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November 5, 1998

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

James J. McNulty
Secretary
Office of the Prothonotary
Pennsylvania Public Utility Commission
North Office Building
Harrisburg, Pa. 17105-3265

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

Dear Secretary McNulty:

Enclosed for filing is supplemental information regarding Duquesne's Generation Auction Plan. This information relates to (i) the effect of the auction on employees, (ii) the auctioning of the provider of last resort ("POLR") service, and (iii) responses to certain data requests of the Office of Trial Staff ("OTS"). To ensure that parties have the opportunity to review this material before filing comments (which are due, at the latest, on November 9, 1998), Duquesne is serving all active parties by facsimile.[1]

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1 The response time is not significantly shorter than the seven days' response time the Commission has provided for comments on Duquesne's compliance filings, which are far more complex than the materials being submitted herewith. However, to the extent parties believe additional time is necessary to comment on the materials contained herein, Duquesne would not object to supplemental comments being filed on these items by November 13, 1998.

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1. Effect on Employees

Duquesne is pleased to submit, attached as Exhibit A, a description of the enhanced severance, early retirement plan, retraining program and outplacement services that are being offered to management (non-union) employees of Duquesne. This plan will provide such employees commercially reasonable protections during the course of the auction. These protections are consistent with Duquesne's stated objective to treat its employees fairly during the auction process. Duquesne believes that its employees will be valuable assets to potential generation purchasers and that, for such employees that are not retained by the asset purchaser(s), there should be adequate protections as set forth in Exhibit A.

Duquesne's union employees will be protected by the terms of the existing Collective Bargaining Agreement ("CBA") between Duquesne and the Union.[2] The CBA, negotiated in 1996 when Duquesne was developing its response to proposed customer choice legislation, specifically addresses the circumstance of a sale of generating assets. In such a circumstance, the purchaser of Duquesne's generating assets is not required to assume the CBA and Duquesne is permitted to reduce Union workforce levels (and, in such an event, severance benefits are provided for affected workers). The CBA also provided income protection, retraining expenses and an early retirement option similar to that being offered to management employees.

In addition to the foregoing terms, Duquesne commenced negotiations with the Union prior to the filing of the Auction Plan and offered an *enhanced* package providing additional benefits and protections to Union employees. How-

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[2] Duquesne's union employees are represented by System Council U-10 and the affiliated local unions of the International Brotherhood of Electrical Workers ("the Union").

ever, after months of negotiations, including the use of a federal mediator, Duquesne has not been able to reach a new agreement with the Union that is agreeable to both parties. Duquesne believes that its enhanced proposal (attached hereto as Exhibit B) was reasonable, particularly given that the existing CBA already provides for a sale of generating assets. The Union declined to accept this offer, however, and Duquesne therefore will proceed with the auction under the terms of the CBA. This is inherently fair to the Union, as these are the very terms regarding a sale of generating assets that the Union agreed to in 1996. To the extent, however, that a new agreement can be reached with the Union prior to commencement of the auction (expected in January 1999), Duquesne would revise its offering memorandum to potential purchasers to reflect the terms of such new agreement and would promptly inform this Commission of such terms.

The protections offered by Duquesne to Union and non-union employees will result in costs that will reduce the net proceeds from the sale of its generating plants. These costs will be accounted for in a manner consistent with Appendix G to Duquesne's Generation Auction Plan. This accounting is consistent with the Customer Choice Act, which provides for the recovery of "costs of employee severance, retraining, early retirement, outplacement and related expenses, at reasonable levels, for employees who are affected by changes that occur as a result of the restructuring of the electric industry occasioned by this chapter." 66 Pa.C.S. § 2803.

2. POLR Service

In the Generation Auction Plan, Duquesne stated that it would explore the sale of POLR service and, if such a sale was attractive, the net proceeds would be used to reduce stranded costs. Duquesne today is making its third compliance filing implementing the findings in Duquesne's restructuring case. This compliance filing includes (attached as Exhibit C) shopping credits for each rate schedule for each year

of the transition period. It is Duquesne's intention to market the POLR service using these shopping credits. The winning bidder for this service would assume an obligation to supply wholesale power to Duquesne in the quantities required by nonshopping customers at the rates set forth in Exhibit C. To facilitate such an auction, it is important that the Commission provide assurance to potential bidders that these shopping credits will not be changed by the Commission in the future, which could frustrate the terms of the POLR sale. Duquesne is therefore requesting a Commission finding that such shopping credits will not be changed by future order of the Commission.[3] Providing such certainty should materially enhance the value of the POLR service in an auction.

Duquesne notes that it is *voluntarily* offering to auction the POLR service and to use net proceeds to reduce stranded costs. Duquesne is the *only* Pennsylvania utility that has offered to do so. Duquesne's offer, however, is contingent on the Commission accepting, without material modification, the Generation Auction Plan, as amended by the Generation Exchange with FirstEnergy. To the extent material modifications are made, Duquesne could withdraw this proposal, thereby eliminating any potential benefits to customers from an auction of the POLR service.

3. Data Responses to the Office of Trial Staff

Duquesne also is enclosing its response to data requests submitted by the OTS (Exhibit D).

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[3] If the net proceeds from the auction reduce stranded costs, Duquesne would shorten the recovery period for each rate schedule rather than adjusting their shopping credits.

Thank you for your consideration of these additional materials.

Sincerely,

John S. Moot

Enclosures

cc: All persons on official service list (active parties by facsimile)

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EXHIBIT A

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Duquesne Light

CURRENT TOPICS

A ROUND-UP OF COMPANY AND INDUSTRY NEWS ■ PUBLIC AFFAIRS UNIT – 393-6071 (FAX) 393-6085

October 12, 1998

DUQUESNE LIGHT COMPANY APPROVES MANAGEMENT EARLY RETIREMENT OPTION AND DIVESTITURE SEVERANCE PACKAGE

Duquesne Light Company has approved an early retirement option for eligible management employees and a severance package for certain management employees affected by the company's generation divestiture plan. These special programs will be offered if the Pennsylvania Public Utility Commission approves the company's plan for divestiture of its generation plants on terms that are acceptable to the company.

The early retirement option will be available during a stated election period to all management employees of Duquesne Light who are at least 58 years old and have 10 years of service as of the date of the election period. The beginning and ending dates of the election period will be determined and announced in the future. The early retirement option under the Supplemental Plan will include:

- no penalty for early retirement,
- enhanced benefit calculation multiplier of 1.9 percent,
- Social Security bridge payments of $400 per month until age 62, or a minimum of 12 months of such payments, and
- an additional 3 years of service for benefit calculation purposes.

Retirements must occur within the 12 months following the close of the election period. Management will determine the actual retirement date for each employee, but employee preferences will be taken into consideration. An individual must be employed on the date he or she elects to participate in order to be eligible for the early retirement option.

The severance plan will be available to management employees whose positions will be eliminated as a result of the divestiture, who are not offered positions with DQE, and who do not receive a "qualifying offer" from buyer(s) of our generation plants. A qualifying offer is defined as an offer of employment with cash compensation (excluding overtime) of at least 90 percent of the employee's regular cash compensation (excluding overtime and any special compensation).

Components of the severance plan will be:

- 2 weeks of pay for each year of service (six-month minimum, 12-month maximum), payable as salary continuation,
- benefits for term of salary continuation, and
- outplacement, reimbursement for career training and, in some cases, relocation assistance.

This overview is being provided in an effort to keep employees informed about divestiture-related developments in as timely a manner as possible. Additional information will be provided as its becomes available. Actual terms and conditions will be governed by applicable law and legal documents. Questions regarding this announcement can be directed to your group human resources manager.

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SECRETARY'S BUREAU

EXHIBIT B

This offer will remain in effect until 11:59 p.m October 30, 1998.

COMPANY PROPOSAL

MEMORANDUM OF AGREEMENT

This Agreement is made and entered into by and between Duquesne Light Company (hereinafter called the "Company") and System Council U-10 and its affiliated Local Unions 140, 142, 144, 147, 148 and 149 of the International Brotherhood of Electrical Workers (hereinafter collectively called "the Union").

1. Pursuant to the Order of the Pennsylvania Public Utility Commission, the Company is required to sell at auction or otherwise divest itself of those assets generally described in the attached and incorporated Appendix A (hereinafter called "Generation" or "Generation Assets").

2. It is the Company's intent and desire to sell or otherwise divest itself all such assets, but the parties recognize and hereby acknowledge that suitable buyers may not be found for each and every Generation Asset. Accordingly, the Company and the Union have bargained about the effects of the required sale or other disposition, including shutdown of Generation Assets as set forth in more detail below.

3. The parties agree that the provisions set forth in this Agreement are subject to the approval of the Pennsylvania Public Utility Commission (hereinafter called the "Pa PUC") as part of the Company's Generation Auction Plan to be filed with the Pa PUC pursuant to its May 29, 1998 Order, and that this Agreement will not be binding on either party absent such Pa PUC approval except as provided in Paragraph 7 below. The Union agrees that it will not oppose the Company's efforts to obtain the Pa PUC's approval of the provisions contained herein.

4. Where this Agreement conflicts with the Collective Bargaining Agreement effective from October 31, 1996 to September 30, 2001 (hereinafter called the "Labor Agreement"), or any other Company-Union agreement, program or plan, this Agreement will prevail.

5. As part of the divestiture process, the Company will require a buyer (or each buyer if there is more than one) of any portion of the Company's Generation Assets to agree to:

a. Recognize the Union as the exclusive bargaining agent for all those Company employees who become employees of the buyer.

b. Become party to and otherwise assume the Labor Agreement, as amended by this Memorandum of Agreement, including its job security provisions and including all other written agreements that are currently in effect between the Union and the Company The parties agree to meet and identify those other written agreements.

c. Meet its staffing requirements related to that asset by offering work to Company employees then performing such work related to that asset.

d. To the extent a Buyer's staffing requirements are less than current Company staffing, offer work in the needed positions to the most senior Company employees in those positions.

e. Establish, for the length of the Labor Agreement, benefit plans, including a pension plan and 401(k) plan that, to the

extent possible, provide a comparable level of benefits and are based on the same eligibility criteria as those set forth in the Labor Agreement. There will be no transfer of pension plan assets from the Company to the Buyer. The Buyer's pension plan shall provide pension benefits which, in combination with the benefits provided under the Company's pension plan, are no less than the benefits which would be provided to employees whose entire service and earnings history had been covered by the Company's pension plan as presently in effect. Existing balances in the 401(k) Plan will be transferred to the Buyer's 401(k) Plan. All 401(k) participants shall be fully vested in the transferred account balances.

6. The Labor Agreement assumed by a buyer will be amended as necessary and reasonable to reflect the assets purchased by that buyer and positions applicable to those assets.

7. The bidding and bumping provisions in the Labor Agreement are modified effective the date of ratification of this Agreement. The Union agrees that its members, excluding those members who are in Nuclear Operations or Nuclear Maintenance, will be allowed to bid or bump only in the division (i.e., Nuclear, Cheswick, Elrama, or T&D) in which they are employed at the time of the ratification of this Agreement from the date of ratification until the close of the sale, shutdown or other disposition of the Generation Asset to which they are assigned. During this period of time, if the Company deems it necessary to fill positions for which there are no qualified bidders within the division the vacancy occurs, the Company will, when possible, fill such positions with upgrades. When the Company deems it impossible or impractical to upgrade to fill positions, it may fill such positions with new hires and/or contractors. The Union agrees that its members, who at the time of the ratification of this Agreement are in Nuclear Operations or Nuclear Maintenance, will not be eligible to bid or

bump any position from the date of ratification of this Agreement until the close of the sale, shutdown or other disposition of Beaver Valley.

8. The Company will offer a Special Retirement Option to Union employees who are at least 58 years of age, and have at least 10 years of service with the Company as of the date to be determined by the Company. The beginning and ending dates of the election period will be determined and announced in the future. Retirements will occur within the 12 months following the close of the election period. The Company will determine the actual retirement date for each employee but employee preferences will be taken into consideration. The early retirement penalty will be eliminated for purposes of this Special Retirement Option only. The pension multiplier will be increased from 1.4% to 1.5% for past and future service, pursuant to covered compensation as defined under the Trusteed Pension Plan. The past service window will be moved three years forward from where it is at the time of the effective date of the special retirement offer. A $400 per month supplement to age 62, or 12 months at the option of the participant, will also be provided. Employees who elect this Special Retirement Option will not be eligible for any other severance benefits of any kind, including, without limitation, separation allowance as described at Page 173 of the Labor Agreement or the transition package in Paragraph 12.

9. During negotiations, the parties discussed positions that are Generation asset positions. It is understood that all employees located within the plants are "Generation." There are additional positions within T&D, Customer Operations and the Administrative groups that support Generation and therefore will be designated as "Generation positions." The Company will, as soon as practical, create and provide to the Union a list of all such Generation Asset positions and employees designated as "Generation" and currently in such Generation positions. Such employees will be referenced hereinafter as "Generation Employees." Upon the effective date of the sale, shutdown or other disposition of a Generation Asset, Company employment for all such employees who did not elect or were not eligible to elect the Early Retirement Offer in Paragraph 8 and who are offered work with the Buyer will cease for any and all purposes, and such employees will receive no severance benefits of any kind from the Company, including,

without limitation, separation allowance as described at page 173 of the Labor Agreement, or the transition package in Paragraph 12.

10. Generation Employees who did not elect or were not eligible for the Early Retirement Offer in Paragraph 8 and who are not offered work by a buyer of a Company Generation Asset, including those employees who are assigned to a Generation Asset that is not sold and therefore shut down, will be offered a choice of bumping into another position in the Company or accepting the transition package in Paragraph 12. Article VI A.6 of the Labor Agreement will no longer apply to employees who elect to bump into another position within the Company. The Company employment and seniority of those employees who opt for the transition package in Paragraph 12 will cease for all purposes upon the earlier of either of their last day of work for the Company or acceptance of the transition package. Such employees will have no recall rights with the Company.

11. As to those employees who choose to bump, the parties agree to administer the bumping procedure in the most efficient manner, including, without limitation, at the Company's sole discretion, advance and concurrent mass testing, use of electronic media to send and retrieve materials, and waiving demonstration portions of equipment when currently holding similar positions. The Company agrees to meet with the Union to explain the bumping procedures prior to any mass bumping exercise.

12. The Company employment of those employees who are displaced because of the bumping process in Paragraphs 10 and 11, and who are unable to displace other employees, will cease, although such employees will have recall rights in accordance with the Labor Agreement. For all such employees, the following transition package will be paid, subject to legally required deductions, in lieu of any other wages or benefits set forth in the Labor Agreement. If an employee who receives this transition package is recalled to the Company in accordance with the Labor Agreement, it will be in the Company's sole discretion whether, and to what extent, the employee must return a pro-rated portion of the package.

a. The Company will pay separation pay equal to one and one-half weeks of straight time pay, exclusive of any add-ons, such as shift differential, for each completed year of service with a maximum of one year to be paid as salary continuance.

b. Medical and dental coverage for the period covered by the separation pay with employees paying the contribution required by the Labor Agreement to maintain eligibility for such coverage.

c. Outplacement services offered by an outplacement provider of the Company's choosing for the period of the separation pay.

d. Reimbursement up to $2000 for career training upon proof of enrollment and successful completion in such a course or a program. This reimbursement will be available for up to 24 months from the date an employee's employment with the Company ceases.

e. The Company agrees to pay relocation expenses of up to $1500 for the cost of moving household items, upon submission of receipts, and copy of an offer letter from a new employer requiring and verifying relocation.

13. Consistent with Article IV of the Labor Agreement concerning the Company's ability to lay off employees "under extraordinary circumstances, such as sale or shut down of a plant," nothing in this Agreement which results in cessation of employment and/or displacement

of employees will require the Company to reduce the level and/or number of contractors being used.

14. Any disputes arising out of this Memorandum of Agreement will be subject to the Labor Agreement's Grievance and Arbitration procedure.

15. This Memorandum of Agreement will expire on September 30, 2001, but the rights accorded to certain employees in Paragraph 12 will continue as described in Paragraph 12.

WITNESS the execution hereof this _____ day of October, 1998.

INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS, AFL-CIO	DUQUESNE LIGHT COMPANY
By: ______________________	By: ______________________

(ooprop2)

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EXHIBIT C

Shopping Credits (c/kWh)	1999	2000	2001	2002	2003	2004	2005	2006	2007
RA	4.15	4.79	5.02	5.22	5.42	5.62	5.84	5.95	6.05
RS	4.50	4.55	4.63	4.71	4.81	4.93	5.10	5.13	5.15
RH	3.93	2.62	2.71	2.80	2.92	3.05	3.24	3.28	3.30
GS/GM	4.16	4.98	5.12	5.25	5.40	5.56	5.74	5.82	5.89
GMH	3.89	3.65	3.79	3.93	4.07	4.23	4.41	4.49	4.56
GL	3.49	4.04	4.13	4.21	4.30	4.40	4.52	4.57	4.61
GLH	3.52	3.53	3.62	3.71	3.80	3.91	4.04	4.09	4.13
L	3.14	3.05	3.11	3.17	3.23	3.30	3.39	3.43	3.45
HVPS	2.70	3.00	3.03	3.05	3.08	3.12	3.17	3.18	3.18
AL	4.09	3.06	3.15	3.25	3.36	3.50	3.70	3.73	3.75
SE	4.17	2.02	2.09	2.17	2.26	2.36	2.52	2.55	2.56
SM	7.84	2.93	3.08	3.23	3.43	3.66	3.99	4.04	4.07
SH	5.36	8.29	8.36	8.43	8.52	8.62	8.77	8.80	8.81
MTS	4.68	5.74	5.80	5.87	5.95	6.05	6.19	6.21	6.22
System Average	3.79	4.22	4.31	4.40	4.50	4.61	4.75	4.80	4.84

Notes:

Shopping credits in 1999 are based on the pilot methodology. Thereafter, shopping credits (post-auction) are set at levels consistent with the May PaPUC Order. Shopping credits include energy and capacity, T&D losses, ancillary services, and GRT.

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SECRETARY'S BUREAU

EXHIBIT D

DUQUESNE LIGHT COMPANY
RESPONSE TO DATA REQUESTS
OF THE OFFICE OF TRIAL STAFF

OTS-1 Provide a detailed schedule or study that shows a cost/benefit analysis relating to the ratepayers from the generation exchange with FirstEnergy.

Response This information was provided to all parties by letter of October 29, 1998 and accompanying attachments. That information showed that the generation exchange will benefit ratepayers viewed from the perspective of (i) a comparison of the respective values of the assets being exchanged using a discounted cash flow analysis or (ii) from the perspective of the marketability of such assets in an auction.

OTS-2 Provide a detailed explanation discussing Duquesne's statement in the October 14, 1998 report to the Commission, page 3, that "it is expected that wholly owned fossil generation will be more marketable than encumbered nuclear and fossil interests." Provide support for this statement.

Response This information was provided in the attachments to Duquesne's October 29, 1998 letter. As explained therein, <u>every</u> investment banker interviewed by Duquesne supported the generation exchange as preferable to a sale of Duquesne's CAPCO assets.

OTS-3 Will Duquesne be responsible for environmental remediation at the Beaver Valley and Perry plants after the exchange? Explain.

Response The specific allocation of liabilities regarding environmental matters will be set forth in the definitive agreements for the generation exchange and the auction of the fossil assets. It is Duquesne's expectation, however, that, consistent with recent auctions, the purchaser of generating assets will assumes most environmental liabilities associated with the plant site.

OTS-4 — Will Duquesne be legally responsible for environmental remediation at any of its other generation facilities after the generation auction? Explain.

Response — See answer to OTS-3.

OTS-5 — Will Duquesne be responsible for its share of the decommissioning fund for Beaver Valley and Perry after the generation exchange? Is the nuclear decommissioning fund already collected by Duquesne exchanged with the other generation assets? Explain.

Response — The existing decommissioning funds and the additional funding approved by the Commission in the Restructuring Order will be transferred to FirstEnergy, which amounts will serve as a cap on Duquesne's decommissioning liability for these plants.

OTS-6 — Will Duquesne be responsible for its share of the decommissioning fund for all other generation assets after the generation auction? Is the fossil fuel decommissioning fund already collected by Duquesne included with the other generation assets to be transferred? Explain.

Response — Duquesne will not be responsible for fossil decommissioning. Given that no funding for such amounts was authorized by the PaPUC, there is no funding to be transferred to FirstEnergy.

OTS-7 — Explain which party will own the spent fuel rods and be responsible for their disposal after the Beaver Valley and Perry exchange with FirstEnergy.

Response — FirstEnergy.

OTS-8 — Provide a schedule showing a time line of events relating to the generation auction.

Response — See Appendix H of Duquesne's Generation Auction Plan. This time line remains in effect following the generation exchange, with the only exception being that the nuclear interests may be transferred prior to the closing of the auction if practicable. See Agreement in Principle § 7.

OTS-9 Provide OTS with copies of the questions of other parties and Duquesne's response in relation to the generation exchange and auction.

Response Duquesne has and will comply with this request.

OTS-10 If one entity receives the winning bid for all the generation that is to be auctioned, provide a discussion explaining the market power problems that would result.

Response As the OTS is aware, such a market power analysis cannot be performed without knowing the identity of the winning bidder. That is why market power will have to be considered throughout the auction process. See Generation Auction Plan at 11-12.

OTS-11 Provide a detailed discussion explaining Duquesne's plan for supplier of last resort. How will the energy purchases for supplier of last resort be trued up? Please explain.

Response Duquesne is requesting authorization to market the POLR service at the shopping credits set forth in Exhibit C to Duquesne's letter of November 5, 1998. Other material elements regarding the sale of POLR service, if such a sale is determined to be reasonable during the course of the auction, would be described in a subsequent filing with the Commission following the auctioning of the service and would be subject to comment by the parties at that time. OTS should recognize that, because Duquesne is the first company to offer to auction a service of this kind, Duquesne will need to test the market to determine the extent to which the market values the service and, if there is material value, pursuant to which terms. As indicated, Duquesne will make a subsequent filing if the process proves successful.

OTS-12 Provide a study showing the HHIs and market power before and after the generation exchange.

Response As the OTS is aware, such a market power analysis cannot be performed without knowing the identity of the winning bidder for the FirstEnergy plants.

OTS-13 Explain how Duquesne can be unbiased in the market power analysis in determining whether to place any limitations on the generation bidders. Could any of Duquesne's affiliates that bid in the auction benefit from Duquesne's market power analysis and subsequent restrictions?

Response Neither Duquesne nor any affiliate will bid in the auction. The relevant regulatory agencies will make final determinations regarding the effect of the auction on market power and thus the suggestion that Duquesne may have a "bias," even if well founded (which it is not), is irrelevant.

OTS-14 Can a Duquesne affiliate participate in the generation auction?

Response No.

OTS-15 Will the Commission have a final determination of the transferring of plants to any particular bidders? If not, why not?

Response The question calls for a legal opinion. It is Duquesne's intention to make a filing with the Commission subsequent to the announcement of the winning bidder(s) that will give the Commission the opportunity to review the auction results and exercise any jurisdiction that it may have with respect thereto.

SCOTT J. RUBIN
Public Utility Consulting

3 Lost Creek Drive
Selinsgrove, PA 17870-9357

(717) 743-2233 (Voice)
(717) 743-8145 (Fax)
e-mail: sjrubin@ptd.net

November 5, 1998

ORIGINAL EEF

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

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

Dear Mr. McNulty:

Enclosed for filing please find two documents relating to the above-referenced matter: (1) an original and three (3) copies of the Petition to Intervene of Local 272, IBEW, and (2) an original and ten (10) copies of the Comments of Local 272, IBEW. A copy of each document has been served on all parties of record, as shown on the attached certificate of service.

In addition, I have enclosed an extra copy of each document that I would appreciate having time stamped and returned to me in the enclosed envelope. Thank you for your cooperation.

Sincerely,

Scott J. Rubin, Esq.

DOCUMENT FOLDER

Enclosures

cc: All parties of record
Hon. John Quain
Hon. Robert Bloom
Hon. David Rolka
Hon. Nora Mead Brownell
Hon. Aaron Wilson, Jr.
Office of Special Assistants

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BEFORE THE
COMMONWEALTH OF 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

PETITION TO INTERVENE OF
LOCAL 272, INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS

Pursuant to 52 Pa. Code §§ 5.71, *et seq.*, Local 272, International Brotherhood of Electrical Workers ("Local 272") files this Petition to Intervene out of time in this proceeding. In support of this petition, Local 272 states as follows:

1. Local 272 is the authorized bargaining representative for approximately 350 employees of FirstEnergy Corporation ("FirstEnergy") at the Bruce Mansfield generating station in Beaver County, Pennsylvania.

2. All documents should be served on Local 272 in the following manner:

Dennis Bloom
Local 272, IBEW
617 Midland Avenue
Midland, PA 15059
Phone: (724) 643-4210
Fax: (724) 643-8720

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3. Local 272 will be represented in this case by the undersigned who already appears on the service list in this matter as counsel for System Council U-10, IBEW, the authorized bargaining representative of the employees of Duquesne Light Company ("Duquesne").

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4. Local 272 will or may be directly and adversely affected by a decision of the Public Utility Commission ("Commission") in this matter. In particular, under Duquesne's proposed swap of generating plants with FirstEnergy, FirstEnergy would become the operator of the Beaver Valley nuclear station, which is in close proximity to the Bruce Mansfield plant. Local 272 is concerned that FirstEnergy would then attempt to reduce the work force at one or both plants by asking employees to perform functions at both plants, to transfer employees between plants, and to otherwise change the working conditions and job functions of members of Local 272.

5. The Commission is responsible for ensuring that Duquesne's restructuring plan, generation auction plan, and agreement with FirstEnergy are in the public interest. With the proposed generation swap, this now includes not only the interests of Duquesne's employees, but also the interests of FirstEnergy employees who work at the Bruce Mansfield station.

6. Local 272 did not have an interest in this proceeding until Duquesne and FirstEnergy made public their proposed generation swap on or about October 14, 1998. Local 272 has acted expeditiously to determine the existence and nature of the current proceeding and the manner in which its interests might be affected by a Commission decision in this matter.

7. Local 272 is filing brief Comments on this matter simultaneously with this Petition. Therefore, granting Local 272's petition to intervene will not result in any further delay in this proceeding.

WHEREFORE, Local 272, IBEW, respectfully requests the Pennsylvania Public Utility Commission to grant Local 272 the right to intervene in this matter as an active party.

Respectfully submitted,

Scott J. Rubin
3 Lost Creek Drive
Selinsgrove, PA 17870
(717) 743-2233

Counsel for:
Local 272, IBEW

Dated: November 5, 1998

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

In the Matter of Duquesne Light Company's Restructuring Plan	:	Docket No. R-00974104

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the Petition to Intervene and Comments of Local 272, International Brotherhood of Electrical Workers, via First Class Mail upon the participants, listed on the following pages, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).

Scott J. Rubin, Esq.

Counsel for:
Local 272, IBEW

Dated: November 5, 1998

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November 5, 1998

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

ORIGINAL

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

Dear Mr. McNulty:

Enclosed for filing please find two documents relating to the above-referenced matter: (1) an original and three (3) copies of the Petition to Intervene of Local 272, IBEW, and (2) an original and ten (10) copies of the Comments of Local 272, IBEW. A copy of each document has been served on all parties of record, as shown on the attached certificate of service.

In addition, I have enclosed an extra copy of each document that I would appreciate having time stamped and returned to me in the enclosed envelope. Thank you for your cooperation.

Sincerely,

Scott J. Rubin, Esq.

Enclosures

cc: All parties of record
Hon. John Quain
Hon. Robert Bloom
Hon. David Rolka
Hon. Nora Mead Brownell
Hon. Aaron Wilson, Jr.
Office of Special Assistants

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ORIGINAL

BEFORE THE
COMMONWEALTH OF PENNSYLVANIA
PUBLIC UTILITY COMMISSION

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

COMMENTS OF
LOCAL 272, INTERNATIONAL BROTHERHOOD OF ELECTRICAL WORKERS

Local 272, International Brotherhood of Electrical Workers ("Local 272"), files these Comments concerning the proposed Generation Auction Plan ("GAP") of Duquesne Light Company ("Duquesne"). Local 272 is the authorized representative of approximately 350 employees of FirstEnergy Corporation ("FirstEnergy") at the Bruce Mansfield generating station in Beaver County, Pennsylvania.

Local 272 adopts and fully supports the Comments that were filed in this matter by the representative of Duquesne's employees, System Council U-10, IBEW ("System Council"), dated November 3, 1998, as well as the Motion to Suspend this proceeding that was filed by System Council on October 21, 1998.

In addition to the issues raised by System Council, Local 272 is concerned that the proposed generation swap between Duquesne and FirstEnergy could have an adverse effect on FirstEnergy's employees at the Bruce Mansfield plant. Bruce Mansfield and Duquesne's Beaver Valley plant are located next to each other. Local 272 is concerned that if FirstEnergy owns and operates both plants that FirstEnergy will attempt to reduce employment levels at one or both

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plants, combine job functions, transfer employees between the plants, and otherwise change the working conditions for members of Local 272. Given the already drastically reduced employment levels at the Bruce Mansfield plant, any such actions would raise serious concerns about the safety and reliability of the plant.

In its Restructuring Order entered May 29, 1998, the Commission set forth the requirements for Duquesne to file a plan to divest its generating assets. *Application of Duquesne Light Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code*, Docket No. R-00974104 (Pa. PUC May 29, 1998), slip op. at 80-81. The Order lists 16 requirements for Duquesne's divestiture plan. The Commission required Duquesne to set forth, among other matters, "transitional issues and the resolution of those issues in a manner that is fair to customers, investors, the employees of the Company, local communities, and other affected parties." *Id.* at 80-81. Local 272 submits that, in light of the proposed generation swap between Duquesne and FirstEnergy, the employees at the Bruce Mansfield plant are affected parties who could be adversely affected by the proposed transaction. Yet there is nothing in Duquesne's filings that address the effect of the proposed transaction on FirstEnergy's employees.

