



COMMONWEALTH OF PENNSYLVANIA  
PENNSYLVANIA PUBLIC UTILITY COMMISSION  
P.O. BOX 3265, HARRISBURG, PA 17105-3265

IN REPLY PLEASE  
REFER TO OUR FILE

May 28, 1998

R-974104  
R-973981

Mr. Lawrence J. Schiller  
440 Rosewood Drive  
Pittsburgh, PA 15236

Dear Mr. Schiller:

Thank you for your recent letter to Senator Melissa Hart regarding the restructuring filings made by the Duquesne Light Company and the West Penn Power Company which is a part of the Allegheny Power System.

Please know that on May 21, 1998, the Pennsylvania Public Utility Commission voted to finalize the restructuring plans for both of these utilities. The Commission's final approval allows Duquesne to collect \$1.331 billion in stranded costs over seven years starting in January 1999. West Penn is allowed to collect \$524 million in stranded costs over the next seven years beginning in January of 1999. Please find under cover of this letter the press releases summarizing the Commission's decisions. Also, please note that I have taken the liberty of forwarding your letter to the Secretary of the Commission for inclusion into the official file of this proceeding.

Thank you again for the benefit of your thinking on these important issues.

Sincerely,

Rosemary Chiavetta, Esq.  
Director of Legislative Affairs

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Enclosures

cc: The Hon. Melissa Hart  
Secretary James McNulty ✓

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Larry Schiller  
440 Rosewood Drive  
Pittsburgh, PA 15236

April 16, 1998

Senator Melissa Hart  
Senate Box 203040  
Harrisburg, PA 17120-3040

Dear Ms. Hart:

I am very concerned with the course of utility deregulation in our state. It appears to me that the utilities are having their way with our unimpressive group at the P.U.C. And, it disturbs me that our state government is apparently doing nothing to control this situation.

I am personally involved in the Pilot Program, and I see the effects of these programs daily as a Real Estate Manager and member of BOMA. If our state doesn't do something to alter the course of recent changes, Pennsylvania will again lose more businesses to states that have cheaper utilities. The massive "stranded" costs, which the utilities seek are completely unjustified given the above average profits of Duquesne Light and Allegheny Power. I am looking for our elected officials to get involved. This issue will determine the condition of our economy for many years to come.

Sincerely,



Lawrence J. Schiller

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June 12, 1998

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**Via Federal Express**

James J. McNulty  
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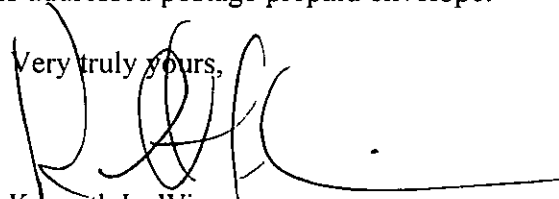
Re: *Application of Duquesne Light Company  
for Approval of Restructuring Plan  
Docket No. R-00974104  
Brief on Exceptions to Recommended Decision*

Dear Mr. McNulty:

Pursuant to Section 5.533 of the Pennsylvania Public Utility Code, enclosed please accept for filing an original and nine (9) copies of Hospital Shared Services ("HSS") and Administrative Resources, Inc. ("ARI") Petition for Reconsideration in the above-captioned proceeding.

Also, please find an additional copy of the cover of HSS/ARI's Petition for Reconsideration to be stamped and returned to me in the enclosed self-addressed postage prepaid envelope.

Very truly yours,



Kenneth L. Wiseman  
Attorney for Hospital Shared Services  
and Administrative Resources, Inc.

Enclosures

cc: All Parties  
Commission's Office of Special Assistants (hard copy and computer diskette version)

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BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

**ORIGINAL**

Application of Duquesne Light Company )  
for Approval of Its Restructuring Plan )  
Under Section 2806 of the Public Utility Code )

Docket Nos. R-00974104 and  
R-00974104C0001-C0004

**PETITION FOR RECONSIDERATION OF HOSPITAL SHARED SERVICES  
AND ADMINISTRATIVE RESOURCES, INC.**

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PA PUBLIC UTILITY COMMISSION  
SECRETARY'S BUREAU

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**ATTORNEYS FOR  
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ADMINISTRATIVE RESOURCES, INC.**

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**PETITION FOR RECONSIDERATION OF HOSPITAL SHARED SERVICES  
AND ADMINISTRATIVE RESOURCES, INC.**

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**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 Nos. R-00974104 and  
R-00974104C0001-C0004**

**PETITION FOR RECONSIDERATION OF HOSPITAL SHARED SERVICES  
AND ADMINISTRATIVE RESOURCES, INC.**

Pursuant to Rule 5.572 of the Rules of the Pennsylvania Public Utility Commission (“Commission”), 66 Pa. C.S. § 5.572 (1997), Hospital Shared Services (“HSS”) and Administrative Resources, Inc. (“ARI”) hereby petition for reconsideration of certain rulings in the Opinion and Order (“Order”) entered in this case on May 29, 1998.

**I.     INTRODUCTION**

HSS/ARI applaud the Commission for what in general is a well-reasoned decision. Specifically, HSS/ARI are gratified that the Commission recognized the contradiction between Duquesne’s claim that it has \$1.9 billion in stranded costs and the evidence presented by HSS/ARI that shows (1) that large capacity generation plants around the country are being sold at multiples of net book value and (2) that Duquesne’s internal studies, as well as studies by its consultant and merger advisor, estimated that Duquesne’s generation plants, in particular, have a market value of hundreds of millions of dollars in excess of Duquesne’s remaining book investment. HSS/ARI further are pleased that the Commission has provided Duquesne the option to sell its generation plants, an option that will provide very substantial ratepayer *and* shareholder benefits if Duquesne’s sales of its generation plants achieve the type of results anticipated under the various Duquesne

studies and experienced in sales in other states, particularly in the northeast. Should Duquesne choose that option, it appears that Duquesne's actual net stranded costs will be substantially reduced and could be eliminated entirely.

Nonetheless, whether Duquesne chooses to divest its generation plants, or decides to opt for an administrative determination of stranded costs, there are particular rulings in the Order that HSS/ARI believe are in error. The issues concerning some of those rulings will be mooted by a Duquesne election to divest its generation plants. Other issues remain even if Duquesne sells its facilities. For the Commission's convenience, in Section II of this petition, HSS/ARI will discuss those rulings that affect Duquesne's stranded cost recoveries and rates, regardless which option Duquesne elects. Section III addresses issues that affect Duquesne's stranded cost recoveries and rates only if Duquesne opts for an administrative determination of stranded costs, *i.e.*, it chooses *not* to sell its generation plants. Accordingly, HSS/ARI respectfully ask for reconsideration as discussed below.

## **II. RULINGS THAT SHOULD BE MODIFIED WHETHER DUQUESNE ELECTS TO DIVEST ITS GENERATION ASSETS OR OPTS FOR AN ADMINISTRATIVE DETERMINATION OF STRANDED COSTS**

Sections 2803, 2804(13) and 2808(a) of the Electric Generation, Customer Choice and Competition Act (the "Act") provide electric utilities the opportunity to recover "net stranded costs" that the Commission finds are just and reasonable. Therefore, to determine the amount that a utility is entitled to recover from ratepayers, the total market value of the utility's generation assets must be measured against the sum total of the utility's remaining net book investment in generation plant, regulatory assets and other categories of costs that the Commission finds appropriately are included in calculating total potential stranded costs. As a consequence, once market value is established,

whether administratively or by divestiture, the ultimate responsibility of ratepayers to fund a greater or lesser amount of net stranded costs will be dependent upon the Commission's determination of total potential stranded costs. Therefore, whether or not Duquesne elects to sell its generation assets, to determine a net stranded cost amount that Duquesne is entitled to recover from ratepayers, it is critical to determine the appropriate costs that potentially are recoverable as stranded under the Act. Separately, there are rate issues that are unaffected by Duquesne's decision to sell or not sell its generation assets. Accordingly, HSS/ARI ask the Commission to reconsider its rulings discussed below regardless what election Duquesne makes in terms of the divestiture of its generation plants.

