums are eliminated, customers in the former "higher premium" classes will receive greater long-term benefits from competition. Assuming the alleged "premiums" are artificially created because of the lack of competition, the "higher premium" rate classes will gain savings in the amount of that premium when full competition is realized; the "lower premium" will logically gain less savings. Consequently, it is appropriate for higher premium classes

to bear a proportionately higher share of the CTC responsibility.

OSBA also faults the DII proposal for not providing immediate rate reductions. OSBA Main Brief, pp. 17-19. OSBA states "an extension of the time period for stranded cost recovery could provide all ratepayers with an immediate (1999) rate reduction, independent of their eligibility in the phase-in process; a reduction which would not be available under an 'accelerated' amortization proposal such as DII." OSBA Main Brief, pp. 17-18 (citations omitted). The OSBA argument is short-sighted. The Commission recognized in the PECO proceeding that stranded cost recovery is a significant interference in the operation of the competitive market. PECO Restructuring Order, slip. op. at 15. If OSBA truly believes that competition will eliminate the premiums that exists between class rates, then OSBA should logically desire to eliminate any interference with the competitive market as soon as possible. OSBA appears content to sacrifice the longer term development of a robust competitive market for an immediate quick fix in the form of rate reductions. OSBA is misguided.

In addition, the Act clearly contemplates that stranded cost recovery be terminated as quickly as possible: "The competitive transition charge shall be included on bills to customers for a period not to exceed nine years from the effective date of this chapter unless an alternative payment methodology is mutually agreed upon by the customer and the utility or unless the Commission in its discretion and for good cause shown orders an alternative payment period." 66 Pa. C.S. § 2808(b). In addition, the rate caps provided by the Act apply for a specified time "or until an electric distribution utility is no longer recovering its transition or stranded costs through a competitive transition charge or intangible transition charge . . . whichever is shorter . . . ." Id. §§ 2804(4)(i) & (ii). The Act specifically acknowledges and requires that the CTC recovery period be accomplished as quickly as possible.

As DII explains fully in its Main Brief, the DII proposed CTC residual methodology appropriately allocates stranded cost responsibility classes in a manner that is both consistent with the utility's last base rate case and that does not affect inter-class cost shifting. See DII Main Brief, pp. 75-

87. The DII proposal fulfills both requirements of Section 2808(a) of the Act. The OSBA and OCA, in their attempt to adhere blindly to the production capacity allocator, submit proposals that promote interclass cost shifting and violate the rate cap. The OCA and OSBA proposals to determine stranded cost responsibility on a customer class basis must be rejected.

(c) Levelized CTC v. Other Methods

As DII explains in its Main Brief, use of a levelized CTC may hinder participation in the competitive market in the later years of the transition period if the levelized CTC plus the market price exceed the generation rate cap. See DII Main Brief, pp. 82-83. The OCA addresses its proposal for a levelized rate reduction with a declining (not levelized) CTC in this portion of its brief. OCA Main Brief, p. 62. As DII shows, however, the OCA proposal violates the rate cap for some customer classes and must be rejected. See DII Main Brief, pp. 75-83 & 86-87. Both a pure "levelized" CTC approach and the OCA's approach are inappropriate and should be rejected.

(d) Duquesne's Rate Redesign Proposal

Duquesne expends considerable effort to justify its rate redesign proposal (which it has now made optional). DLC Main Brief, pp. 65-68. As DII illustrates, the DLC proposal is clearly inappropriate because it amounts to a "take-or-pay" charge for 50% of a customer's stranded cost. DII Main Brief, pp. 83-85. This take-or-pay liability significantly reduces (if not eliminates) any risk that Duquesne could not recover that amount of stranded cost in the fixed portion of the rate. Id. The DLC proposal is clearly inappropriate and must be rejected.

(e) Other Conceptual Disputes

OCA proposes that the statutory annual reconciliation of the CTC must be done on a class-specific basis. OCA Main Brief, pp. 68-69. DII acknowledges that the Commission adopted this approach in the PECO decision. DII continues to believe, however, that it is not appropriate to reconcile and track stranded cost on a class specific basis. DII Statement No. 1, pp. 31. Tracking and

reconciliation on a class basis will lead to different CTC termination times for each customer class. This does not result in an orderly transition to competition as required by the Act. See 66 Pa. C.S. § 2804(14). DII respectfully requests that the OCA proposal be rejected.

B. Other Disputes Regarding Specific Proposals

DII expresses its objections to the CTC proposals of the OCA and DLC in its Main Brief and in other sections of this Reply Brief. See DII Main Brief, pp. 75-89 & Section V.A, supra. Consequently, DII will not repeat its criticisms contained therein. The DII- proposed CTC residual methodology, in which the yearly CTC is fixed in this proceeding based on projected market price, is clearly the most reasonable proposal and should be accepted by the Commission.

C. Other Issues Addressed in PECO Order

In its Main Brief, DII proposes a tracking mechanism to reconcile Duquesne's stranded cost recovery. See DII Main Brief, pp. 87-88. No other major party submits a similar proposal. See DLC Main Brief, pp. 71-72; OCA Main Brief, pp. 63-69; OSBA Main Brief, pp. 17-21.

D. Conclusion

As DII explains in its Main Brief, the DII-proposed, fixed CTC residual methodology is reasonable, consistent with the Act, and should be accepted by the Commission. See DII Main Brief, pp. 75-89. Only the DII proposal ensures that rate caps are not violated, costs are not shifted, and all customer classes have a realistic opportunity to participate in the competitive market during each year of the transition period. The proposals submitted by DLC, OCA and OSBA are inadequate and must be rejected.