The agreement in principle between Duquesne and FirstEnergy states only that Duquesne and FirstEnergy "will cooperate to resolve labor-related matters, including with respect to union contracts, workforce levels, severance, and employee benefits, in a matter that treats employees fairly and equitably apportions any related costs between the parties. The definitive agreements for the Generation Exchange shall clearly define and apportion the rights and obligations of the parties regarding these matters." Agreement in principle, paragraph 6. Thus, at the present time,

there is no way of knowing the effect that the proposed exchange would have on FirstEnergy's employees.

This is important because the agreement in principle, by its own terms, is ***not*** the final agreement between Duquesne and FirstEnergy. In fact, it expressly states that it is "specifically agreed and understood by the parties that the terms set forth in this agreement in principle do not constitute all of the major terms which will be included in the Exchange Agreements, that the terms set forth herein are subject to further discussion, negotiation, due diligence, and that this agreement in principle is an expression of intent only and is not intended, nor will it be alleged by either party, to create or result in any legally binding obligation upon the parties ..." Agreement in principle, paragraph 14.

There also is nothing in Duquesne's filings that address the effect of the generation swap on the safety and reliability of the Bruce Mansfield station. Duquesne should not be permitted to transfer its ownership interest in that station unless and until it demonstrates that the transfer, and the resulting actions that are taken by FirstEnergy, will not have an adverse effect on the safety and reliability of that station. So far, Duquesne has not provided any information about any effects of the proposed transfer on the safety and reliability of the Bruce Mansfield station.

Simply, the auction plan and the agreement in principle between Duquesne and FirstEnergy do not provide sufficient information for the Commission to assess the effects of the proposed transaction on FirstEnergy's employees or on the safety and reliability of the Bruce Mansfield station. Duquesne or FirstEnergy must provide additional information that addresses the effect of any such transfer on FirstEnergy's employees and the Bruce Mansfield plant before the Commission can determine whether the proposed transaction is in with the public interest.

Local 272 would emphasize that it is not seeking to negotiate any labor-related issues before this Commission. Rather, Local 272 submits, consistent with the requirements of the Commission's decision in Duquesne's restructuring case, that the Commission must be aware of the full impact of Duquesne's plans on other people who will be affected by the plan. At the present time, it is not possible for the Commission to make such an evaluation because neither Duquesne nor anyone else can tell how the Bruce Mansfield plant and the people who work there will be affected by Duquesne's generation auction plan and its proposed swap with FirstEnergy.

For the reasons set forth above, Local 272, IBEW, respectfully requests the Pennsylvania Public Utility Commission to refuse to approve Duquesne's Generation Auction Plan at the present time. Duquesne must provide substantially more information about the effects that its plan would have on the safety and reliability of the Bruce Mansfield station and the effects that its proposed generation swap would have on the employees of FirstEnergy who work at the Bruce Mansfield station. Until Duquesne provides information that can be used to determine these impacts, and until the Commission determines that those impacts are consistent with the public interest, the Commission must not approve Duquesne's plan.

Respectfully submitted,

Scott J. Rubin
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(717) 743-2233

Counsel for:
Local 272, IBEW

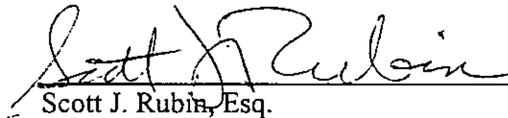
Dated: November 5, 1998

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

In the Matter of Duquesne Light Company's Restructuring Plan	:	Docket No. R-00974104

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the Petition to Intervene and Comments of Local 272, International Brotherhood of Electrical Workers, via First Class Mail upon the participants, listed on the following pages, in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant).



Scott J. Rubin, Esq.

Counsel for:
Local 272, IBEW

Dated: November 5, 1998

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November 5, 1998

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

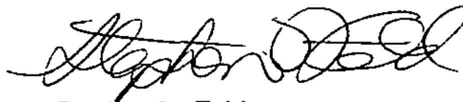
Re: Restructuring Plan of Duquesne Light Company
Docket No. R-00974104

Dear Secretary McNulty:

Enclosed are an original and ten (10) copies of the Comments of FirstEnergy Corp. on Duquesne's Generation Assets Auction Plan filed in the above docket. These comments are filed pursuant to the Commission's Order of May 21, 1998 as modified by the secretarial letter dated October 27, 1998.

Please contact me if you have any questions.

Very truly yours,



Stephen L. Feld
Senior Attorney

sf
enclosures

cc: Service List - w/enclosure

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ORIGINAL

BEFORE THE

PENNSYLVANIA PUBLIC UTILITY COMMISSION

DOCKET NO. R-00974104

DOCKETED
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GENERATION AUCTION PLAN

OF

DUQUESNE LIGHT COMPANY

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

COMMENTS

of

FIRSTENERGY CORP.

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November 5, 1998

Before the

Pennsylvania Public Utility Commission

Docket No. R-00974104

Generation Auction Plan
Of
Duquesne Light Company

COMMENTS
of
FIRSTENERGY CORP.

Pursuant to the Pennsylvania Public Utility Commission's ("PaPUC" or "Commission") May 29, 1998 order in the above docket and the Generation Auction Plan ("Plan") filed by Duquesne Light Company ("Duquesne") on August 27, 1998, FirstEnergy Corp. and its Pennsylvania affiliated electric utility operating company, Pennsylvania Power Company (collectively, "Company"), hereby submit these comments to the Plan.

I. INTRODUCTION

FirstEnergy is a diversified energy services company with more than $18 billion in assets and more than $5 billion in annual revenues. FirstEnergy's electric utility generating companies comprise the nation's 12th largest investor-owned electric system and includes The Cleveland Electric Illuminating Company, Ohio Edison Company, Pennsylvania Power Company and The Toledo Edison Company (collectively, "FE Companies"). Pennsylvania Power Company ("Penn Power") is a subsidiary of Ohio Edison Company and is an electric utility subject to the jurisdiction of the PaPUC. Penn Power has intervenor status in the underlying proceeding at Docket No. R-00974104.

The FE Companies and Duquesne are the members of CAPCO. This organization was formed in 1967 to jointly develop power generation and transmission facilities in an effort to enhance

power coordination and reliability in the region. The CAPCO companies jointly own and operate nine generating units at six power plants located in northern Ohio and Western Pennsylvania. The CAPCO companies became parties to numerous agreements establishing the foundation for the financing and construction of, and the subsequent operation of the jointly-owned generating units. Some of these agreements also included provisions for the equitable use of designated portions of each joint-owner's own transmission facilities and for the reciprocal provision of various power interchanges. The transmission facilities were not to be, and did not become, jointly owned.

These Comments present three fundamental issues that need to be resolved in the Commission's consideration of the Plan. First, the sale of CAPCO jointly-owned units by Duquesne requires the consent of the FE Companies as joint-owners. Second, the right to use CAPCO transmission lines is essentially limited under existing agreements to the owners of CAPCO units. Third, the "Draft Interconnection Term Sheet" included as Appendix E to the Plan, does not and can not alter the FE Companies' operation and maintenance of jointly-owned units.

These issues may be entirely obviated upon the consummation of the recently announced exchange of generating units between Duquesne and FirstEnergy. If the exchange is completed as planned, the FE Companies will have complete ownership of the former CAPCO units. Duquesne's rights and obligations under the various CAPCO agreements will have been determined by mutual agreement between it and FirstEnergy. The issues cited above will be resolved and the auction of the substituted units may proceed (assuming Duquesne's merger with Allegheny Power is not consummated). If, however, the exchange of units does not occur, the issues may present major hurdles for the auction to be completed.

II. ISSUES

(A) Sale of CAPCO Units Requires FirstEnergy's Consent

FirstEnergy believes that the various CAPCO agreements require Duquesne to obtain the consent of the other joint owners of CAPCO units for Duquesne to sell its interests in these units. For example, the September 14, 1967 Memorandum of Understanding among the CAPCO companies provides in part, "each party . . . shall waive, at least for the useful life of the [undivided interests in the generating units and the related facilities to be constructed], its right to bring any action for partition or sale of the real property conveyed or the improvements thereon." In addition, the CAPCO Basic Operating Agreement and the unit operating agreements for the CAPCO generation units state that no party to the agreements will, without the prior written consent of the other parties assign the agreements. The waiver of the right to sell its interests and the required consent before assignment provisions are clear in their meaning and intent, i.e., no CAPCO party may sell its interests in any CAPCO unit without obtaining the agreement of the other CAPCO owners.

Duquesne referred in its Plan (pp. 11, 20) to one legal proceeding that has arisen from FirstEnergy's position that its agreement is required prior to any transfer of Duquesne's ownership in any CAPCO unit. Duquesne's petition for declaratory order and other relief before FERC was denied by Order dated September 24, 1999. (See Attachment 1 hereto). Additional litigation in federal district court continues in Ohio involving, inter alia, its ability to sell its interest in the Eastlake Plant, a CAPCO unit. (Case No. 1:95 CV 2307, U.S. District Court, Northern District of Ohio Eastern Division). The fact that litigation in two forums has occurred or is ongoing supports FirstEnergy's contention that sale of CAPCO units without its consent is problematic.

(B) Only the Owners of CAPCO Plants Have a Pre-existing Right to Use CAPCO Transmission Facilities

Duquesne states (Plan, P. 20-21) that its divestiture of CAPCO units will not require the assignment of the Transmission Facilities Agreement (TFA). Implicit in this position is that Duquesne will retain its rights under the TFA to use the transmission facilities built in conjunction with the CAPCO generating units. However, the right to use CAPCO transmission lines is tied to ownership interests in the CAPCO units. CAPCO members, or their successors in interest, have a "pre-existing contractual right" to take transmission service over these facilities within the meaning of FERC Order 888. Only the unused capacity of these lines is available for service under the transmission owner's Open Access Transmission Tariff. (CAPCO transmission lines are owned by one company and the other members compensate the owner for their proportional use.)

In its divestiture of the CAPCO generating units, Duquesne must sell the CAPCO lines it owns or assign its interests in the TFA to the new owner of a CAPCO unit. The new owner would then have either ownership or a "pre-existing contractual right" to use the CAPCO lines to get its generation out of the unit. Duquesne's Plan does not acknowledge the need to compensate FirstEnergy for the use of FirstEnergy's CAPCO lines. Use of the unused capacity of the lines would be subject to FirstEnergy's OATT. Following divestiture, Duquesne would have no right to apply its OATT for service over CAPCO lines.

(C) FirstEnergy's Operation of Jointly Owned Units Is Not Subject to Duquesne's Interconnection Agreements

The operating agreements for each CAPCO unit place operating and maintenance responsibilities for the units upon the designated operating company. The other non-operating owners have limited rights in the plant's operations. Although non-operating owners may decide, within limits, the quantity of generation they take, they may not dictate when and to what extent a particular CAPCO unit

runs. The existing CAPCO agreements have no provision that allows a single owner to provide ancillary services to a third party, e.g., Duquesne. Duquesne apparently believes that its proposed Interconnection Agreement will provide its desired ancillary services to maintain Duquesne's status as a control area. These Interconnection Agreements lack any legal validity in determining how CAPCO units will be operated and maintained in the absence of agreement by FirstEnergy.

III. CONCLUSION

FirstEnergy files these comments in the spirit of full disclosure to potential bidders. It believes that the issues raised herein are substantial impediments to the implementation of the Plan as originally proposed and should be considered by participants in Duquesne's auction.

The proposed exchange of generating units evidences the desire of both FirstEnergy and Duquesne to resolve important issues related to the ownership of the CAPCO generating plants. That consummation of the proposed exchange will avoid possible lengthy negotiations and litigation over the application of the CAPCO agreements to Duquesne's divestiture plan. FirstEnergy strongly urges the Commission to allow the Plan to proceed as modified by the proposed exchange of CAPCO generating units.

Respectfully submitted,

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November 5, 1998

[29272]

ATTACHMENT 1

UNITED STATES OF AMERICA 84 FERC 61,309
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: James J. Hoecker, Chairman;
Vicky A. Bailey, William L. Massey,
Linda Breathitt, and Curt H,bert, Jr.

Duquesne Light Company) Docket No. EL98-68-000

ORDER DISMISSING PETITION FOR DECLARATORY ORDER

(Issued September 24, 1998)

Duquesne Light Company (Duquesne) has filed a petition for a declaratory order (petition), requesting that the Commission rule that FirstEnergy Corporation (FirstEnergy), may not unreasonably withhold its consent to the transfer by Duquesne of an operating agreement for a jointly owned and operated generating unit. For the reasons discussed below, we will dismiss Duquesne's petition.

Background

Duquesne and FirstEnergy jointly own and operate a number of generating units and pool their resources under a pooling arrangement known as the Central Area Power Coordinating Group (CAPCO). 1/ Duquesne states that it intends to divest its generating resources as part of the Commonwealth of Pennsylvania's retail competition restructuring program.

Duquesne and FirstEnergy are parties to a state court proceeding initiated by FirstEnergy's request for an injunction against Duquesne's disposition of its ownership interest in one of the generating units jointly owned with FirstEnergy. FirstEnergy has argued to the court that the contracts between the parties prevent the "partition" of generating units. FirstEnergy also has argued to the court that the assignment provisions in a CAPCO unit operating agreement (on file with the Commission) require FirstEnergy's consent prior to any transfer of the operating agreement.

The Petition

On July 31, 1998, Duquesne filed the instant petition arguing that, if FirstEnergy's consent is required to assign the operating agreement, FirstEnergy may not unreasonably withhold its consent and Duquesne asks, among other things, that the

1/ Duquesne holds a minority interest in each unit, while FirstEnergy is the majority owner and is the operator of all but two units.

Commission issue a ruling stating that consent to the assignment

of the operating agreement can be withheld only on reasonable grounds. Duquesne alleges that FirstEnergy is refusing consent both to the sale of the generating units and to the assignment of the operating agreement because it has an interest in acquiring the units from Duquesne and wants to eliminate any competing purchase offers.

In the alternative, Duquesne asks that, if the Commission holds that the assignment provisions give FirstEnergy the sole discretion to consent or not, the operating agreement be summarily reformed so that FirstEnergy cannot stand in the way of Duquesne's planned divestiture.

Duquesne also contends that the Commission may issue a remedial order in Docket No. EC97-5-000 (the proceeding in which the Commission approved the FirstEnergy merger) imposing changes to the assignment provisions as a condition of the merger. Duquesne explains that the sale of these units to FirstEnergy will simply increase FirstEnergy's generation market power, a matter that was of concern to the Commission when it approved the FirstEnergy merger.

Notice and Interventions

Notice of Duquesne petition was published in the Federal Register, 63 Fed. Reg. 43,150 (1998), with comments, protests and motions to intervene due on or before August 31, 1998

FirstEnergy filed a timely motion to intervene and answer opposing Duquesne's petition for reformation of the generation unit operating agreement. Allegheny Energy, Inc. (Allegheny) filed a timely motion to intervene raising no substantive issues.

Discussion

A. Procedural Matters

Pursuant to Rule 214 of the Commission's Rules of Practice and Procedure, 2/ the timely, unopposed motions to intervene of FirstEnergy and Allegheny serve to make them parties to this proceeding.

B. Jurisdictional Issues

Duquesne's petition concerns Duquesne's disposition of its ownership interest in jointly owned and operating generating units, and involves no jurisdictional transmission facilities, and therefore does not fall within the reach of the Federal Power

2/ See 18 C.F.R. 385.214 (1998).

Act. Section 201(b)(1) of the Federal Power Act provides in pertinent part:

> The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy [i.e., transmission in interstate commerce or sale of electric energy at wholesale in interstate commerce], but shall not have jurisdiction, except as specifically provided in this Part and the Part next following, over facilities used for

the generation of electric energy . . . .
[3/]

Pursuant to section 201(b)(1), the Commission has no jurisdiction over the sale or other disposition of generating units, such as that proposed by Duquesne. 4/ While it is true that the operating agreement referenced by Duquesne in its petition is on file with the Commission, that is because it includes jurisdictional services separate and distinct from the terms of ownership and operation of the generating units; e.g., economy energy and backup power sales.

Moreover, the contractual dispute, i.e., the appropriate interpretation of the assignment provisions in the operating agreement, fails to meet the requirements set forth in Arkansas Louisiana Gas Company v. Hall. 5/ In Arkla, the Commission found that it should assert jurisdiction over contractual issues otherwise litigable in state courts if: (1) the Commission possesses some special expertise which makes the case particularly appropriate for Commission decision; (2) there is a need for uniformity of interpretation of the type of question raised in the dispute; and (3) the case is important in relation to the regulatory responsibilities of the Commission.

First, this case does not require the interpretation of disputed contractual terms involving technical matters demanding the Commission's special expertise. We thus do not believe that we are in a better position than a court to address such

3/ See 16 U.S.C. 824(b) (1994).

4/ See Entergy Services, Inc. 51 FERC 61,376 at 62,285-86 n.27, reh'g denied, 52 FERC 61,317 (1990); United Illuminating Company, 29 FERC 61,270 at 61,558 (1984).

5/ 7 FERC 61,175 at 61,322, reh'g denied, 8 FERC 61,031 (1979) (Arkla).

disputes. 6/ Second, there is no need for a uniform interpretation of the contractual provisions here at issue. The interpretation of the operating agreement will not affect other public utilities since the dispute is unique to these parties (and this agreement). Resolution of the dispute thus should have no impact beyond the particular parties involved. Third, this case is not important to the regulatory responsibilities of this Commission. As we stated above, this dispute revolves around questions of contract interpretation unique to the terms of the agreement at issue here and to the parties.

Therefore, we decline to entertain the contractual dispute. The appropriate forum for resolution of this dispute is a court, not at the Commission.

For these reasons, we will dismiss Duquesne's petition.

The Commission orders:

Duquesne's petition for a declaratory order is hereby dismissed.

By the Commission.

(S E A L)

David P. Boergers,
Secretary.

6/ This contractual dispute is already the subject of an ongoing state court proceeding.

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 a copy of the foregoing document was served, 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 5th day of November, 1998.

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November 6, 1998

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SECRETARY'S BUREAU

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

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

Dear Secretary McNulty:

Enclosed for filing please find an original and ten (10) copies of the Comments of Representative Mike Veon in the above referenced proceeding. A copy of this document has been served on all parties of record, as shown on the attached certificate of service.

Sincerely,

Mike Veon
State Representative

DOCUMENT FOLDER

Enclosures

cc: All parties of record
Hon. John Quain
Hon. Robert Bloom
Hon. David Rolka
Hon. Nora Mead Brownell
Hon. Aaron Wilson, Jr.
Office of Special Assistants

EEF

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ORIGINAL

PENNSYLVANIA PUBLIC UTILITY COMMISSION

COMMENTS IN RESPONSE TO DUQUESNE LIGHT COMPANY RESTRUCTURING PLAN STATE REPRESENTATIVE MICHAEL R. VEON

These comments refer to Docket No. R-00974104, the Restructuring Plan submitted by the Duquesne Light Company. State Representative Michael R. Veon is an elected State Representative from Beaver County and is also the Chairman of the House Democratic Policy Committee. In this capacity, Mr. Veon represents the interests of the Duquesne Light Company customers within his district. Representative Veon was instrumental in enacting the Electricity Generation Customer Choice and Competition Act, particularly those elements of that act which related to fair treatment of utility employees. Mr. Veon is also a residential and commercial customer of *Duquesne Light Company*. Representative Veon is also the Chairman of the Beaver Initiative for Growth, an economic development enterprise located in Beaver County that is dependent on a reliable and affordable source of electricity.

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SECRETARY'S BUREAU

Through the release of the agreement in principle between Duquesne Light Company and FirstEnergy concerning the potential "swap" of generating assets, for the first time, the consequences of Duquesne Light's restructuring proposal have become apparent. For this reason, Representative Veon is offering comments on both the agreement in principle as well as the overall restructuring proposal.

DOCUMENT FOLDER

COMMENTS OF REPRESENTATIVE MICHAEL R. VEON

Employee Issues

The Public Utility Code provides at section 2802 (10) that "[i]n order to ensure the safety and reliability of the electric system, ensure the continued provision of high quality customer service and avoid economic dislocation, utilities shall consider the experience and expertise of their work force in moving towards competition."

In section 2802 (18) of the Public Utility Code, it is further stated that:

> There are certain changes to a utility that will create transition costs to accomplish the move to a competitive market. These changes may entail the closure of facilities or reduction in employee levels. If such actions are to be undertaken, the utility must fully inform the commission of the impact of such decisions on local communities and on social services and of any tax implications of the actions. The utility is expected to discuss the transition to competition with its employees or their certified representatives and may provide severance, retraining, early retirement and outplacement services. Such transition costs may be recoverable under the competition transition charge.

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Because the agreement to swap generation assets between Duquesne Light and FirstEnergy is occurring as an element of the restructuring plan submitted by Duquesne Light, these principles should apply not only to the auction of generating capacity which Duquesne has proposed as a part of that plan, but also in relation to the proposed swap of assets with FirstEnergy. In the October 21st conference, officials of Duquesne Light conceded that the experience and qualifications of employees were a component of the value of the assets that are being swapped with FirstEnergy. However, the agreement in principle, dated October 14, 1998, simply states:

> The Parties will cooperate to resolve labor-related matters, including with respect to union contracts, workforce levels, severance, and employee benefits, in a manner that treats employees fairly and equitably apportions any related costs between the parties. The definitive agreements for the generation exchange shall clearly define and apportion the rights and obligations of the Parties regarding these matters.

The clear intent of the General Assembly in enacting sections 2802 (10) and (18), was to have the employees of the affected generating facilities, or their duly recognized representative, actively participating in "competition" related decisions, including the divestiture of any asset, or any other change in work conditions. Duquesne Light appears to recognize the responsibility to include express provisions related to labor matters in the agreement for the generation exchange. The commission should require, prior to approving both the transfer of generation assets and the final restructuring plan, clear and compelling evidence that the employees of all affected parties have actively participated in discussions and agree with decisions about such issues as continuation of collective bargaining agreements; reductions in force; severance pay; early retirement incentives; retraining, relocation and outplacement services; protection of employee pension rights; protection of health care benefits and other benefits of employment which those employees now enjoy.

It is not clear from the agreement in principle when and by whom the costs will be borne for any changes in the terms or conditions of employment of employees of either Duquesne Light Company or FirstEnergy. Because the allocation of these costs will affect ratepayers, it is important that all such decisions be finally decided prior to the final approval of the asset transfer and the final restructuring plan.

In addition, the commission should require each of the parties, including Duquesne Light, FirstEnergy and the ultimate purchaser of Duquesne's generating operations through auction to provide evidence that they have fully and fairly assessed the impact of the proposed transfer of generating assets on the local community. Such an investigation should include evidence of meetings with the affected local government officials. The assessment should include consideration of the consequences of restructuring related activities on local social service agencies, education and training programs and community institutions, such as hospitals and other health care providers. Finally, Duquesne should be required to show evidence that they have fully evaluated the potential tax implications of their restructuring program, including the impact on local property and wage taxes, as well as the consequence for the Public Utility Realty Tax.

Provider of Last Resort

Even as the competitive market emerges, it is clear that there will be customers who either fail or refuse to find an alternative provider of electricity. By statute, Duquesne retains the responsibility to serve these customers, unless and until the Commission approves an alternative supplier. Rather than accepting widely varying alternative plans for addressing this requirement, the Commission should develop, through the regulatory process, clear guidelines for establishing the provider of last resort and for determining how to set prevailing market prices. In so doing, the Commission should consider proposals that encourage broader consumer choice among providers of last resort and the economic benefit that may accrue to entities that are selected as providers of last resort.

Until the commission establishes uniform guidelines, Duquesne should serve as the provider of last resort, offering electricity to consumers who fail to select an alternative provider at rates comparable to those they would pay if they had in fact exercised their ability to select an alternative provider.

Plant Decommissioning Responsibility.

Duquesne proposes to transfer its ownership interest in several generating facilities, including its interest in a nuclear facility located in Beaver County. Duquesne would retain responsibility for its share of the cost for decommissioning that nuclear facility. Duquesne proposes to quantify that liability in present value dollars and transfer that amount to FirstEnergy in "a tax advantaged way."

Our concern is that be sufficient assets pledged to ensure this facility is safely and appropriately decommissioned, in a way that protects both the public health and safety and the natural environment. The assessment of that responsibility by the Office of Consumer Advocate, setting Duquesne's liability at $7.949 million dollars annually for the seven year CTC recovery period appears to be reasonable and fair. These funds should be segregated and maintained solely and exclusively for the purposes of decommissioning the affected nuclear power plants.

Other Environment Protections

Duquesne apparently has assembled substantial air quality credits for instituting aggressive pollution controls under the state and federal Clean Air Acts. These credits were generated by improvements financed in the large part by the current ratepayers of Duquesne Light. Moreover, these credits either do now or may have in the future, significant economic value. Duquesne apparently is prepared to transfer ownership of these credits with the transfer of generating facilities.

The commission should require Duquesne to attach a market value to these assets.

Continuation of Service

Duquesne intends to transfer its ownership interest in the generating facilities to FirstEnergy immediately upon approval of the Commission. But it does not intend to take ownership of the FirstEnergy facilities until immediately before they will finally be auctioned off. Thus it appears that Duquesne could be in a position where it does not own or control generating capacity before it is fully restructured and before all of its current ratepayers have the opportunity to select alternative providers.

This situation does not appear to be in the best interest of either the current or the future customers of Duquesne. They must be assured that throughout the entire restructuring process they have access to a reliable supply of energy at a reasonable and fair cost. Consequently, the Commission should require Duquesne to retain ownership of sufficient generating capacity to ensure that all of its current customers have access until such time as these customers have had ample opportunity to select alternative providers.

Impact on Local Zoning and Planning.

We are concerned about the impact that the transfer of ownership of generation facilities or the divestiture of generating capacity will have on the ability of local governments to implement local zoning ordinances and comprehensive plans. We also are concerned about the potential impact restructuring could have on local economic development activities.

Impact on Economic Development Efforts.

The availability of stable, reliable and efficient electricity service is vital to regional economic development efforts. As the regional supplier of electricity, Duquesne Light has historically been a partner in these efforts. As an element of its evaluation of the impact of the proposed restructuring on the local community, the commission should require clear, definitive statements from Duquesne Light and FirstEnergy about their

willingness to support local economic development activities, expressing the extent of their financial commitment to support such activities.

Conclusion

As a member of the General Assembly, I have supported electric competition and utility restructuring, believing that a competitive market can best serve the interests of all consumers. Nevertheless, I am concerned that, in making the transformation to that competitive market, the implications and consequences for consumers, workers and the affected communities must carefully measured. The proposed transfer of generating facilities between Duquesne Light and FirstEnergy is a critical element of Duquesne's restructuring plan. There are significant and substantial concerns about the proposed transfer of assets, which in turn raise legitimate concerns about the restructuring plan. As outlined above, I believe that commission must address these issues, before allowing the restructuring plan and the transfer of assets to proceed.

Respectfully submitted,

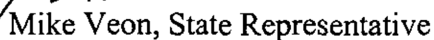
Michael R. Veon, State Representative

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

In the Matter of Duquesne Light Company's Restructuring Plan	: Docket No. R-00974104

CERTIFICATE OF SERVICE

I hereby certify that I have this day served a true copy of the Comments with regard to the Duquesne Light Company's Restructuring Plan via First Class Mail upon the participants, listed on the following pages, in accordance with the requirements of 52 Pa Code § 1.54 (relating to service by a participant).



Mike Veon, State Representative

Dated: November 6, 1998

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NOV 06 1993

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SECRETARY'S BUREAU

November 6, 1998

James J. McNulty
Secretary
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Harrisburg, PA 17105-3265

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

KJR

Dear Mr. McNulty:

Enclosed for filing please find the original and ten copies of Enron Power Marketing, Inc.'s Comments to the Generation Auction Plan of Duquesne Light Company, in the above-referenced matter. As evidenced by the attached Certificate of Service, all parties of record have been served in the manner indicated.

If you have any questions, please contact the undersigned.

Respectfully,

Alan C. Kohler
For WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP

ACK/jlg
Enclosures

cc: Parties of Record

DSH:14147.1

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

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

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY COMMISSION	:	
v.	:	Docket No. R-00974140
DUQUESNE LIGHT COMPANY Application to Approve Restructuring Plan Pursuant to 66 Pa. C.S. § 2806(d)	:	

COMMENTS OF ENRON POWER MARKETING, INC. TO THE GENERATION AUCTION PLAN OF DUQUESNE LIGHT COMPANY

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DOCKETED
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Date: November 6, 1998

I. PROCEDURAL BACKGROUND

Enron Power Marketing, Inc. ("Enron") submits these comments to the Generation Auction Plan of Duquesne Light Company ("Duquesne") filed on August 27, 1998. By way of background, as part of its May 29, 1998 Restructuring Order the Commission directed that a 60 day comment period be provided for interested parties to respond to the Generation Auction Plan of Duquesne. On October 14, 1998, Duquesne filed supplemental information pertaining to a Generation Exchange with First Energy Corp. which substantially altered the make up of Duquesne's generation assets to be auctioned. On October 27, 1998, by Secretarial Letter, the Commission extended the comment period to Duquesne's Auction Plan to October 6, 1998. On November 5, 1998 Duquesne, filed supplemental information regarding Duquesne's Generation Auction Plan. Duquesne, by footnote in its cover letter, indicated that it would not object to comments being filed by parties addressing supplemental information up and until November 13, 1998.