**A. The Commission's Disallowance of only \$65.58 Million of Duquesne's Remaining Net Book Investment in the Phillips and Brunot Island Plants is Inadequate (Order at 87-91)**

The Commission correctly ruled that

[i]t is evident that the Act and the transition to a competitive generation market played no role in [Duquesne's] decision to "cold reserve" [the Phillips and Brunot Island plants]. Accordingly, consistent with the provisions of the Act we find that the Company's claim, for inclusion of the net book value of Phillips and Brunot Island in our stranded cost determination, is not meritorious and, therefore, is denied.

Order at 91.

Based upon that conclusion, the Commission disallowed \$65.58 million. *Id.* However, the \$65.58 million represents only a portion of Duquesne's net book investment; it is net of \$41.22 million in deferred taxes related to the plants. Order at 87, n.16. By disallowing only \$65.58 million, Duquesne inappropriately will recover \$41.22 million of its net book investment in Phillips and Brunot Island as stranded costs.

It is undisputed that Duquesne's net book investment in Phillips and Brunot Island is \$106.8 million. Duquesne St. No. 4 at 15:12-14. The predicate for allowing Duquesne the recovery of \$41.22 million of that amount apparently reflects acceptance of Duquesne's general claim associated with deferred taxes, *i.e.*, that, through reduced rates, ratepayers received the benefit of deferred taxes and, therefore, should not avoid liability for Duquesne's higher tax bill in the future when the "tax benefits" turn around. Duquesne St. 4 at 8:14-9:1 However, as HSS/ARI pointed out in their Exceptions to Administrative Law Judge ("ALJ") Corbett's Recommended Decision (which also recommended a disallowance of only \$65.58 million), that argument cannot apply in the case of the cold-reserved Phillips and Brunot Island units. Those units were taken out of rate base in 1986. Because Duquesne never filed a new rate case after that date, Duquesne did not reduce its rates to provide ratepayers the benefit of the deferred taxes, and thus the benefit of \$41.22 million in deferred taxes flowed to Duquesne's shareholders, not its ratepayers. HSS/ARI Exceptions at 16. Accordingly, the Order should be modified to provide for the disallowance of the full \$106.8 million of Duquesne's net book investment in the cold-reserved units.

**B. Duquesne's Net Book Investment in Generation Plant Should be Reduced Because Duquesne Failed to Show that its Capital Expenditures Over a Ten-Year Period Were Reasonable (Order at 89-92 and 138)**

According to Duquesne's FERC Form 1 reports, from 1987 through 1996, Duquesne spent \$382 million on generation-related capital additions. HSS/ARI St. 1 at 55-56. HSS/ARI objected to Duquesne's proposal to include the entirety of \$382 million in capital expenditures in its calculation of net book value because none of those expenditures ever had been reviewed by the Commission, nor had Duquesne presented any evidence to attempt to show that those expenditures were reasonable. HSS/ARI M.B. at 24-25. For the same reasons, HSS/ARI objected to Duquesne's

request to include the entirety of those expenses in its 1996 cost of service for purposes of determining an unbundled generation rate. *Id.* at 81. In his Recommended Decision, the ALJ recommended against acceptance of HSS/ARI's arguments stating that HSS/ARI had failed to raise a "credible issue" because "HSS/ARI fail[ed] to identify even a single expenditure as unreasonable." R.D. at 176.

In the Order, the Commission acknowledges that HSS/ARI filed exceptions to the Recommended Decision's failure to recommend reductions based upon HSS/ARI's arguments. Order at 89; *see also* HSS/ARI Exceptions at 6-10 and 13-15. Nonetheless, the Commission's Order does not directly address HSS/ARI's exception in the section of the Order concerning net book value. *See* Order at 90-92. However, in an unrelated section of the Order, it appears that the Commission accepted the ALJ's reasoning in concluding that "HSS/ARI fail[ed] to identify a single expenditure since the last base rate proceeding as unreasonable." <sup>1</sup> Order at 138. The Commission then went on to state that HSS/ARI "confuse[d] the issue of a utility's 'burden of proof' with the issue of an intervenor's burden of going forward with 'credible evidence' to contest the reasonableness of particular cost items." *Id.*

HSS/ARI submit that it is inconsistent with traditional ratemaking standards, and with standards relating to the burdens of proof and going forward with evidence, to place the onus on intervenors to go forward with evidence to contest the reasonableness of particular cost items given

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<sup>1</sup>As will be discussed *infra* at 16, the Commission's ruling at page 138 confuses two issues raised by HSS/ARI that have nothing do with each other, and which rely entirely upon different evidence and legal arguments. The issue discussed above relates solely to Duquesne's actual *past* capital expenditures during the period 1987 through 1996. The issue discussed *infra* at 16 and at pages 137-38 of the Commission's Order relates exclusively to Duquesne's *projections* of amounts that it estimates it will spend for capital additions during the future.

that Duquesne did not place in the record even a general description of the capital additions it made over a ten-year period, let alone a single sentence that attempts to explain why its expenditures associated with those capital additions were reasonable. In fact, because Duquesne put on no evidence concerning its past expenditures, the burden of going forward with evidence, credible or otherwise, never even shifted to intervenors.

A recent case, *Aronson v. Duquesne Light Co.*, 1996 Pa. PUC Lexis 106 (1996), sets forth the well-established principle concerning the shifting of the burden of going forward with evidence. In *Aronson*, it was noted that Section 332(a) of the Public Utility Code, 66 Pa. C.S. §332, provides that the party seeking affirmative relief has the burden of proof. *Aronson v. Duquesne Light*, 1996 Pa. PUC Lexis 106 at \*7. It then was held that the burden of going forward with evidence shifts only at such time as the party with the burden of proof establishes a *prima facie* case. *Id.*, 1996 Pa. PUC Lexis 106 at \*8. See also *Burleson v. Pennsylvania Public Util. Comm'n*, 501 Pa. 433, 461 A.2d 1234 (Pa. 1983).

It is undisputed that Duquesne had the burden of proof in this case. *Application of PECO Energy Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code*, 181 P.U.R. 4th 517 (Pa. PUC Dec. 23, 1997), (hereinafter "*PECO Order*") *mimeo* at 68. Thus, because Duquesne had the burden of proof, but put in no evidence even to attempt to demonstrate the reasonableness of its past capital expenditures, the burden of going forward with evidence never shifted to intervenors. As a result, as HSS/ARI argued in their Exceptions, *Pennsylvania Pub. Util. Comm'n v. Philadelphia Electric Co.*, 1990 Pa. P.U.C. LEXIS 155 at p\* 54-57 (1990) sets forth the relevant standard by which to determine whether Duquesne should be permitted to pass through to ratepayers the costs of its past generation-related capital expenditures

of \$392 million. HSS/ARI Exceptions at 8. That standard provides that “[i]f and when [a utility] seeks recognition of [capital expenditures], it will then be required to support the prudence of those expenditures.” *Pennsylvania Pub. Util. Comm’n v. Philadelphia Electric Co.*, 1990 Pa. P.U.C. LEXIS 155 at p\* 56. Given that Duquesne put on no evidence whatsoever to describe the additions that were made, the costs associated with any particular addition or an explanation of why such costs should be found to have been reasonable, Duquesne cannot be found to have established a *prima facie* case and, as such, HSS/ARI had no burden to go forward with evidence suggesting that Duquesne’s past expenditures were unreasonable.

As a result, HSS/ARI submit, as they previously have stated, under a strict application of the law, the Commission could disallow the entirety of Duquesne’s past capital expenditures that never have been shown to be just and reasonable. HSS/ARI M.B. at 25. Nonetheless, HSS/ARI do not seek such a harsh result. As they stated in their Exceptions, to balance ratepayers and shareholders interests, it would be appropriate to disallow 50% of the \$382 million (net of depreciation) in generation-related capital expenditures that Duquesne made between 1986 and the present and to order a concomitant rate reduction. HSS/ARI Exceptions at 15. However, if the Commission believes that a 50% disallowance is excessive, then the Commission, in its discretion, can provide for a lesser disallowance. But, in no event should Duquesne be permitted, with impunity, to shield almost \$400 million in expenditures from scrutiny over a ten-year period and then get a “free pass” to foist the entirety of those costs on ratepayers without any proof that the expenditures were reasonable. HSS/ARI continue to believe that failure to grant substantial, meaningful relief with respect to this issue is error.