VI. RATE OF RETURN/DISCOUNT RATE

DII takes no position on this issue.

VII. SPECIAL CUSTOMER CLASSES

A. Rule 4 Contracts

Duquesne refuses to unbundle Rule 4 Contracts and permit those customers to have access to competitive generation supply. See DLC Main Brief, pp. 76-77. Duquesne's selective quotation of the PECO restructuring decision in this regard must be rejected. Id. at 76. The PECO order clearly states:

> We conclude that PECO should unbundle existing contracts for customers not prohibited from shopping based on the same guidelines as we have provided for interruptible customers.

PECO Restructuring Order, slip op. at 120. PECO proposed (and the Commission accepted) the following treatment for special contracts: "Existing customers under contracts that are silent concerning future opportunities to chose competitive suppliers will be permitted to enter into separate generation contracts." Id. at 119. In other words, the correct interpretation of the PECO Order is that, unless a contract specifically prohibits unbundling and access to competitive supply, that contract must be unbundled and the customer must have the opportunity to obtain competitive supply. DII Main Brief, pp. 89-90. The DLC interpretation of the PECO precedent is flawed.

In its Main Brief, Enron suggests that Duquesne should be forced to fulfill only the non-generation portions of its Rule 4 contracts. Enron Main Brief, pp. 31-33. Enron misconstrues the PECO decision as requiring that any generation-related competitive rate or rider, currently offered by Duquesne, can no longer be offered in a competitive environment; rather, the PECO decision mandates that Duquesne must unbundle those rates in order to provide customers with the opportunity for direct access. PECO Restructuring Order, slip op. at 119-20. Customers' right to direct access is guaranteed in the PECO decision and under the Act, not the alternative suppliers' right to prevent Duquesne from serving customers under its tariff in effect as of January 1, 1997. Moreover, as DII explains in its Main Brief, it is not only possible but mandatory that Duquesne unbundle Rule 4 Contracts. See DII Main Brief, at pp. 89-90.

B. Riders 8 and 20

Duquesne proposes to phase out the availability of Riders 8 and 20 to existing customers as contracts expire. DLC Main Brief, pp. 77-78. DII objects to this proposed phase-out because all tariff offerings in place as of January 1, 1997, (including Riders 8 and 20) must remain available throughout the transition period. DII Main Brief, pp. 90-92. In response to the DII argument, Duquesne states that the riders are unnecessary because Duquesne's proposed rate redesign will accomplish the same objective for incremental usage. DLC Main Brief, pp. 77-78. The Company is misguided.

The Commission's Order in the PECO restructuring proceeding specifically requires that: "All existing tariffs shall remain available through the transition period, and all special contracts shall remain in force, except as modified pursuant to this Opinion and Order or other tariff modifications approved by the Commission." PECO Restructuring Order, slip op. at 117. See also DII Main Brief, pp. 90-92. PECO is required to continue to offer its Economic Efficiency Rider to existing customers (Id.); Duquesne should be required to do the same.[11]

Moreover, the Company claims that continuing availability of the riders will provide customers with "a discount on a discount." DLC Main Brief, p. 78. This assertion only applies (if it applies at all) when customers take advantage of DLC's rate redesign proposal, which is now optional. Furthermore, it is illogical to call economic efficiency riders to existing customers as a "discount on a discount" without also calling the economic development riders that will be available to new customers the same. The Company's purported rationale is baseless and must be rejected.

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[11]Duquesne supports the elimination of these riders based on the availability of its proposed rate redesign. DLC Main Brief, p. 77-78. The availability of this optional redesign is irrelevant. The Act clearly requires that all current tariff offerings continue to be provided throughout the transition period. If the rate redesign truly satisfies the same goals as the economic development riders, then the customers on those riders will logically and naturally take advantage of the rate redesign. However, DII submits that the decision to switch from the development rider to the rate redesign must be the customer's and the existing tariff riders must remain in effect.

C. Self-Generation

DII takes no position on self-generation.

D. Other Tariff-Related Issues

DII addresses three other tariff-related issues related to Interruptible Service, Time of Day Service and Generation Avoidance energy. DII Main Brief, pp. 93-95. These issues involve inappropriate restrictions on the availability of Interruptible Service and Time of Day Service and the elimination of the Generation Avoidance provision from the HVPS tariff rate. Id. Duquesne fails to address DII's "other tariff-related issues." DLC Main Brief, p. 78. DII urges the PUC to ensure that all Duquesne tariff offerings remain in tact throughout the transition period.

VIII. COMPETITIVE SAFEGUARDS

DII supports all Commission efforts to ensure a level playing field for all market participants.

IX. DUTY TO SERVE

The Commission must not eliminate the statutory right of all customers to return to service from DLC at the capped rate levels specified in the Act during the transition period. 66 Pa. C.S. § 2804(4)(i) & (ii). As DII explains fully in other sections of this brief, and its Main Brief, the rate cap is a necessary consumer protection that must not be impinged. See, e.g., DII Main Brief, pp. 43-44 & 75.

X. UNIVERSAL SERVICE AND ENERGY CONSERVATION

A. Introduction

The Act requires that Universal Service protections continue in the competitive market. 66 Pa. C.S. § 2802(10). DII agrees that such programs should continue to exist.

B. Overall Funding and Rate Issues

1. Eligibility and Funding Levels

DII takes no position on the eligibility and funding levels for universal service.