II. INTRODUCTION AND SUMMARY

This matter originated per a Commission directive that Duquesne file an auction plan to sell certain generation assets as proposed in Duquesne's restructuring order. The generation assets subject to auction were a significant determinate in the Commission's calculation of Duquesne's approved stranded cost recovery amount. On October 14, Duquesne submitted to the Commission, an Agreement in Principle, between Duquesne and First Energy which would transfer to First Energy all of Duquesne's rights and interests in the Beaver Valley Power Station Units Nos. 1 and 2, Perry Unit No. 1, W.H. Sammis Unit No. 7, Bruce Manfield Units Nos. 1, 2 and 3, and East Lake Unit No. 5 (together "DLC Interest"), while First Energy agreed to transfer

to Duquesne its rights and interests to Avon Lake, New Castle and Niles Generating Stations (together, "FE Interest").[1] Even with this dramatic shift in the generation assets subject to the auction, Duquesne has taken the position that the generation auction can continue under the original schedule. Although Enron takes no position in regard to the generation exchange between Duquesne and First Energy, it is clear that such a dramatic change from that contemplated in its restructuring plan will result in numerous delays and probable litigation unless Duquesne attempts to be creative in addressing the concerns of the various commentors.

In all the settlement negotiations involving other Electric Distribution Companies and their attempts to avoid litigation of their restructuring plans, two issues most important to Enron have been resolved. The issue of Provider of Last Resort ("POLR") and the Unbundling of Metering and Billing, have been addressed in each of the settlement negotiations. In fact, in the GPU Joint Settlement, a detailed eight page settlement regarding POLR was negotiated by many of the same parties who have been involved in Duquesne's restructuring proceeding and are likely to comment to this auction plan. Since GPU is the only other company that has a generation Auction Plan to implement, the POLR plan approved by the Commission in that proceeding should be incorporated in Duquesne's Auction Plan.

Duquesne, while recognizing in its Auction Plan, the necessity of addressing the Provider of Last Resort issue, does so only in the context of evaluating a wholesale, competitive bidding market and not that of a retail competitive bidding POLR as envisioned by the GPU approved negotiated plan. It is clear to Enron that the GPU retail POLR provided via competitive bid, will

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[1] "Agreement in Principle" filed October 14, 1998 at 1-2.

be far superior to that of only a wholesale market bidding process. Enron further requests that as part of the POLR bidding function pertaining to any company exiting the generation business the unbundling of metering and billing be a necessary component of that process.

II. COMMENTS

A. Provider of Last Resort

Duquesne recognized in its Auction Plan, that once the auction closes Duquesne will no longer have its own generation to meet the Provider of Last Resort function.[2] In its Auction Plan, Duquesne notes three proposed options giving the provision of POLR service once its generation has been auctioned. One proposal presented was that of considering auctioning the POLR service via a wholesale bidding process.[3] Duquesne formalized its intent to auction a wholesale POLR service in its supplemental filing of November 5, 1998 in which it explained:

> It is Duquesne's intention to market the POLR service using these shopping credits. The winning bidder for this service would assume an obligation to supply wholesale power to Duquesne in the quantities required by non shopping customers at the rates set forth in Exhibit C.[4]

Enron believes that this is an excellent first step by Duquesne in addressing the Provider of Last Resort issue and advocates inclusive use of this wholesale auction process but does not agree that the Commission should approve at this time the shopping credits as proposed by Duquesne. Enron cannot agree that in this instance that when the Auction Plan is complete that keeping the

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2 Auction Plan at 24.

3 Auction Plan at 25.

4 Supplemental Auction Plan information of November 5, 1998 at 6.

shopping credits the same and reducing the time frame for collecting the CTC would necessarily be the appropriate manner to implement or reduce CTC. Duquesne makes the above POLR wholesale competitive bidding process subject to the Commission accepting without material modification the general auction plan. However, Duquesne fails to recognize that its Auction Plan, as amended and supplemented, is substantially different than that envisioned in the restructuring proceedings. To accommodate these modifications, flexibility and cooperation is required of Duquesne to ensure the Auction Plan's success. In that spirit, Enron proposes that the precedent set by the only other electric distribution company implementing the total sale of its generation assets, GPU Energy, be given special consideration by Duquesne in order to expedite its own generating auction process.

Duquesne's proposed wholesale auction of its POLR obligation would leave Duquesne as the only party with Provider of Last Resort responsibility. However, as a company which will auction off all of its generating assets, it is prudent and necessary to offer customers different options as to who provides the Provider of Last Resort function at the retail level. In the GPU Joint Settlement, a transition plan for allowing competitive bidding of the negotiated retail POLR service was approved by the Commission. (For ease of reference Enron has attached Section 4 – Provider of Last Resort – to be included as part of these comments.[5]) The time frame for the transition to POLR retail competitive bidding as outlined in the GPU settlement and as suggested by Enron for Duquesne is as follows.

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[5] Joint Petition for Full Settlement of the Restructuring Plans of Metropolitan Edison Co. and Pennsylvania Electric Company and Related Dockets and Related Court Proceedings at 36-43 (Attachment "1").

> Retail POLR service to 20% of the Companies' retail customers shall be provided via competitive bid on June 1, 2000; 40% of the Companies' retail customers shall be provided via competitive bid on June 1, 2001; 60% of the Companies' retail customers shall be provided via competitive bid on June 1, 2002; and 80% of the Companies' retail customers shall be provided via competitive bid on June 1, 2003. The competitive bid process used to assign to retail customers a Provider of Last Resort other than the Companies shall be referred to as Competitive Default Service ("CDS"). Commencing on January 1, 2001, the Commission will conduct an annual review of the CDS process to consider whether it is in the public interest to continue implementing the schedule set forth above. During that review, the Commission will accept comments from any interested party relating to the economic and practical impacts of the retail competitive bid process.[6]

This negotiated retail POLR service also includes the following terms and conditions: a) POLR service shall be subject to the applicable generation rate caps;[7] b) customer eligibility and Commission responsibility for determining alternative POLR;[8] c) qualifications for a bidding Electric Generation Supplier including various sources of power;[9] d) the Commission's responsibility for establishing rules for CDS service;[10] e) Commission's obligation to develop qualifications for an EGS to bid on Competitive Default Service;[11] the rules for determining winning bidders and responsibilities when there are no winning bidders;[12] f) the types of service

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[6] Id. at 36 ¶ F.2.

[7] Id. at 36, 37 ¶ F.3.

[8] Id. at 37 ¶ F.4.

[9] Id. at 37, 38 ¶ F.5.

[10] Id. at 38 ¶ F.6.

[11] Id. at 39 ¶ F.7.

[12] Id. at 39, 40 ¶¶ F.8, 9.

a retail customer may expect from the competitive default supplier;[13] g) the competitive default supplier ("CDS") to rebid annually and the rules pertinent thereto;[14] h) EGSs POLR obligations and responsibilities associated with POLR service;[15] i) rules regarding the company's Provider of Last Resort default service as well as various pricing mechanisms in relation to the rate cap;[16] the company's obligation to serve after the CTC transition period and the company's *responsibility* regarding GPU specific non-utility generation capacity;[17]

It is Enron's position that the negotiated GPU Provider of Last Resort retail competitive bid solution is an appropriate precedent to be utilized by Duquesne as part of this auction process. Enron recognizes that certain of the terms, conditions and qualifications that were negotiated specifically for GPU will necessitate modifications for Duquesne's unique circumstances. Regardless, Enron believes that retail POLR service is a necessary next step for the approval of Duquesne's auction plans. Duquesne, in its reply to these comments, should review the attached retail POLR service plan negotiated by the parties in the GPU settlement and suggest modifications to meet its own unique circumstances while at the same time taking that next step to provide retail POLR service at the same time it implements this auction plan.

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13 Id. at 40 ¶ F.10.

14 Id. at 41 ¶ F.11.

15 Id. at 41 ¶ F.12.

16 Id. at 41, 42 ¶¶ F.13, 14, 15.

17 Id. at 42, 43 ¶¶ F.16, 17.

B. Unbundling of Metering and Billing Services

In any retail provision of POLR service, the customer is going to expect the electric generation supplier ("EGS") to be a full service company. This will not be possible without Duquesne agreeing to allow the competitive provision of billing and metering. The CDS provider under the GPU settlement envisions a customer option of choosing a single bill from the CDS provider. As Duquesne, the Commission and the other parties to Duquesne's restructuring proceeding are aware, in all of the other restructuring settlements, competitive entry into billing and metering functions have been approved and are being implemented in other service territories. It is most notable that the recent West Penn Power Settlement includes the provision of competitive metering and billing.[18]

What is obvious is that customers surrounding Duquesne's service territory and the rest of the state will be enjoying competitive services not available in Duquesne's service territory. Accordingly, to avoid disparities between service territories, it is important that the Duquesne Auction Plan and POLR Retail Service Plan include a projected date of July 1, 1999 for unbundling billing and metering services.

The terms and conditions agreed to in the West Penn Settlement regarding the unbundling of billing and metering.[19] as modified to accommodate Duquesne's special circumstances are

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18 This is noteworthy since West Penn is Duquesne's former merger partner. Although Duquesne has now notified the Commission that it no longer sees the merger as viable.

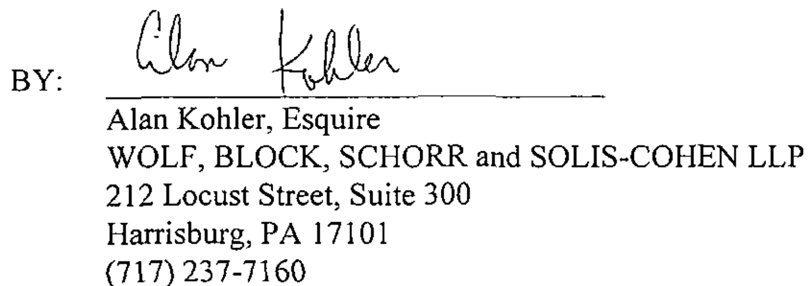
19 Joint Petition for Full Settlement of West Penn Power Company's Restructuring Plan and Related Court Proceedings, Docket No. R-00973981 at 29-34 (¶¶ G-1 - G-10).

appropriate for implementation by Duquesne. As part of the implementation, credits for unbundled metering and billing would need to be calculated based on an embedded cost analysis consist with the West Penn Settlement.[20] With these modifications, West Penn's POLR service will be brought into conformance with other service territories in final preparation for the initiation of direct access.

III. CONCLUSION

Under the Commission's procedures, Duquesne has an opportunity to respond to Comments filed by interested parties to the Auction Plan. Enron requests, especially in light of the substantial changes made by Duquesne to the Auction Plan, that Duquesne seriously evaluate all comments and attempt to incorporate these Comments. In the absence of adoption of the proposals by Duquesne, Enron requests that the Commission order Duquesne to incorporate them or in the alternative, disapprove Duquesne's Auction Plan.

Respectfully submitted,



BY: ______________________

Alan Kohler, Esquire
WOLF, BLOCK, SCHORR and SOLIS-COHEN LLP
212 Locust Street, Suite 300
Harrisburg, PA 17101
(717) 237-7160

Date: November 6, 1998

[20] Id. At G.6 and Appendices B and D.

1

2 **F. Provider of Last Resort**

3 F.1. The Joint Petitioners agree that the Companies' obligations to serve as
4 the provider of last resort ("PLR") for all retail electric customers in their respective
5 service territories that do not choose or cannot choose to purchase power from
6 alternative suppliers, shall be subject to the following terms, conditions and
7 qualifications.

8 F.2. Retail PLR service to 20% of the Companies' retail customers shall be
9 provided via competitive bid on June 1, 2000; 40% of the Companies' retail
10 customers shall be provided via competitive bid on June 1, 2001; 60% of the
11 Companies' retail customers shall be provided via competitive bid on June 1, 2002;
12 and 80% of the Companies' retail customers shall be provided via competitive bid
13 on June 1, 2003. The competitive bid process used to assign to retail customers a
14 provider of last resort other than the Companies shall be referred to as Competitive
15 Default Service ("CDS"). Commencing on January 1, 2001, the Commission will
16 conduct an annual review of the CDS process to consider whether it is in the public
17 interest to continue implementing the schedule set forth above. During that review,
18 the Commission will accept comments from any interested party relating to the
19 economic and practical impacts of the retail competitive bid process.

20 F.3. Regardless of whether PLR service is provided by GPUE or a

1 competitive PLR supplier, all retail PLR service shall be subject to the applicable
2 generation rate caps.
3 F.4. The customers eligible for each competitively bid phase of CDS shall
4 (i) be determined by random selection, (ii) include low-income and inability-to-pay
5 customers, (iii) be selected without regard to whether such customers are obtaining
6 generation service from an EGS and (iv) be allocated proportionately among the
7 Companies' customer classes. Except for PLR obligations that are fulfilled by
8 alternative suppliers through CDS, the Companies shall remain as the default PLR
9 until such time as the Commission approves a petition transferring this
10 responsibility to an alternative PLR. The Companies shall not engage in marketing
11 activities relating to its default PLR function.
12 F.5. To qualify for the CDS bidding process an EGS shall, among other
13 applicable requirements, agree to provide at least 0.2% of its generation portfolio
14 necessary to satisfy the yearly PLR obligation from among any or all of the
15 following: solar, wind, sustainable biomass (including landfill gas), geothermal,
16 ocean power, waste coal, and The York Authority (to the extent of its current design
17 capacity), provided however that no more than 40% of this generation may be from
18 waste coal and/or The York Authority. The expansion of eligible technologies
19 beyond those included in the Pennsylvania Power & Light Company settlement at
20 Docket No. 00973954 is not intended, nor shall it be construed as a precedent in this

1 or any other jurisdiction. The requirement to include these levels of sources in the
2 resource mix may be lowered by the Commission if either 1) adequate supply from
3 these sources is not available, 2) the cost of the power from these sources increases
4 the cost of the entire block by more than 2% over what the cost would be without
5 these sources, or 3) the total cost of power of the portfolio as a result of the
6 increased costs resulting from this requirement would not permit service under the
7 generation rate cap of the EDC.

8 F.6. The Commission will establish, through a collaborative approach with
9 the Joint Petitioners, the rules for CDS in the service territories of Met-Ed and
10 Penelec, including appropriate bidding blocks, competitive bidding and other
11 options to procure generation that will reduce costs and maximize customer
12 benefits. During that process, any Joint Petitioner may raise the issue of whether the
13 GPUE "system administrator" function should be subjected to the competitive
14 bidding process, and any other Joint Petitioner may respond or otherwise address
15 issues concerning the impact of bidding out the system administrator function on
16 NUG contracts, operations and the Company's customers. Notwithstanding the
17 foregoing, this Settlement is not intended to limit, in any way, any argument or
18 claim any Joint Petitioner may make in any future proceeding regarding the system
19 administrator function, including but not limited to legal, jurisdictional,
20 constitutional and any other argument, claim or challenge.

1 F.7. The Commission shall also develop qualifications for an EGS to bid
2 on CDS, including credit worthiness and increased bond amount, prior to the
3 Companies' initial competitive bid for such service. No EGS affiliated with the
4 Companies may bid (either directly or as a partner or participant in any business
5 combination with a bidder) on CDS. Any EGS or consortium of such EGSs, not
6 affiliated with the Companies, that are licensed by the Commission and that meet
7 applicable terms, conditions and standards for CDS may bid to provide such service.
8 The Companies shall unbundle Chapter 56 billing and collection costs, uncollectible
9 expense, and Universal Service costs. The revenues equal to the amount of these
10 unbundled costs shall be portable with customers randomly assigned to the CDS and
11 shall be provided to the CDS supplier to the extent it is providing services funded by
12 these unbundled costs. Subject to the standards established pursuant to this
13 Settlement, rules clarifying the Companies' obligations in providing PLR service
14 will be established in the Commission's proceeding at Docket No. M-00960890,
15 F.0017.
16 F.8. The Companies shall provide to the Commission not later than fifteen
17 (15) days after the completion of the competitive bid process, the names and
18 addresses of all winning bidders and the terms and conditions of all winning bids.
19 F.9. Any bid for CDS that exceeds the Companies' generation rate caps
20 shall be rejected. If no qualified bids for CDS are received at or below the

1 Companies' generation rate caps, GPUE shall provide PLR service at the rate cap
2 levels unless GPUE files a petition with the Commission, served on the Joint
3 Petitioners, and receives authorization from the Commission to provide PLR service
4 at rates that exceed the rate cap levels. The Commission will act on a petition filed
5 under this section within ninety (90) days of its filing. If, as a result of that
6 proceeding, the Commission establishes a new generation rate cap for the provision
7 of PLR service by the Companies, that new cap will be the ceiling for the
8 competitive bidding process conducted in the following years.

9 F.10. Any retail customer assigned to CDS may elect a competitive EGS or
10 return to the Companies as the default PLR at no charge. Any retail customer who
11 returns to CDS for any reason shall receive service from its CDS provider on the
12 same terms and conditions and at the same rate available to other CDS customers
13 within that customer's rate class. The CDS provider shall, at the customer's option,
14 provide a single bill, subject to the same standards for EGS consolidated billing as
15 provided in this Settlement, including Appendix G, and as established by the
16 Commission. The CDS provider shall include all customer care functions, including
17 processing customer accounts in accordance with all applicable regulations,
18 including but not limited to Chapter 56. Subject to the standards established
19 pursuant to this Settlement, rules clarifying the obligations of EDCs in providing
20 PLR service will be established in the Commission's proceeding at Docket No. M-

1 00960890, F.0017.

2 F.11. The CDS will be rebid annually. If, 30 days prior to the annual bid

3 the number of customers served by the CDS has fallen 3% below the competitive

4 bid percentages set forth in F.2.(2), a further random selection of customers shall be

5 assigned to CDS service to restore the number for the appropriate level. The further

6 random selection shall be chosen in a manner to be determined by the Commission.

7 F.12. The EGS(s) selected as the CDS provider(s) shall assume all

8 responsibilities and obligations associated with PLR service that may be specified

9 by the Commission from time to time.

10 F.13. Any customer that remains with or returns to the Companies in their

11 role as provider of last resort-default service shall pay the applicable generation rate

12 cap. Returning customers shall also have the option of receiving service on a

13 monthly published generation market rate basis without the benefit of the applicable

14 generation rate cap, but such rate may not be less than the prices charged by the

15 lowest priced CDS provider.

16 F.14. On and after January 1, 2001, GPUE as provider of last resort-default

17 supplier will price its generation service to residential customers at its sole

18 discretion with the following limitations: (1) the rate will be no less than the lowest

19 price charged by the CDS selected to be the alternative provider of last resort-

20 default supplier in the 20% bid, and (2) in no event will the price exceed the

1 *shopping credit.*

2 F.15. The Joint Petitioners agree that through December 31, 2010,
3 customers may choose to purchase power from alternative suppliers and later return
4 to take generation service from the Companies, or to their assigned provider of last
5 resort-default supplier.

6 F.16. The Settlement does not address, and Joint Petitioners make no
7 commitment regarding GPUE's obligation to serve after December 31, 2010, or the
8 continuance or discontinuance of the right to choose an alternative supplier and later
9 return after December 31, 2010.

10 F.17. The Companies may exercise options retained in divested generation
11 assets, as described in paragraph A.6. and Appendix M, only as necessary to satisfy
12 their PLR obligations or to meet existing GPU obligations to PJM for Installed
13 Capacity. At the request of a successful CDS bidder, and only as needed to meet
14 such bidder's PLR obligations, the Companies shall transfer their capacity rights
15 pursuant to these options to such bidder, if permitted by the transition contracts, and
16 at the same terms and conditions imposed on the Companies. Further, to the extent
17 not needed to serve the Companies' PLR obligations, the Companies shall offer to
18 sell existing NUG capacity into the market at market prices, and shall file annual
19 reports with the Commission, served on all Joint Petitioners, beginning on
20 September 1, 2000 and terminating on September 1, 2005, containing the amount of

Pennsylvania Public Utility Commission v. PECO Energy Company

R-00974009, R-00974008, R-00973953, R-00973954, R-00973975, R-00973981, R-00974104 and I-00980078.

NOTICE OF PETITION by PECO Energy Company, at No. 2865 C.D. 1998, Commonwealth Court of Pennsylvania, from the order of the Commission dated September 21, 1998 in the above-captioned proceeding.

B-00983763 Filed: October 21, 1998

KJR

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Pennsylvania Public Utility Commission v. Metropolitan Edison Company and Pennsylvania Electric Company

R-00974009, R-00974008, R-00973953, R-00973954, R-00973975, R-00973981, R-00974104 and I-00980078

NOTICE OF PETITION by Metropolitan Edison Company and Pennsylvania Electric Company, at No. 2848 C.D. 1998, Commonwealth Court of Pennsylvania, from the order of the Commission dated September 21, 1998 in the above-captioned proceeding.

B-00983761 Filed: October 21, 1998

KJR

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November 6, 1998

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

Via Federal Express

James J. McNulty
Prothonotary
Pennsylvania Public Utility Commission
North Office Building, Room B-20
Harrisburg, Pennsylvania 17101

R-00974104

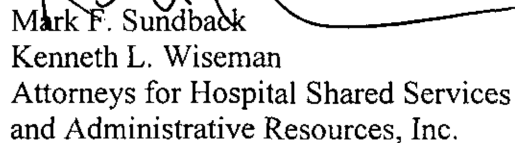
KJR

Re: Application of Duquesne Light Company for Approval of Its Restructuring Plan

Dear Mr. McNulty:

Enclosed please find an original and fifteen copies of the "Comments of Hospital Shared Services and Administrative Resources, Inc. Concerning Duquesne Light Company's Generation Auction Plan" in the referenced proceeding.

Respectfully submitted,



Mark F. Sundback
Kenneth L. Wiseman
Attorneys for Hospital Shared Services and Administrative Resources, Inc.

Enclosures

cc: All parties of record, *via first class mail*

43

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

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**

DOCUMENT FOLDER

COMMENTS OF HOSPITAL SHARED SERVICES AND ADMINISTRATIVE RESOURCES, INC. CONCERNING DUQUESNE LIGHT COMPANY'S GENERATION AUCTION PLAN

Pursuant to the procedural schedule established in the Order entered in this proceeding on May 29, 1998 by the Pennsylvania Public Utility Commission ("Commission"), as modified on October 27, 1998, Hospital Shared Services ("HSS") and Administrative Resources, Inc. ("ARI") hereby submit their comments concerning the Generation Auction Plan submitted to the Commission by Duquesne Light Company ("Duquesne"). In support hereof, HSS/ARI state as follows:

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I. INTRODUCTION

From the outset of their participation in this case, HSS/ARI have supported the proposition that Duquesne should divest its generation assets as a means to establish the actual market value of Duquesne's generation plants and as an effective way to mitigate stranded costs, if any, associated with Duquesne's generation business as a whole. That being said, HSS/ARI never have supported a proposition that Duquesne should be given *carte blanche* to divest jurisdictional assets without substantive Commission review and consideration of the propriety of all material matters concerning the divestiture. In fact, HSS/ARI strenuously oppose any such proposition and submit that Duquesne must subject its decisions concerning material matters to the Commission for review of

actual divestiture results as a necessary correlative to the Commission carrying out its responsibility to protect ratepayers from negative consequences that can result from unreasonable utility actions.

Unfortunately, Duquesne's Auction Plan does not afford ratepayers the protections to which they are entitled and which are necessary in this case. Duquesne's plan would eviscerate those protections, *i.e,* Duquesne requests that the Commission conduct no "*post-hoc* review of matters related to the conduct of [Duquesne's] auction." Auction Plan at 5. But, there is a critical need for such a review here in view of two factors: (1) Duquesne's belated, sketchy, still-evolving and potentially detrimental proposal, submitted to the Commission on October 14, 1998, to swap some of its generation assets for generation assets owned by FirstEnergy Corp. ("FirstEnergy") and (2) Duquesne's proposed Accounting Protocols (set forth in Appendix G to Duquesne's Auction Plan). Therefore, for the reasons discussed below, HSS/ARI request that the Commission accept Duquesne's Auction Plan only subject to the post-auction review that Duquesne is so anxious to avoid, but which is required to promote competition and protect ratepayers.

II.
ARGUMENT

A. A Review Of Auction Results Will Not In Any Way Diminish Potential Auction Revenues

In its Auction Plan, Duquesne asserts that it is "important that neither Duquesne nor the buyers [of Duquesne's generation plants] be subject to a *post-hoc* review of matters related to the conduct of the auction." Audit Plan at 5. As an immediate predicate to making that statement, Duquesne states that "certainty will be important to buyers, giving them confidence that the asset sale will close on a timely basis without regulatory delays." *Id.* The obvious inference Duquesne hopes that the Commission will draw by linking the two statements is that the maximization of

auction revenues may in some way be endangered if the Commission conducts a review of the auction process and results. The inference that Duquesne would have the Commission draw is a bogey that does not exist in reality.

Duquesne is right that buyers will want certainty when they bid on plants and that a lack of certainty on their ability to close could negatively impact auction results. However, the *post-hoc* review that HSS/ARI seek would not introduce any uncertainty *vis-a-vis* buyers. The *post-hoc* review would not entail any question of whether it is appropriate for Duquesne to transfer the assets to the buyers, nor would the orders resulting from the review provide for any increase in the prices buyers commit to pay under the bids they submit in the auction.

The orders stemming from the review that HSS/ARI seek would affect only matters between Duquesne and its ratepayers. The review would focus exclusively on Duquesne's actions and the relationship of those actions to auction results and net stranded cost liabilities. If the review shows that Duquesne acted reasonably, then the auction results, without adjustment, would be accepted as the market value upon which stranded costs and resulting competitive transition charges ("CTCs") would be calculated. If, however, the review shows that Duquesne acted in an unreasonable way that produces auction results that are less than reasonably should have been achieved, Duquesne would be held accountable. It would be held accountable by a Commission decision to impute, solely for purposes of calculating stranded costs, a higher market value than established by the auction, thereby reducing the amount of stranded costs Duquesne would be entitled to recover from ratepayers as compared to stranded costs derived purely from the auction results.

Thus, whether Duquesne is found to have acted reasonably or not, the Commission's determinations in the review HSS/ARI seek would not modify in any way the contractual

arrangements that Duquesne enters into with successful bidders in the auction. The Commission's decision only would affect the amount of dollars that Duquesne is entitled to recover from ratepayers as legitimate stranded costs. Thus, just as in other actions by a regulated utility, Duquesne would be held accountable by the Commission if Duquesne's actions are deemed imprudent. Therefore, there is no basis to infer that the review HSS/ARI seek will in any way impact, let alone diminish, the revenues that Duquesne can achieve in the sales of its generation plants. To the contrary, with knowledge that the Commission will review the auction results, Duquesne would have an incentive to assure that it uses its best efforts to capture the maximum market values. Without the review, Duquesne has no incentive to attempt to achieve that result because Duquesne will have an assurance that any market value Duquesne fails to capture in the auction will be recovered from ratepayers in the form of stranded costs.

Thus, the review HSS/ARI seek both will provide Duquesne an incentive to maximize its capture of market value and will serve as an insurance policy, providing indemnification by Duquesne, in the event that Duquesne does not do its job right. That is an insurance policy that is particularly important in view of Duquesne's contemplated arrangements with FirstEnergy.

B. There Are Many Uncertainties Concerning The Prudence Of Duquesne's Proposed Swap With FirstEnergy

By letter dated October 14, 1998, Duquesne submitted to the Commission certain information concerning a non-binding letter agreement between Duquesne and FirstEnergy. The letter agreement provides, *inter alia*, that Duquesne will exchange its partial ownership interests in three nuclear and five fossil generating units for FirstEnergy's full ownership interests in three fossil plants. Duquesne's plan is to sell the wholly owned plants obtained from FirstEnergy rather than

selling Duquesne's partial interests in the plants it will provide in the swap to FirstEnergy under the letter agreement. From the technical conference Duquesne convened in Harrisburg, it is HSS/ARI's understanding that Duquesne wants the Commission to grant final approval of the swap arrangement as part of a final Commission decision in December on Duquesne's Auction Plan. *See also* Duquesne's October 14, 1998 letter to the Commission, page 5. As supplemented by a submission Duquesne made on October 29, 1998, Duquesne touts several claimed major benefits that allegedly support Commission approval of the proposed swap: (1) higher market values for wholly owned versus partially owned assets; (2) higher market values for fossil versus nuclear assets; (3) resolution of disputes between Duquesne and FirstEnergy that might have impacted auction results; and (4) a financial guarantee provided by First Energy that Duquesne's customers will pay no more in stranded costs than under the Commission's administrative determination.[1]

When viewed in a vacuum, Duquesne's claims on a purely theoretical basis may be correct. Nonetheless, the swap, if it takes place, will not take place in a vacuum, and there are a host of fact questions that arise in the specific context of the proposed transaction. Some of those questions concern the material terms of the agreement with FirstEnergy. Also, actual plants are involved, and there are a host of questions concerning the value of the plants Duquesne will obtain from FirstEnergy, *i.e.*, real issues concerning, at a minimum, physical condition, maintenance and environmental compliance. Those issues are of significant concern, particularly given the value of the partially owned plants that Duquesne will give up in the swap.

[1] A complete description of the benefits Duquesne alleges will result from the proposed swap are set forth in Duquesne's October 29, 1998 submittal.

First, consider the questions concerning the specific terms of the letter agreement with FirstEnergy. The most critical such term is that the letter agreement is no agreement at all. It expressly provides that:

> the terms set forth in this agreement in principle do not constitute all of the major terms which will be included in the Exchange Agreements, that the terms set forth herein are subject to further discussion, negotiation, and due diligence, and that this agreement in principle is an expression of intent only and is not intended, nor will it be alleged by either party, to create or result in any legally binding obligation upon the parties . . . .