**C. The Commission Should Reverse Three Rulings Providing for Duquesne's Recovery of Claimed Regulatory Assets**

There are three rulings in which the Commission allowed Duquesne to recover amounts that Duquesne claimed as regulatory assets that HSS/ARI submit are in error. As discussed below, HSS/ARI seek reconsideration of the Commission's rulings on those items.

**1. SFAS 109 Deferred Taxes (Order at 153-55)**

Duquesne claimed SFAS deferred taxes of \$179 million on a net present value basis as a regulatory asset. Duquesne had removed that amount from the balance of plant in service and claimed it as a regulatory asset. Order at 155. The Order states that Duquesne's "final regulatory asset claim reflects [an] OCA adjustment of \$62.94 million for SFAS 109 plant obligation . . ." *Id.*

The Commission found that the deferred taxes should not be treated as a regulatory asset and concluded that Duquesne's adjustment should be reversed. *Id.* As a result, to reflect the adjustment recommended by OCA, the Commission reduced Duquesne's regulatory asset by \$62.94 million. By ordering a reversal of Duquesne's prior accounting adjustment, the Commission nonetheless is permitting Duquesne to include the deferred taxes in Duquesne's calculation of potential stranded costs, albeit as part of plant in service.

HSS/ARI seek reconsideration on two grounds. First, as previously indicated in the discussion of deferred taxes associated with the Phillips and Brunot Island cold reserved plants, Duquesne's claim associated with these deferred taxes is that ratepayers received the benefit of deferred taxes and, therefore, should not avoid liability for Duquesne's higher tax bill in the future when the "tax benefits" turn around. Duquesne St. 4 at 8:14-9:1 Duquesne's express argument was as follows:

[t]his regulatory asset was booked in recognition of the fact that the tax benefits will “turn around” in the future, leading to a higher tax expense which must be paid by the Company. At that time, however, the plant which gave rise to the accelerated depreciation will no longer be in jurisdictional rates. Ratepayers, therefore, would have gotten the benefit of lower rates in the past due to the tax advantages of the accelerated depreciation, but also would be able to avoid the higher tax bill in the future when the assets which gave rise to be (sic) depreciation become deregulated.

Duquesne Statement No. 4 at 8:19-9:1.

However, as HSS/ARI previously discussed, because Duquesne chose not to file a rate case subsequent to 1986, Duquesne retained any tax benefits for its shareholders; it did not pass those benefits back to ratepayers, *i.e.*, to pass through the benefit to ratepayers, Duquesne would have had to file a rate case to make an appropriate adjustment to reduce its rates. HSS/ARI Exceptions at 20; HSS/ARI M.B. at 69-70. Thus, Duquesne’s entire claim basis should be disallowed, both as a regulatory asset and as plant in service, because Duquesne’s shareholders, not its ratepayers, received the benefit of the deferred taxes.

HSS/ARI’s second objection to the Commission’s ruling on this issue relates to the amount of the disallowance. The Order states that Duquesne’s “final regulatory asset claim reflects [an] OCA adjustment of \$62.94 million for SFAS 109 plant obligation, so no further adjustment is necessary.” Order at 155. However, the tables attached to Duquesne’s Main Brief, which HSS/ARI understand to reflect Duquesne’s final claim, lists \$179 million for SFAS 109 deferred taxes. HSS/ARI submit that the proper disallowance therefore is \$179 million.

2. Deferred Rate Synchronization Costs (Order at 159-60)

The Order allows Duquesne to recover \$23.5 million in deferred rate synchronization costs as a regulatory asset. Order at 160. The Commission reasoned that:

[d]eferred rate synchronization costs are early window costs associated with Perry and Beaver Valley 2 that the Company is permitted to amortize through 2006, as part of the Ft. Martin settlement.

*Id.*

HSS/ARI seek reconsideration of this ruling because it is based upon a premise that does not accurately reflect the terms and conditions of the Ft. Martin settlement and because it ignores the Commission's prior ruling concerning these costs.

The Ft. Martin settlement does not provide Duquesne an unqualified right to amortize the early window costs. Rather, the settlement provided that the provision allowing for amortization "shall not imply that the OCA agrees that an annual amortization of the "early window" costs is recoverable in rates in Duquesne's next base rate proceeding." Exh. RBW-38. That proviso is particularly relevant because in a November 1987 Order, the Commission previously had declined to approve the recovery of these costs, declined to pass on the costs' prudence or whether the units at issue were used and useful, declined to adjudicate the justness and reasonableness of the expenditures and specified that "this Order is not to be construed as a determination by the Commission . . . that Duquesne . . . may recover any of the deferred costs . . . ." Exh. RBW-36. Thus, any right Duquesne gained under the Ft. Martin settlement to amortize the "early window" costs was subject to the right of any party to challenge those costs on grounds of prudence, *etc.* and there never has been a Commission finding that the costs are in fact just and reasonable and

recoverable in rates as such. Therefore, under the Commission's decision in *PECO*, the "early window" costs should be disallowed because they are not presently included in rates and Duquesne does not have any unqualified right to recover those costs. *PECO Order, mimeo* at 66.

**3. Warwick Mine Costs (Order at 170-72)**

The ALJ recommended that Duquesne be denied recovery of \$15 million in costs associated with the Warwick Mine. R.D. at 397. The claimed \$15 million represents the net book value of Duquesne's investment in the mine. Order at 171. In the Order, the Commission reversed the ALJ concluding that "[t]he net cost is the cost that would have had rate recovery through the ECR absent the Act. Duquesne never sought treatment of the property as a regulatory asset as claimed by HSS." Order at 172. HSS/ARI submit that this ruling fundamentally is in error for two reasons.

The first of those reasons relates to the Commission's apparent belief that HSS/ARI argued that Duquesne had sought and apparently been denied treatment of the costs as a regulatory asset. HSS/ARI are unsure what led the Commission to conclude that HSS/ARI had made that contention, but so the record is clear, the Commission should note that HSS/ARI made no such argument.

HSS/ARI's argument in favor of a disallowance was based upon the undisputed fact that on February 21, 1981, the Commission required Duquesne to remove Warwick Mine from the Company's rate base. HSS/ARI M.B. at 75; *see also* Exh. RBW-40. After 1981, Duquesne was permitted to recover its investment in Warwick Mine through the cost of coal subject to the coal cost cap in the ECR. *Id.* As a result, Duquesne's recovery of Warwick Mine costs never was assured. Recovery of costs only would have occurred when costs fell within the ECR charge.<sup>2</sup> However, in

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<sup>2</sup>Because recovery of the Warwick Mine capital costs was dependent upon successfully mining the coal at or below the price prevailing in the competitive market, and because Duquesne

1996, the operator of the mine informed Duquesne that it was ceasing to operate the mine. Exh. RBW-39. Thus, HSS/ARI argued that because production had ceased from the mine well before this restructuring proceeding, Duquesne is not entitled to collect any cost of, much less its capital investment associated with, the mine under the coal cost cap. HSS/ARI M.B. at 76. Stated another way, paraphrasing the Commission's ruling disallowing Phillips and Brunot Island costs,

[c]osts for . . . plants that are not 'used and useful' are not traditionally recoverable under a regulated environment.

While the Act provides an exception for costs attributable to physical plants no longer used and useful because of the transition to retail competition, . . . [i]t is evident that the Act and the transition to a competitive generation market played no role in [the operator's decision to cease operating the Warwick Mine].

See Order at 91.

Therefore, the Commission should reverse itself and require the disallowance of the Warwick Mine costs.