2. Cost Allocation and Rate Redesign

Several parties object to Duquesne's proposal to allocate universal service and energy conservation cost recovery based on the manner in which those costs are embedded in current class rates. Specifically, OTS recommends the use of a uniform customer charge to recover these costs. OTS Main Brief, pp. 88-90. OCA recommends that universal service cost responsibility be assigned to classes based on a non-production revenue allocator. OCA Main Brief, pp. 84-86. As DII explains in its Main Brief, the Company has properly allocated universal service costs to each rate class for recovery and the OCA and OTS proposals should be rejected. DII Main Brief, pp. 96-98. The Commission has consistently stated that universal service cost recovery must be allocated consistent with the utility's prior rate case allocations of those costs. Guidelines for Universal Service and Energy Conservation Programs Made Pursuant to 66 Pa. C.S. § 2803, § 2802(17), 2804(8) and 2804(9), Docket No. M-960890F00010, Order entered on July 11, 1997, slip op. at 20; PECO Restructuring Order, slip op. at 146. The rate cap and anti-cost shifting provisions in the Act mandate that, as Duquesne's rates are unbundled into components (including the component previously used to support universal service costs), those cost allocations must be maintained. 66 Pa. C.S. § 2808(a) & 2804(7).

Both OCA and OTS opine that relying on the allocations in current rates (as established in the last base rate case) inappropriately results in the residential class bearing most of the costs of these programs. OTS Main Brief, pp. 88-89 & OCA Main Brief, pp. 84-86. These parties view the DII (and OSBA) arguments for allocation consistent with the last base rate allocation as attempts to avoid responsibility for providing social support to the ratepayers in the Duquesne service territory. The OCA and OTS arguments are baseless and misguided.

First, the Act clearly requires that universal service costs be allocated in a manner consistent with the last base rate proceeding. In PECO's restructuring proceeding, the Commission allocated PECO's universal service costs solely to residential customers because the costs were allocated solely

to residential customers in PECO's last base rate proceeding. PECO Restructuring Order, slip op. at 146. As DII witness Baron illustrates, this result follows sound costs of service ratemaking principles. See DII Statement No. 1-R, pp. 7-8.

Second, businesses and industry in the Duquesne service territory contribute to remedying "social problems" in many other ways beyond paying a subsidy for the electricity costs of low income ratepayers. OTS Main Brief, p. 89. Businesses contribute to the well-being of the community by providing jobs and, in some cases, by providing corporate donations to community organizations that far exceed the cost responsibility that will be placed on any single Duquesne ratepayer by allocating costs based on those embedded in the last base rate proceeding. OCA claims that there are "benefits to the system as a whole" that flow from the existence of energy conservation and universal service programs. OCA Main Brief, p. 685. For example, OCA notes that these programs promote economic stability. Id. at 85-86. No better contributor to the economic stability of the Duquesne service territory exists, however, than the continued operation and viability of businesses and industry. The imposition of a confiscatory energy tax for social programs as proposed by OCA undercuts the viability of businesses and eviscerates the free will of corporations to determine whether and to what extent they will participate in the community. This result is unwarranted under the Act which solely intends to provide all customers with fair and non-discriminatory access to generation supply. The Act is not intended to cure all social ills nor serve as a vehicle to shift costs.

Consistent with the Act and Commission precedent, the OCA and OTS arguments to shift cost responsibility for universal service and energy conservation costs must be rejected. DII recommends that the DLC proposed universal service cost recovery mechanism be accepted.

C. Specific Programs

DII is not addressing specific universal service programs.

D. Energy Conservation

DII is not addressing energy conservation.

XI. CUSTOMER EDUCATION

DII is not addressing customer education.

XII. MISCELLANEOUS ISSUES

The Environmentalists propose that uniform environmental standards should be imposed on all retail suppliers that sell electricity in Pennsylvania. Environmentalists Main Brief, pp. 65-66. This requirement is unnecessary and could hinder development of a robust competitive market. One of the goals of the Act is to provide businesses a cost-effective market in which to operate. 66 Pa. C.S. §§ 2802 (4)-(7). Businesses in Pennsylvania will not be provided with a cost-effective environment if restrictions are levied on electricity supply that surrounding states do not place on that supply. Moreover, the Commission cannot accurately assess the impacts of the ill-defined and potentially administratively-complex Environmentalists' proposal. The proposal must be rejected.

XIII. CONCLUSION

For the foregoing reasons, DII respectfully requests that the DII modifications to the Duquesne Light Company Restructuring Plan explained in this Reply Brief and the DII Main Brief be accepted by the Commission. As noted in its Main Brief, DII respectfully makes the following recommendations:

- The Commission must adopt a definitive level of stranded costs to be recovered through DLC's CTC. The Act and precedent mandate that this issue be decided in this proceeding.
- The Commission must establish DLC's stranded generation costs as part of this proceeding. This could be done through an immediate, full and unconditional auction of DLC's assets or through the application of a market price forecast. The DII forecast is reasonable and should be relied on.
- The Commission must reject DLC's delayed asset valuation proposals. In addition, DLC's range of market prices is inadequate to establish the Company's stranded generation costs.
- The Commission should adopt DII's well-reasoned and appropriate regulatory asset analysis.
- The Commission must reject DLC's future fossil decommissioning claim as contrary to

Commission precedent.

- The Commission must net DLC's nuclear decommissioning claim by offsetting it against nuclear decommissioning trust fund earnings.

- Stranded costs should be shared between ratepayers and shareholders. An appropriate method for this sharing is applying DII's equity return disallowance to stranded generation costs.

- DLC should securitize its authorized stranded costs as a final mitigation effort.

- The Commission must adopt the DII recommended "CTC residual" methodology. This methodology properly assigns stranded cost responsibility and will encourage the development of a robust competitive market.