October 14, 1998 letter agreement between Duquesne and FirstEnergy at page 7. Accordingly, in asking the Commission to approve the swap arrangement in a December 1998 order, Duquesne is asking the Commission to give Duquesne *carte blanche* to agree to any terms whatever concerning the swap of jurisdictional assets, notwithstanding ratepayer impacts that may result when Duquesne and FirstEnergy negotiate the actual terms of a legally binding agreement. Those terms could include terms as yet undisclosed and perhaps not yet memorialized between the two utilities with physically adjacent service territories and interests that could converge to create opportunities for their mutual benefit to the detriment of ratepayers, competitors and competition itself. Thus, the procedure that Duquesne proposes is unacceptable because ratepayers will have no recourse if impacts of the actual swap transaction are detrimental, rather than beneficial, as Duquesne claims on a theoretical basis.

Further, there is more than a theoretical basis for believing such detrimental impacts are possible, if not likely. As is evident from the language quoted above from the letter agreement, as well as paragraph 15 of the agreement, to date, Duquesne has not completed its own due diligence examination of the transaction. Duquesne also has not reported to the Commission the results of any such due diligence effort. Further, Duquesne representatives have advised that the due diligence

contemplated in the letter agreement is not the full type of due diligence effort they anticipate bidders will engage in before making binding bids. But, Duquesne is unlikely to volunteer, or even admit, that it got a bad deal once the swap is consummated. Further still, while bidders, by conducting their own due diligence, will be able to protect themselves from presently unknown conditions and costs associated with the FirstEnergy plants, Duquesne's ratepayers will be left holding the bag for any such unknown conditions or costs if the Commission approves the swap transaction at this juncture. Ratepayers will be left holding the bag because the traditional safeguards inherent in an arms' length transaction -- namely that the buyer risks serious financial harm if it does not do its homework and thoroughly scrutinize the proposed transaction -- will be missing here, and Duquesne asks that the fall-back safeguard of a meaningful Commission review also be eliminated with respect to the transaction. That is an onerous result given what is known about the FirstEnergy plants, particularly as compared to Duquesne's plants.

Consider the differences. For one thing, there is a significant mismatch in capacity. The plants Duquesne will provide to FirstEnergy have 1435 MW of capacity versus only 1298 MW of capacity associated with the plants Duquesne will obtain from FirstEnergy, *i.e.*, 10% less capacity. That factor alone mitigates in part the theoretical benefits Duquesne touts in support of its proposal, but there is much more.

To be charitable, the three plants Duquesne will obtain from FirstEnergy represent an aging fleet. The Avon, New Castle and Niles plants commenced service in 1924, 1939 and 1954, respectively. *See* Exhibit 2 to the October 14 letter agreement. Further, of the 11 currently operating units at the plants, two began service in 1949; one in 1952; one in 1953; one in 1954; and, one in 1958. Response to Question No. 6 in the attachment to Duquesne's October 29, 1998 submittal.

Three other units began service in the 1960s. *Id.* The remaining two units went in service in 1970 and 1973, respectively. *Id.*

The plants Duquesne will be giving up are youngsters by comparison. The oldest plant, Sammis, began operations in 1959, *i.e.*, five years after Niles, the newest FirstEnergy plant. *See* Exhibit 1 to the October 14 letter agreement. Duquesne's other plants, *i.e.*, Eastlake, Beaver Valley, Mansfield and Perry, began operations in 1972, 1976 and 1987. Thus, Duquesne's plants clearly are of a later vintage than FirstEnergy's plants, another factor that offsets some of the benefits Duquesne touts in favor of the proposed swap. For instance, only one unit that would be acquired by Duquesne, *i.e.*, a unit at the Avon plant, is supplied from a supercritical coal fired steam generator, while all of Duquesne's fossil plants utilize that technology. *Compare* Exhibits 1 and 2 to the October 14 letter agreement.

There also are substantial environmental costs associated with the FirstEnergy plants. On the final page of the attachment to Duquesne's October 29, 1998 submittal, it is disclosed that a purchaser can expect an estimated $17 million capital cost at Avon 9 "for retrofit of LNB and SOFA." The same page reveals that SCR installation at Avon 9 will be required at a capital cost of $41 million. Total NOx related estimated costs at New Castle are estimated at $41.1 million. *Id.* Further, the document shows that in the future, all three plants to some degree will need emission allowances or will need to be operated at reduced capacity factors. Moreover, the letter agreement does not specify whether existing "banked" emissions credits will transfer with the plants, or whether FirstEnergy will retain those credits.

Of course, the ultimate impact of the foregoing factors on the value of the plants is unknown at this time, and, in fact, cannot be assessed with the dearth of information currently available. Nonetheless, it is worthwhile to examine some valuation materials that are available.

Duquesne's October 29, 1998 submittal discloses that FirstEnergy estimated stranded costs of $67,423,000 associated with the three plants.[2] At the same time, CS First Boston estimated in the market value study it performed for Duquesne that Duquesne's fossil plants that it will transfer to FirstEnergy have a net positive market value of almost $272 million. *See* HSS/ARI Statement No. 1, Exh. RBW-10 concerning Sammis, Eastlake and Mansfield. While HSS/ARI recognize that FirstEnergy's and CS First Boston's market value estimates are based upon different assumptions, it nonetheless cannot be ignored that at least one well-known financial advisor saw substantial value that Duquesne now proposes to give away for older plants, with substantial associated environmental compliance costs, upon which FirstEnergy places minimal value.[3]

In view of the foregoing, HSS/ARI submit that it is unacceptable to grant Duquesne's request for final approval of the proposed swap transaction with no recourse against Duquesne for unreasonable results that are contrary to ratepayer interests.

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[2] According to an attachment to the submittal, total net book value is $260,923,000, and FirstEnergy calculated market value of only $193,000,000. The attachment immediately follows Duquesne's narrative responses to questions concerning the Avon, New Castle and Niles plants.

[3] It also should be pointed out that under the letter agreement, Duquesne would give up its claims for money damages in the "Eastlake Litigation" it is engaged in against FirstEnergy. October 14, 1998 letter agreement at 6. The letter agreement does not reveal the amount of the damage claim Duquesne is conceding or the potential ratepayer benefits that could result from Duquesne's successful prosecution of that case.

C. Duquesne's Convoluted Accounting Protocols Are Suspect

With the sale of its generation assets, a calculation of Duquesne's remaining stranded costs, if any, should be easy. From the gross proceeds of the sale (reviewed in accordance with the procedure discussed in Section II.A above), Duquesne should deduct then-current net book value, transaction costs and actual taxes paid (in accordance with Commission precedent) to determine net proceeds. Duquesne then should compare the net proceeds against stranded cost recoveries authorized by the Commission with regard to regulatory assets and nuclear decommissioning costs to determine net stranded costs, if any, to be collected from ratepayers.[4] Assuming there are such stranded costs, Duquesne then would use net proceeds to offset the stranded costs paid by ratepayers prior to Duquesne's divestiture of its generation plants. To the extent that Duquesne has any stranded costs remaining after this exercise, a CTC should be designed to recover the remaining stranded costs. It also would be necessary to design an appropriate shopping credit.

Instead of using this straight-forward method for determining stranded costs, Duquesne's proposed accounting protocols attempt to reconcile final auction results against the Commission's administrative determination of stranded costs and to set shopping credits equal to the shopping credits established in the Commission's May 29, 1998 Order. *See, e.g.*, Auction Plan at 36. Duquesne's accounting protocols are so complex that it needs 23-pages to outline its proposal. *See* Appendix G to Auction Plan. To perform its calculations, Duquesne must make adjustments based

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[4] In making the foregoing statement, HSS/ARI are not acknowledging that the Commission's Order in this case properly determined Duquesne's stranded costs. HSS/ARI have appealed the Commission's determination and the foregoing statement should not be construed as a waiver or reversal of HSS/ARI's positions on the issues that are being pursued before the Commonwealth Court.

upon the Office of Consumer Advocate's ("OCA's) forecasted market prices, and Duquesne's methodology inherently takes into account such factors as projected capital additions, projected O&M expenses, assumed merger savings and other factors that are wholly irrelevant in view of the fact that Duquesne is selling its generation assets.

HSS/ARI cannot state with certainty that Duquesne's proposed accounting protocols will produce a result that will differ from the result that would occur if Duquesne determined stranded costs using the methodology described in the first paragraph of this section. Nonetheless, HSS/ARI also cannot state with certainty that Duquesne's convoluted methodology will not produce results that are skewed because of the reliance on the market price forecasts and other assumptions and irrelevant factors subsumed within the administrative determination. HSS/ARI can state with certainty, however, that transparency of results is critical if an evaluation is to be made as to the accuracy of the net stranded costs, if any, to be imposed upon ratepayers.

As a result, there is no reason for the Commission to accept Duquesne's convoluted accounting protocols. Notwithstanding any claim to the contrary, the most simple, accurate and verifiable accounting methodology to use to account for Duquesne's sale of its generation plants is that set forth in the first paragraph of this section. As such, the Commission should reject Duquesne's accounting protocols and require Duquesne to account for the auction results in a straight-forward manner that excludes consideration of forecasts and assumptions that are irrelevant to a determination of stranded costs in the context of an actual asset sale. Actual sale results then easily can be verified by the Commission's audit staff, thereby avoiding the unnecessary delay, confusion and potential overcharges that could result from the use of Duquesne's proposed protocols. Further, appropriate shopping credits can be established based upon actual stranded cost

results, rather than based upon what would be at that point, an irrelevant and most likely substantially different administrative determination of stranded costs.

A second accounting issue that arises under Duquesne's Auction Plan relates to the categories of costs that Duquesne can deduct from gross proceeds to determine net stranded costs. Both Duquesne and ratepayers need certainty as to those categories of costs. With one exception that HSS/ARI will discuss below, HSS/ARI agree that, in general, the categories of costs Duquesne identifies as transaction costs are appropriate and that after-tax proceeds must be compared to Duquesne's authorized recoveries of regulatory assets and nuclear decommissioning costs to determine net stranded costs. *See* Appendix G to Auction Plan at pp. 1-3. Of course, the propriety of Duquesne's actual transaction costs only can be determined on an after-the-fact basis because they are unknown at this time. Thus, Duquesne should submit a report of its accounting of the final auction results to the parties and the Commission's audit staff for review. Assuming that the transaction costs Duquesne incurs are reasonable, there should be no need to debate the final accounting other than to assure that any inaccuracies are corrected.

However, as indicated above, there is one category of costs that the Commission should not allow. In its Auction Plan, Duquesne states that "After-tax Auction Proceeds shall be defined as Net Auction Proceeds less current taxes *payable* ('Current Taxes') as a result of the Utility Assets divested." Appendix G to Auction Plan at p. 3 (emphasis added). Duquesne goes on to state in numerous instances that Current Taxes on a combined federal-state basis are 41.4935%. *See, e.g.*, Appendix G to Auction Plan at p. 4. The level of Current Taxes as discussed by Duquesne either has to be clarified or modified depending upon what Duquesne means by "current taxes *payable*."

Based upon Pennsylvania case law, the taxes to be deducted to determine "After-tax Auction Proceeds" should not be taxes payable based upon the maximum combined federal-state income tax

rate. The taxes to be deducted should be actual taxes paid in accordance with the Commissions long-standing practice. In other words, regardless whether the maximum combined federal-state income tax rate is 41.4935% or any other rate, Duquesne's actual, effective tax rate may be lower than the maximum depending upon any number of factors that may exist at the time of the closing on the sales of the plants. If that is the case, Duquesne should not be permitted to retain for shareholders any benefit that might result from Duquesne paying taxes at a lower rate than the maximum.

There is one other accounting matter that needs to be corrected now. Appendix G to Duquesne's Auction Plan reveals that Duquesne is attempting to recover $179 million as a regulatory asset associated with FAS 109 deferred taxes. HSS/ARI are contesting before the Commonwealth Court Duquesne's right to recover the deferred taxes as stranded costs. However, there is an independent problem associated with Duquesne's inclusion of the $179 million as a regulatory asset in its Auction Plan.

HSS/ARI understand that under the plan, deferred taxes are being treated as part of Duquesne's net plant balances. That is consistent with the Commission's resolution of arguments made concerning Duquesne's right to recover deferred taxes as stranded costs. May 29, 1998 Order at 155. But, in listing the $179 million as a regulatory asset, Duquesne is double counting the deferred taxes. Under Appendix G, Duquesne would recover the deferred taxes twice, *i.e.*, once in the calculation of net plant and a second time as a regulatory asset. Duquesne, thus, should be required to remove the $179 million in deferred taxes as a regulatory asset.

III.
CONCLUSION

For the foregoing reasons, the Commission should:

(1) order that Duquesne's auction results be subjected to a prudence review solely for the purpose described in Section II.A hereof;

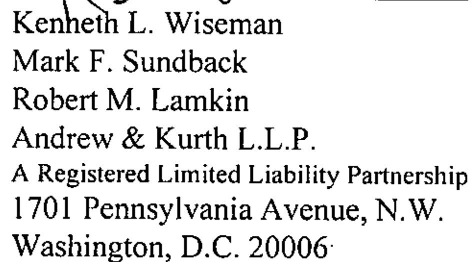
(2) decline to provide final approval of Duquesne's proposed transaction with FirstEnergy;

(3) reject Duquesne's accounting protocols as discussed in Section II.C hereof;

(4) clarify that Duquesne will be permitted to deduct from the auction proceeds only the actual taxes that Duquesne pays; and,

(5) require Duquesne to eliminate its double counting of deferred taxes as discussed in Section II.C.

Respectfully submitted,



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

Dated: November 6, 1998

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

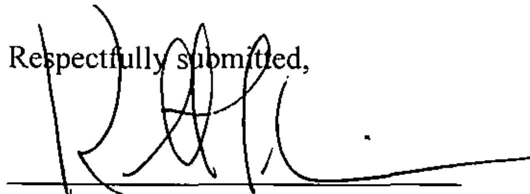
Application of Duquesne Light Company	)	
for Approval of Its Restructuring Plan	)	**Docket Nos. R-00974104 and**
Under Section 2806 of the Public Utility Code	)	**R-00974104C0001-C0004**

COMMENTS OF HOSPITAL SHARED SERVICES AND ADMINISTRATIVE RESOURCES, INC. CONCERNING <u>DUQUESNE LIGHT COMPANY'S GENERATION AUCTION PLAN</u>

I hereby certify that I have this day served a true copy of the foregoing Comments of Hospital Shared Services and Administrative Resources, Inc. Concerning Duquesne Light Company's Generation Auction Plan upon each person designated on the official service list in this proceeding a copy of which is attached.

Dated this 6th day of November.

Respectfully submitted,



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BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Application of Duquesne Light Company	)	
for Approval of Its Restructuring Plan	)	**Docket Nos. R-00974104 and**
Under Section 2806 of the Public Utility Code	)	**R-00974104C0001-C0004**

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+ MEMBER OF MD BAR ONLY
~ MEMBER OF DC BAR ONLY
# MEMBER OF IA BAR ONLY

November 6, 1998

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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

Via Next-Business-Day Courier

Prothonotary
Pennsylvania Public Utils. Commission
North Office Building
Harrisburg, PA 17120

Re: Application of Duquesne Light Company, Docket No. R-00974104

Dear Prothonotary:

Enclosed for filing please find one original and three copies each of two documents submitted for filing on behalf of the Utility Workers Union of America, AFL-CIO, in the above-captioned docket. The two documents are:

1. "Petition of the Utility Workers Union of America, AFL-CIO to Intervene Out of Time"
2. "Comments of the Utility Workers Union of America, AFL-CIO on Generation Exchange and Generation Auction Plan"

I also enclose one additional copy of each document, which I ask be date-stamped and returned in the enclosed self-addressed stamped envelope. Please call me if you have any questions.

Very truly yours,

David E. Pomper
Attorney for the
Utility Workers Union of America,
AFL-CIO

cc: All Parties (by U.S. Mail)
Counsel for Duquesne
(additional copy by next-business-day hand delivery)

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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 No. R-00974104

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PA PUBLIC UTILITY COMMISSION
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**PETITION OF THE
UTILITY WORKERS UNION OF AMERICA, AFL-CIO
TO INTERVENE OUT OF TIME**

Pursuant to 52 Pa. Code §§ 5.71 and 5.74(a), the Utility Workers Union of America, AFL-CIO ("the UWUA"), hereby petitions to intervene in the remaining proceedings in this docket. In support of its Petition, the UWUA states as follows:

1. Although the UWUA did not intervene in this proceeding when Duquesne Light Company ("Duquesne") filed its proposed Restructuring Plan in August 1997, Duquesne has recently filed herein proposals that directly affect the UWUA's interests. On October 14, 1998, Duquesne filed an agreement in principle with FirstEnergy Corp. for a substantial exchange of generating assets, after which Duquesne would auction off its reconstituted generation holdings pursuant to its Generation Auction Plan, filed herein on August 27, 1998. The Commission has invited comments on these related proposals, and set a due date of November 6 or 9, 1998 for such comments. [1] The UWUA seeks to

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[1] See Order dated October 27, 1998. The Order provided a November 9, 1998 date for comments (rather than November 6, 1998) "if such additional time is necessary to evaluate supplemental information received from Duquesne regarding the generation exchange." The UWUA has needed the additional time to evaluate the Generation Auction Plan in light of its supplementation through the generation exchange plan. Accordingly, the UWUA believes that the November 9 date would apply. Out of an abundance of caution, if the November 6 date would be applicable, the UWUA requests a waiver of that date to permit it to file on November 9. To ensure that application of the latter date does not prejudice Duquesne in

intervene for the purpose of filing comments on the Generation Auction Plan and on the generation exchange and participating in future proceedings in this docket. The UWUA accepts the existing record as it stands.

2. The UWUA is the national union representing 50,000 workers primarily in electric, gas and water industries across the United States. UWUA's principal office is at 815 16th Street, NW, Washington, D.C. 20006.

3. The UWUA represents most of the nonclerical and nonmanagerial workers at the New Castle coal plant in New Castle, Pennsylvania. The New Castle plant is one of the plants currently owned by FirstEnergy that would be transferred to Duquesne as part of the generation exchange, thence to be sold at auction to an as-yet-unidentified new owner.

4. The Pennsylvania Power Company, FirstEnergy's Pennsylvania operating company, had not heretofore planned to divest itself of New Castle (or its other generation plants) as part of its restructuring.[2] Thus, the proposed exchange-and-auction plan will result in the New Castle plant being sold at auction to an as-yet-unidentified new owner, an event that would not occur but for the exchange-and-auction.

5. Auctioning the New Castle plant will subject its workers, including numerous workers represented by the UWUA through its Local No. 140, to a direct and substantial threat to their livelihoods and terms of employment. For example, as proposed, the terms

---

preparing its reply comments, the UWUA will today hand-deliver this petition and the accompanying UWUA comments to Duquesne's Washington, D.C. counsel.

[2] *See In re Application of Pennsylvania Power Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code,* Docket No. R-00974149 (June 18, 1998), slip op. at 19 ("we note that Penn Power does not propose divestiture of its generating facilities as have other companies").

of the disposition to Duquesne do not include binding assurances that Duquesne and any successor to which Duquesne may auction the plant will retain existing employees and maintain the terms of their employment. [3] Nor does the exchange-and-auction plan appear to provide for severance, early retirement, retraining or job retention in other positions, as expressly contemplated by the Act, 66 Pa. C.S.A. §§ 2802(8), 2802(11), 2802(18), 2803(3), and 42 § 3806(E).

6. Similarly, the exchange-and-auction plan provides no assurance that Duquesne, and the purchaser of New Castle at auction, will continue existing safety-related work rules and practices. Thus, the exchange-and-auction may not adequately ensure the safety of the electric system to workers and others, as expressly contemplated by the Act, 66 Pa. C.S.A. §§ 2802(11), and by 66 Pa. C.S.A. § 1501.

7. The proposed generation exchange will also include transfer of Duquesne's rights and interests in the Beaver Valley Power Station Units Nos. 1 & 2 to FirstEnergy. To date, Duquesne has operated and maintained the Beaver Valley plant on behalf of its joint owners. As part of the generation exchange, this role would be transferred to the FirstEnergy Nuclear Operating Company. See Roque Letter at 3, ¶ 7(a). Thus, the generation exchange would jeopardize the continued employment and the employment terms of the workers now employed at Beaver Valley by Duquesne. At best, it would result in their being employed by FirstEnergy. As the UWUA will explain in its

[3] See the Enclosure to Duquesne's October 14, 1998 filing, Letter from Victor A. Roque, Duquesne Vice President and General Counsel, to FirstEnergy Corp. (October 14, 1998) ("Roque Letter"), at 6 (stating that the exchanging companies will "cooperate to resolve" labor-related matters, but not expressly committing either company to specific worker protection obligations).

substantive comments on the generation exchange, which are being filed separately today, FirstEnergy's labor relations have been and remain poor.

8. In light of FirstEnergy's poor labor relations, transferring the Beaver Valley operator role to FirstEnergy may also adversely affect the plant's reliability and safety. Such degradation would violate the express intent of the Electricity Generation, Customer Choice and Competition Act. *See, e.g.*, 66 Pa. C.S.A. §§ 2802(11), (12), (20), and 2804(1), (14) and 2807.

9. Transferring the Beaver Valley operator role to FirstEnergy will also affect workers at other generating plants across Pennsylvania, including the New Castle workers represented by the UWUA. In the competitive marketplace contemplated by utility restructuring, New Castle will stand at risk of being shut down if its operating costs are not competitive with those of other plants. Thus, a Beaver Valley plant that cuts corners on labor costs will further a "race to the bottom," subjecting New Castle workers to economic pressure to work under similarly unfavorable conditions. Moreover, FirstEnergy will remain predominantly an Ohio-based company. Because Ohio has not enacted electricity restructuring legislation comparable to Pennsylvania's, FirstEnergy will retain a secure Ohio customer base for the foreseeable future. This advantage will enable FirstEnergy to put additional economic pressure on New Castle and other Pennsylvania plants, and their workers.

10. The Company's proposal not only threatens the livelihoods of UWUA members, but it also affects the interests that UWUA's members who are residential customers of Pennsylvania utilities have in continuing to receive reliable electric service at reasonable

cost. The UWUA therefore has a direct interest in protecting the interests of its members as electricity consumers.

11. The UWUA's participation will be in the public interest. Its members have knowledge, information and a perspective to present regarding the remaining Duquesne restructuring issues that cannot be provided by other parties.

12. No other participant can adequately represent the interests of the UWUA and its members. Although the UWUA's interests are generally aligned with those of the International Brotherhood of Electric Workers ("IBEW"), the UWUA and IBEW represent different workers and may not have identical interests.

13. Therefore, the UWUA meets the eligibility criteria of Pa. Code §§ 5.72(a)(2)-(3), and its situation presents both good cause and extraordinary circumstances justifying intervention out of time under Pa. Code §§ 5.74(a).

14. The UWUA will be represented in this proceeding by the following counsel, who should be placed on the Commission's service list and receive copies of all correspondence and other documents:

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To speed communications, the UWUA requests that its President and National Representative also be placed on the service list and receive copies:

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WHEREFORE, for the reasons set forth above, the UWUA's petition to intervene out of time should be granted, and the UWUA should be made a full party to this proceeding.

Respectfully submitted,

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Pennsylvania Bar No. 55998

Attorneys for the Utility Workers
Union of America, AFL-CIO

Law Offices of:
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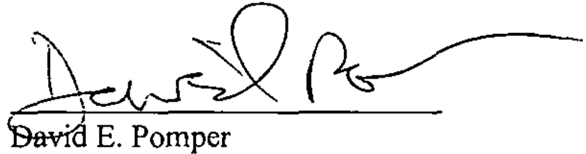
November 6, 1998

CERTIFICATE OF SERVICE

I certify that I have this day served a true copy of the foregoing document (Petition of the Utility Workers Union of America, AFL-CIO to Intervene Out of Time) upon the participants on the attached list, in accordance with the requirements of § 1.54 (relating to service by a participant).

Dated this 6th day of November, 1998.



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PA PUBLIC UTILITY COMMISSION
SECRETARY'S BUREAU

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

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COMMENTS OF THE UTILITY WORKERS UNION OF AMERICA, AFL-CIO ON GENERATION EXCHANGE AND GENERATION AUCTION PLAN

Pursuant to the Order dated October 27, 1998, the Utility Workers Union of America, AFL-CIO ("the UWUA") [1] hereby submits its comments on two recent, related proposals of Duquesne Light Company ("Duquesne"). On October 14, 1998, Duquesne filed an agreement in principle with FirstEnergy Corp. for a substantial exchange of generating assets, after which Duquesne would auction off its reconstituted generation holdings pursuant to its Generation Auction Plan, filed herein on August 27, 1998. The combined exchange-and-auction plan raises and fails to answer numerous questions about how the resulting restructuring will protect the statutorily-recognized interests of workers, reliability, safety, and consumers.

I. THE PLAN MUST PROTECT NEW CASTLE WORKERS

The UWUA represents most of the nonclerical and nonmanagerial workers at the New Castle coal plant in New Castle, Pennsylvania. The New Castle plant is one of the

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[1] By a separate, contemporaneous motion, the UWUA is petitioning to intervene in this docket out of time.

plants currently owned by FirstEnergy that would be transferred to Duquesne as part of the generation exchange, thence to be sold at auction to an as-yet-unidentified new owner.

The Pennsylvania Power Company, FirstEnergy's Pennsylvania operating company, had not heretofore planned to divest itself of New Castle (or its other generation plants) as part of its restructuring.[2] Thus, the proposed exchange-and-auction plan will result in the New Castle plant being sold at auction to an as-yet-unidentified new owner, an event that would not occur but for the exchange.

Auctioning the New Castle plant will subject its workers, including numerous workers represented by the UWUA through its Local No. 140, to a direct and substantial threat to their livelihoods and terms of employment. For example, as proposed, the terms of the disposition to Duquesne do not include binding assurances that Duquesne and any successor to which Duquesne may auction the plant will retain existing employees and maintain the terms of their employment.[3] Nor does the exchange-and-auction plan appear to provide for severance, early retirement, retraining or job retention in other positions, as expressly contemplated by the Electricity Generation, Customer Choice and Competition Act, 66 Pa. C.S.A. §§ 2802(8), 2802(11), 2802(18), 2803(3), and 42 § 3806(E).

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[2] *See In re Application of Pennsylvania Power Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code,* Docket No. R-00974149 (June 18, 1998), slip op. at 19 ("we note that Penn Power does not propose divestiture of its generating facilities as have other companies").

[3] See the Enclosure to Duquesne's October 14, 1998 filing, Letter from Victor A. Roque, Duquesne Vice President and General Counsel, to FirstEnergy Corp. (October 14, 1998) ("Roque Letter"), at 6 (stating that the exchanging companies will "cooperate to resolve" labor-related matters, but not expressly committing either company to specific worker protection obligations).

Similarly, the exchange-and-auction plan provides no assurance that Duquesne, and the purchaser of New Castle at auction, will continue existing safety-related work rules and practices. Thus, the exchange-and-auction may not adequately ensure the safety of the electric system to workers and others, as expressly contemplated by the Act, 66 Pa. C.S.A. §§ 2802(11), and by 66 Pa. C.S.A. § 1501.

Duquesne's Generation Auction Plan recognizes (at 34-35) that employee impacts must be considered in this proceeding, but fails to provide any specifics as to how workers will be protected. This lack of information and assurance renders the plan inconsistent with *In re Application of Duquesne Light Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code,* 185 P.U.R.4th 389, 430 (Pa. PUC 1998) ("*Duquesne Restructuring Order*"), which requires the plan to set forth and fairly resolve transitional issues affecting "customers, investors, the employees of the Company, local communities, and other affected parties." This deficiency precludes approval of Duquesne's plans as filed.

II. THE PLAN MUST PROTECT WORKERS WHOSE PLANTS WOULD BE TRANSFERRED TO FIRSTENERGY

The proposed generation exchange will also include transfer of Duquesne's rights and interests in the Beaver Valley Power Station Units Nos. 1 & 2 to FirstEnergy. To date, Duquesne has operated and maintained the Beaver Valley plant on behalf of its joint owners. As part of the generation exchange, this role would be transferred to the FirstEnergy Nuclear Operating Company. See Roque Letter at 3, ¶ 7(a). Thus, the generation exchange would jeopardize the continued employment and the employment

terms of the workers now employed at Beaver Valley by Duquesne. At best, it would result in their being employed by FirstEnergy.

FirstEnergy's labor relations have been and remain poor. For example, when FirstEnergy acquired Cleveland Electric Illuminating's generating plants, it took the position that it was not obligated to honor an "evergreen" successorship provision in CEI's labor agreements. FirstEnergy refused to arbitrate or meaningfully negotiate with the UWUA regarding this issue. Instead, it declared an impasse, implemented its own unilateral proposal, and laid off approximately 500 employees. [4]

FirstEnergy has also been cutting corners on worker training and preventative maintenance at its generating plants. For example, at its W.H. Sammis plant, [5] FirstEnergy is seeking to replace experienced workers, lost to early retirement, with inexperienced workers who do not meet FirstEnergy's own qualification standards. Also, preventative maintenance at W.H. Sammis (and at the nearby R.E. Burger plant [6]) has been cut back in recent years. Not coincidentally, the Sammis forced outage rate, which had previously been declining, is now rising, and its safety record is getting worse.

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[4] The UWUA-FirstEnergy labor dispute is the subject of an ongoing National Labor Relations Board investigation. It also involves ongoing litigation in the United States District Court for the Northern District of Ohio, before Judge Aldrich, regarding the evergreen provision. The UWUA has no intention of attempting to litigate these matters before the Commission. However, in the exercise of its own regulatory responsibilities, the Commission should be aware of the state of FirstEnergy's labor relations before it approves the proposed generation exchange.