**D. The Distribution Component of Duquesne's Unbundled Rate Should Be Reduced (Order at 54-56)**

HSS/ARI argued that the distribution component of Duquesne's unbundled rates should be reduced to reflect a partial disallowance of Duquesne's past capital additions for distribution plant. The Order rejected HSS/ARI's arguments. Order at 34. HSS/ARI ask that the Commission reconsider the issues.

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made no showing that the delivered cost of Warwick's production would be below the prevailing market price of coal, the Warwick Mine's capital costs were not assured of recovery through the ECR had rate regulation continued. Thus, there is no foundation for the Commission's conclusion that Duquesne would have had rate recovery through the ECR absent the Act.

HSS/ARI's legal argument in favor of a disallowance with respect to past distribution-related capital additions was identical to its argument in favor of a disallowance for past generation-related capital additions. See HSS/ARI M.B at 9-12 and 24-25; HSS/ARI Exceptions at 6-10, 13-15 and 26-27. Thus, HSS/ARI rely upon the argument set forth *supra* at 4-7 to show that the Commission, under a strict application of the law, could disallow the entirety of Duquesne's past distribution-related capital expenditures that never have been shown to be just and reasonable. Those expenditures totaled \$473 million. HSS/ARI St. 1 at 55-56. Nonetheless, again, to balance ratepayers and shareholders interests, HSS/ARI submit that it would be appropriate to disallow 50% of the \$473 million (net of depreciation) in distribution-related capital expenditures that Duquesne made between 1986 and the present and to order a concomitant rate reduction. And again, if the Commission believes that a 50% disallowance is excessive, then the Commission, in its discretion, can provide for a lesser disallowance, albeit one that grants substantial, meaningful relief.

### **III. RULINGS THAT SHOULD BE MODIFIED IF DUQUESNE ELECTS NOT TO DIVEST ITS GENERATION ASSETS**

The rulings discussed below are moot if Duquesne elects to sell its generation assets. However, in the event that Duquesne does not elect to sell its generation plants, HSS/ARI seek reconsideration of these issues as set forth below.

#### **A. The Commission Should Adopt HSS/ARI's Market Valuation In An Administrative Determination Of Stranded Costs (Order at 116-17)**

The record amply demonstrates that generation plants around the country are being sold at multiples of net book value. The market valuation utilized by HSS/ARI's witness, Dr. Weisenmiller, is the only market valuation that captures that dynamic. As the Commission noted, under Dr. Weisenmiller's valuation, which utilizes CS First Boston's price projections performed for

Duquesne, Duquesne's generation assets would have positive market value. Order at 116; *see also* Exh. RBW-57. Thus, Dr. Weisenmiller's analysis is consistent with actual market transactions. OCA's valuation study, which concludes that Duquesne will have stranded costs, is inconsistent with those real world transactions. Accordingly, HSS/ARI submit that the Commission should modify its Order and utilize Dr. Weisenmiller's valuation if Duquesne elects an administrative determination of stranded costs, *i.e.*, it elects not to sell its generation plants.

**B. The Commission Should Order An Adjustment For Life Extension  
(Order at 123)**

The ALJ recommended that the Commission adopt an adjustment of \$170.72 million to Duquesne's stranded cost claim to reflect an extension of the economic life of Duquesne's generating units. R.D. at 281. The Commission's Order rejected that recommendation, approving Duquesne's argument that because of "probable significant changes in technology over the remaining years of life of [Duquesne's] plants," the eventuality of life extension "is uncertain, unknown, and unmeasurable at this time." Order at 123. Thus, the Order allows Duquesne's stranded cost calculations to assume that the actual shut-down of Duquesne's plants will coincide with the book retirement date of those facilities. *Id.*

HSS/ARI believe that such an assumption is economically irrational. Full discussions supporting HSS/ARI's position are set forth in their Main Brief at 58-59 and their Reply to Exceptions at 11-13.

HSS/ARI would add, however, that if probable significant changes in technology make the eventuality of life extension uncertain, unknown, and unmeasurable, the same must be said for Duquesne's wholly unsupported estimate that it will spend \$352 million in generation-related capital

additions through December 31, 2005. In other words, why is it not the case that probable significant changes in technology render that estimate of capital additions equally uncertain, unknown, and unmeasurable? Thus, if the Commission accepts Duquesne's argument that probable significant changes in technology make the eventuality of life extension uncertain, unknown, and unmeasurable, it should accept an argument that probable significant changes in technology make Duquesne's projections of capital additions equally uncertain, unknown, and unmeasurable. As a consequence, the Commission should adjust Duquesne's stranded cost calculations to eliminate in their entirety Duquesne's projected generation-related capital additions. That conclusion is required because Duquesne has made no showing that the forecast additions are known and measurable or just and reasonable, particularly if the additions will not extend the useful life of the facilities. Alternatively, if the Commission allows Duquesne to calculate stranded costs based upon projected generation-related capital additions, as is discussed in Section III.C below, that is all the more reason why the Commission needs to adjust Duquesne's projections to account for its history of over-budgeting for generation-related capital additions.

**C. The Commission Should Reduced Duquesne's Stranded Costs To Adjust For Excessive Projections Of Capital Additions (Order at 138)**

HSS/ARI argued that in the event that there is an administrative determination of stranded costs, the Commission should require a reduction to Duquesne's projections of amounts it estimates it will spend in the future on generation-related capital expenditures. HSS/ARI's recommendation to disallow amounts that Duquesne projects it will spend was based upon the unrebutted evidence that shows that Duquesne has a history of over-budgeting for generation-related capital additions. HSS/ARI obtained that evidence from Duquesne's internal "Corporate Budget Variance Reports"

for the years 1987 through 1996. Exh. RBW-22. Those reports showed that from 1987 through 1996, Duquesne's actual expenditures for generation-related capital additions were 17% lower than its twelve-month ahead budget forecasts. HSS/ARI St. No. 1 at 60; Exh. RBW-21. Based upon that history of over-budgeting, HSS/ARI argued that for purposes of determining stranded costs, the Commission should reduce Duquesne's projection of \$352 million by 20%. HSS/ARI Exceptions at 12. The recommendation for a 20% reduction was intended to capture, conservatively, the likelihood that Duquesne's error rate over a longer forecast period would exceed the 17% over-budgeting error Duquesne makes in its twelve-month ahead forecasts.

HSS/ARI argued in their Exceptions that the requested disallowance was fully consistent with the Commission's ruling in *PECO*, wherein the Commission ordered a reduction of 5% to PECO Energy's cost projections to reflect its history of over-budgeting by that percentage. HSS/ARI Exceptions at 11-12, *relying upon PECO Order, mimeo* at 82. The ALJ previously had recommended against adoption of HSS/ARI's argument concluding that HSS/ARI had put in insufficient evidence to support its position. R.D. at 302. The Commission also rejected HSS/ARI's arguments, appearing to adopt the ALJ's reasoning.

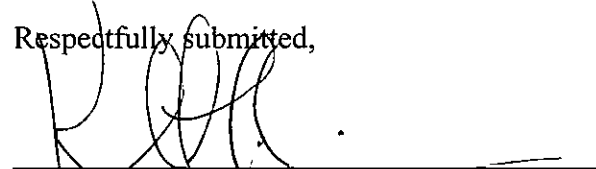
There are two matters that require clarification with respect to this issue. First, the Commission's Order appears to confuse HSS/ARI's argument concerning past capital additions, with entirely separate arguments concerning projected capital additions. More specifically, in considering HSS/ARI's arguments, the Order states that "HSS/ARI fail to identify a single expenditure since the last base rate proceeding as unreasonable." Order at 138. However, with respect to *projected* capital additions, HSS/ARI could not under any scenario identify an expenditure that is unreasonable because the expenditures neither have been made yet, nor did Duquesne provide any description of

the additions it might add. Thus, HSS/ARI's recommendation to disallow amounts that Duquesne *projects* it will spend is based upon the difference between amounts Duquesne assumed it would spend for budgeting purposes and actual amounts it did spend during the years 1987 through 1996. Again, HSS/ARI obtained those data from Duquesne's internal "Corporate Budget Variance Reports" for the years 1987 through 1996. Exh. RBW-22. It is implausible to conclude that this evidence is insufficient because the Corporate Budget Variance Reports are Duquesne's own internal reports that, by design, show the differences between its budget projections and actual expenditures. Again, these are precisely the types of materials that the Commission relied upon for ordering a disallowance for projected costs in *PECO*. Thus, as HSS/ARI previously argued, it is implausible that the Commission should not rely upon these same types of data obtained from Duquesne. That conclusion is all the more warranted given that, not surprisingly, Duquesne neither did nor can challenge the accuracy of the data. As a result, HSS/ARI submit that if Duquesne opts for an administrative determination of stranded costs, the Commission should reduce Duquesne's projections of generation-related capital additions by 20% to reflect Duquesne's documented, and undisputed, history of over-budgeting for generation-related capital additions.