- The Commission must reject DLC's proposed tariff change that limits the availability of Interruptible Service and Time of Day Service.

- The Commission must mandate that DLC unbundle "Rule 4" contracts to allow customers access to the competitive market.

- The Commission must mandate that DLC continue to offer economic development incentive rates to current customers through the transition period.

- The Commission must reject DLC's attempt to inflate inappropriately its monopoly transmission and distribution rates through using the Company's "required" rate of return and the inclusion of distribution losses and certain generation-related ancillary services in those rates.

- The Commission must adopt DII's accelerated phase-in proposal, in which over-subscription for any stage of direct access phase-in results in a pro-rata reduction of competitive load for all customers desiring participation in that phase.

WHEREFORE, the Duquesne Industrial Intervenors respectfully requests that the Commission modify Duquesne Light Company's restructuring plan consistent with the foregoing arguments.

Respectfully submitted,

McNEES, WALLACE & NURICK

By Pamela C. Polacek

David M. Kleppinger
James P. Dougherty
Pamela C. Polacek
100 Pine Street
Harrisburg, PA 17108-1166
(717) 232-8000
Counsel to the Duquesne Industrial Intervenors

Dated: February 17, 1998

APPENDIX A

REQUIRED SUMMARY TABLES
(REVISED)

Duquesne Light Company
Summary of DII Recommended
Stranded Costs (Revised)
($000)

	Company Claim	DII Adjustments	DII Recommendation/ Adjusted Amount
Nuclear	$934,390	(165,066) [1]	$769,324
Fossil	$607,260	(337,753)	$269,507
Regulatory Assets	$462,800	117,820 [1]	$580,620
Total Net Present Value (NPV) in 1999 $	$2,004,450	(384,999)	$1,619,451
PUC NPV in 1999$			$1,617,982 [2]
PUC Jurisdictional Percent			99.909% [3]

All items are stated on a pre-tax basis.

[1] A portion of these adjustments are due to the treatment of the Beaver Valley 2 lease expense. DII includes a portion of the Beaver Valley 2 lease expense in Regulatory Assets, while DLC includes all of the lease expense in Nuclear Generating stranded costs.

[2] In order to produce a just and reasonable level of stranded costs to be recovered from ratepayers, DII proposes an "equity return disallowance" which would reduce the Total Net Present Value in 1999 $ by $232,500,000 to $1,385,693,000. Tables in Appendix B and C contain a full presentation of the DII position including the equity return disallowance.

[3] Actual jurisdictional percentage is 99.9093%.

Duquesne Light Company
DII Recommended Stranded Cost Calculation - Nuclear
($000)

	Company Claim	DII Adjustments	DII Recommendation/ Adjusted Amount
a. Net Book Value	$788,590	(291,220)	$497,370 [1]
b. (Market Value)	($7,200)	236,195	$228,995 [2]
c. PV of Nuclear Decommissioning	$57,400	(14,441)	$42,959 [3]
d. PV of Costs Independent Operation	$95,600	n/a [4]	n/a [4]
e. **Net Present Value (NPV) in 1999 $ (a+b+c+d)**	$934,390	(165,066)	$769,324 [5]
Discount Rate	7.83%	-	7.83%
PUC Jurisdictional Percent	99.93%	-0.021%	99.909% [6]

All items are stated on a pre-tax basis.

[1] DII Statement No. 1, p. 10; Duquesne Statement No. 2-R, Exhibit No. DJC-21.
[2] DII Statement No. 2, Exhibit No. RJF-5.
[3] DII Statement No. 3, p. 31-33, Exhibit No. LK-5.
[4] These costs, net of incremental margins, were separated out by DLC in its rebuttal testimony. DII includes these costs and margins as part of the calculation of Market Value. Tr. at 547-551.
[5] DII proposes an equity return disallowance which would reduce the Nuclear Generation Stranded Costs by $165,580,000 to $599,744,000. See the tables in Appendix B for a full presentation of the DII position including the equity return disallowance.
[6] Actual jurisdictional percentage is 99.9093%.

Duquesne Light Company
DII Recommended Stranded Cost Calculation - Fossil
($000)

	Company Claim	DII Adjustments	DII Recommendation/ Adjusted Amount
a. Net Book Value	$448,360	33,400	$481,760 [1]
b. (Market Value)	($20,200)	(192,053)	($212,253) [2]
c. PV of Fossil Decommissioning	$66,500	(66,500)	$0 [3]
d. PV of Costs Independent of Operation	$112,600	n/a [4]	n/a [4]
e. **Net Present Value (NPV) in 1999$ (a + b + c + d)**	$607,260	(337,753)	$269,507 [5]
Discount Rate	7.83%	-	7.83%
PUC Jurisdictional Percent	99.93%	-0.021%	99.909% [6]

All items are stated on a pre-tax basis.

[1] DII Statement No. 1, p. 10; Duquesne Statement No. 2-R, Exhibit No. DJC-21.
[2] DII Statement No. 2, Exhibit No. RJF-5.
[3] DII Statement No. 3, pp. 26-30; DII Statement No. 3-S, pp. 24-25.
[4] These costs, net of incremental margins, were separated out by DLC in its rebuttal testimony. DII includes these costs and margins as part of the calculation of Market Value. Tr. at 547-551.
[5] DII proposes an equity return disallowance which would reduce the Fossil Generation Stranded Costs by $62,920,000 to $206,587,000. See the tables in Appendix B for a full presentation of the DII position including the equity return disallowance.
[6] *Actual jurisdictional percentage is 99.9093%.*

Duquesne Light Company
DII Recommended Stranded Cost Calculation (Revised)
Regulatory Assets
($000)