[5] The W.H. Sammis plant is located in Stratton, Ohio. Part of the plant is currently owned by Duquesne and would be transferred to FirstEnergy as part of the proposed exchange. The plant is described in the appendix to Duquesne's October 14, 1998 filing. UWUA Local No. 457 represents more than 200 workers at the Stratton plant.

[6] UWUA Local No. 350 represents numerous workers at the Burger plant.

In light of FirstEnergy's poor labor relations and corner-cutting, transferring the Beaver Valley operator role to FirstEnergy may also adversely affect the plant's reliability and safety. FirstEnergy presumably will apply to Beaver Valley the same questionable management methods that is applying to its other baseload plants. Such degradation would violate the express intent of the Electricity Generation, Customer Choice and Competition Act. *See, e.g.*, 66 Pa. C.S.A. §§ 2802(11), (12), (20), and 2804(1), (14) and 2807.

Transferring the Beaver Valley operator role to FirstEnergy will also affect workers at other generating plants across Pennsylvania, including the New Castle workers represented by the UWUA. In the competitive marketplace contemplated by Duquesne's restructuring, New Castle will stand at risk of being shut down if its operating costs are not competitive with those of other plants. Thus, a Beaver Valley plant that cuts corners on labor costs will further a "race to the bottom," subjecting New Castle workers to economic pressure to work under similarly unfavorable conditions. Moreover, FirstEnergy will remain predominantly an Ohio-based company. Because Ohio has not enacted electricity restructuring legislation comparable to Pennsylvania's, FirstEnergy will retain a secure Ohio customer base for the foreseeable future. This advantage will enable FirstEnergy to put additional economic pressure on New Castle and other Pennsylvania plants, and their workers.

III. THE PLAN MUST PROTECT CONSUMERS

As filed, the Company's proposal may also harm the interests of consumers (including UWUA members who are residential customers of Pennsylvania utilities) in

continuing to receive reliable electric service at reasonable cost. The Commission should, at minimum, impose conditions on the proposed asset transfers to FirstEnergy and at auction to ensure continued reliable service at reasonable prices.

A. Duquesne's Generation Transfers to FirstEnergy and at Auction Should Include Conditions Requiring the New Owner(s) to Provide Ancillary Services and Must-Run Generation

The Commission's May 29, 1998 Order directed that Duquesne's divestiture plan "disclose those assets and/or operational criteria of an asset essential for the continued reliability of service in the Duquesne territory." *Duquesne Restructuring Order,* 185 P.U.R.4th 389, 430 (Pa. PUC 1998) (required item No. 6). Duquesne's plan (Generation Auction Plan at 28-34) discloses that in order to maintain the integrity of its transmission system, Duquesne will have to procure both generation-based ancillary services [7] and must-run (Elrama and Cheswick) generation output. But the plan lacks adequate provisions for securing these services on reasonable terms.

The potential sources of economic supply for these services are limited. For example, reactive power must be provided from sources suitably located in relation to the transmission system. See Federal Energy Regulatory Commission Order 888 [8] at 31,716; Order 888-A at 31,235 ("reactive power obligations ... cannot be completely supplied by

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[7] The generation-based ancillary services include reactive power supply and voltage control, regulation and frequency response, energy imbalance, and spinning and supplemental reserves.

[8] *Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities*, Order No. 888, 61 Fed. Reg. 21,540, [1991-1996 Regs. Preambles] FERC Stat. & Regs. ¶ 31,036, *clarified*, 76 F.E.R.C. ¶ 61,009 (1996), *modified*, Order No. 888-A, 62 Fed. Reg. 12,274, III FERC Stat. & Regs. ¶ 31,048 (1997), *order on reh'g*, Order No. 888-B, 62 Fed. Reg. 64,688, 81 F.E.R.C. ¶ 61,248 (1997), *petitions for review docketed sub nom. Transmission Access Policy Study Group v. FERC*, No. 97–1715 (D.C. Cir. Dec. 5, 1997), *order on reh'g*, Order No. 888-C, 82 F.E.R.C. ¶ 61,046 (1998).

distant sources"). Regulation and energy imbalance require either load-following capabilities located in the control area or dynamic scheduling. FERC Order 888 at 31,717; see also Duquesne Generation Auction Plan at 30-31 & n.32. Because the telemetering and communications costs of dynamic scheduling can be hefty, local generation on Automatic Generation Control may be the only economic source of supply. There are similar restrictions on the location and responsiveness of spinning reserves. See Generation Auction Plan at 32. There is no known substitute for Elrama and Cheswick generation in providing the must-run output needed at those locations to maintain system reliability. Thus, the purchasers of the auctioned plants will have significant market power in selling these essential ancillary and must-run services. [9]

Duquesne proposes to pass on to transmission customers whatever it pays for these essential services. Generation Auction Plan at 28-29 & n.29. That amount could be exorbitant if Duquesne divests itself of supply sources without attaching conditions requiring the plants' new owner(s) to supply these services to Duquesne on reasonable terms. Duquesne appears to recognize the problem, at least as to must-run generation, but does not propose an adequate solution. Duquesne proposes only a five-year commitment to sell must-run generation (Generation Auction Plan, Appendix F, § 2.1), and at a market-based price rather than one capped at Duquesne's original cost less accumulated depreciation. This pricing proposal violates Federal Energy Regulatory Commission

[9] Although the new plant owners' sales of must-run power or power used to supply ancillary services might be regulated by the Federal Energy Regulatory Commission (e.g., if structured as a sale for resale), there is no assurances that FERC would continue to insist that the rates for these plants be based on Duquesne's net original cost, as opposed to the purchaser's acquisition price or market prices.

precedent.[10] Duquesne also fails to propose any similar commitments regarding ancillary services.

The Commission should require that the purchasers for Duquesne's plants commit, as a condition of the sale, to supply these services to Duquesne until they either retire the plants or demonstrate in an appropriate regulatory proceeding that there is a workably competitive market for these specific services. The ancillary service rates and must-run generation rates should be capped based on the plants' original net cost, *i.e.* Duquesne's original net cost, minus accumulated depreciation, and not marked up for any market-value premium that the new owner may pay for the plants. Otherwise, an above-original-cost premium paid for the underlying generation assets will be passed on to Duquesne's transmission customers. Ironically, this pass-through would reintroduce the "water in the rate base" painstakingly wrung out of consumers' electricity prices at the outset of regulation.[11]

Further, to ensure transmission system reliability, sales of the Elrama and Cheswick plants need to be conditioned to ensure that they are not retired before the transmission system is upgraded to maintain reliability and system security in their absence.

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[10] *See Duke Energy Moss Landing LLC et al.*, 83 FERC ¶ 61,318 (1998) (rate for must-run power sold to independent transmission operator from unit divested by Pacific Gas & Electric must be based on unit's net original cost, without acquisition adjustment for above-book price paid by plant's new owner).

[11] *See id.*, 83 FERC at 62,304 & n.39 ("Reliance on original cost ratemaking began decades ago because utilities were engaging in multiple asset transfers for the sole purpose of increasing their plant investment rate base and, thus, increasing their rates.").

B. The Full Terms of Duquesne's Generation Exchange Must be Carefully Scrutinized to Prevent an End-Run of the Objective Plant Valuation Intended by the Restructuring Order

In its May 29, 1998 order on the basic Duquesne restructuring plan, the Commission found that the value of Duquesne's plants could be properly determined only through an arms-length sale:

> We find that only a market-based determination of stranded costs can reasonably satisfy the "known and measurable" criteria set forth in the Act. Expert predictions based upon market price projections are subject to errors of estimation and are inherently inferior to valuations based upon market data.

Duquesne Restructuring Order, 185 P.U.R.4th 389, 431 (Pa. PUC 1998). To achieve such an objective valuation and maximize the price received for its plant, Duquesne's Generation Auction Proposal set forth an elaborate, multi-stage auction process open to multiple bidders.

Now, however, Duquesne proposes to take more than 1,400 MW of its generation out of the auction process. Instead of auctioning that generation, Duquesne will exchange it for other generation, through a bilateral swap with FirstEnergy. Implicitly, this plan requires the Commission to make an administrative determination that the value Duquesne would receive from FirstEnergy is at least equal to the value that Duquesne would give up in exchange.

Duquesne has not provided a sufficient basis for such a determination. For example, as discussed above Duquesne may have to purchase ancillary services and must-run generation from the plants' new owner(s) at rates above net original cost. This possibility detracts from the value of the exchange, in ways that are not accounted for by

the asserted FirstEnergy guarantee that the net proceeds from its generation auction will maintain or reduce the stranded cost level determined administratively in the May 29, 1998 *Duquesne Restructuring Order*. The "guarantee" also relegates Pennsylvania consumers to the administratively-determined valuation that the Commission found to be an inadequate substitute for a market-based valuation.

Furthermore, although at first glance fossil units might appear to be more marketable than shares in nuclear plants, Duquesne would remain liable for the open-ended costs of terminating its Beaver Valley Unit 2 lease agreements, and would receive 138 fewer MW of capacity from FirstEnergy than it would give up. And as discussed in Part II above, the plants to be transferred by FirstEnergy may come with the detriment of significant deferred maintenance (especially now that FirstEnergy is planning to turn those plants over to Duquesne).

Thus, the Commission needs to closely scrutinize whether the swap is a good deal for the consumers who will have to pay off Duquesne's stranded costs.

IV. THE PLAN MUST BE MADE MORE SPECIFIC

The Commission's May 29, 1998 Restructuring Order set forth sixteen requirements for Duquesne's divestiture plan. *Duquesne Restructuring Order,* 185 P.U.R. 4th 389, 430 (Pa. PUC 1998). These requirements include (*id.*):

> 16. The plan shall set forth transitional issues and the resolution of those issues in a manner that is fair to customers, investors, the employees of the Company, local communities, and other affected parties.

Duquesne's Generation Auction Plan, in combination with proposed swap, utterly fails to meet this requirement. There is no way the Commission, or the public, can tell from what is admittedly only an agreement in principle, expressly subject to change (see Agreement in Principle at ¶14), how transitional issues with regard to customers, investors, employees or local communities are being addressed. *A fortiori,* it cannot be determined that such treatment is appropriate and consistent with Pennsylvania's restructuring act. Indeed, as pointed out in its November 3, 1998 Comments of System Council U-10, International Brotherhood of Electrical Workers on Duquesne Light Company's Generation Auction Plan at 11, the swap agreement in principle is inconsistent with the auction plan in material respects. Thus, the proposal on the table is confused and insufficiently specified.

Particularly in light of the proposed swap's significant impact on the auction plan, the Commission and the public must have an opportunity to fully evaluate the auction plan in the context of the fully developed swap agreement. Thus, the UWUA agrees with the IBEW that the auction plan and the agreement in principle with FirstEnergy do not provide sufficient information for the Commission to assess several critically important issues and that Duquesne must provide additional information that addresses the effect of any such transfer on its employees, the local communities that will be affected, and the safety and reliability of the Duquesne system. The UWUA further requests an opportunity to comment on such completed plan.

V. CONCLUSION

For the reasons discussed above, Duquesne's Generation Action Plan should not be approved as filed. To permit the Commission to carry out its obligations under the Pennsylvania Restructuring Act, Duquesne should be required to provide additional information, including the complete, definitive swap agreement, and the public provided an opportunity for further comment. The Commission should then modify and condition the revised complete plan in a manner that is consistent with the Duquesne restructuring order and the Act to protect the statutorily-recognized interests of workers, reliability, safety and consumers.

Respectfully submitted,

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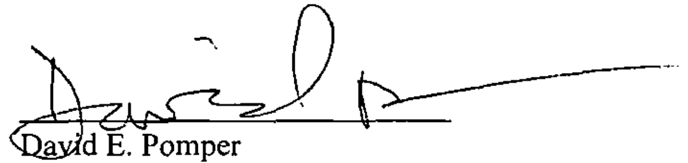
November 6, 1998

CERTIFICATE OF SERVICE

I certify that I have this day served a true copy of the foregoing document (Comments of the Utility Workers Union of America, AFL-CIO on Generation Exchange And Generation Auction Plan) upon the participants on the attached list, in accordance with the requirements of § 1.54 (relating to service by a participant).

Dated this 6th day of November, 1998.



David E. Pomper

Attorney for
Utility Workers Union of America, AFL-CIO

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

IN REPLY PLEASE REFER TO OUR FILE

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November 9, 1998

JAMES MCNULTY SECRETARY
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HARRISBURG PA 17105-3265

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SECRETARY'S BUREAU

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

Dear Secretary McNulty:

Enclosed please find an original and ten (10) copies of the **Comments of the Office of Trial Staff on Duquesne Light Company's Generation Auction Plan** for filing in the above-docketed matter.

If you have any questions, please contact me at (717) 787-1976.

68

Very truly yours,

Kandace F. Melillo

Kandace F. Melillo
Prosecutor
Office of Trial Staff

KFM:sjh

c: Chairman Quain
Vice Chairman Bloom
Commissioner Rolka
Commissioner Brownell
Commissioner Wilson
Cheryl Walker-Davis
Bohdan Pankiw
Donald Muth
Parties of Record

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

ORIGINAL

PENNSYLVANIA PUBLIC UTILITY COMMISSION	:	
v.	:	
DUQUESNE LIGHT COMPANY	:	Docket No. R-00974104
(Application to approve restructuring plan pursuant to 66 Pa. C.S. §2806)	:	

COMMENTS OF THE OFFICE OF TRIAL STAFF ON DUQUESNE LIGHT COMPANY'S GENERATION AUCTION PLAN

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Kandace F. Melillo
Prosecutor
Office of Trial Staff

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Pennsylvania Public Utility Commission
P.O. Box 3265
Harrisburg, PA 17105-3265
(717) 787-1976

Dated: November 9, 1998

I. INTRODUCTION

On May 29, 1998, the Pennsylvania Public Utility Commission entered an Order in the Duquesne Light Company (Duquesne) electric restructuring proceeding which established various requirements to be followed by Duquense in divesting its generation assets. See, Application of Duquesne Light Company for Approval of its Restructuring Plan Under Section 2806 of the Public Utility Code (Restructuring Order), Docket No. R-00974104, Order entered May 29, 1998, pp. 80-81. Specifically, Duquesne was directed to file a divestiture plan within 90 days which addressed, inter alia, (1) treatment of Duquesne's minority shares in nuclear and fossil units; (2) provision for fulfillment of Duquesne's provider of last resort (POLR) responsibility; (3) full disclosure of operational criteria necessary for maintenance of service reliability; (4) detail on environmental obligations; and (5) a resolution of transitional issues that is fair to customer, investors, Company employees, local communities, and other affected parties.

On August 27, 1998, Duquesne filed its Generation Auction Plan (the "Auction Plan"), pursuant to the Commission's May 29 Restructuring Order. Subsequently, on October 14, 1998, Duquesne submitted a non-binding Agreement in Principle ("Agreement") which provided for a generation swap with FirstEnergy Corp. to address Duquesne's minority ownership situation. Under the Agreement with FirstEnergy, Duquesne will transfer to FirstEnergy its partial ownership interest in three nuclear and five fossil generating units, while FirstEnergy will transfer to Duquesne its ownership interest in three fossil generating stations.

Under the May 29 Restructuring Order, interested parties were given 60 days to file comments to the Auction Plan, or until either October 27 or October 30 (depending upon the method of service upon the party). However, by Secretarial Letter, the comment period was extended until November 6, 1998, and was further extended until November 9, 1998, if additional time was needed to review supplemental data filed by Duquesne in relation to the Auction Plan. Duquesne filed supplemental information related to the generation exchange, including certain plant market value information, on October 29, 1998. Further supplemental information related to the Auction Plan, including responses to data requests, was received by Office of Trial Staff (OTS) counsel from Duquesne on November 5, 1998. Since additional time was needed to review the November 5 submission, OTS is filing the within Comments on November 9, 1998, as provided in the Secretarial Letter.

OTS is not opposed, in principle, to Duquesne's proposed Auction Plan and generation exchange. However, for the reasons set forth herein, further information and assurances should be provided by Duquesne prior to Commission approval of the proposals. This information is necessary to address the Commission's directives in the Restructuring Order, as noted above, concerning what must be included in Duquesne's auction plan. In addition, since, as noted by Duquesne, the Commission may consider market power implications in its decisions concerning the Auction Plan, Duquesne should be required to provide a market power study subsequent to completion of the generation auction.

II. COMMENTS

A. Additional Assurances Are Required To Protect Duquesne's Ratepayers In The Generation Exchange With FirstEnergy.

As stated above, Duquesne has entered *into* an Agreement for a generation exchange with FirstEnergy, to address the issue of minority ownership. One of the principle benefits of this Agreement, as expressed by Duquesne, is a financial commitment from FirstEnergy that the net proceeds from Duquesne's generation auction will be sufficient to, at a minimum, maintain the level of administratively determined stranded costs approved in the Commission's Restructuring Order. Agreement, p. 2. This financial commitment from FirstEnergy appears as the fourth term in the Agreement. However, item #14 provides that the Agreement is generally an expression of intent only and not legally binding upon the parties.

Therefore, as a condition of approval of the Auction Plan and generation exchange, the Commission should require Duquesne to obtain a legally binding financial commitment from FirstEnergy sufficient to ensure that the net proceeds from the generation auction will be sufficient, at a minimum, to maintain the level of stranded cost recovery administratively determined by the Commission in Duquesne's Restructuring Order.

Also, while a binding financial commitment from FirstEnergy would set a **ceiling** on the level of stranded cost recovery at the Commission's administratively-

determined level, the **actual** level of stranded costs to be recovered could be lower, depending upon the auction results. Since Duquesne's ratepayers will receive any **additional** value that results from Duquesne's generation sale, a cost/benefit analysis needs to be performed to compare values for the assets traded with values for the assets to be obtained in exchange. Duquesne has supplied some cost/benefit data in its October 29 submission to the Commission, and this information needs to be incorporated into the Auction Plan as support for the generation exchange. However, further detail may be required regarding the stranded cost levels which could result from the generation exchange, as compared to stranded cost levels associated with auction of Duquesne's existing generation assets.

B. Duquesne's November 5 Proposal To Auction The POLR Service Should Be Incorporated Within Duquesne's Auction Plan And Supplemented With Information Demonstrating Why This Proposal Is Beneficial To Ratepayers.

Under the Customer Choice Act, 66 Pa. C.S. §2801 et seq., Duquesne generally must continue to serve as provider of last resort (POLR), as long as it is collecting a CTC. See, 66 Pa. C.S. §2807(e). Also, a Duquesne retail customer has an ongoing right to take bundled service at the rate cap level, even if the customer initially elected to be served by another supplier. Auction Plan, p. 24.

In its August 27 Auction Plan, Duquesne set forth three basic options available to it for reliably meeting its price cap obligation to serve following the auction of its generating assets. First, Duquesne proposed to bundle transition power

contracts with some or all of its generation assets to provide a contractual source of capacity and energy during the rate cap period. Second, Duquesne proposed to auction the POLR service. Third, Duquesne proposed that it could contract for power in the wholesale power markets to provide this service. Auction Plan, pp. 24-25. Duquesne did not definitively choose any of these options in its initial Auction Plan.

Subsequently, on November 5, 1998, Duquesne submitted supplemental information which indicated Duquesne's intention to market the POLR service using the shopping credits set forth in its Third Compliance Filing. Duquesne requests that the Commission agree not to change these shopping credits in the future so as to enhance the value of POLR service in an auction.

In OTS' view, Duquesne has not yet adequately supported its choice to auction the POLR service. Duquesne should refile or supplement its Auction Plan to include its selection of a POLR auction and a detailed analysis showing why this choice is beneficial to ratepayers, and why it should be selected over other options. In addition, Duquesne should address whether the successful POLR bidder would be permitted a true-up of its costs.

C. In Addressing System Reliability Post Divestiture, Duquesne Should Consider Whether Additional Protections Are Required To Protect Duquesne's T&D Ratepayers From Excessive Costs.

The Commission's Restructuring Order directed that Duquesne's Auction Plan address operational criteria essential for the continued reliability of service in Duquesne's service territory. Restructuring Order, p. 80. Accordingly, in its Auction

Plan, Duquesne revealed that its Cheswick and Elrama plants must be operating in order for the system to withstand a single generation or transmission contingency during peak load times. To accommodate this constraint, Duquesne indicated that it will impose certain operating restrictions on the new owners of Cheswick and Elrama in operating agreements that permit Duquesne to call on the new owners to operate each plant at a minimum output level (or greater) during certain hours of peak load. These new owners are then to be reimbursed for the amount by which their costs to generate at the levels required in the operating agreements exceed the market price for the energy produced. Auction Plan, pp. 33-34.

Further detail is needed concerning these "must run" agreements to ascertain whether additional protection is needed for Duquesne's ratepayers. For example, the Auction Plan contains no limitation on the level of costs to be reimbursed to the new owners of Cheswick and Elrama. If the difference between the new owners' purported costs of generation and market price is to be recovered from Duquesne's T&D customers (as, e.g., a system reliability cost), there should limitations on these costs (such as a "rule of reasonableness") written into the operation agreements to protect ratepayers.

D. Further Detail In The Auction Plan Is Required Concerning Environmental Remediation And Nuclear Plant Decommissioning.

The Commission's Restructuring Order requires that Duquesne's Auction Plan disclose environmental obligations and enforcement agreements entered into by

Duquesne and should detail the handling of current trust funds associated with environmental liabilities. Restructuring Order, p. 81.

In OTS' view, the current Auction Plan does **not** contain sufficient information to satisfy the Commission's directive concerning environmental obligations. OTS asked Duquesne in a data request to provide more detail on the entity responsible for environmental remediation after the asset exchange. Duquesne's response follows:

> The specific allocation of liabilities regarding environmental matters will be set forth in the definitive agreements for the generation exchange and the auction of the fossil assets. It is Duquesne's expectation, however, that, consistent with recent auctions, the purchaser of generating assets . . . assumes most environmental liabilities associated with the plant site.

This response reveals the current uncertainty with respect to responsibility for environmental remediation. These responsibilities need to be clearly set forth, at this time, so that they may be considered by the Commission in its deliberations on the Auction Plan.

OTS also asked Duquesne for information on ownership and responsibility for disposal of the spent nuclear fuel rods at Beaver Valley and Perry after the asset exchange with FirstEnergy. While Duquesne clarified that FirstEnergy would have this responsibility, this information is not definitively contained in either

the Auction Plan or Agreement with FirstEnergy. These documents need to be amended to clearly reflect this obligation.

In addition, while Duquesne confirmed in another data request response that the existing nuclear decommissioning funds and the additional funding approved by the Commission in the Restructuring Order will be transferred to FirstEnergy, this information again was not set forth in the Auction Plan and asset exchange Agreement. Duquesne's amended Auction Plan and final Agreement with FirstEnergy should set forth this arrangement.

E. Duquesne's Auction Plan, As Supplemented On November 5, Fails To Satisfy The Commission's Directive That Transitional Issues Be Resolved In A Manner That Is Fair To Duquesne's Employees, Local Communities, And Other Affected Parties.

The Commission's Restructuring Order **directs** Duquesne to set forth, in its Auction Plan, a **resolution** of transitional issues in a manner that is fair to employees, local communities, and other affected parties. Restructuring Order, p. 81.

In its August 27 Auction Plan, Duquesne stated that it is currently developing procedures for transferring non-union employees and is in ongoing negotiations concerning the effects of the divestiture on union employees. Auction Plan, pp. 34-35. The October 14 Agreement with FirstEnergy simply states that future definitive agreements will set forth the rights and obligations of the parties regarding labor-related matters.

On November 5, 1998, Duquesne filed additional information concerning the effect of the divestiture on employees. For non-union employees, Duquesne submitted an enhanced severance, early retirement, retraining and outplacement services package. For union employees, Duquesne indicated that negotiations for additional benefits and protections, over and above that provided in the current contract for divestiture, have not been successful. Therefore, Duquesne is reverting to the existing contract as its "resolution" of labor-related matters. It is OTS' understanding that the current contract permits Union workforce reductions. Duquesne has not provided any assessment of the impacts of these potential workforce reductions on the local communities.

In OTS' view, Duquesne has not satisfied the Commission's directive to **resolve** labor-related transitional issues with fairness to the employees and the local communities. This should be done prior to Commission approval of Duquesne's Auction Plan.

F. Duquesne Should Be Directed To Provide A Market Power Study To The Commission At The Conclusion Of The Generation Auction.

As indicated by Duquesne in its August 27 Auction Plan, there are several scenarios under which market power concerns may be relevant to a generation auction. The Commission must approve the disposition of Duquesne's plants and may consider market power implications in its decision. Auction Plan, pp. 11-12.

In recognition of the market power implications, Duquesne states that it will request that each bidder that owns substantial assets in the market area (ECAR) submit an analysis of the degree to which its planned acquisition would impact wholesale or retail power markets. Also, Duquesne will request that the purchaser utilize the FERC's Merger Guidelines as a guide in analyzing such effects. Duquesne will then consider this market power analysis in determining whether to place any limitations on the bidders. Auction Plan, p. 12.

In addition to the foregoing, Duquesne should be required to perform a market power analysis at the conclusion of the auction and to submit this study to the Commission. This market power study should utilize the FERC's Merger Guidelines in analyzing market power effects.

III. CONCLUSION

In conclusion, as conditions for approval of the Auction Plan and generation exchange, the Commission should direct Duquesne to do the following:

1. Obtain a legally binding financial commitment from FirstEnergy sufficient to ensure that the net proceeds from the generation auction will, at a minimum, maintain the level of stranded cost recovery administratively determined by the Commission in Duquesne's Restructuring Order;

2. Incorporate the October 29 cost/benefit information into the Auction Plan as support for the generation exchange and provide further detail regarding the stranded cost levels which could result from the generation

exchange, as compared to stranded cost levels associated with auction of Duquesne's existing generation assets;

3. Refile or supplement its Auction Plan to include the selection of a POLR auction to fulfill POLR obligations, along with a detailed analysis showing why this choice is beneficial to ratepayers, and why it should be selected over other options. In addition, Duquesne should address whether the successful POLR bidder would be permitted a true-up of its costs;

4. Provide further detail concerning "must run" operational agreements for Elrama and Cheswick to ascertain whether additional protection is needed to avoid ratepayer responsibility for unreasonable costs;

5. Provide further detail in the Auction Plan and Agreement with FirstEnergy, as indicated herein, on environmental and decommissioning obligations;

6. Resolve labor-related transitional issues in a manner that is fair to employees and the local communities, and set forth that arrangement in the Auction Plan and Agreement with FirstEnergy; and,

7. Provide a market power analysis to the Commission at the conclusion of the generation auction, which utilizes FERC Merger Guidelines in analyzing market power effects.

Respectfully submitted,

Kandace F. Melillo

Kandace F. Melillo
Prosecutor

Office of Trial Staff
Pa. Public Utility Commission

P.O. Box 3265
Harrisburg, PA 17105-3265
(717) 787-1976

Dated: November 9, 1998

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Pennsylvania Public Utility Commission	:	
v.	:	**Docket No. R-00974104**
Duquesne Light Company	:	

CERTIFICATE OF SERVICE

I hereby certify that I am serving the foregoing, the **Comments of the Office of Trial Staff on Duquesne Light Company's Generation Auction Plan** dated November 9, 1998, either personally, by first class mail, express mail or by fax upon the persons addressed below:

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Kandace F. Melillo

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Dated: November 9, 1998
R-00974104

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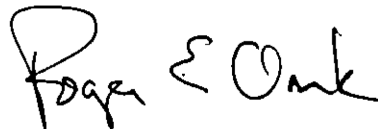
Re: Duquesne Light Company Application to Approve Restructuring Plan, Docket No. R-00974104

Dear Mr. McNulty:

Enclosed for filing please find an original and ten copies of the Comments of the Environmentalists on Duquesne Light Company's Generation Auction Plan in the above-referenced proceeding.

A copy of this document has been served on all parties of record as shown on the attached certificate of service.

Sincerely,



Roger E. Clark
Attorney for the Environmentalists

Copies: All parties of record
Honorable John Quain
Honorable Robert Bloom
Honorable David Rolka
Honorable Nora Mead Brownell
Honorable Aaron Wilson, Jr.
Office of Special Assistants

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

DOCKETED
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COMMENTS OF THE ENVIRONMENTALISTS
ON DUQUESNE LIGHT COMPANY'S GENERATION AUCTION PLAN

The Environmentalists have reviewed the Generation Auction Plan dated August 297, 1998 and the Generation Exchange Agreement in Principle dated October 14, 1998 and several supplemental filings made since then and offer these comments. Many of these comments consist of questions whose answers are not found in the auction plan. The Environmentalists assert that the Commission needs to find satisfactory answers to these questions before approving this auction.

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INTRODUCTORY COMMENTS

Comment 1: **Commission action on these proposals is premature because Duquesne has submitted an incomplete and tentative plan which must be revised in the future.**

The Environmentalists have filed a Motion to Suspend which addresses this issue. Those arguments are incorporated here by reference. The agreement in principle for the generation exchange is an "expression of interest only" which does not create "any legally binding obligation upon the Parties." [Agreement, ¶ 14]. In our

Motion, we argued that, since more agreement terms will be added by Duquesne[1] and each term now included is subject to change, there is literally nothing we can comment on in final form. As such, our comments should be seen as preliminary, like the document we have been provided.

Moreover, Duquesne's representatives have made many assurances about the plan in the form of work papers, interrogatory responses and oral comments. The Commission needs to be certain that its order in this matter captures all of these assurances and provisions.

Comment 2: Duquesne's plan for a capacity swap and then an auction actually constitutes two distinct parts that must be handled sequentially, but the first part contains several inherent delays that inhibit the evaluation of the second part.