IV. CONCLUSION

For the foregoing reasons, HSS/ARI respectfully request that the Commission reconsider and modify its Order consistent with the discussions herein.

Respectfully submitted,



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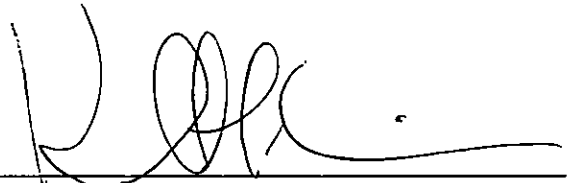
Dated: June 12, 1998

**BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served a true copy of the foregoing document on the appropriate parties in accordance with Section 1.54 of the Commission's regulations.

Dated this 12th day of June, 1998.



---

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**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 Nos. R-00974104 and  
R-00974104C0001-C0004**

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DATE: June 15, 1998

SUBJECT: R-00974104, R-00974104C0001-C0004

TO: Office of Special Assistants

FROM: *WJZ* James J. McNulty, Secretary

APPLICATION OF DUQUESNE LIGHT COMPANY  
FOR APPROVAL OF RESTRUCTURING PLAN

---

KJR

Attached is copy of a Petition for Reconsideration of Hospital Shared Services and Administrative Resources, Inc. filed in connection with the above docketed proceeding.

This matter is assigned to your Office for appropriate action.

Attachment

cc: Chairman and Commissioners  
Law Bureau

wjz

**DOCKETED**  
JUN 16 1998

DOCUMENT  
FOLDER

Pennsylvania Public Utility Commission v. Hospital Shared  
Services and Administrative Resources, Inc.

R-00974104

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NOTICE OF PETITION by Hospital Shared Services and  
Administrative Resources, Inc., at No. 1592 C.D. 1998,  
Commonwealth Court of Pennsylvania, from the order of  
the Commission dated May 29, 1998 in the above-captioned  
proceeding.

B-00983701

Filed: June 15, 1998

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BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

KJR

Joint Application of DQE, Inc., )  
Allegheny Power System, Inc. and )  
AYP Sub, Inc. for approval of the )  
transfer by merger of the )  
property and rights of Duquesne )  
Light Company to Allegheny )  
Power System, Inc. )

Docket No. A-110150F.0015

Application of Duquesne Light )  
Company for approval of its )  
restructuring plan under Section )  
2806 of the Public Utility Code )

Docket No. R-00974104  
(not consolidated)

RECEIVED  
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SECRETARY'S BUREAU

PETITION FOR EXPEDITED RECONSIDERATION  
OF DQE, INC. AND DUQUESNE LIGHT COMPANY  
REGARDING MERGER AND JOINT RESTRUCTURING PLAN

Pursuant to 52 Pa. Code § 5.572, DQE, Inc. and Duquesne Light Company ("Duquesne") hereby petition the Commission for expedited reconsideration of its findings that (i) the merger cannot be consummated until the applicants join a fully functioning ISO that mitigates market power, and (ii) stranded cost recovery in the context of the merger should be based on an administrative forecast of market value. The first finding, relating to market power, imposes a condition that likely cannot be satisfied for another two years. The second finding, relating to stranded costs, will impose severe financial harm on the companies. Duquesne currently believes that if both findings are not reversed the merger may not be

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consummated. See Appendix A (Form 8-K). This represents the current view of Duquesne, not necessarily the belief or opinion of Allegheny Energy, Inc. ("Allegheny").

On June 12, 1998, Allegheny filed a separate petition for reconsideration in the merger proceeding requesting that the Commission modify its findings regarding market power mitigation and merger savings and furthermore requesting that the Commission confirm the applicants' right to conduct a generation auction to determine their stranded costs. While Duquesne did not join that petition, we support adoption of the market power mitigation measures set forth in Allegheny's petition and Allegheny's request for confirmation of the right to conduct a generation auction to determine stranded costs, provided that the Commission clarify whether there is a specific date by which that right must be exercised. In our view, unless the requested findings are made, the merger may not be consummated. Duquesne also requests that the Commission decide this petition, and the petition filed by Allegheny, on an expedited basis. Duquesne more fully explains its position with respect to these matters below.<sup>1</sup>

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<sup>1</sup> Duquesne is filing this petition in both the merger docket and Duquesne's restructuring docket out of an abundance of caution. Even though all the issues addressed herein arise in the context of the merger, the stranded cost issues were addressed in the final order in Duquesne's restructuring proceeding.

1. The Commission's final order in the merger proceeding ("Merger Order") permits the merger to be consummated only if, prior to closing, the applicants join a fully functioning Independent System Operator ("ISO") that adequately mitigates market power and meets seven criteria specified by the Commission. Duquesne understands, and agrees with, the proposition that requiring the applicants to join an ISO is an appropriate market power mitigation condition. Duquesne has long supported ISOs and the elimination of pancaked transmission rates, which is the source of the market concentration at issue here.

This notwithstanding, it is clear that this condition may cause the merger to fail. The Merger Agreement provides that either party may terminate the Agreement by October 5, 1998 if certain conditions have not been satisfied by that date or, if that date has been extended pursuant to the agreement, closing has not occurred by April 5, 1999. The Midwest ISO is not, however, expected to be fully operational until June 30, 2000. See Appendix C, Petition of Allegheny Energy for Reconsideration (Docket No. A-110150F.0015). In addition, the Midwest ISO, as presently constituted and as proposed to the Federal Energy Regulatory Commission, does not meet the seven criteria specified by the PUC.<sup>2</sup> It is therefore apparent that

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<sup>2</sup> For example, the Midwest ISO, as proposed, does not meet the criteria related to single system rates and marginal cost pricing.

the Midwest ISO does not presently satisfy the conditions set forth in the Merger Order, nor is it likely to satisfy such conditions in the near future.<sup>3</sup>

In recognition thereof, the Applicants have offered other forms of market power mitigation, particularly the sale of 570 MW of capacity from the Cheswick plant. This sale, and its impact on market concentration, is described in detail in Allegheny's petition for reconsideration. Duquesne supports Allegheny's request that the Commission adopt additional conditions, including the sale of Cheswick capacity, that permit the merger to be consummated on a timely basis.

2. The other potential impediment to merger consummation, in Duquesne's view, is the stranded cost disallowances imposed on both companies in the context of the merger. These disallowances differ from the stranded cost findings applicable to the stand-alone restructuring plans of Duquesne and West Penn in two important respects. The first is that the stranded costs approved in the context of the merger are "net" of merger synergies, consistent with the recommendation of the Office of Consumer Advocate ("OCA").<sup>4</sup> The second difference is that these

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<sup>3</sup> The Merger Order also references the possibility of joining the PJM ISO, provided that it can be shown to mitigate market power. The applicants' witness Dr. Pifer testified that joining the PJM ISO would not provide sufficient mitigation to permit the merger to pass applicable market concentration screens.

<sup>4</sup> Allegheny has fully addressed the treatment of merger synergies in its petition for reconsideration.

findings are based on an administrative determination of stranded costs, while in Duquesne's stand-alone proceeding the Commission approved a generation auction to determine stranded costs. The Commission did so based on a finding that "only a market-based determination of stranded costs can reasonably satisfy the 'known and measurable' criteria set forth in the Act." Duquesne Light Company, No. R-00974104, slip op. at 83.