	Company Claim [1]	DII Adjustments	DII Recommendation/ Adjusted Amount[2]
a. Regulatory Tax Receivable	236,480	0	236,480
b. Post-2005 Unamortized Debt Costs	29,920 [5]	-29,920	0
c. Pre-2006 Unamortized Debt Costs	16,760	-16,760	0
d. Deferred Rate Synchron Costs	25,580 [6]	0	25,580 [6]
e. Deferred Employee Costs	13,830 [7]	-13,830	0
f. Deferred Nuclear Maintenance	3,250	0	3,250
g. DOE Decommissioning	5,580 [7]	0	5,580 [7]
h. Deferred Coal Costs	13,500	-13,500	0
i. Deferred Caretaker Costs	6,770	-6,770	0
j. BV2 Training Costs	2,420	0	2,420
k. Low Level Radioactive Waste	2,270	0	2,270
l. Coal Cost Equalization	120	0	120
m. Pre-Accrued Nuclear Outages	17,600 [7]	-17,600	0
n. FAS 106 Deferral	3,280 [7]	-3,280	0
o. Deferred Fuel Costs	11,510 [7]	0	11,510 [7]
p. Other Regulatory Assets			
1. Beaver Valley Lease	0	227,780	227,780
2. Other	700	0	700
q. BV2 Sale/Leaseback Premium			0
r. Gain on Sale/Leaseback Tax Effect	55,130	0	55,130
s. Deferred Rate Synchr Tax Effect			n/a [3]
t. Beaver Valley 2 Tax Effect			n/a [4]
u. SFAS 109 Plant	0	0	0
v. Other Transition Expenses	18,100	-8,300	9,800
w. **Net Present Value (NPV) in 1999 $ (Sum of a. to v.)**	462,800	117,820	580,620
PUC Jurisdictional Percent	99.93%	-0.021%	99.909% [8]

Notes:

All items are stated on a pre-tax basis.

[1] The Company's claim amounts are based upon the Company's position as stated in its Main Brief and. the Company's Exhibits DJC-10 (after tax basis) and DJC-15 (pre-tax basis). DII's adjustments have been restated to be consistent with the revised Company claim.

[2] DII Statement No. 3, pp. 6-25; DII Statement No. 3-S, pp. 6-23; DLC Main Brief, Regulatory Asset Table.

[3] Treated as part of "Deferred Rate Synchronization Costs" regulatory asset listed at f. above.

[4] Treated as part of "Other" regulatory assets listed at p.2. above.

[5] DII's main brief included an amount for Beaver Valley 2 Lease Premium in this item. The Company is evidently not now claiming the Beaver Valley 2 Lease Premium as a regulatory asset.

[6] The Company's original claim was stated on a nominal basis, while the revised claim is on a net present value (NPV) basis. Although DII's restatement of the claim was slightly different due to the amortization period ($24.870 million), DII accepts the Company's quantification of the NPV. DII has included the $0.210 million in deferred rate synchronization (tax) effect in this line item.

[7] The Company's original claim was on a nominal basis, while the revised claim is on an NPV basis.

[8] Actual jurisdictional percentage is 99.9093%.

APPENDIX B

SUMMARY TABLES INCLUDING EQUITY RETURN DISALLOWANCE (REVISED)

Duquesne Light Company
Summary of DII Recommended
Stranded Costs Including Equity Return Disallowance (Revised)
($000)

	Company Claim	DII Adjustments	DII Recommendation/ Adjusted Amount
Nuclear	$934,390	(334,646) [1]	$599,744
Fossil	$607,260	(400,673)	$206,587
Regulatory Assets	$462,800	117,820 [1]	$580,620
Total Net Present Value (NPV) in 1999 $	$2,004,450	(617,499)	$1,386,951
PUC NPV in 1999$			$1,385,693
PUC Jurisdictional Percent			99.909% [2]

All items are stated on a pre-tax basis.

[1] A portion of these adjustments are due to the treatment of the Beaver Valley 2 lease expense. DII includes a portion of the Beaver Valley 2 lease expense in Regulatory Assets, while DLC includes all of the lease expense in Nuclear Generating stranded costs.

[2] Actual jurisdictional percentage is 99.9093%.

Duquesne Light Company
DII Recommended Stranded Cost Calculation - Nuclear
($000)

	Company Claim	DII Adjustments	DII Recommendation/ Adjusted Amount	
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b. (Market Value)	($7,200)	236,195	$228,995	[2]
c. PV of Nuclear Decommissioning	$57,400	(14,441)	$42,959	[3]
d. PV of Costs Independent Operation	$95,600	n/a	n/a	[4]
e. **Net Present Value (NPV) in 1999 $ (a+b+c+d)**	$934,390	(165,066)	$769,324	
f. Equity Return Disallowance	$0	(169,580)	($169,580)	[5]
g. **Net Present Value (NPV) in 1999 $ with Disallowance (e+f)**	$934,390	(334,646)	$599,744	
Discount Rate	7.83%	-	7.83%	
PUC Jurisdictional Percent	99.93%	-0.021%	99.909%	[6]

All items are stated on a pre-tax basis.

[1] DII Statement No. 1, p. 10; Duquesne Statement No. 2-R, Exhibit No. DJC-21.
[2] DII Statement No. 2, Exhibit No. RJF-5
[3] DII Statement No. 3, pp. 31-33, Exhibit No. LK-5.
[4] These costs, net of incremental margins, were separated out by DLC in its rebuttal testimony. DII includes these costs and margins as part of the calculation of Market Value. Tr. at 547-551.
[5] DII Statement No. 1, pp. 9-12, Exhibit No. SJB-3.
[6] Actual jurisdictional percentage is 99.9093%.