The plan Duquesne has advanced has two distinct parts that must be handled sequentially. First, under the CAPCO agreements, Duquesne was required to receive approval of the other joint owners of the CAPCO units before it could auction the units off as part of its capacity. Duquesne is presently in federal court in Ohio seeking a ruling that would allow it to auction its share of the CAPCO units without interference

[1] In its Answer to our Motion, Duquesne claims it is uncertain whether there will be any significant changes to current documents (Answer, p.2). We note, however, that paragraph 14 of the filed document says "the terms set forth in this agreement in principle do not constitute *all* of the major terms which will be included in the Exchange Agreements". It does not say *may not include*, it says *do not include*, without qualification. That same paragraph also says that all terms included so far "are subject to further discussion, negotiation, and due diligence".

from other joint owners.[2] Duquesne sought a similar ruling from FERC, but was denied by a FERC Order, dated September 24. Having been stymied in getting the approval it sought in either forum, Duquesne now proposes to swap its shares in CAPCO units for some generating units with First Energy. Then it will proceed to step two and auction the units it gets from First Energy, together with the ones it retains. Evaluation of the auction, however, must await the completion of the swap.

But the swap it now proposes faces several kinds of delays. As we asserted in our Motion to Temporarily Suspend, the swap is jurisdictional to FERC because Duquesne is selling transmission to First Energy as part of the deal and the CAPCO Transmission Facilities Agreement will be modified. The swap cannot be finalized until FERC approves it. In our Motion, we asserted that Duquesne must wait for a final, legally binding agreement before filing it at FERC because FERC will not consider anything less (as the Commission should not).

Duquesne's Answer offered no rebuttal on either point we made about FERC jurisdiction. But even if the Commission approved the swap and auction by mid-December, Duquesne's hands will be tied until FERC completes its review.

Second, the Ohio Public Service Commission must also review the swap. Duquesne has offered no assurances that the Ohio commission will review the transaction on the basis of these preliminary agreements.

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[2]Case No. 1:95 CV 3207, U.S. District Court, Northern District of Ohio Eastern Division. See Comments of First Energy Corp., this docket, filed November 5.

Third, litigation involving Duquesne's right to dispose of its generators is proceeding in two forums. Allegheny Energy has asked the federal district court to rule that Duquesne may not terminate the proposed merger between them for the reasons Duquesne has so far given. In its Answer to our Motion, Duquesne points out that the court has denied Allegheny's motion for a temporary restraining order and its request for a preliminary injunction against Duquesne (Answer, p. 4). What Allegheny does not tell the Commission is that the court has reached no decision on the merits of Allegheny's claims and additional hearings are scheduled. In earlier hearings, Duquesne had offered that "First Energy is unlikely to continue to negotiate a definitive agreement for the power plant swap if the deal is going to be subject to the uncertainty of Allegheny Energy's approval and possible court action." The court action about the merger continues and so does the uncertainty.

Also, Duquesne's dispute about certain CAPCO capacity remains in Ohio federal court. When finalized, the swap is intended to resolve those issues. But nothing is certain. It depends on the specifics of the final agreement between Duquesne and First Energy. As First Energy states in its Comments (p. 2), "These issues *may* be entirely obviated upon the consummation of the recently announced exchange of generating units between Duquesne and First Energy." *(emphasis added)*

Comment 3: The generation swap transforms the auction from a market-based valuation of the generation assets to a process which merely ratifies the administratively-determined value of the generation assets.

Throughout this proceeding, the Environmentalists have taken the position that a market-based valuation of generation assets was preferable to an administratively-determined valuation. The use of the administratively-determined value was seen as a temporary necessity because the auction process would take some time to complete.

In response to the parties' questions about the relative value of the two sets of generation assets being exchanged, Duquesne has told us not to worry because First Energy guarantees that "the net proceeds from the DLC Auction will be sufficient, at a minimum, to maintain or reduce the level of stranded cost recovery approved by the PaPUC in its May 29, 1998 restructuring order." [Agreement, ¶4, page 2]. There is no way, they say, that ratepayers will be worse off than they are under the order. First Energy will guarantee that the net proceeds of the auction will not fall below $110 million, the figure assigned in the restructuring order as the market value of Duquesne's generation assets.

This argument is evidence that Duquesne's thinking about the auction has shifted from a true market-based approach to determine the market value of Duquesne's generation units to an exercise whose success is measured by its ratification of the administratively-determined value. The Commission should instead focus on whether Duquesne is doing all that it can to get full value for its plants.

Comment 4: First Energy's willingness to guarantee a net plant value of at least $110 million, despite all of the risk and uncertainty in the transaction, indicates that the administratively-determined generation asset value significantly underestimates the value of these assets.

The Environmentalists cannot help but think that the administratively-determined value of Duquesne's generation assets of $110 million was dreadfully low. How else to explain the willingness of First Energy to guarantee this level of net proceeds despite the risk and uncertainty (nuclear decommissioning, labor costs, Beaver Valley 2 lease costs, transaction costs, etc.) of the swap and auction? This guarantee should prompt the Commission to be especially vigilant in using the auction to obtain maximum value for the ratepayers and not be content with simply achieving the administratively-determined market value.

THE GENERATION AUCTION PLAN

Comment 5: The Commission should have oversight of the auction.

It is critical that the Commission clearly delineate the review it will make of the auction and its results. Duquesne proposes no Commission oversight of the conduct of the auction. [Auction Plan , p. 5]. This carte blanche for Duquesne should be rejected, especially given the large number of matters which are subject to Duquesne's discretion. The auction will be the methodology for quantifying the stranded costs and it should be subject to the same oversight as the administrative determination of stranded

costs. Duquesne asserts it wants an auction that best maximizes the value of Duquesne's assets, but it is important to note that Duquesne is indifferent as to the results of the auction. A high sales price means nothing because the dollars go to the ratepayers and net proceeds below $110 million do not matter because the shortfall will be made up by First Energy . The Commission therefore must be vigilant to protect the interests of the ratepayers and assure that the auction results in the maximum value for the generation assets. This can only be done by a thorough Commission review of the auction procedures to encourage the maximum number of bid and the highest bid prices and careful oversight of Duquesne's decisionmaking in the auction process.

Comment 6: The plan contains inadequate guidance about asset bundling.

Duquesne acknowledges that bundling of plants may be an important strategy to maximize the value of the generation assets and it has a good two-step process which will allow it to determine which asset bundles make good sense. However, the decisions about bundling are left solely to Duquesne. [Auction Plan , p. 10]. The Environmentalists suggest that Duquesne should confer with the Commission after the first round of bidding to present its plan for the second round and to receive some Commission input about the strategy for moving forward.

Comment 7: The plan does not require alternative strategies if plants are not sold in the auction.

The Auction Plan states that plants which are not sold in the initial auction are deemed to have a value of $0. [Auction Plan , Appendix G, p. 1, footnote 1]. Are those plants given away or do they remain with Duquesne? Will the Commission look at Duquesne's grouping of the plants to determine if another grouping would have avoided this result? Will the Commission order Duquesne to try again to sell? What if Duquesne later sells a plant? These are all questions which the Commission needs to have answered in its ruling on the auction.

Comment 8: The Provider of Last Resort proposal is incomplete.

Duquesne is now offering to auction off the Provider of Last Resort ("PLR") service. [Supplemental Filing of November 5, 1998, pages 3-4]. The winning provider would supply wholesale power to Duquesne at the shopping credit rates contained in the compliance filing. The Environmentalists accept this strategy, but we are concerned that the first couple of years will be very problematic for a PLR auction. Until some data is collected about how many customers are shopping, Duquesne will likely have to pay a premium for the risk and uncertainty of the size of PLR service. The Commission should consider a requirement in the sale of Duquesne's generation assets that these plants provide some PLR service for the first two years until the market works smoothly.

Comment 9: The plan wrongly requires ratepayers pay all of the costs of the auction and the swap.

The Auction Plan requires all transaction costs to be born by the ratepayers. [Auction Plan, Part VII, page 35]. The Environmentalists suggest that the treatment of transaction costs should reflect the value of these actions to the shareholders. Duquesne chose to proceed with the generation auction for a whole host of reasons, not the least of which was the self-interest of the company and its shareholders. Duquesne has stated that the proposed generation swap would relieve Duquesne of the cost of litigation and other actions to obtain legal authority to sell the assets it jointly owns with CAPCO. The Commission should allocate much of the transaction cost to the shareholders.

Comment 10: The plan fails to adequately address employee impacts.

Duquesne's presentation on employee impacts is divided into non-union and union. The action taken for non-union employees is an early retirement program for management employees at least 55 years old with at least 10 years service. [see Attachment A in the company's November 5 fax of supplemental information]. Neither the Auction Plan nor the supplemental filings provide any data about the number of non-union employees who are eligible for and likely to take this option and the number of non-union employees who will be able to continue their employment.

For union employees, Duquesne has submitted its expired and rejected offer to the IBEW. There is no analysis of future employment, the number of lay-offs, the new wages or other critical data.

The Commission needs much more data about employee impacts before it can approve the Auction Plan.

Comment 11: The plan fails to adequately address community impacts.

The Auction Plan is silent on the issues of its impacts on local communities. The Plan's section of Impact on Employees and Communities [pages 34-35] addresses only employee impacts. The Auction Plan is silent about a host of potential community impacts such as tax revenues, local community support, local control, safety, and indirect community employment impacts. The slew of intervention requests from local elected officials is an indication that these issues are real and important to the affected communities. The Commission needs much more information about these issues before it can approve the Auction Plan.

Comment 12: The bidder confidentiality agreement will discourage bidder participation in the auction.

Appendix C of the Auction Plan is a draft confidentiality agreement which interested buyers must sign to participate in the auction. The appendix requires interested buyer to agree not to challenge the auction results, not to disclose any

information about the auction for three years, to agree that Duquesne is entitled to equitable relief and attorneys fees in any action to enforce the agreement, etc. These provisions tend to discourage participation in the bidding and also tend to hold down the bid prices. Only the truly-necessary provisions should be permitted.

Comment 13: Duquesne's claim of the right to call on Buyer's assets to provide ancillary services will reduce the value of the generation assets.

In § 3.18 of Appendix E of the Auction Plan, Duquesne reserves the right to call on the Buyers assets to provide Duquesne with ancillary services in the future. Is this claim on the buyers' assets appropriate? This reservation is likely to decrease the market value of the generation assets. Is that decrease reasonable?

Comments 14: The accumulated SO_2 allowances should be retired.

The Auction Plan states that the Cheswick station has accumulated approximately 12,000 tons SO_2 of allowances which will be assigned to the new owner of the facility. [Auction Plan , p. 22]. The Environmentalists would like to see the Commission require Duquesne to retire these allowances, thus preventing the future release of 12,000 tons of SO_2 into Pennsylvania's environment. This would be a significant step in reducing pollution.

If the allowances are not retired, the Environmentalists suggest that they be auctioned separately and not as part of the Cheswick plant. There is a healthy market for SO_2 allowances and they will likely fetch a better price if they are auctioned to a broader market of companies needing SO_2 allowances but not necessarily in purchasing the Cheswick station.

On this same topic, will Duquesne acquire any SO_2 allowances from the First Energy coal units?

THE GENERATION EXCHANGE

Comment 15: Are the two sets of plants of comparable value?

In order for the Commission to approve the swap, it must determine that the generation assets which Duquesne obtains in the swap are no less valuable than the generation and transmission assets it is giving to First Energy. It is not enough to say that First Energy has guaranteed that the auction will produce net proceeds of at least $110 million.

Several parties have asked, and Duquesne has attempted to provide data, about the book value of each set of plants, the expected market value of each set of plants, the respective costs of environmental compliance and life extensions, etc. The Commission needs to address this data very carefully to determine that the generation assets which Duquesne obtains in the swap are no less valuable than the generation

assets it is giving to First Energy. In particular, the Commission must consider the extra value Duquesne is giving to First Energy for the transmission capacity.

Comment 16: What will be the responsibility for nuclear decommissioning costs?

Paragraph 5 of the Agreement addresses nuclear decommissioning costs. According to Duquesne, their intent is to negotiate an agreement with First Energy whereby Duquesne will be responsible for coming up with a figure for the nuclear decommissioning exposure to date and First Energy will be responsible for handling all decommissioning costs which accumulate and arise in the future. This is similar to the decommissioning provisions made by GPU in the sale of Three Mile Island.

The Commission must protect the ratepayers by assuring that the nuclear decommissioning provision is clear and tight. The exposure of Duquesne's ratepayers must be capped.

Comment 17: The exclusion of transmission capacity for the First Energy plants reduces their market value.

The First Energy plants in Ohio will have no transmission capacity guaranteed to make certain the power can reliably and economically be transmitted to the Duquesne service territory or anywhere the buyer wishes to reach customers. This will reduce

their market value, since the new operators will have to acquire (and pay for) transmission capacity to get the power to customers in the Duquesne service territory. Morever, any buyer interested in bundling the First Energy and the Duquesne plants will have to separately contract for transmission access from both companies to sell the power in the Duquesne service territory.

Comment 18: The exclusion of transmission capacity for the First Energy plants will likely limit their ability to serve customers in the Duquesne service territory.

As noted in the previous comment, the First Energy plants in Ohio will have no capacity guaranteed to make certain the power can reliably and economically be transmitted to the Duquesne service territory. What will be the effect of this on customers in the Duquesne service territory? Will the power from these plants be offered at competitive prices in the Duquesne service territory, or will the cost of the transmission capacity discourage the power's sale in Pennsylvania?

Comment 19: Does the transfer of transmission to First Energy exacerbate transmission access problems for customers in the Duquesne service territory?

In the generation swap, First Energy insisted that the Duquesne plants it acquires under the agreement be accompanied by transmission lines so that its ability to transmit the power to Ohio is guaranteed. [Agreement, ¶ 10]. The Commission

needs to understand what impact will this have on the remainder of the transmission system in the Duquesne service territory.

CONCLUSION

Duquesne will be submitting additional proposals, agreements and documents for comment. Because the issues in this matter are so interrelated, a future filing may change our position on an unchanged issue. We encourage the Commission to grant wide latitude in future comments on the generation swap, the auction plan and any other new elements of this matter.

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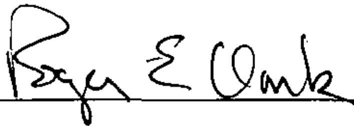
Respectfully submitted,

The Environmentalists
by:



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Date: November 9, 1998

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 Comments of the Environmentalists on Duquesne Light Company's Generation Auction Plan in the above-referenced docket upon the following persons, in the manner specified and on the dates indicated:

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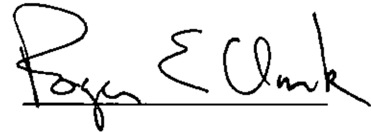

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DOCUMENT FOLDER

RE: Pennsylvania Public Utility Commission v. Duquesne Light Company; Docket No. R-00974104: Generation Auction Plan

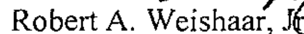
Dear Secretary McNulty:

Enclosed for filing are the original and nine (9) copies of the Comments of Duquesne Industrial Intervenors on the Generation Auction Plan of Duquesne Light Company.

As evidenced by the attached certificate of service, all parties to this proceeding have been duly served. Please date stamp the extra copy of this transmittal letter and return it for our filing purposes.

Very truly yours,

McNEES, WALLACE & NURICK



By Robert A. Weishaar, Jr.

Counsel to Duquesne Industrial Intervenors

RAW:mas
Enclosures

c: Certificate of Service

ORIGINAL

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

PENNSYLVANIA PUBLIC UTILITY COMMISSION, ET. AL. :

v. :

DUQUESNE LIGHT COMPANY : DOCKET NO. R-00974104

APPLICATION FOR APPROVAL OF ITS RESTRUCTURING PLAN UNDER SECTION 2806 OF THE PUBLIC UTILITY CODE :

COMMENTS OF DUQUESNE INDUSTRIAL INTERVENORS ON THE GENERATION AUCTION PLAN OF DUQUESNE LIGHT COMPANY

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BOC Gases
J&L Specialty Steel, Inc
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Nova Chemicals, Inc.
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I. INTRODUCTION

By Opinion and Order entered in this proceeding on May 29, 1998, the Pennsylvania Public Utility Commission ("PUC" or "Commission") accepted the rejoinder offer of Duquesne Light Company ("DLC," "Duquesne," or "Company") to divest its generation assets. See Pennsylvania Public Utility Commission v. Duquesne Light Company, Docket No. R-00974104, Opinion and Order entered May 29, 1998 ("Final Order"). In accordance with the timeline established in the Commission's Final Order, Duquesne submitted its Generation Auction Plan ("Plan") on August 27, 1998. On October 14, 1998, Duquesne filed a description of, and an agreement in principle for, a proposed "capacity swap" with FirstEnergy Corp. ("FirstEnergy").

The Final Order directs that interested parties may file comments on the Plan within 60 days of the filing thereof. Pursuant to that directive, as modified by Secretarial Letter issued October 27, 1998, the Duquesne Industrial Intervenors ("DII"), an active participant in this proceeding, provide these Comments on Duquesne's Plan and the proposed capacity swap.

DII's Comments are limited primarily to ensuring that actual divestiture results are properly calculated and reconciled with correct Commission-determined stranded cost levels. DII encourages prompt Commission approval of the divestiture process included in the Plan, but recommends that the Commission withhold final approval of the Accounting Protocols in the Plan until a subsequent, stranded cost true-up proceeding. Accordingly, DII's Comments address only the more egregious components of the Accounting Protocols (e.g., FAS 109 and deferred fuel regulatory asset). Finally, DII hereby reserves further comments on the FirstEnergy capacity swap.

II. COMMENTS

A. The Company's FAS 109 Regulatory Asset Must Be Eliminated Because Net Divestiture Proceeds Are Calculated On An After-Tax Bases.

Duquesne proposes to use "After-tax Auction Proceeds" as the basis for adjusting Commission-determined stranded cost levels following generation divestiture. See Plan, Appendix G, p. 8. Duquesne defines "After-tax Auction Proceeds" as "Net Auction Proceeds less current taxes payable," which include all applicable gross receipts, excess dividends, property transfer, sales, and federal and state income taxes. See Plan, Appendix, G, p. 4. Calculating net divestiture proceeds on an after-tax basis, as compared to a pre-tax basis, reduces the potential offset to stranded costs by the amount of income taxes paid to the state and federal government.

Despite proposing to calculate divestiture proceeds on an after-tax basis (and thus reducing the stranded cost offset), Duquesne retains a FAS 109 regulatory asset of $179 million and associated deferred taxes of $57.48 million in its stranded cost totals. See Plan, Appendix G, p. 2a. Duquesne's Accounting Protocols include no adjustment to the FAS 109 regulatory asset, but do clearly indicate that divestiture proceeds will be calculated on an after-tax basis.

Duquesne's Accounting Protocols are inherently incongruous in this regard. Under Generally Accepted Accounting Principles and fundamental notions of equity, Duquesne cannot reduce net divestiture proceeds to reflect income taxes payable and maintain a stranded FAS 109 regulatory asset to cover future income taxes payable. Either Duquesne pays income taxes at the time of divestiture (in which case divestiture proceeds are properly shown on an after-tax basis and the FAS 109 regulatory asset is eliminated from stranded costs) or Duquesne does not reflect income taxes payable at the time of divestiture (in which case divestiture proceeds are shown on

a pre-tax basis and the FAS 109 regulatory asset remains). Calculating divestiture proceeds on an after-tax basis and retaining the FAS 109 regulatory asset effectively charges ratepayers twice for income taxes that Duquesne will pay only once. Given Duquesne's intention to calculate proceeds on an after-tax basis (to which DII does not object), Duquesne must be required to eliminate its FAS 109 regulatory asset of $179 million and associated deferred taxes of $57.48 million. See Plan, Appendix G, p. 2a.

As explained in the Affidavit of Lane Kollen, which is attached to these Comments, the FAS 109 regulatory asset represents the revenue requirement effect of deferred taxes that have not yet been collected from customers due to book/tax basis differences and the previous flow-through of tax benefits. Calculating divestiture proceeds on an after-tax basis reduces the amount of proceeds that can be used to offset stranded costs, which essentially charges ratepayers for income taxes at the time of closing on the asset sale. Calculation of net divestiture proceeds on an after-tax basis provides Duquesne full recovery of its past, present, and future income taxes on those generation assets at the time of sale. Because treatment of net divestiture proceeds on an after-tax basis provides Duquesne full recovery of all income taxes payable on those generation assets, Duquesne has no entitlement to a FAS 109 regulatory asset that is fundamentally premised upon future income tax payments.

Accordingly, the FAS 109 regulatory asset of $179 million and related deferred income taxes of $57.48 million must be removed from Duquesne's stranded cost totals reflected on Appendix G, p. 2a, if Duquesne calculates net divestiture proceeds on an after-tax basis, as

proposed.[1]

B. The Company's Claim For An Increase In Its Deferred Fuel Cost Regulatory Asset Must Be Firmly Rejected.

In Appendix G to its Divestiture Plan, Duquesne includes one sentence to purportedly justify a significant increase in Duquesne's deferred fuel cost regulatory asset. Duquesne states:

> [P]ursuant to the Compliance Order[,] the Deferred Fuel Cost Regulatory Asset should be shown at its updated value of $25.00 million because Duquesne has been denied a roll-in of its ECR at the higher value reflected in the original compliance filing.

See Plan, Appendix G, p. 6. Duquesne provides a no basis for its proposed $18.27 million dollar increase in its deferred fuel regulatory asset (from $6.73 million to $25.00 million) and an associated deferred tax increase of $12.95 (from $4.78 million to $17.73 million). Compare Plan, Appendix, G, p. 2a with Plan, Appendix G, p. 4b. Duquesne's unsupported adjustment increases Duquesne's deferred fuel regulatory asset and associated deferred tax by a total of $31.22 million. See id.

Duquesne's adjustment to its deferred fuel regulatory asset constitutes a blatant attempt to reargue a position that the Commission previously considered twice and previously rejected twice. In its First Compliance Order, the Commission stated as follows:

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[1] In the GPU settlement, the FAS 109 regulatory asset was not eliminated from Met-Ed's and Penelec's stranded cost totals because GPU opted to calculate net divestiture proceeds on a pre-tax basis. See Joint Petition for Full Settlement of the Restructuring Plan of Metropolitan Edison Company and Pennsylvania Electric Company and Related Dockets and Related Court Proceedings, Docket Nos. R-00974008 and R-00974009, Sept. 23, 1998, pp. 12-13 and Appendix E; compare Application of Metropolitan Edison Company for Approval of Restructuring Plan Under Section 2801 of the Public Utility Code, Opinion and Order entered June 30, 1998, Attachment A. For example, Metropolitan Edison Company's stranded cost totals in the Settlement continued to include $50.48 in regulatory assets, $40.8 million of which represented a FAS 109 regulatory asset.

> OCA noted that the Company has designed its CTC to collect a higher amount of stranded cost then that reflected by the Commission in its Order. According to the OCA, the difference appears to be $18.25 million in deferred fuel costs that the Company is now including in its stranded cost calculation.
>
> The Company indicated in its filing, and in its Petition for Clarification, that it intended to include this amount pursuant to the Commission's Order regarding Duquesne's ECR roll-in, which allowed for the opportunity to update this claim.
>
> The OCA argues that the Company's base rates and ECR in effect, on the effective date of the Act, were designed to recover 12.8 mills per kWh. The OCA noted that throughout the restructuring case the Company indicated that the proposed Energy Cost Rate (ECR) was higher then the ECR that was in effect at the effective date of the Act.
>
> We will adopt the position of the OCA. Therefore, we direct Duquesne to reflect the ECR, in effect on the effective date of the Act, which is designed to recover 12.8 mills/kWh in energy costs in rate calculations.

See Application of Duquesne Light Company for Approval of Restructuring Plan under Section 2806 of the Public Utility Code, Docket No. R-00974104, Opinion and Order entered Aug. 13, 1998, pp. 11-12. As shown, the Commission expressly rejected Duquesne's proposal to recover approximately $18.25 million in deferred fuel costs that result from the differential between the ECR amount presumptively rolled into Duquesne's base rates and the ECR amount that Duquesne attempted to reflect in base rates in its initial compliance filing. Importantly, the Commission's First Compliance Order did not permit Duquesne to record as a regulatory asset the differential between its proposed ECR roll-in amount and ECR roll-in amount presumptively approved by the Commission in Duquesne's unbundled rates.

The Commission obliquely addressed this issue again in its Second Compliance Order. In that Order, the Commission directed Duquesne again to "roll its ECR into base rates at 12.8 mills/kWh," which is the ECR roll-in amount recommended by OCA exclusive of the $18.25

million in deferred fuel costs that Duquesne attempted to include in its initial compliance filing.[2]

Duquesne's attempt to increase its deferred fuel regulatory asset through an Appendix to its Generation Auction Plan represents the third time that Duquesne has attempted to make this unjustified increase in stranded costs. Duquesne's previous two attempts were firmly rejected by the Commission. The Commission must, once again, rebuff Duquesne's attempts to increase the deferred fuel regulatory asset included among Duquesne's stranded costs.

C. The Commission Should Reject An Arbitrary Assumed $0 Sales Price For Unsold Units.

In the Company's Accounting Protocols, the Company states it will assume a sales price of $0 "for any Utility Asset for which a transfer is not completed, whether because no qualifying bids where received or because conditions precedent to such a transfer were not satisfied." See Plan, Appendix, G, pp. 1-2 n.3. At a Technical Conference held on October 21, 1998, the Company explained that this provision was included in the Generation Auction Plan to address the possibility that no bids would be received for Duquesne's nuclear generating facilities. Notably, the Generation Auction Plan, including the provision assuming a $0 sales price for any unsold assets, was developed and submitted to the Commission prior to announcement of Duquesne's agreement in principle to transfer all of Duquesne's nuclear interests to FirstEnergy. As such, Duquesne's stated basis for including a $0 sales price assumption in the Generation Auction Plan no longer applies in light of the FirstEnergy transaction. Because Duquesne's rationale for including the $0 sales price provision evaporates upon completion of the

---

[2] See Application of Duquesne Light Company for approval of restructuring plan under Section 2806 of the Public Utility Code, Docket No. R-00974104 Opinion and Order entered October 16, 1998, p. 14.

FirstEnergy transaction, the provision must be removed.

Assuming a $0 market value for unsold assets undermines one of the fundamental purposes of generation divestiture, namely, to substitute actual market value for an administratively determined market value. See Final Order, p. 79. Instead of replacing actual market value for assumed market value, Duquesne's $0 sales price provision would replace an assumption with another, but less valid, assumption. Duquesne simply assumes, without more, that a plant that is not sold through the divestiture process, for whatever reason, is worth $0. Duquesne's proposal would result in an arbitrary and unsupported $0 market value replacing a Commission-determined market value that was premised upon substantial evidence in Duquesne's on-the-record restructuring proceeding. The Commission should reject Duquesne's assumption of a $0 market value for unsold plans and, instead, address this issue in further detail in the stranded cost true-up proceeding following divestiture.

Moreover, Duquesne's proposal, as stated, would permit Duquesne to game the divestiture process. Duquesne states that it will assume a $0 market value for any unsold plants, even if the plants are unsold because "conditions precedent to such a transfer were not satisfied." See Plan, Appendix G, pp. 1-2 n.3. Duquesne does not identify the universe of "conditions precedent," and fails to note that Duquesne will be the final arbiter of whether a bidder satisfies "conditions precedent." Assuming a $0 sales price for any asset with a positive Commission-determined market value would reduce the offset to stranded costs and, thus, increase Duquesne's total stranded cost recovery. Given the amount of discretion retained by Duquesne and the distinct possibility that failure to satisfy "conditions precedent" could result in an asset not being sold, Duquesne should not be permitted to assume automatically a $0 sales price for

unsold assets so as to potentially increase overall stranded cost recovery. Footnote 3 from Duquesne's Accounting Protocols must be redacted, and this issue should be addressed, if necessary, in Duquesne's stranded cost true-up proceeding.

D. The Commission Should Provide Parties The Opportunity to Address Duquesne's Accounting Protocols Further In Duquesne's Stranded Cost True-Up Proceeding.

The three DII concerns identified above in connection with Duquesne's proposed Accounting Protocols represent obvious shortcomings in Duquesne's proposal. There may be others that surface when actual divestiture results are known, the Accounting Protocols are applied to those results, and stranded costs are reconciled with actual divestiture results.[3] The Accounting Protocols, with the exception of the obvious errors discussed above, need not be resolved definitively at this time. The Commission should expressly reserve the opportunity for further comments on the Accounting Protocols, during subsequent proceedings that address stranded cost true-up, as necessary to ensure that stranded costs are accurately and fairly reconciled with actual divestiture results. Accordingly, DII requests that the Commission order the three adjustments (i.e., FAS 109, deferred fuel, and $0 sales price) discussed above and tentatively approve the remainder of the Accounting Protocols subject to additional comment when actual divestiture results are known and the Accounting Protocols are capable of actual

[3] For example, it appears that the Company failed to include as a reduction to book value (and, thus, as a further reduction to stranded costs) certain book depreciation amounts that will be paid by customers that purchase generation service from the Company between January 1, 1999 and the divestiture closing date. A correct statement of net book value on the divestiture closing date would reflect not only book depreciation recovered through the interim CTC, but also book depreciation that was included in the "non-stranded" components of rates and recovered from customers that purchase generation from the Company between January 1, 1999 and the divestiture closing date. The Accounting Protocols must be clarified, following divestiture closing, on this issue and other issues that may arise when actual divestiture results are known.

application.