The administrative determination of stranded costs applied to the companies in the context of the merger will cause severe financial harm to Duquesne and West Penn. As West Penn demonstrates in its petition for reconsideration in Docket No. R-00973981, it has suffered a disallowance of approximately \$1 billion. By Duquesne's calculation, \$830 million of this disallowance is due to the market forecasts adopted by the Commission. The disallowance imposed on Duquesne in the context of the merger, while not as severe, is substantial as well. The disallowance due to the administrative determination of stranded costs for Duquesne is \$370 million on a net present value (pre-tax) basis. Together, the combined disallowance due to the administrative determination of stranded costs is \$1.2 billion.

The Commission could have, and should have, avoided reliance on these administrative determinations by adopting the market-based, "second look" proceeding proposed by the applicants. Under this approach, the applicants' stranded costs would have been established in a future proceeding using actual market

evidence. The applicants committed to auction 5% of their Pennsylvania-jurisdictional generation assets as part of this market-based valuation. Clearly, this proposal should have been accepted, given that "only a market-based determination of stranded costs can reasonably satisfy the 'known and measurable' criteria set forth in the Act." Duquesne Light Company, No. R-00974104, slip op. at 83. Regrettably, however, the Commission rejected the second look proceeding, and instead relied on a one-time administrative determination of stranded costs,<sup>5</sup> finding that a delay in the final calculation of stranded costs until 2001-2003 was not appropriate or permitted under the Customer Choice Act. Id. at 78-79.

If the Commission is unwilling to reconsider its administrative determination of stranded costs, however, it should address whether the applicants may use a generation auction to determine their stranded costs. The Merger Order did not recognize that applicants had referenced such an auction in their joint brief on exceptions; there, the applicants stated:

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<sup>5</sup> Duquesne, as West Penn, has argued that the administrative determination of stranded costs advocated by the OCA is deficient in many respects, including its modeling of the generation market, and that, if adopted, the OCA's recommendations will cause severe financial harm. Duquesne will not repeat these arguments and testimony here, but rather we incorporate them by reference. The explanation of the financial harm to Duquesne from various disallowances, including a default on the covenants in the Beaver Valley 2 lease, was described in the testimony of Mr. O'Brien and Mr. Clayton. DLC Statement Nos. 2, 2-A, 4, 4-A. The criticism of the administrative determination of stranded costs was contained in the testimony of Mr. Schnitzer. DLC Statement No. 3, 3-A.

West Penn strongly believes the Presiding Judge's stranded cost recommendations suffer from numerous legal and factual deficiencies, and cannot withstand court review, and that the Commission cannot force the sale of generation. West Penn would not voluntarily divest itself of its generating assets. Nevertheless, to preserve the chance to survive restructuring with the potential to maintain their financial viability, West Penn and Duquesne Light Company recognize that the forced sale of generating assets may become an economic necessity. West Penn and Duquesne would, if necessary, exercise their right to sell generation and set their CTC under the same terms and conditions as the auction proposed by Duquesne, and recommended for approval by Judge Corbett in Duquesne's stand-alone restructuring case.

Brief on Exceptions of Allegheny Energy and DQE at 3-4 (emphasis in original).

It is unclear why the Merger Order did not specifically address this statement. In the Duquesne restructuring proceeding, the Commission specifically considered and approved Duquesne's plan to auction its generating assets, finding that "the Company constructed a detailed plan and presented it of its own volition." Duquesne, slip op. at 82. The Commission also addressed the issue of divestiture in the West Penn restructuring proceeding, finding that "we must reject divestiture as the method [for determining stranded costs] because West Penn does not favor divestiture and the Act does not permit the Commission to order divestiture as part of a restructuring plan." West Penn Power Co., No. R-00973981, slip op. at 72.

Given that the Commission addressed the issue of an auction in both the Duquesne and West Penn restructuring proceedings, it is unclear why the Commission failed to address an auction in the Merger Order. Given the gravity of

the stranded cost disallowances associated with the merger, it is imperative that the Commission address the matter now. Specifically, the Commission should determine whether the applicants may auction their generation to determine stranded costs under the same terms and conditions as adopted in Duquesne's stand-alone restructuring proceeding.

Furthermore, assuming the Commission permits the applicants to auction their generation to determine stranded costs, the Commission should also clarify whether there is a specific date by which the applicants must commit to such an auction or forego the right to use that valuation method for purposes of setting the CTC. There is no time limit proposed in Allegheny's petition. The Commission should accept this approach or, if it does not, specify the date by which the companies must commit to an auction. Clarification on this point is important, as the applicants must be aware if there is a deadline by which they must exercise the auction option (or thereafter forego it) as a remedy to the financial harm associated with the stranded cost disallowances.

3. Duquesne fully supports Allegheny's request for expedited reconsideration of the Merger Order. The uncertainty with regard to the merger should be resolved as soon as possible. Customer education and selection will commence July 1, 1998. Under Duquesne's restructuring order, there are two potential sets of rates and shopping credits that could apply to customers: (i) if the

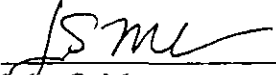
merger is not consummated, Duquesne must commence a generation auction and establish interim CTCs on the basis of the pilot credits; or (ii) if the merger is consummated, Duquesne must establish CTCs and shopping credits on the basis of the Commission' administrative determination, as well as reducing distribution rates to reflect merger synergies. It is important for customers and suppliers to know, as soon as possible, the rates and shopping credits they will face in the first year of the transition period. They will not, however, know which rates will apply until the present uncertainty regarding the merger is removed.

Duquesne also notes that its auction plan is due August 27, 1998. Preparation of the auction plan will require substantial time and resources, as well as coordination with the joint owners of Duquesne's generating plants. Duquesne must immediately commence work on that plan, if it is to be filed. For all of these reasons, it is important for the Commission to decide the petitions for reconsideration as promptly as possible.

WHEREFORE, the petition for reconsideration should be granted on  
an expedited basis.

Respectfully submitted,

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Richard S. Herskovitz  
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Dated: June 15, 1998

**Appendix A**  
**Duquesne Form 8-K**

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

FORM 8-K

CURRENT REPORT  
PURSUANT TO SECTION 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934

Date of Report (Date of earliest event reported):  
May 29, 1998

DQE, Inc.  
-----

(Exact name of registrant as specified in its charter)

Pennsylvania -----	1-10290 -----	25-159843 -----
(State or other jurisdiction of incorporation or organization)	(Commission File Number)	(I.R.S. Employer Identification No.)

Cherrington Corporate Center, Suite 100  
500 Cherrington Parkway, Coraopolis, Pennsylvania 15108-3184  
-----  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (412) 262-4700

N/A  
(Former name or former address, if changed since last report.)

Items 1-4. Not applicable.

Item 5. Other Events.

On May 29, 1998, the Pennsylvania Public Utility Commission ("PUC") issued final orders on the stand-alone restructuring plan ("Stand-Alone Plan") filed by Duquesne Light Company ("Duquesne"), a wholly owned subsidiary of DQE, Inc. ("DQE"), and on the application for approval to merge and a restructuring plan ("Restructuring Plan") filed by DQE and Allegheny Energy, Inc. ("AYE"). The restructuring plans were filed in compliance with the Pennsylvania Electricity Generation Customer Choice and Competition Act ("Customer Choice Act"), which permits retail electric customers a choice of generation supplier and authorizes utilities to recover their known and measurable transition or stranded costs. The PUC's final orders are described below.

Order on Duquesne's Stand-Alone Plan.  
-----

The PUC ordered a phase-in of customer choice under the following timetable: on January 1, 1999, 33% of the peak load of each customer class will be eligible for direct access; on January 2, 1999, 66% of the peak load of each customer class will be eligible for direct access; and on January 2, 2000, all customers will be eligible for direct access.