Duquesne Light Company
DII Recommended Stranded Cost Calculation - Fossil
($000)

	Company Claim	DII Adjustments	DII Recommendation/ Adjusted Amount
a. Net Book Value	$448,360	33,400	$481,760 [1]
b. (Market Value)	($20,200)	(192,053)	($212,253) [2]
c. PV of Fossil Decommissioning	$66,500	(66,500)	$0 [3]
d. PV of Costs Independent Operation	$112,600	n/a	n/a [4]
e. **Net Present Value (NPV) in 1999 $ (a+b+c+d)**	$607,260	(337,753)	$269,507
f. Equity Return Disallowance	$0	(62,920)	($62,920) [5]
g. **Net Present Value (NPV) in 1999 $ with Disallowance (e+f)**	$607,260	(400,673)	$206,587
Discount Rate	7.83%	-	7.83%
PUC Jurisdictional Percent	99.93%	-0.021%	99.909% [6]

All items are stated on a pre-tax basis.

[1] DII Statement No. 1, p. 10; Duquesne Statement No. 2-R, Exhibit No. DJC-21.
[2] DII Statement No. 2, Exhibit No. RLF-5.
[3] DII Statement No. 3, pp. 26-30; DII Statement No. 3-S, pp. 24-25.
[4] These costs, net of incremental margins, were separated out by DLC in its rebuttal testimony. DII includes these costs and margins as part of the calculation of Market Value. Tr. at 547-551.
[5] DII Statement No. 1, pp. 9-12, Exhibit No. SJB-3.
[6] Actual jurisdictional percentage is 99.9093%.

Duquesne Light Company
DII Recommended Stranded Cost Calculation (Revised)
Regulatory Assets
($000)

	Company Claim [1]	DII Adjustments	DII Recommendation/ Adjusted Amount[2]
a. Regulatory Tax Receivable	236,480	0	236,480
b. Post-2005 Unamortized Debt Costs	29,920 [5]	-29,920	0
c. Pre-2006 Unamortized Debt Costs	16,760	-16,760	0
d. Deferred Rate Synchron Costs	25,580 [6]	0	25,580 [6]
e. Deferred Employee Costs	13,830 [7]	-13,830	0
f. Deferred Nuclear Maintenance	3,250	0	3,250
g. DOE Decommissioning	5,580 [7]	0	5,580 [7]
h. Deferred Coal Costs	13,500	-13,500	0
i. Deferred Caretaker Costs	6,770	-6,770	0
j. BV2 Training Costs	2,420	0	2,420
k. Low Level Radioactive Waste	2,270	0	2,270
l. Coal Cost Equalization	120	0	120
m. Pre-Accrued Nuclear Outages	17,600 [7]	-17,600	0
n. FAS 106 Deferral	3,280 [7]	-3,280	0
o. Deferred Fuel Costs	11,510 [7]	0	11,510 [7]
p. Other Regulatory Assets			
1. Beaver Valley Lease	0	227,780	227,780
2. Other	700	0	700
q. BV2 Sale/Leaseback Premium			0
r. Gain on Sale/Leaseback Tax Effect	55,130	0	55,130
s. Deferred Rate Synchr Tax Effect			n/a [3]
t. Beaver Valley 2 Tax Effect			n/a [4]
u. SFAS 109 Plant	0	0	0
v. Other Transition Expenses	18,100	-8,300	9,800
w. **Net Present Value (NPV) in 1999 $ (Sum of a. to v.)**	462,800	117,820	580,620
PUC Jurisdictional Percent	99.93%	-0.021%	99.909% [8]

Notes:

All items are stated on a pre-tax basis.

[1] The Company's claim amounts are based upon the Company's position as stated in its Main Brief and. the Company's Exhibits DJC-10 (after tax basis) and DJC-15 (pre-tax basis). DII's adjustments have been restated to be consistent with the revised Company claim.

[2] DII Statement No. 3, pp. 6-25; DII Statement No. 3-S, pp. 6-23; DLC Main Brief, Regulatory Asset Table.

[3] Treated as part of "Deferred Rate Synchronization Costs" regulatory asset listed at f. above.

[4] Treated as part of "Other" regulatory assets listed at p.2. above.

[5] DII's main brief included an amount for Beaver Valley 2 Lease Premium in this item. The Company is evidently not now claiming the Beaver Valley 2 Lease Premium as a regulatory asset.

[6] The Company's original claim was stated on a nominal basis, while the revised claim is on a net present value (NPV) basis. Although DII's restatement of the claim was slightly different due to the amortization period ($24.870 million), DII accepts the Company's quantification of the NPV. DII has included the $0.210 million in deferred rate synchronization (tax) effect in this line item.

[7] The Company's original claim was on a nominal basis, while the revised claim is on an NPV basis.

[8] Actual jurisdictional percentage is 99.9093%.