E. DII Reserves Further Comment On The Proposed Capacity Swap with FirstEnergy.

DII has reviewed Duquesne's October 14, 1998 submittal outlining Duquesne's agreement in principle for a capacity swap with FirstEnergy. DII has received additional clarification and information from Duquesne in several Technical Conferences held since the October 14, 1998 submittal. Duquesne has indicated that it intends to conduct a due diligence review of the three FirstEnergy plants that will be transferred to Duquesne if the capacity swap is consummated. Duquesne intends to retain independent consultants for this purpose and complete the review over the next few weeks.

On the basis of the information in Duquesne's October 14, 1998 submittal and Duquesne's representations subsequent to that submittal, DII respectfully submits that the proposed capacity swap may be in the best interests of Duquesne ratepayers. The agreement in principle includes, inter alia, a guarantee that the capacity swap will not cause Duquesne ratepayers to pay more stranded costs than the amounts that the Commission determined for each of the assets that will be transferred. Duquesne ratepayers' liability for nuclear decommissioning will be capped at the level assumed in the Commission's Final Order. Additionally, Duquesne has represented that several investment banking firms view whole ownership in generation assets, which Duquesne would obtain through the capacity swap, as being superior to partial ownership in generation assets for purposes of generation divestiture. These investment bankers have also indicated that ownership of fossil units is superior to ownership of nuclear units for purposes of generation divestiture, given current market conditions. Consequently, if the investment bankers' perceptions are accurate, the capacity swap would enhance the attractiveness

of Duquesne's overall generation portfolio and increase net divestiture proceeds used to offset stranded costs. However, the Commission should consider the regional impact of this transaction on retail markets, particularly issues concerning transmission access coordination and pricing. DII does not have sufficient information to analyze this issue fully at this time.

DII respectfully reserves the opportunity to offer additional comments on the capacity swap if the final agreement between Duquesne and FirstEnergy differs materially from the agreement in principle, if Duquesne's due diligence review of the three plants to be acquired indicates potential problems that may detract from these plants' market value, or if further analysis indicates an adverse impact on the development of a regional retail market.

III. CONCLUSION

WHEREFORE, Duquesne Industrial Intervenors requests that the Commission:

- Permit Duquesne to proceed with its divestiture plan;
- Require, at this time, that Duquesne eliminate the SFAS 109 regulatory asset because Duquesne is stating net divestiture proceeds on an after-tax basis;
- Reject, at this time, Duquesne's attempt to increase its deferred fuel regulatory asset and associated deferred taxes by $31.12 million;
- Reject, at this time, Duquesne's assumption of $0 market value for unsold plants;
- Expressly provide parties an opportunity to address all aspects of Duquesne's Accounting Protocols further in the stranded cost true-up proceeding, when divestiture results will be known and parties are able to test the Accounting Protocols against actual divestiture results; and
- Permit Duquesne to continue pursuing a capacity swap with FirstEnergy, subject to further Commission review to protect against adverse findings in Duquesne's due diligence review, adverse provisions in the final agreement, and adverse implications for regional retail markets.

Respectfully submitted,

McNEES, WALLACE & NURICK

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Dated: November 9, 1998
A045522

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	)	

AFFIDAVIT

OF

LANE KOLLEN

J. KENNEDY AND ASSOCIATES, INC.
ATLANTA, GEORGIA

NOVEMBER 1998

AFFIDAVIT OF LANE KOLLEN

STATE OF GEORGIA
COUNTY OF FULTON

Before me, the undersigned Notary Public in and for the County of Fulton, State of Georgia, personally came and appeared Lane Kollen, who was sworn by me and attested to the following facts:

1. I am a Vice President and Principal of J. Kennedy and Associates, Inc. ("Kennedy and Associates"). Kennedy and Associates provides rate, planning, accounting, financial, and economic consulting services in the electric, gas, and telecommunications utility industries.

2. I am a Certified Public Accountant and a Certified Management Accountant. I have earned Bachelor of Business Administration (Accounting) and Master of Business Administration degrees from the University of Toledo.

3. I have been actively involved in the electric utility industry for more than twenty years as an employee of an electric utility, as a consultant to electric and gas utilities, and as a consultant to consumers of utility services and state government agencies. My specializations are accounting, tax, and finance.

4. I have testified as an expert witness in more than 100 proceedings on accounting, tax, and finance issues, including deferred taxes and regulatory assets. I have testified in seven Pennsylvania restructuring proceedings, including the Duquesne restructuring proceeding. I have testified on SFAS 109 regulatory assets in five of those Pennsylvania proceedings.

5. I have reviewed the "Generation Auction Plan of Duquesne Light Company" ("Plan") dated August 27, 1998 filed with this Commission, including all appendices. I have reviewed the Duquesne "Accounting Protocol" described in detail in Appendix G to the Plan. The Duquesne Accounting Protocol describes the computational methodologies proposed by the Company to quantify the effects of its divestiture plan on the Commission's determination of stranded costs.

6. The Company proposes a market credit and a deferred tax credit, both of which represent appropriate reductions to the Commission's determination of stranded costs and the related deferred taxes, respectively.

7. The market credit is computed as the gross sales proceeds less transaction costs less current income taxes. The deferred tax credit is computed as the market credit times the income tax rate divided by one minus the income tax rate, which the Company simplified to the market credit times .71.

8. The Company's market credit and deferred tax credit proposals fail to fully identify and quantify the effects of Duquesne's divestiture. The Company has failed to remove the SFAS 109 regulatory asset of $179.00 million and the related deferred taxes of $57.48 million from the stranded regulatory assets authorized for recovery by the Commission. These amounts are detailed in the Commission's Order and reflected on Duquesne's Appendix G page 2A.

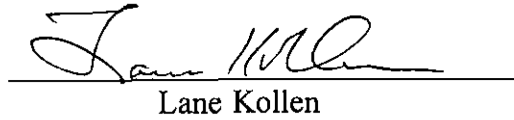
9. The SFAS 109 regulatory asset represents the revenue requirement effect of deferred taxes that have not yet been collected from customers, and which are created due to book/tax

basis differences (primarily AFUDC included in the book basis but not in the tax basis) and the previous flow through of tax benefits.

10. The Duquesne Accounting Protocol defines the computation of "net proceeds" on an after tax basis. Net proceeds, which are used to compute the market credit, are reduced for the current income tax effects of the sale proceeds. Because the net proceeds are reduced for the entire income tax effect of the sale and because Duquesne no longer will own the divested assets, there will be no longer any future tax obligation. All tax obligations will be paid fully by the Company and its customers under this formula. Thus, the SFAS 109 accumulated deferred tax liability and the SFAS 109 regulatory asset will no longer exist under Generally Accepted Accounting Principles ("GAAP").

11. At the closing date for the assets divested, the accounting entry to recognize the complete elimination of the future tax obligation in accordance with GAAP will be to debit (eliminate) the SFAS 109 deferred tax liability and to credit (eliminate) the equivalent SFAS 109 regulatory asset. These are balance sheet reversals that simply reflect the reality that there is no longer any future tax obligation of the Company or its customers related to the assets divested. There is no income statement effect and thus, no loss to the Company, just as there was no income statement effect and thus, no loss to the Company when the SFAS 109 deferred tax liability and SFAS 109 regulatory asset balances were created.

12. In addition to the market credit and the deferred tax credit described by Duquesne, the Commission should direct that additional credits be made to remove the $179.00 million SFAS 109 regulatory asset and the $57.48 million related deferred tax amounts from the total stranded costs detailed in the Commission's Order. Only in this manner will Duquesne's customers receive the proper credits to which they are entitled upon divestiture.



Lane Kollen

Sworn to and subscribed before me on this
5th day of November 1998.

Notary Public

Notary Public, Cobb County, Georgia.
My Commission Expires January 26, 2001

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 52 Pa. Code § 1.54 (relating to service by a participant).

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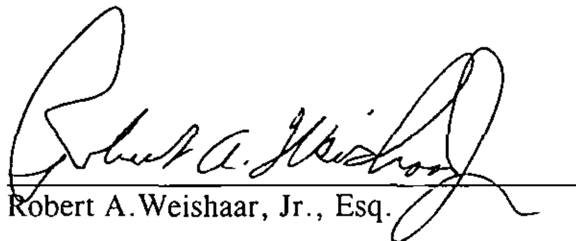

Robert A.Weishaar, Jr., Esq.

Counsel to Duquesne Industrial Intervenors

Dated this 9th day of November, 1998, in Harrisburg, Pennsylvania.

COMMONWEALTH OF PENNSYLVANIA

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ORIGINAL

November 9, 1998

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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 please find an original and (10) copies of the Office of Consumer Advocate's Comments to the Generation Auction Plan of Duquesne Light Company, in the above-captioned proceeding.

Copies of this document have been served on all parties of record as shown on the attached Certificate of Service.

Sincerely,

Tanya J. McCloskey
Assistant Consumer Advocate

Enclosure
cc: All parties of record
Office of Special Assistants
Donald H. Muth, FUS

93

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

DOCKETED
NOV 12 1998

DOCUMENT FOLDER

OFFICE OF CONSUMER ADVOCATE'S COMMENTS TO THE GENERATION AUCTION PLAN OF DUQUESNE LIGHT COMPANY

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Dated: November 9, 1998

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I. INTRODUCTION AND SUMMARY OF COMMENTS

In Duquesne's restructuring proceeding as well as the restructuring proceedings of the other Electric Distribution Companies ("EDCs") in Pennsylvania, the Office of Consumer Advocate ("OCA") has recognized that the most accurate way to measure a utility's stranded costs is for the utility to divest those assets. Although the Electricity Generation Customer Choice and Competition Act, 66 Pa.C.S. §2801 et seq. does not allow the Commission to order a divestiture of generation assets as part of a utility's restructuring plan, a voluntary divestiture of such assets is permitted under the Act. From a ratepayer perspective, the OCA supports such steps to properly value stranded cost, and to increase generation competition within the newly developing markets. Recent divestitures of generating assets have demonstrated that market values determined from sales of generating assets can differ substantially from the administrative valuations. Additionally, in most cases, the market valuations indicated by auctions of coal-fired generating plants have far exceeded the book values of the plants, thus eliminating or minimizing stranded cost. In this light, the OCA agrees that a timely and properly conducted divestiture of Duquesne's generating assets as a means of determining stranded costs should be beneficial to Duquesne's ratepayers in that it is likely to produce an appropriate valuation of stranded costs and it is likely to stimulate the competitive generation market in the Western portion of Pennsylvania.

The OCA expects that the divestiture of Duquesne's generating assets should help to boost competition in both the wholesale and retail markets in the ECAR region.[1] In this respect,

---

[1] This assumes that the assets are not sold to an entity already possessing large amounts of generation capacity in the relevant market. The OCA notes that Duquesne requires that bidders submit a market power analysis from bidders that own substantial assets in ECAR.

OCA would emphasize that together with the divestiture of GPU's generating assets in the PJM market, a divestiture of Duquesne's generating assets which resulted in a diversity of generation owners would help to discipline the generation market and reduce market power throughout Pennsylvania, providing substantial benefits to both wholesale and retail purchasers of generation.

For both of these reasons -- maximizing ratepayer value and providing a boost to competition, OCA continues to support in principle a timely and properly conducted divestiture as a means of valuing stranded costs. At this juncture, however, the OCA would note that although the OCA supports divestiture as a route to maximize ratepayer value, the OCA recognizes that a large number of interests must be recognized and balanced by the Commission. For example, the Commission must thoroughly consider environmental concerns, labor concerns, community impacts and safety issues. The OCA anticipates that other interested parties will present positions and information regarding these concerns.

If, in fact, a divestiture process is to be utilized to determine stranded cost, then it is essential that the process be conducted in a manner that maximizes the value of the assets being divested. In its initial review of Duquesne's Generation Plan, the OCA was concerned that Duquesne was attempting to auction partial ownership shares of plants, and was trying to auction nuclear plants that were encumbered with many liabilities, including an unusual sale/leaseback agreement for Beaver Valley 2. On October 14, 1998, Duquesne modified its Plan to include an exchange of generation assets with FirstEnergy. The OCA sought to determine whether this swap would improve the divestiture process.

Based on the still limited information received to date, the OCA generally expects that, from a ratepayer perspective, Duquesne's proposal of October 14, 1998, to swap certain

generating assets with FirstEnergy Corporation ("FirstEnergy") will likely improve the divestiture process.[2] Although the OCA's initial analysis raises concerns that the potential operating value of the Duquesne assets being exchanged may exceed the value of the FirstEnergy assets being received, the OCA recognizes that in the context of a divestiture proposal, the swap may in fact benefit Duquesne and its ratepayers.

As Duquesne emphasized in its correspondence of October 29, 1998 to the Commission regarding this transaction, the proposed asset swap is likely to increase the sale values realized through the divestiture by substituting Duquesne's partial, minority ownership interest in eight generating units with total capacity of approximately 1400 MW, including three nuclear units and only two units which it operates, with an undivided ownership and operational control interest in three coal-fired stations with a generating capacity of 1300 MW. At the same time, Duquesne has acquired a financial commitment from FirstEnergy to ensure that Duquesne ratepayers are protected on the downside, through FirstEnergy's commitment that the net proceeds from Duquesne's transfer of assets will be sufficient, at a minimum, to maintain or reduce the level of stranded cost recovery

---

[2] According to Duquesne, the proposed asset swap was arranged for the purpose of addressing concerns regarding the marketability of Duquesne's minority ownership of some generating assets, as set forth as follows:

> 7. The plan shall include a discussion of the treatment of shares of nuclear and fossil units for whom Duquesne is a minority owner. Specifically, the plan shall delineate Duquesne's proposed treatment of nuclear ownership shares should no bids materialize for those shares, as well as Duquesne's ability to sell its stake in Beaver Valley 2 and Perry 1 to the other owners of those units or to swap Duquesne's stake in these units with the owners for the output of other fossil units.

Opinion and Order of May 29, 1998, at 80-81.

in the Commission's administrative determination of Duquesne's stranded costs. The OCA finds this guarantee to be a key element of the proposed generation swap. Additionally, if Duquesne has successfully capped its nuclear decommissioning liability, and other potential environmental liabilities, Duquesne has achieved some additional, although unquantifiable, value in this transaction for both itself and its ratepayers.

While OCA generally agrees with Duquesne's divestiture plan and swap with FirstEnergy, OCA has specific concerns over certain aspects of each proposal, which are set forth in detail below. Furthermore, and perhaps more importantly, with respect to the Agreement in Principle with FirstEnergy, OCA would emphasize that this is not a final and definitive agreement but is subject to change. In this regard, the Agreement in Principle states:

> It is specifically agreed and understood by the Parties that the terms set forth in this agreement in principle do not constitute all of the major terms which will be included in the Exchange Agreements, that the terms set forth herein are subject to further discussion, negotiation, and due diligence, and that this agreement in principle is an expression of intent only and is not intended, nor will it be alleged by either Party, to create or result in any legally binding obligation upon the Parties, - with the sole exception being this sentence and Section 7(b) and 23.

Agreement in Principle of October 14, 1998, ¶ 14.[3] Furthermore, while the Agreement in Principle specifically requires that the parties cooperate "to resolve labor-related matters . . . in a manner that treats employees fairly and equitably apportions any related costs between the parties," it specifically

[3] OCA would note that while the Agreement in Principle is subject to change, Duquesne expects nonetheless that the Agreement in Principle will form the basis for obtaining Commission approval of the asset exchange with FirstEnergy, which it seeks by December 21, 1998. Agreement in Principle, ¶23(b).

leaves the delineation of these rights and obligations to be set forth in the definitive agreement. Agreement in Principle, ¶ 6.

Moreover, as noted above, there are important labor, environmental, community impact and safety issues that have yet to be resolved by the Generation Auction Plan and the Agreement in Principle with FirstEnergy which must be addressed before the Commission can make a final determination in a reasoned manner on these proposals. In particular, Duquesne has recently indicated that it has been unable to reach agreement with its unions regarding enhanced benefits in the context of a divestiture.

In addition, the OCA submits that Duquesne must continue to work on its plan for meeting its Provider of Last Resort obligation under the Act. In no event should the Commission allow Duquesne's divestiture of its generating assets to abrogate Duquesne's responsibility to provide generation service to customers at capped rates, pursuant to the Act. The OCA submits that Duquesne has provided a number of viable options for providing this service that should be explored during the divestiture process.

Duquesne's Generation Auction Plan provides a framework through which the Company will sell its generating assets. It addresses the administrative review process through which the Commission will evaluate the auction plan, the auction design and timetable, an overview of the significant assets and encumbrances being transferred, Duquesne's proposal with respect to Provider of Last Resort Service ("PLR"), operational issues and, in particular, the preservation of reliability, the impact on employees and communities, the accounting for auction proceeds, and the required regulatory approvals associated with the divestiture.

The OCA recognizes Duquesne's efforts to address all of these issues, its efforts to facilitate its divestiture plan, and the opportunity to resolve issues informally, through technical conferences or otherwise. As indicated above, the OCA also continues to support Duquesne's decision to divest its generation resources as the most appropriate means to determine stranded costs and to advance the competitive generation market in the Duquesne region. If indeed a divestiture is to occur, it should be conducted in a manner that maximizes the potential for a successful auction. To that end, based on the information available, the asset exchange with FirstEnergy appears to be a positive development in that it will likely improve the value to be realized from Duquesne's divestiture of its generating plants, although a final agreement detailing the terms of the exchange is not yet available. Nonetheless, as indicated above, OCA recognizes that there are important labor, environmental, community impact and safety issues pertaining to the divestiture and the asset exchange with FirstEnergy that must be addressed before these transactions should go forward.

In sum, the OCA supports in principle many aspects of Duquesne's divestiture plan, but submits that the Commission cannot give any type of final approval to this plan until a final agreement is submitted and a number of other important issues are addressed.

II. COMMENTS

A. While OCA Supports The Asset Exchange With FirstEnergy As Likely To Maximize The Value To Be Realized By Duquesne From A Divestiture, The Commission Must Await The Results Of Due Diligence And A Final Agreement Before Reaching A Final Decision With Respect To The Merits Of The Proposal.

1. Introduction

Duquesne submitted its Agreement in Principle to exchange certain generating assets with FirstEnergy on October 14, 1998. As emphasized above, this agreement is not a final and definitive agreement, leaves certain matters, in particular labor matters, undecided, is subject to "further discussion, negotiation and due diligence," and does not produce any legally binding obligation with respect to the exchange of assets. Nonetheless, Duquesne expects that this Agreement in Principle will form the basis for obtaining Commission approval of the asset exchange with FirstEnergy, which it seeks by December 21, 1998. Agreement in Principle, ¶23(b).

While the asset exchange with FirstEnergy is not final, to the extent that the Agreement in Principle reflects the material terms of the final agreement, the OCA has determined, as indicated above, that it is likely to enhance Duquesne's ability to maximize the value of the generation assets that are subject to divestiture and, therefore, that it is likely to maximize the value of the divestiture to ratepayers, subject to the resolution of important labor, environmental, and safety-related issues, and the performance of due diligence. Until these steps are completed, the Commission cannot grant final approval of the asset exchange. Furthermore, as discussed further below, the Commission should require that a report should be prepared and provided to the parties summarizing the results of due diligence and certain specific terms of the agreement may need to be clarified or modified.

2. OCA's Evaluation Of The Asset Exchange

OCA's determination that the asset exchange is likely to increase the value of the assets that are subject to the divestiture began with a comparison of the market value of the assets being exchanged. Based on FirstEnergy's analysis utilizing the market prices from the Penn Power case, it appears that the assets Duquesne is proposing to transfer to FirstEnergy might have greater operating value than the assets it would receive from FirstEnergy. The evaluation of a number of other key considerations, however, has led OCA to the conclusion that the transaction will aid in maximizing the value of the divestiture process. In this regard, OCA would emphasize that there is a different value to Duquesne's current generating assets in the context in which Duquesne continues to operate the plants versus the value of those plants in the context of a divestiture. Thus, while this exchange might not make sense if Duquesne were to stay in the generation business, it does make sense where Duquesne is attempting to maximize value from the sale of the assets.

More specifically, OCA's analysis indicates that the coal-fired generating assets which Duquesne is exchanging with FirstEnergy have similar market value and, thus, on a coal-for-coal basis, Duquesne will be in a similar position. However, while the nuclear assets that Duquesne would transfer to FirstEnergy would appear to have some market value under the Penn Power analysis and thus might appear to make this deal worse for Duquesne, other factors clearly weigh in favor of Duquesne making this transaction in order to maximize market value in the context of a sale of the assets. In particular, the substitution of partial, minority ownership interests in the plants that Duquesne is transferring to FirstEnergy with an undivided interest in the plants that FirstEnergy is transferring to Duquesne is critical to Duquesne's maximization of market value in the context of a generation auction. In this regard, it is also important to emphasize that Duquesne

has operational control of only 2 of the 8 units that it is transferring to FirstEnergy but will obtain the ability to transfer operational control of all of the FirstEnergy plants it receives as part of the swap.

In addition to general concern over the marketability of minority, non-operating, partial ownership interests in the generating plants, it is the OCA's understanding from the technical conference that the specific operating agreements with FirstEnergy may have been problematic in that they require FirstEnergy's approval of any buyer of Duquesne's interest and FirstEnergy's cooperation would be required for any bidders to conduct on-site due diligence at such plants. Additionally, the agreements give FirstEnergy the right to match the highest bidder in an auction of Duquesne's interest, which would be inconsistent with the Commission's objective of facilitating a more competitive marketplace since it would provide greater concentration of generating facilities in the ECAR market.

Finally, OCA has questions over the marketability of partial, minority ownership interest in nuclear power plants, and is concerned that the sale of partial, minority ownership interests in coal plants may be difficult to maximize.

As Duquesne indicated in the Overview of the swap agreement, which it filed with the Commission on October 29th, the swap would permit the divestiture to proceed in a timely fashion by eliminating uncertainty created by shared ownership interests and agreements. Together with the value created by sole ownership and control of the plants, it is OCA's view that the swap is likely to create greater value for Duquesne's ratepayers than would a divestiture of its partial, minority ownership share in its current plants. Furthermore, OCA recognizes that this agreement is an integrated package and that other assets cannot be substituted.

Additionally, FirstEnergy's minimum financial guarantee provides an "insurance policy" that consumers will not incur a higher level of stranded costs than the level determined by the Commission. This is an extremely important assurance in an infant marketplace for generating assets and, while it does not ensure that ratepayers are better off as a result of the asset exchange, it at least means that they won't be worse off than under the PUC's administrative determination of stranded costs, and provides an important protection from that volatility. It is also worth pointing out, as further discussed below, that the Agreement in Principle caps Duquesne's nuclear decommissioning liability at the level funded at the time of transfer.

Finally, FirstEnergy's agreement not to bid on the plants when they come up for auction helps ensure that the ECAR market will not become even more concentrated as a result of the asset swap.

3. The Commission Can Give Final Approval To The Asset Exchange Only After The Company Has Completed Due Diligence, Resolved Outstanding Labor, Environmental And Safety Issues, Signed A Definitive Agreement, And All Parties Have Had A Reasonable Opportunity To Review These Issues.

Paragraph 15 of the Agreement in Principle provides that Duquesne will have the opportunity to conduct due diligence, including evaluation of relevant books and records, financial, and operating data, and environmental audits prior to execution of a definitive agreement. The OCA submits that Duquesne remains responsible for ensuring that the value of the swap to Duquesne and its ratepayers will not be adversely affected by as yet unknown factors (*e.g.* environmental liabilities, equipment deficiencies). While the OCA expects that Duquesne's due diligence will not be as

detailed as a potential bidders, it should identify any issues which could fundamentally affect the divestiture.

As noted above, the agreement also provides for resolution of certain other issues, in particular labor issues, prior to the execution of a final agreement. Given that the agreement is subject to change, including changes related to these particular items of importance, OCA submits that it is critical that all parties and the Commission have the opportunity to review and comment on the definitive agreement and any due diligence conducted by the Company prior to the Commission taking any final action on this matter. These should be submitted to the Commission and all parties in a timely fashion. Thus, the Commission should postpone final action on this agreement until all of these steps are completed.

4. The Language Of The Agreement Should Be Clarified With Respect To Duquesne's Nuclear Decommissioning Liability.

Paragraph 5 of the Agreement in Principle provides that Duquesne is "responsible for its share of nuclear decommissioning costs for the Beaver Valley Power Station and Perry Unit 1" and indicates that efforts will be made to cap this liability at the total funding amount in the Duquesne restructuring order. However, the agreement is unclear as to what is meant by this provision and whether Duquesne has established a firm cap on its nuclear decommissioning liability. Duquesne has indicated to OCA in the technical conference that the provision is intended to limit Duquesne's nuclear decommissioning liability to the amount included in the Commission's Restructuring Order. In other words, neither Duquesne, nor its ratepayers, will be liable for any additional nuclear decommissioning costs. The language set forth in paragraph 5, however, needs to be clarified to make it plain that this is the case since otherwise it could possibly be interpreted

to suggest that Duquesne is liable for the total nuclear decommissioning liability associated with its percentage ownership share of these nuclear plants. If, in fact, Duquesne has limited nuclear decommissioning liability for itself and its ratepayers, this additional unquantifiable benefit must be considered.[4]

5. Duquesne Should Continue To Evaluate Any Alternatives To Buy-Out Of Its Beaver Valley 2 Lease.

Paragraph 3 of the Agreement in Principle requires Duquesne to terminate its lease arrangement for its Beaver Valley 2 interest in order to transfer ownership to FirstEnergy. The Company has indicated that the cost of termination of this arrangement may be as much as $90 million and is to be deducted from the divestiture proceeds as a transaction cost.[5] In light of this substantial cost, which Duquesne asserts is in addition to any stranded costs determined based on the book value of the plant (i.e., the net present value of the lease), the OCA submits that the Company should explore with FirstEnergy any possible alternatives to termination of this lease, such as the possibility of the assignment of the lease to FirstEnergy. Moreover, further analysis is needed to determine whether all of the $90 million cost is incremental cost to Duquesne.

6. Conclusion

While OCA believes that with the information now available, the FirstEnergy transaction is likely to enhance the benefits to ratepayers, OCA submits that the Commission should

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[4] The OCA would note that if Duquesne has not limited its nuclear decommissioning liability, this factor would need to be considered in evaluating the swap as well.

[5] This termination fee for Duquesne's 113 MW share of Beaver Valley 2 is approximately $800/KW.

await a definitive agreement, resolution of outstanding labor, environmental and safety issues, and due diligence before acting to finally approve the transaction, with an opportunity for other parties to review any engineering and environmental analysis that is done as part of due diligence and to comment on such analysis. Further, the Commission should require clarification of the nuclear decommissioning liability and further efforts to reduce the cost associated with the Beaver Valley 2 lease.

B. Duquesne Should Continue To Explore Alternative Methods Of Meeting Its Provider of Last Resort Obligation.

1. Background

One of the key elements of the Electricity Generation Customer Choice and Competition Act is ensuring that electric service is available to all customers on affordable terms and conditions. The General Assembly, in setting forth its policy regarding electric competition, recognized this fact in several critical sections. Importantly, the Act provides:

> Electric service is essential to the health and well-being of residents, to public safety and to orderly economic development, and electric service should be available to all customers on reasonable terms and conditions.

66 Pa.C.S. §2802(9). The Act further provides:

> Electric distribution companies should continue to be the provider of last resort in order to ensure the availability of universal electric service in this Commonwealth unless another provider of last resort is approved by the commission.

66 Pa.C.S. §2802(16). This obligation has become known as the provider of last resort (POLR) obligation.

As noted above, the Office of Consumer Advocate submits that regardless of the divestiture by Duquesne of its generating assets, Duquesne must uphold its statutory obligation to provide full service to customers as the provider of last resort at or below its capped rates. Section 2807(e), governs the utility's obligation to serve. This section provides:

> **(e) Obligation to serve.**--An electric distribution company's obligation to provide electric service following implementation of restructuring and the choice of alternative generation by a customer is revised as follows:
>
> > (1) While an electric distribution company collects either a *competitive transition charge or an intangible transition charge or* until 100% of its customers have choice, **whichever is longer**, the electric distribution company shall continue to have the full obligation to serve, including the connection of customers, the delivery of electric energy and the production or acquisition of electric energy for customers.

66 Pa.C.S. §2807(e)(1)(emphasis added).

In addition, the OCA submits that regardless of a divestiture of its generation assets, Duquesne must provide service to its customers, consistent with the its obligation to serve, at or below the rate cap levels set forth in Section 2804(4). Importantly, Section 2804(4) provides for a total rate cap through June, 2001 and a generation rate cap that extends through 2005 under Duquesne's currently anticipated collection period for stranded cost. 66 Pa.C.S. §2804(4)(i)(ii). The provision of provider of last resort service, whether a customer remains with Duquesne or returns to Duquesne, must be in accordance with these rate caps for the statutory period.

In light of the divestiture of Duquesne's own generation assets, the question becomes one of how Duquesne should meet its obligation in a manner that provides reliability to consumers, and mitigates the risk to Duquesne. Initially, it is important for the Commission to make clear that Duquesne retains its obligations under the Act, even after divestiture of its assets. The inquiry

should be focused on how this obligation can be met in a manner that forwards the competitive market and results in reliable service at capped rates.

Duquesne has set forth several options for meeting these objectives. First, Duquesne proposes to bundle transition power contracts with some or all of its generation assets to provide a contractual source of capacity and energy during the rate cap period. This is sometimes referred to as a "buyback option." Duquesne Plan at 24. Second, Duquesne proposes to auction the provider of last resort function to an alternative provider. Duquesne Plan at 25. By letter dated November 5, 1998, Duquesne submitted another proposal to complete a competitive auction of its POLR obligation. Third, Duquesne proposes to provide this service by contracting for power in the wholesale market. Duquesne Plan at 25. Although the OCA expects that Duquesne will have to utilize all three options to some extent to serve its provider of last resort function, the OCA submits that a combination of the first two options may be the most appropriate way to proceed at this time. The OCA anticipates that as more experience is gained in understanding the provider of last resort function, additional options may become available for Duquesne in the provision of this service.