With respect to stranded cost recovery, the PUC's order on Duquesne's Stand-Alone Plan approved Duquesne's proposal to auction its generating assets and use the proceeds to offset stranded costs. The remaining balance of such costs (with certain exceptions described below) would be recovered from ratepayers through a competitive transition charge ("CTC"). The order approves the auction only in the context of Duquesne's Stand-Alone Plan, not the Restructuring Plan associated with the merger with AYE (which is discussed below).

By conducting the auction, Duquesne expects to recover (through the auction proceeds or the CTC), or avoid the incurrence of, all its stranded generation costs, with the exception being a \$65 million disallowance (net present value, after tax) related to Duquesne's cold reserved units at the Phillips Power Station and Brunot Island Power Station. The PUC's final order also approves recovery of \$339 million of the \$357 million in regulatory assets claimed by Duquesne. The disallowed regulatory assets relate primarily to deferred coal costs under previously applied coal caps and deferred caretaker costs associated with the cold reserved units.

Duquesne will account for the impacts of the PUC order by taking a charge to its earnings for the second quarter period ending June 30, 1998. This charge will reflect the disallowance associated with the investments in cold reserved units and the disallowance of a portion of the regulatory asset claim.

Order on Merger and Restructuring Plan Under the Merger.  
-----

The PUC's final order on the merger proceeding allows the transaction to be consummated but imposes certain conditions to be satisfied prior to closing. The conditions relate to the mitigation of market power through membership in an independent system operator ("ISO"), an entity that would operate the transmission facilities of Duquesne, AYE and other utilities in the region. The PUC order will allow DQE and AYE to satisfy this condition through their current membership in the Midwest ISO, but the PUC held that the Midwest ISO must be "fully functional" and it must satisfy seven criteria specified by the PUC before the merger is consummated.

DQE does not expect that these conditions can be satisfied within the time periods specified in the Merger Agreement. The Merger Agreement provides that either party may terminate the Agreement by October 5, 1998, if certain conditions have not been satisfied by that date or, if that date has been extended pursuant to the Agreement, closing has not occurred by April 5, 1999. The Midwest ISO is not expected to be fully operational until June 30, 2000. In addition, the Midwest ISO, as presently constituted and as proposed to the Federal Energy Regulatory Commission, does not meet the seven criteria specified by the PUC.

There can be no assurance that the foregoing conditions will be modified on a timely basis. If the foregoing conditions are not removed, or alternative conditions acceptable to DQE are not adopted, in a timely manner, the merger may not be consummated.

The PUC's final orders also addressed the companies' Restructuring Plan for the recovery of stranded costs by Duquesne and AYE's wholly owned utility subsidiary West Penn Power Company ("West Penn") in the event the merger is consummated. The order on the Restructuring Plan sets stranded costs using an administrative forecast of generation market values and costs. Applied to Duquesne, and compared to Duquesne's Stand-Alone Plan, this methodology results in the disallowance of an additional \$370 million in stranded costs (net present value, pre-tax). The PUC order also reduces Duquesne's recoverable stranded costs by \$152 million for estimated generation-related merger synergies and reduces distribution rates beginning January 1, 2000, by \$15 million annually to reflect estimated distribution-related merger synergies.

With respect to West Penn, the PUC's order disallows recovery of approximately \$1 billion of West Penn's stranded cost claim (net present value, pre-tax). Of the disallowed amount, approximately \$830 million relates to the impact of the administrative determination of generation market value and costs. The other disallowances relate to regulatory assets, non-utility generation and other transition costs. In addition, the PUC order reduces West Penn's recoverable stranded costs by \$71 million for generation-related merger synergies and reduces distribution rates beginning January 1, 2000, by \$9 million for distribution-related merger synergies. AYE has indicated that it will seek reconsideration and/or judicial review of the stranded cost disallowances.

There can be no assurance that the disallowances associated with the merger and the Restructuring Plan will be modified by the PUC or on appeal. If the disallowances are not reversed on a timely basis, the merger may not be consummated.

DQE presently is assessing the status of its proposed business combination with AYE in light of the recent orders issued by the PUC. In the event that such orders are not modified on a timely basis, DQE will determine whether, to the extent all conditions necessary to consummate the merger are not satisfied, any such conditions should be waived by DQE.

Items 6-9. Not applicable.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

DQE, Inc.

-----  
(Registrant)

Date June 12, 1998  
-----

/s/ Morgan K. O'Brien  
-----

(Signature)

Morgan K. O'Brien  
Vice President and Controller

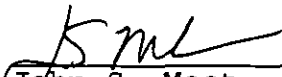
BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Joint Application of DQE, Inc.,	)	
Allegheny Power System, Inc. and	)	
AYP Sub, Inc. for approval of the	)	
transfer by merger of the	)	Docket No. A-110150F.0015
property and rights of Duquesne	)	
Light Company to Allegheny	)	
Power System, Inc.	)	
Application of Duquesne Light	)	
Company for approval of its	)	Docket No. R-00974104
restructuring plan under Section	)	(not consolidated)
2806 of the Public Utility Code	)	

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of the foregoing document, by overnight courier, upon the participants on the attached service list in accordance with Section 1.54 of the Commission's regulations.

Dated this 15<sup>th</sup> day of June, 1998.

  
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HONORABLE H WILLIAM DEWEESE  
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JUN 15 1998 3:03PM

PUC (Sec. Bureau)

Hbg. Pa. 17105 F0015

NO. 8785 P. 12

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90TH LEGISLATIVE DISTRICT

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

**ORIGINAL**

KJR

Pennsylvania Public Utility )  
Commission, )  
v. )  
Duquesne Light Company )  
Application to approve )  
restructuring plan pursuant )  
to 66 Pa. C.S. § 2806(d) )

Docket No. R-00974104

**PETITION FOR CLARIFICATION OR RECONSIDERATION  
OF DUQUESNE LIGHT COMPANY  
REGARDING STAND-ALONE RESTRUCTURING PLAN**

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Pursuant to 52 Pa. Code § 5.572, Duquesne Light Company

("Duquesne") hereby petitions the Commission for clarification or, in the alternative, reconsideration of its final order issued on May 29, 1998 regarding Duquesne's stand-alone restructuring plan ("Final Order"). The stand-alone restructuring plan applies in the event that DQE's merger with Allegheny Energy, Inc. is not consummated. Duquesne also is submitting today a separate petition for reconsideration that addresses additional issues that arise only if the merger is consummated.<sup>1</sup>

The principal purpose of this petition is to correct computational errors that appear in the attachments to the Final Order. These errors affect the

<sup>1</sup> The petition addresses the Commission's administrative determination of stranded costs and its findings on market power mitigation.

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calculation of transmission and distribution rates ("T&D rates"), competitive transition charges ("CTC") and shopping credits. While these errors appear inadvertent, and Duquesne will submit a compliance filing that corrects these errors, Duquesne is addressing them here as well to provide interested parties an additional opportunity to review and comment on the corrections.<sup>2</sup> Duquesne also is requesting clarification or, in the alternative, reconsideration on other rate and CTC issues that are not purely computational errors.

The Commission should expedite consideration of this petition. Expedition will ensure that the calculational issues are resolved in the event that any appeal of the Final Order is taken.<sup>3</sup> Such an appeal could preclude the Commission from clarifying the computational issues raised here.<sup>4</sup>

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<sup>2</sup> It should be noted that many of these calculational issues arise whether or not the merger is consummated – *i.e.*, they are relevant to the calculation of CTCs regardless of whether stranded costs are determined through an auction, whether merger synergies are deducted from T&D rates, and whether shopping credits are based on the pilot credits or the PECO methodology.

<sup>3</sup> A *petition for review* in the Commonwealth Court already has been filed by an intervenor, Hospital Shared Services. In addition, it may be necessary for Duquesne to appeal the Commission's administrative determination of stranded costs that applies in the context of the merger, depending on the outcome of the petitions for reconsideration filed by Duquesne and West Penn on that issue.

<sup>4</sup> The Commission may, however, chose to resolve these issues in the context of Duquesne's compliance filing, rather than this petition for reconsideration.