APPENDIX C

DII STRAND COST RECOMMENDATION: SUMMARY OF ADJUSTMENTS (REVISED)

Summary of Adjustments (Revised)

	Company Claim	DII Adjusted Amount
Recoverable Regulatory Assets		
Regulatory Tax Receivable	236,480	236,480
Post-2005 Unamortized Debt Costs	29,920	0
Pre-2006 Unamortized Debt Costs	16,760	0
Deferred Rate Synchron Costs	25,580	25,580
Deferred Employee Costs	13,830	0
Deferred Nuclear Maintenance	3,250	3,250
DOE Decommissioning	5,580	5,580
Deferred Coal Costs	13,500	0
Deferred Caretaker Costs	6,770	0
BV2 Training Costs	2,420	2,420
Low Level Radioactive Waste	2,270	2,270
Coal Cost Equalization	120	120
Pre-Accrued Nuclear Outages	17,600	0
FAS 106 Deferral	3,280	0
Deferred Fuel Costs	11,510	11,510
Other Regulatory Assets		
BV Lease	0	227,780
Other	700	700
BV2 Sale/Leaseback Premium	0	0
Gain on Sale/Leaseback Tax Effect	55,130	55,130
Deferred Rate Synchr Tax Effect	0	n/a
Beaver Valley 2 Tax Effect	0	n/a
SFAS 109 Plant	0	0
Other Transition Expenses	18,100	9,800
Subtotal	462,800	580,620
Offsetting Regulatory Liabilities	0	0
Subtotal of Regulatory Assets and Liabilities	462,800	580,620
Non-Utility Generating Contracts	0	0
Nuclear Decommissioning Expense	57,400	42,959
TOTAL Section 2808(c)(1) and (2) STRANDED COSTS	520,200	623,579
Utility Generation		
Book Value	1,236,950	979,130
Less: Market Value	-180,800	-16,742
Total Stranded Generation Costs	1,417,750	995,872
Fossil Decommissioning Expense	66,500	0
Other Transition Costs Disallowance	0	-232,500
TOTAL RECOVERABLE STRANDED COSTS	2,004,450	1,386,951
PUC Jurisdictional Amount [1]		1,385,693

[1] Jurisdictional percentage is 99.9093%.

CERTIFICATE OF SERVICE

I hereby certify that I am this day serving a true copy of the foregoing document upon the participants listed below in accordance with the requirements of Section 1.54 (relating to service by a participant).

VIA FIRST CLASS MAIL

John S. Moot, Esq.
Skadden, Arps, Slate, Meagher & Flom LLP
1440 New York Avenue NW
Washington DC 20005

Angela Jones, Esq.
Office of Small Business Advocate
Suite 1102, Commerce Building
300 North Second Street
Harrisburg, PA 17101

Kandace Melillo, Esq.
Wayne Scott, Esq.
Pennsylvania Public Utility Commission
Office of Trial Staff
901 Rear North 7th Street
P.O. Box 3265
Harrisburg, PA 17105-3265

Larry R. Crayne, Assistant General Counsel
Richard S. Herskovitz, Esq.
Duquesne Light Company
411 Seventh Avenue
P.O. Box 1930
Pittsburgh, PA 15230-1930

Irwin A. Popowsky, Esq.
Marisa A. Sifontes, Esq.
Steven K. Steinmetz, Esq.
Tad Berger, Esq.
Office of Consumer Advocate
1425 Strawberry Square
Harrisburg, PA 17120

David Hughes
4037 Ludwick Street
Pittsburgh, PA 15217

Jim Ferlo, Councilman
510 City-County Building
Pittsburgh, PA 15219

Scott J. Rubin, Esq.
IBEW System Council U-10
3 Lost Creek Drive
Selinsgrove, PA 17870

Timothy Moran
986 Greentree Road
Pittsburgh, PA 15220

Patricia Armstrong, Esq.
Thomas, Thomas, Armstrong & Niesen
Allegheny Electric Cooperative
212 Locust Street, Suite 500
P.O. Box 9500
Harrisburg, PA 17108-9500

Mary McFall Hopper, Esq.
PECO Energy Company
2301 Market Street S23-1
P.O. Box 8699
Philadelphia, PA 19101-8699

Jacqueline R. Morrow, Esq.
Rodney R. Akers, Esq.
Assistant City Solicitor
313 City County Building
414 Grant Street
Pittsburgh, PA 15219

Stephen J. Baron
J. Kennedy & Associates
35 Glenlake Parkway, Suite 475
Atlanta, GA 30328

Howard M. Louik, Esq.
Allegheny County Law Department
300 Fort Pitt Commons
445 Fort Pitt Boulevard
Pittsburgh, PA 15219

Deneice Covert Zeve, Esq.
Terry Lupia, Esq.
Office of Attorney General
14th Floor, Strawberry Square
Harrisburg, PA 17120

Steven Baicker-McKee, Esq.
Wanda Schiller, Esq.
Babst, Calland, Clements & Zomnir, PC
8th Floor, Two Gateway Center
Pittsburgh, PA 15222

Kenneth L. Wiseman, Esq.
Mark F. Sunback, Esq.
Peter J. Thompson, Esq.
Andrews & Kurth, LLP
1701 Pennsylvania Avenue NW
Washington DC 20006

Kenneth Maiman, Esq.
Robert M. Lamkin, Esq.
Andrews & Kurth L.L.P.
425 Lexington Avenue
New York, NY 10017-3903

Exeter Associates, Inc.
12510 Prosperity Drive, Suite 350
Silver Spring, MD 20904

Michael L. Kurtz, Esq.
David F. Boehm, Esq.
Boehm, Kurtz & Lowry
2110 CBLD Center
36 East Seventh Street
Cincinnati, OH 45202

Terrance J. Fitzpatrick, Esq.
David M. DeSalle, Esq.
Ryan, Russell, Ogden & Seltzer, LLP
Suite 101, 800 North Third Street
Harrisburg, PA 17102-2025

Robert B. Weisenmiller
MRW & Associates, Inc.
1999 Harrison Street, Suite 1440
Oakland, CA 94612-3517

Michael Reid, Director
Materials Management Services
Administrative Resources, Inc.
500 Commonwealth Drive
Warrendale, PA 15086-7513