2. The OCA Recommends That Duquesne Continue To Pursue A Combination Of Approaches To Meet Its Statutory Obligation.

a. The OCA Recommends That Duquesne Continue To Explore The Use Of Transition Contracts To Meet Its POLR Obligation.

In its first option, the Company proposes to meet its provider of last resort obligation by bundling transition power contracts with some or all of its generation assets to provide a contractual source of capacity and energy during the rate cap period. Duquesne indicates that it will evaluate this option through the generation auction process in an attempt to reach a balance between

maximizing auction proceeds and reliably meeting the POLR obligation. Duquesne Plan at 26. The OCA submits that the Company should continue to pursue this option as a means of meeting its POLR obligation. In several divestitures to date, a variety of "buyback options" have been utilized to ensure a reliable supply of electricity at certain prices while also attempting to maximize the proceeds from the sale of the assets. Notably, the GPU generation divestiture is proceeding with the possibility of a number of transition contracts structured as "puts" and "calls" on the capacity and energy from certain generating stations. Given that the preliminary results of the GPU divestiture are due in November or December, the Commission should direct Duquesne to review the GPU divestiture process regarding transition contracts in developing a more specific plan for meeting its POLR obligation. Additionally, several divestitures in New York and New England have been conducted utilizing a variety of buyback options. Duquesne should be directed to investigate other divestiture processes that have used this mechanism to further evaluate this option. Finally, the OCA recommends that Duquesne evaluate a combination of short-term and long-term transition contracts when evaluating this option, particularly as it considers whether an auction process for a portion of its POLR obligation is viable.

b. Duquesne Should Explore The Use Of Competitive Default Service In Conjunction With The Commission's Efforts To Establish Such Service For Other Utilities.

The second option--seeking POLR through a competitive auction of other competitive suppliers--should also be considered by Duquesne in seeking to meet its POLR obligation. Initially, the OCA would note that provision of POLR service by an alternative provider approved by the Commission was specifically considered by the General Assembly in enacting the legislation. See, 66 Pa.C.S. §2802(16). Thus, Duquesne's proposal to auction its POLR obligation to other providers

was contemplated in the Act, provided that the Commission approves the alternative provider. In its Generation Plan, Duquesne did not specifically set forth how it intended to auction its POLR function, but several methods may be available. By letter dated November 5, 1998, the Company provided an additional proposal regarding an auction of the POLR obligation. The OCA will discuss this alternative, based on the limited information available, below.

In several recent settlement agreements of electric utility restructuring proceedings, the parties have agreed to a competitive process, referred to as Competitive Default Service (CDS), for the provider of last resort function. Under this process, alternative suppliers, that meet certain standards, terms, conditions and criteria to be established by the Commission, can bid to provide the CDS, including all customer cares functions. *Importantly, all Competitive Default Service must be provided at or below the rate cap levels.* The percentage of customers to be served by CDS varies somewhat between the Settlements. For example, for PECO and PP&L, 20% of residential customers will be assigned to CDS. For GPU, however, which is also divesting its generation assets, 20% of **all** customers are provided with CDS in 2001, and this percentage may increase over a four year period, after review by the Commission, to 80% of **all** customers.

The OCA submits that Duquesne should pursue the option of meeting some portion of its POLR obligation through Competitive Default Service. At this time, without an evaluation of the impact of transition contracts of varying terms on the auction process, it is difficult to determine exactly what percentage of Duquesne's POLR obligation should be provided through CDS. The OCA anticipates, however, that properly structured Competitive Default Service will aid in bringing the benefits of a competitive market to residential and small commercial customers. In essence, CDS could be viewed as a form of "regulatory aggregation," that is, the provision of a

regulated POLR service by competitive suppliers by means of an auction that occurs under the Commission's supervision. The OCA anticipates that because these customers will be transferred to the winning bidder after the auction without incurring the normal marketing costs and expenses associated with obtaining customers, the POLR service may be valuable and competitive bidders may be willing to pay a per-customer fee to obtain such customers, even under the rate cap provisions of the Act. Such fees could then be used to reduce stranded costs.

By Letter dated November 5, 1998, Duquesne submitted an additional request regarding an auction of the POLR function. In its Letter, Duquesne requested that the Commission determine that the shopping credits that the Company filed as part of its Third Revised Compliance Filing on November 5, 1998 be locked in and not subject to change in the future by the Commission. Duquesne would then market the POLR function based on these shopping credits and the winning bidder would assume an obligation to supply wholesale power to Duquesne in the quantities required by non-shopping customers at these shopping credit levels. Any net proceeds that Duquesne receives would be used to offset stranded cost.

The OCA has only had a limited time to review Duquesne's new proposal and has not had an opportunity to further discuss this proposal with the Company. Duquesne seems to be suggesting that the shopping credits are to be locked in and serve as a form of a cap for POLR service. It is the OCA's understanding of Duquesne's proposal that the CTC would then become a residual number so that the sum of the shopping credit and the CTC does not exceed the generation rate cap. If stranded cost is lowered, Duquesne anticipates that it would shorten the CTC, although the OCA recommends that a reduced CTC level over the same amortization period approved by the Commission also be considered as an option.

If in fact Duquesne is proposing a cap on POLR charges through 2007, the OCA submits that Duquesne's proposal may have merit and should be further considered.[6] At this time, the OCA would not recommend that 100% of Duquesne's POLR obligation be met in this manner until this proposal is more fully developed and analyzed. Among other concerns, the OCA is concerned that this proposal may not bring the benefits of competition to non-shopping customers as would the Competitive Default Service contemplated by the Settlements of the Restructuring proceedings. As the OCA understands Duquesne's proposal, the shopping credits would be not only a cap, but a floor. This could preclude any reductions below the shopping credit levels even if such reductions are warranted. Additionally, since Duquesne anticipates receiving wholesale power, it is not clear from its proposal which entity would continue to provide all customer care functions, and how this would be addressed in the auction process.

The OCA submits that Duquesne's auction proposals should, to the extent possible, be coordinated with and operated with the same or similar policies applicable to the Competitive Default Service contemplated by the Settlements reached for PECO Energy, PP&L, GPU Energy, and now West Penn Power Company. The Commission may wish to establish a generic proceeding for consideration of the details of such auctions and work through a collaborative process to establish consistent standards and procedures throughout the Commonwealth.

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[6] The OCA would note that it remains concerned about the shopping credit level for Rate RH and would oppose this shopping credit being locked in without a resolution of this issue. As the OCA pointed out in its Compliance Filing Comments, a proper development of Rate RH shopping credits may be dependent upon a final stranded cost amount and the proper design of the CTC.

c. Duquesne Should Not Rely Upon Wholesale Markets To Meet Its POLR Obligation.

The third option proposed by Duquesne--contract for power in the wholesale markets to provide POLR service--may be too uncertain to reliably fulfill Duquesne's POLR obligation. As Duquesne recognizes, it is unknown at this time whether there will be adequate market liquidity to obtain option contracts in sufficient quantity and duration to reliably meet the obligation to serve. Generation Plan at 25. As such, the OCA agrees with Duquesne that it should not rely on these types of contracts at this time as a means of providing its POLR function. These types of contracts, however, could be utilized, if necessary, to fill gaps in the provision of POLR service, or to provide benefits to POLR customers if market prices become advantageous.

3. Conclusion

In summary, the OCA submits that Duquesne should continue to work with the Commission and the parties to develop a plan for meeting its provider of last resort obligation that combines all three options that it has discussed. The OCA anticipates that it is through a combination of these options that Duquesne will best be able to serve its POLR function at the capped rates and in a manner that reduces risks to Duquesne. The OCA recommends that the Commission direct Duquesne to continue to evaluate a combination of its first two options through the generation auction process. The Commission should direct Duquesne to file a follow-up Report upon completion of this evaluation with the Commission and all interested parties. A collaborative process, including all interested parties, may then be appropriate to develop a process for Duquesne to meet its POLR obligation. Additionally, the OCA recommends that Duquesne's efforts to establish a competitive default service be coordinated with the Commission's on-going efforts to

establish standards, terms, conditions and processes for Competitive Default Service throughout the Commonwealth.

C. Auction Design and Timetable

1. Auction Process

The Company has proposed a two-phase sealed bid process that has been used in most of the asset divestitures conducted to date. Under this process, the first bidding phase solicits nonbinding indicative bids that allow the Company to identify the bidders placing the highest value on the assets, and to determine whether there is a preference for bundling of any particular assets. After determining a short list of bidders from these indicative bids, the Company solicits final sealed bids.

The OCA submits that the Company's auction design is generally reasonable. This process has been used successfully in other divestitures, and if implemented properly by Duquesne, this process would be acceptable. The OCA submits, however, that it should be clear that Duquesne retains the obligation to conduct the auction process in accordance with its design and in a manner that maximizes the proceeds from the auction. Duquesne has retained a certain amount of discretion in the auction process to determine such things as how various assets are to be bundled for auction or sale. Duquesne must continue to attempt to achieve maximum proceeds in these efforts. Moreover, it is critical that Duquesne retain the right to reject all bids if it determines that there were factors in the process which significantly affected the number of participants and the level of bids. Duquesne has indicated in its Plan that it is reserves such authority. Plan at 15, fn.15.

Although the OCA generally agrees with the two-phase bidding process outlined by Duquesne, the OCA submits that it is critical for the Company and the Commission to be cognizant

of a potential problem associated with a two-phase bidding procedure. A two-phase bidding procedure could be subject to gaming since the first bids are non-binding. In particular, since the first bids are non-binding, it is possible that some bidders will submit unrealistically high bids in order to get into the second phase of the bid procedure, and then reduce their bids significantly in phase two. Consequently, the Company should consider imposing some type of boundary on the downward variation between the first-phase bid and the second-phase bid that would, at a minimum, trigger a review by the Company of the bid results.

2. Affiliate or FirstEnergy Participation

In its Generation Auction Plan, Duquesne did not clearly state whether its affiliates would be permitted to bid in the auction. During the technical conference, Duquesne confirmed that its affiliates would not bid for the generation assets in this process. See also, Duquesne Response to OTS-14. The OCA submits that this should be clearly spelled out in the bidding procedures. If, in fact, affiliates were going to participate in the bidding process, the OCA submits that adequate protections, beyond those contained in the Plan, must be put into place to assure successful completion of the divestiture. As currently presented, there are insufficient protections to allow affiliate bidding in the auction.

In regard to the exchange of assets with FirstEnergy, it is the OCA's understanding that the agreement between Duquesne and FirstEnergy will prohibit FirstEnergy from bidding on the exchanged assets. See, Letter of October 14, 1998, Agreement in Principle, ¶8(b). This agreement is also critical to both a successful divestiture and the developing competitive market. The OCA recommends that this agreement be specifically stated as well in the Commission's Order and in the divestiture procedures.

3. Market Power Considerations

At pages 11-12 of its Plan, Duquesne notes that it will require each bidder that owns substantial assets in ECAR to submit an analysis of the degree to which the planned acquisition would impact wholesale and retail markets. The OCA agrees with this requirement but would recommend that Duquesne clearly identify the circumstances under which a market power analysis is required from a bidder. In addition, Duquesne should explain in additional detail how these analyses will impact upon Duquesne's decisions regarding such things as accepting final bids, limiting bidders, or bundling of assets. Moreover, Duquesne should explain whether it intends for the Commission to review these market power analyses in relation to the winning bidders.

D. Phillips and Brunot Island Must Be Sold In A Separate Package From Other Generation Assets To Accurately Determine The Value Placed On These Assets, The Net Proceeds From Which Will Be Retained By The Company.

In its Opinion and Order of May 29, 1998, the Commission adopted the position of the Office of Trial Staff that two of the Company's fossil plants, which are currently in cold reserve -- Phillips (308 MW) and Brunot Island (234 MW) -- should be excluded in the determination of stranded costs. Opinion and Order, at 91. In light of this determination, Duquesne proposes to retain the net proceeds from the sale of these two generating plants. While OCA does not disagree with Duquesne's proposal to retain the net proceeds of these plants in light of the Commission's determination, OCA submits that it is critical that these plants be bundled separately for auction purposes from the other generating plants with respect to which the net proceeds will be used in determining stranded costs. If Phillips and Brunot Island were to be bundled with other plants, it may be difficult to identify the market value of these units, or of the units with which Phillips and Brunot Island were bundled, even under a separate bid procedure. Even under a separate bid

procedure, if bidders are able to link bids, or condition bids for rate based plants based on non-rate based plants, it is difficult to determine the exact value of each plant. This would create difficulty in reconciling the stranded cost amounts with the net proceeds. Consequently, it is essential that, in light of the differing treatment of the proceeds of the sale of Phillips and Brunot Island, that the sale of these plants be packaged separately, and that the market value and transaction costs for the sale of these proceeds be tracked separately.

E. Duquesne's Obligations Under Its Eight-Year Power Sale Agreement ("PSA") Should Not Be Part Of The Auction.

On pages 19-20 of its Generation Auction Plan, Duquesne proposes to transfer its rights and obligations under its 100 MW, eight year Power Sale Agreement ("PSA") to one of the winning bidders. Duquesne states that its eight year agreement was consistent with the Commission's Order of October 2, 1997, which encouraged all Pennsylvania utilities to "sell an amount of capacity into the market equivalent to the pilot amount." Plan at 19. The OCA submits, however, that the eight year Power Sale Agreement was undertaken by Duquesne, before the Commission's October 2, 1997 Order, through its own initiative.[7] The eight year nature of the transaction was not consistent with the Commission's Order regarding the Pilot Program, which was only intended to be a one year program. The Company's decision to enter into an eight year Power Sale Agreement was never presented to the Commission for review and was never approved by the Commission. Moreover, the PSA is a wholesale transaction and is non-jurisdictional to retail service.

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[7] A review of Duquesne's Exhibit referenced at page 19, fn. 20 on the Power Sale Agreement makes clear that Duquesne initiated its Request For Proposal in June 1997. Duq. St. 7, Exh. RAI-4, p.1.

Whatever the genesis of Duquesne's Power Sale Agreement, the OCA is concerned with Duquesne's proposal to include the Power Sale Agreement as part of the auction process. Duquesne's proposal to bundle the Power Sale Agreement with generating units could result in a diminished market value for those assets that are properly being auctioned. The OCA submits that the PSA, like Phillips and Brunot Island, should be separately auctioned by Duquesne, or auctioned in conjunction with the auction of Phillips and Brunot Island. The OCA submits that ratepayers should not be held liable for this PSA.

F. Duquesne Should Continue To Evaluate Alternatives To The Auction Plan For Cheswick And Elrama In Light Of Duquesne's Proposed Operating Restrictions For Owners Of These Units.

Duquesne has indicated that it relies on its combined generation and transmission resources to provide reliable service during peak periods across the eastern half of its system. As a result, during such periods, both Elrama and Cheswick generating plants must be operating. Consequently, Duquesne intends to impose certain operating restrictions on the purchasers of these units to ensure that reliability is maintained. These restrictions allow Duquesne to call on the new owners to operate each plant at a minimum output level, or greater, during certain hours of peak load. Plan at 33. Duquesne will reimburse the new owners for the amount by which their cost to operate at the minimum levels exceed the market price for the energy produced. Id. at 34. If the new owners cannot sell the output during these hours, Duquesne will purchase the minimum amounts of output under the agreements at cost-based rates. Id. at 34. Additionally, Duquesne has reserved the right to cancel these agreements if adequate transmission or distribution remedies become available.

The OCA agrees with Duquesne that reliability is critical and must be maintained. The OCA is concerned, however, with the impact that these required agreements may have on the

generation divestiture process. While Duquesne's proposed compensation arrangement to these plant owners for production during these hours makes this less of a concern in the context of the generation auction, OCA submits that it could nonetheless have an adverse impact on the value placed on these units. In addition, it is possible that these agreements could limit any market incentive to provide more efficient solutions to these problems. Duquesne should be directed to continue to pursue the most cost-effective and reliable solutions to this problem in a timely manner.[8]

G. Ancillary Services

At page 28, the Company begins a discussion of Ancillary Services necessary to maintain the integrity of the transmission system. The Company proposes to purchase these services from either the asset purchaser or the regional market, if possible. The OCA would encourage the Company to continue to consider purchases of these services in the most cost-effective manner.

The Company then indicates that it will recover these costs from retail customers through FERC-approved charges. In a footnote, the Company indicates that it anticipates using a formula rate that allows it to recover these costs on a dollar-for-dollar basis. No further detail was provided. Plan at 29, fn. 29. Initially, the OCA is concerned with the imposition of an automatically adjusting formula rate mechanism on retail customers' bills in the environment of competitive supply. At this time, the Commission should reserve judgment on whether such mechanism is appropriate for the recovery of costs associated with ancillary services. At a minimum, however,

[8] The OCA would note that the Company has not indicated how it would address the additional costs that are contemplated under the agreement. The OCA expects that since these costs are based on Duquesne's current generating units, the costs are reflected in current capped rates. The OCA submits that it should be made clear that these costs cannot form the basis for exceeding the rate cap levels.

the Commission should make clear that if a formula rate is permitted at all, such rate is limited by the rate cap provisions of the Act. Specifically, Section 2804(4)(i) caps a utility's total charges for customers who do not shop, or its transmission and distribution charges for customers who shop, through June, 2001. The OCA submits that all ancillary services charges must be in accordance with these rate cap provisions.

H. Net Auction Proceeds Should Be Utilized To Determine The Stranded Cost Amount But The Accounting And Ratemaking Details Should Not Be Finalized And Approved By The Commission Until The Auction Has Closed.

The Company sets forth its "Accounting Protocols" for the auction on pages 35-36 of its Generation Auction Plan, and more specifically in Appendix G. The Company provides detailed provisions for the treatment of auction proceeds, tax treatment and reconciliation of the CTC collected during the interim period with the final stranded cost determination based upon the results of the auction.

While OCA recognizes the Company's concern that the Commission should assure it that it will be permitted recovery of reasonably incurred transaction costs associated with divestiture, OCA does not believe it is necessary or appropriate at this time to determine accounting protocols or ratemaking treatment with the type of specificity shown in Appendix G. It is not necessary because the auction itself will not be impacted by the accounting protocols or rate treatment afforded the Company after the sale. The Commission does not need to approve or establish such protocols at this stage in the process since asset bidders will not be concerned with the accounting protocols, CTC treatment and stranded cost determination used in establishing the Company's final allowable stranded cost.

Furthermore, there are many uncertainties associated with the divestiture which would make it impractical to establish an accounting protocol and final CTC treatment at this time. A variety of factors may impact the accounting and final ratemaking between now and the time the divestiture is complete, not the least of which is the proposed generation asset swap with First Energy. There is also uncertainty associated with the timing of the closings on the various assets which will be divested. It is conceivable that closing will occur at different times for various assets. Therefore, the accounting protocol used during the final accounting and ratemaking will have to account for this timing differential.

In addition, a final determination regarding the reasonableness of transaction costs and the final net book value of the plants should be made after the auction has closed, since these costs will not be determinable until that point in time. The final net book value of the plants will be impacted by not only the timing of the closing on divested assets, but also by any reasonable plant capital additions made prior to the closing. Consequently, the Commission should address these issues at the conclusion of the auction but in no event earlier than the date at which the asset sales agreements have been finalized. It is the OCA's understanding that in those states which have already conducted generation auctions, accounting and ratemaking treatment was addressed after the asset sales agreements were completed. Therefore, the OCA submits that the Commission should wait until the auction is complete before approving an accounting and ratemaking protocol to be used for determining a final stranded cost amount and establishing a final CTC.

If the Commission wishes to approve an accounting and ratemaking protocol at this time, the OCA submits that the accounting protocol and ratemaking treatment used after the divestiture must account for several factors. First, the change in book value which occurs between

the time of the Commission's administrative determination of stranded cost as of January 1, 1999 and the time of the final determination of stranded cost must be reflected in the final accounting. Second, the final determination of stranded cost must take into account the amount of CTC revenues paid by ratepayers during the interim period. In the final calculation of stranded cost, the net margins of the assets must be adjusted to account for the later valuation date. Finally, the administrative determination must be adjusted to reflect the actual net proceeds realized from the auction.

In addition, all transaction costs which the Company seeks to deduct out of the gross proceeds of the divestiture must be determined by the Commission to be reasonable, verifiable and necessary. Finally, a new CTC should be designed which will recover the actual amount of stranded cost as determined by the results of the auction. The duration of the CTC will depend upon the final amount of recoverable stranded cost remaining after the divestiture.

Initially, the OCA believes that the accounting protocol proposed by the Company in its divestiture plan may be unnecessarily complex. More importantly, the OCA is concerned that it may not capture all of the factors referenced above. It is the OCA's understanding of the Company's proposal that the Company will first start with the Commission's administrative determination of net margins as of January 1, 1999. This amount will be brought forward and adjustments made to account for the timing difference between January 1, 1999 and the time of closing. This will provide an administrative determination of the net margins for the Company's generation assets as of the time of closing to be used in making an administrative determination of stranded cost as of the time of closing. This recoverable balance of stranded cost will then be adjusted for two factors. First, the actual proceeds of the auction will be used to adjust net margins.

Second, the recoverable balance of stranded cost will be reduced by the principal amount of CTC revenues paid by customers during the interim period.

The OCA submits that what the Company may not have captured in its methodology is the depreciation and capital cost recovery that is recovered through market prices, or in this case, the shopping credit. The Company is only reflecting the depreciation and capital cost recovery that is stranded and recovered through the CTC. However, the Company is also receiving depreciation and capital cost recovery that is **not** stranded and is recovered through market prices, or the shopping portion of the rate for customers who do not shop. Thus, the final net book value amount of depreciation and capital recovery must reflect the depreciation and capital cost recovery assumed to be collected from the market.

The OCA submits that even if the Company's proposed accounting protocol, with adjustment, results in an accurate adjustment of final stranded costs, the Commission should still postpone determination of accounting protocols and ratemaking treatment until after the auction has closed. At that time, many of the uncertainties surrounding the auction will be resolved and an accounting protocol can be adopted which will account for all known and unknown aspects of the divestiture.

I. Other Issues Concerning the Company's Accounting Protocol Proposed In Appendix G.

1. Treatment of Unsold Assets

In footnote 3 of Appendix G, the Company proposes that the market value for any asset which remains unsold after the auction is zero. The OCA submits that it is unreasonable to assume that all unsold assets have a market value of zero without looking into the underlying reasons

why the asset was not bid on or did not sell. For instance, the Company proposes to bundle its 100 MW Power Sale Contract with its generation assets during the auction. The Company has also proposed to bundle its PLR requirements with the generation assets in the auction as one option for serving its PLR function. Duquesne also proposes to impose certain operating restrictions on certain "must-run" plants which will be part of the auction. It is conceivable that a plant with an administratively determined positive net margin could become unattractive to bidders due to the aforementioned encumbrances and conditions placed upon the sale. Therefore, if an asset remains unsold after the auction, the Commission must examine the underlying reasons why it did not sell and determine whether the Company placed any undue restrictions on the sale of that asset. Moreover, Duquesne may be able to sell the capacity and energy from an unsold asset. As such, during the final reconciliation of stranded cost, any unsold asset should be valued at its administratively determined market value unless Duquesne can demonstrate that a different valuation is appropriate.

2. Deferred Fuel

On page 2a of Appendix G, the Company sets forth stranded cost allowance for its Stand Alone Base Case. The Company's regulatory assets include a claim of $25 million dollars for deferred fuel costs. In the Restructuring Order entered May 29, 1998, the Commission allowed the Company to recover $6.73 million for deferred fuel. In its first compliance filing, the Company sought to include $18.25 million in stranded cost for deferred fuel. The Commission's August 13, 1998 Order on Compliance Filing disallowed this claim and allowed recovery of only $6.73 million for deferred fuel.

The Company claims that the deferred fuel regulatory asset should now be increased to $25 million since the Commission denied Duquesne a roll-in of its ECR at the higher value that it sought. The OCA submits that the Commission has fully addressed this issue in its August 13, 1998 Order when it directed Duquesne to utilize the 12.8 mills/kWh energy cost and allowed $6.73 million in deferred fuel. There has been no additional information provided by Duquesne to change this determination. Therefore, the Company's claim for deferred fuel should be reduced to $6.73 million as ordered by the Commission in both the restructuring and compliance orders.

3. Allowances For Capital Additions Must Be Removed

As noted in Section II.H. above, the Company's accounting protocol first starts with the Commission's administrative determination of net margins as of January 1, 1999. This amount is brought forward and adjustments made to account for the timing difference between January 1, 1999 and the time of closing. This will provide an administrative determination of the net margins for the Company's generation assets at the time of closing which is then adjusted to reflect the results of the auction and the CTC revenues collected during the interim period.

However, the Commission's administrative determination of net margins as of January 1, 1999, included allowances for capital additions to generation plants. These capital addition projections assumed that the Company would continue to own and operate these plants. With the divestiture, many of these capital additions will never be completed by Duquesne. Instead, the cost of these projected capital additions will be factored into the price a bidder is willing to pay for these assets. Therefore, any capital additions during 1999 until the time the sale is closed which were included in the administrative determination must be removed at the time of reconciliation after the auction. Only those capital additions which were actually completed prior to closing should be

included in the administrative determination of net margins which is used as a starting point in the final reconciliation.

4. SFAS 109 Recoverable Taxes

Another concern which the OCA has identified with regard to the Company's proposed treatment of the generation proceeds relates to treatment of income taxes. Duquesne proposes to determine the net auction proceeds on an after-tax basis based on the actual taxes paid as a result of the sale. This procedure will account for the income taxes associated with differences between tax and book value which have not been normalized because only the tax basis will be recognized in determining income tax. As a result, the use of after tax proceeds will fully account for SFAS No. 109 recoverable taxes. In its Divestiture Plan, the Company does not propose to adjust the Commission's finding regarding SFAS 109 recoverable taxes. This would result in a double-counting of these recoverable taxes.

Stated another way, with the sale of its generation assets, all of these future tax obligations become due and payable immediately. There is no longer a need to separately account for these taxes again by recording it as a SFAS 109 future obligation. These taxes will be paid out of the proceeds of the divestiture as part of the reconciliation.

The OCA submits that since the Company is divesting its generation assets and will pay taxes associated with these assets at the time of the sale, the SFAS 109 regulatory asset should be removed from the stranded cost calculation.

J. Administrative Procedures

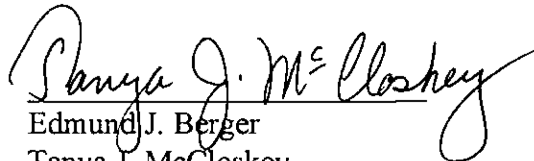
The Company has not set forth a definitive administrative procedure following the conclusion of the divestiture and the receipt of the divestiture proceeds. The Company is requesting

that the Commission not conduct a *"post hoc"* review of matters related to the conduct of the auction. The OCA agrees with the Company that to the extent the Commission finds Duquesne's auction procedures and protocols to be reasonable at this time, the Commission should not conduct a *post hoc* review of those procedures and protocols. The OCA would note, however, that there are several steps during the auction process that require Duquesne to exercise its discretion as to certain matters which must be reviewed by the Commission. Duquesne may wish to file periodic reports with the Commission and the parties to assure that the process is progressing as intended. The OCA agrees with Duquesne's proposal to submit any modifications to the Auction Plan to the Commission for review and approval after comment by the parties to the case.

III. CONCLUSION

As set forth above, the OCA generally supports Duquesne's proposal to conduct a timely divestiture of its generation assets to determine stranded cost and to stimulate the competitive generation market in the Western portion of Pennsylvania. Based on the information available, the OCA expects that the generation exchange with FirstEnergy is likely to improve the value realized by Duquesne through the divestiture process. The OCA would note, however, that there is no final agreement between FirstEnergy and Duquesne for review by the Commission and the parties, and such final agreement will be necessary for a proper determination. Additionally, the OCA recognizes that the Commission must balance many interests, particularly those regarding environmental issues, labor issues, community impacts, and safety issues that have not been addressed by the OCA. As such, the Commission may not grant any final approval of Duquesne's proposal until the final agreement is submitted and these other issues addressed.

Respectfully submitted,



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CERTIFICATE OF SERVICE

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

I hereby certify that I have this day served a true copy of the foregoing document, Office Consumer Advocate's Comments to the Generation Auction Plan of Duquesne Light Company, upon parties of record in this proceeding in accordance with the requirements of 52 Pa. Code § 1.54 (relating to service by a participant), in the manner and upon the persons listed below:

Dated this 9th day of November, 1998.

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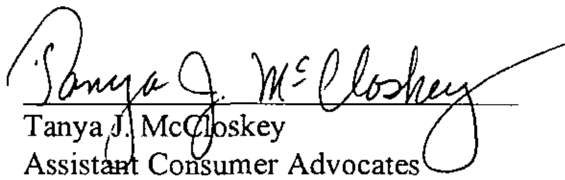

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COMMONWEALTH OF PENNSYLVANIA

DATE: November 10, 1998

SUBJECT: R-00974104

TO: Law Bureau

FROM: James J. McNulty, Secretary

DOCKETED
NOV 10 1998

APPLICATION OF DUQUESNE LIGHT COMPANY FOR APPROVAL OF RESTRUCTURING PLAN

Attached is copy of a Petition to Intervene Out of Time and Comments on Generation Exchange and Generation Auction Plan filed by Utility Workers Union of America, AFL-CIO in connection with the above docketed proceeding.

This matter is assigned to your Bureau for appropriate action.

Attachment

cc: BFUS

DOCUMENT FOLDER

wjz

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