Duquesne requests clarification or, in the alternative, reconsideration of the following issues:

**Total Bundled Rate**

1. Attachment A to the Final Order calculates shopping credits using a total bundled rate that reflects Duquesne's proposed roll-in of the ECR at 14.7 mills/kWh. Duquesne requests clarification that the ECR roll-in was approved by the Commission. For the reasons stated in Duquesne's Brief on Exceptions, the statute requires the roll-in under the circumstances here. DLC Br. on Exc. at 30.

2. Attachment A reflects a system average bundled rate for 1999 of 8.93¢/kWh. This rate is based on 1996 volumes inclusive of the ECR roll-in. Applying projected 1999 volumes to currently approved rates (inclusive of the ECR roll-in) results in a system average bundled rate of approximately 8.75¢/kWh for 1999. This correction, which will be reflected in the compliance filing, should be approved.

**Transmission and Distribution Rates**

3. Attachment E reflects a distribution revenue requirement (\$253,687,253) that already has distribution losses removed. Attachment E then removes them a second time in calculating an approved system-average distribution rate. Because the resulting figure reflects the removal of distribution losses twice,

Duquesne's compliance filing will include the corrected figure. This correction should be approved.

4. Attachment E reflects the transmission revenue requirement filed by Duquesne in its case-in-chief. Since that time, however, the FERC has approved a lower transmission revenue requirement in the settlement of Duquesne's open access transmission rate case. Duquesne Light Co., FERC Docket No. OA96-56-000. Duquesne will use the FERC-approved revenue requirement in developing retail transmission and ancillary service rates. Consistent with the Final Order (p. 51), these rates will not be "filed" with this Commission, but rather will be included for informational purposes only. Duquesne will charge transmission and ancillary service rates directly to suppliers unless the retail customer contracts directly with Duquesne pursuant to its open access tariff. These clarifications, which will be reflected in the compliance filing, should be approved.

5. Attachment E reflects a transmission and distribution revenue requirement calculated on the basis of required, rather than realized, rates of return. Consistent with the Final Order, Duquesne's compliance filing will calculate the total T&D revenue requirement using realized rates of return. This correction should be approved.

6. Attachment E reflects a single calculation of the "Total T&D Rate." The Final Order, however, recognizes that the transmission component of this

rate is FERC-jurisdictional and states that the transmission rates should not be filed with this Commission. Final Order at 51. Consistent with that finding, Duquesne will calculate PaPUC-jurisdictional distribution rates for inclusion in the compliance filing. Duquesne will calculate distribution charges by deducting the FERC-approved transmission revenue requirement from the PaPUC-approved total T&D revenue requirement. This correction should be approved.

7. Attachment E reflects a total T&D rate using a 1996 revenue requirement divided by 1999 sales volumes (projected by the OCA). The correct calculation divides the approved 1996 revenue requirement by 1996 sales volumes. The resulting T&D rates for each class will not change throughout the rate cap period. (The system average T&D rate, however, will change over time due to changes in sales growth among classes.) The correction should be approved.

8. The Final Order approves an increase in funding for universal service. Consistent with the Final Order, Duquesne will track and reconcile these costs as follows. Universal service program related costs will be estimated for service rendered April 1 through March 31 of each year, commencing in 2000. These costs will be allocated to each class according to each classes' distribution allocation factor. The difference (determined to the nearest 1 mill/kWh) will be applied to all kWh delivered under the tariff and compared to the base universal service charges approved for each class. This tariff also includes an over/under

collection provision as computed for each rate schedule as of the end of the reconciliation period. The application of the universal service charge mechanism will be subject to continuous review and audit by the Commission at such intervals as it shall determine appropriate. These are the same procedures Duquesne has used historically for reconciliation of the ECR.

### **CTC Calculation and Stranded Cost Issues**

9. Attachment D sets forth a revenue requirement for deferred taxes and a monthly schedule for a return "on" (but not of) the deferred tax balance. The appropriate treatment of deferred taxes, which will be reflected in the compliance filing, is as follows. First, the Final Order approves a specific level of stranded costs (net of deferred taxes) and also determines a deferred tax balance associated with the approved stranded cost amount.<sup>5</sup> Second, Duquesne is entitled to recovery of the deferred tax balance, but is not entitled to a return on that balance. This is consistent with traditional ratemaking practice, which calculates "rate base" net of deferred taxes and allows amortization of the outstanding deferred tax balance. Third, pursuant to the Final Order, the deferred tax balance will be amortized on a straight-line basis (i.e., an equal amount of deferred taxes is amortized each month of

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<sup>5</sup> If, however, the approved level of stranded costs is modified on reconsideration, or when the auction is completed, the deferred tax balance would be adjusted accordingly.

the transition period) to ensure that the CTC is levelized. These clarifications should be accepted.

10. Duquesne's Brief on Exceptions stated that, consistent with the Commission's decision in Docket No. M-00970917, the compliance filing will include an updated deferred fuel balance as of the date of the Final Order (May 29, 1998). DLC Br. on Exc. at 22-23. Duquesne will include this updated amount in its compliance filing. This clarification should be approved.

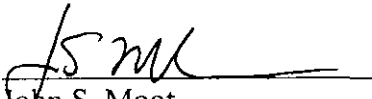
11. The Final Order finds that, if the merger is approved, the approved stranded costs and T&D rates shall be net of merger synergies. Duquesne's compliance filing for its stand-alone restructuring plan, which applies in the event the merger is not consummated, will not include merger synergies. This clarification should be approved.

12. The Recommended Decision approved the recovery of \$221,000 of Deferred Rate Synchronization Costs (Tax Effect) as a regulatory asset. The Final Order appears to have inadvertently omitted this regulatory asset from Attachment B. The Commission should clarify that this regulatory asset was approved.

WHEREFORE, the petition for clarification or reconsideration should be granted. In the alternative, the Commission should find that these matters are more appropriate addressed in Duquesne's compliance filing.

Respectfully submitted,

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Dated: June 15, 1998

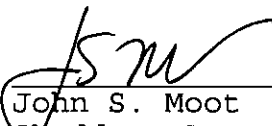
BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

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 a copy of the foregoing document, by overnight courier, upon the participants on the attached service list in accordance with Section 1.54 of the Commission's regulations.

Dated this 15<sup>th</sup> day of June, 1998.

  
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COMMONWEALTH OF PENNSYLVANIA

DATE: June 17, 1998

SUBJECT: A-110150F0015, R-00974104  
(not consolidated)

KJR

TO: Law Bureau

FROM: *WJZ* James J. McNulty, Secretary

JOINT APPLICATION OF DQE, INC., ALLEGHENY POWER SYSTEM, INC. AND AYP SUP, INC. FOR APPROVAL OF THE TRANSFER BY MERGER OF THE PROPERTY AND RIGHTS OF DUQUESNE LIGHT COMPANY TO ALLEGHENY POWER SYSTEM, INC. (A-110150F0015)

APPLICATION OF DUQUESNE LIGHT COMPANY FOR APPROVAL OF RESTRUCTURING PLAN (R-00974104)

Attached is copy of a Petition for Expedited Reconsideration of DQE, Inc. and Duquesne Light Company Regarding Merger and Joint Restructuring Plan filed in connection with the above docketed proceeding.

This matter is assigned to your Bureau for appropriate action.

**DOCKETED**

JUN 18 1998

Attachment

cc: OSA

wjz

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COMMONWEALTH OF PENNSYLVANIA

DATE: June 17, 1998

SUBJECT: R-00974104

TO: Office of Special Assistants

KJR

FROM: *WJZ* James J. McNulty, Secretary

APPLICATION OF DUQUESNE LIGHT COMPANY FOR APPROVAL OF  
RESTRUCTURING PLAN

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Attached is copy of a Petition for Clarification or Reconsideration of Duquesne Light Company Regarding Stand-Alone Restructuring Plan filed in connection with the above docketed proceeding.

This matter is assigned to your Bureau for appropriate action.

Attachment

cc: Law Bureau

wjz

**DOCKETED**  
JUN 18 1998

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FOLDER