Robert J. Stefanko, Esq.
Pittsburgh School District
341 South Bellefield Avenue
Pittsburgh, PA 15213

Margaret Peters, Esq.
The Peoples Natural Gas Company
625 Liberty Avenue
Pittsburgh, PA 15222-3197

John Stember, Esq.
Low Income Advocate Parties
1705 Allegheny Building
429 Forbes Avenue
Pittsburgh, PA 15219

Stephen L. Feld, Esq.
Pennsylvania Power Company
1 East Washington Street
P.O. Box 891
New Castle, PA 16103-0891

Donald R. Ayersman, Jr., Esq.
IBEW Local 2357
1125 Denver Avenue
Morgantown, WV 26505

Tim Merrill, Esq.
The Eastern Group
Suite 200, 4 Penn Center West
Pittsburgh, PA 15276

Kevin J. McKeon, Esq.
Malatesta, Hawke & McKeon, LLP
P.O. Box 1778
Harrisburg, PA 17101

Thomas P. Gadsden, Esq.
Morgan, Lewis & Bockius
2000 One Logan Sqaure
Philadelphia, PA 19103

William T. Hawke, Esq.
Mid Atlantic Power Supply Association
100 North 10th Street
Harrisburg, PA 17105

Attorney of Record
Environmental Energy Project
3700 Vartan Way
Harrisburg, PA 17110

Paul E. Russell, Esq.
Pennsylvania Power & Light Company
Two North Ninth Street
Allentown, PA 18101

Donald A. Kaplan, Esq.
Lisa M. Helpert, Esq.
Preston Gates Ellis & Rouvelas Meeds LLP
Suite 500
1735 New York Avenue, NW
Washington, DC 20006-4759

David M. Boonin
New Energy Ventures
1845 Walnut Street, Suite 2525
Philadelphia, PA 19103

Roger Clark, Esq.
The Environmentalists
905 Denston Drive
Ambler, PA 19002-3901

John O'Brien, Esq.
Wheeled Electric Power Company
50 Charles Lindburgh Boulevard, Suite 207
Uniondale, NY 11553

Daniel Clearfield, Esq.
Gerald Gornish, Esq.
Alan Kohler, Esq.
Robert J. Longwell, Esq.
Tanya C. Leshko, Esq.
Wolf, Block, Schorr & Solis-Cohen, LLP
212 Locust Street
Harrisburg, PA 17101

James D. Steffes
Enron Power Marketing, Inc.
1400 Smith Street
P.O. Box 4428
Houston, TX 77002

Brian Kalcic
Excel Consulting
Suite 720-T
225 S. Meramec Avenue
St. Louis, MO 63105

Albert M. Benincasa, Esq.
Director, Regulatory Affairs
Skipping Stone
46 9th Avenue
Sea Cliff, NY 11579

Kenneth Zielonis, Esq.
Stevens & Lee
208 North Third Street, Suite 310
P. O. Box 12090
Harrisburg, PA 17108-2090

Brian A. Rider, President
Pennsylvania Retailers' Association
224 Pine Street
Harrisburg, PA 17101-1325

Joseph A. Dworetzky, Esq.
John P. Lavelle, Jr., Esq.
Luke E. Dembosky, Esq.
Hangley Aronchick Segal & Pudlin
One Logan Square, 12th Floor
Philadelphia, PA 19103

Mr. John Horton
Senior Regulatory Analyst
MidCon Corporation
701 East 22nd Street
Lombard, IL 60148

Craig Nifong
MidCon Corporation
3200 Southwest Freeway
Houston, TX 77027

Emmitt C. House, Esq.
Thomas J. Augspurger, Esq.
MidCon Corporation
Office of General Counsel
701 East 22nd Street
Lombard, IL 60148

Mark J. McGuire, Esq.
Ronald N. Carroll, Esq.
Jenner & Block
601 Thirteenth Street, N.W.
Twelfth Floor, Suite 1200
Washington, DC 20005

Gordon J. Smith, Esq.
Douglas F. John, Esq.
John & Hengerer
1200 17th Street, N.W.
Suite 600
Washington, DC 20036

Mary A. Ralls, Esq.
Stephanie A. Sugrue, Esq.
Sheila Hollis, Esq.
Duane, Morris & Heckscher LLP
1667 K Street NW, Suite 700
Washington, DC 20006-1608

Vickiren S. Aeshleman
QTS Energy Inc.
Suite 300
300 Hamilton Blvd.
Peoria, IL 61602

Gary A. Jeffries, Esq.
CNG Energy Services Corporation
One Park Ridge Center
P. O. Box 15746
Pittsburgh, PA 15244-0746

David Cruthirds, Esq.
Electric Clearinghouse, Inc.
1000 Louisiana, Suite 5800
Houston, TX 77002-5050

Keith M. Sappenfield, II
Director of Marketing Support
NorAm Energy Management, Inc.
P. O. Box 2628
Houston, TX 77252-2628

John R. Orr, Esq.
Duke Energy Trading & Marketing, LLC
One Westchester Center
10777 Westheimer, Suite 650
Houston, TX 77042

Lawrence E. Moncrief, Esq.
1364 Silverton Avenue
Pittsburgh, PA 15206

Samuel W. Braver, Esq.
Bruce A. Americus, Esq.
Buchanan Ingersoll PC
One Oxford Centre — 20th Floor
301 Grant Street
Pittsburgh, PA 15219-1410

John Wilson, Executive Director
Community Action Association of PA
222 Pine Street
Harrisburg, PA 17101

Pamela C. Polacek

Pamela C. Polacek, Esq.

Dated this 17th day of February, 1998, in Harrisburg, Pennsylvania.