

**STATE OF NEW JERSEY  
BOARD OF PUBLIC UTILITIES**

**In The Matter Of The Joint Petition Of  
Public Service Electric And Gas Company  
And Exelon Corporation  
For Approval Of A Change In Control Of  
Public Service Electric And Gas Company,  
And Related Authorizations**

**DIRECT  
TESTIMONY**

**OF**

**JOHN W. ROWE**

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**DIRECT TESTIMONY  
OF  
JOHN W. ROWE**

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**I. INTRODUCTION AND QUALIFICATIONS**

11 **Q. Please state your name and business address.**

12  
13 **A.** My name is John W. Rowe. My business address is Exelon Corporation, 10  
14 South Dearborn Street, 37th Floor, Chicago, Illinois 60680-5379.

15 **Q. What positions do you hold at Exelon Corporation (Exelon)?**

16  
17 **A.** I am the Chairman, President, and Chief Executive Officer of Exelon.  
18

19  
20 **Q. What is the purpose of your testimony in this proceeding?**

21 **A.** The purpose of my testimony is to (i) provide an overview of the proposed  
22 merger (“Merger”) of Public Service Enterprise Group Incorporated (“PSEG”)   
23 into Exelon, (ii) describe the benefits the Merger is expected to create for  
24 customers, employees and shareholders, (iii) describe generally the effects the  
25 Merger will have both on Public Service Electric and Gas Company  
 (“PSE&G”) and, more broadly, on the State of New Jersey, and (iv) describe  
 the policies that the corporation formed by the Merger, Exelon Electric & Gas  
 Corporation (“EEG”), will employ to assure that PSE&G continues to provide  
 safe, adequate and proper service at reasonable rates in New Jersey.

1 **Q. Please summarize your professional background and your experience in**  
2 **the utility industry.**

3  
4 **A.** I have led electric utilities since 1984, consecutively serving as the Chief  
5 Executive Officer of Central Maine Power Company, the New England  
6 Electric System, Unicom Corporation, one of Exelon's predecessor companies,  
7 and now Exelon. I am a past Chairman of the Edison Electric Institute  
8 ("EEI"), and currently serve on EEI's Board and Executive Committee, as well  
9 as that of the Nuclear Energy Institute and Institute of Nuclear Power  
10 Operations ("INPO"). I also serve on the Boards of Unum Provident  
11 Corporation, Sunoco, and the Northern Trust Company.

12 I am a lawyer by training, with undergraduate and law degrees from the  
13 University of Wisconsin, where I was elected to Phi Beta Kappa and the Order  
14 of the Coif. Prior to my utility experience, I served as General Counsel of  
15 Consolidated Rail Corporation, and as a Partner with the Chicago law firm of  
16 Isham, Lincoln and Beale.

17  
18 **Q. Who will hold the positions of Chairman, Chief Executive Officer and**  
19 **President of EEG after the Merger?**

20  
21 **A.** When the Merger is consummated, I will be President and Chief Executive  
22 Officer of EEG and a member of the Board of Directors, and Jim Ferland,  
23 currently Chairman, President, and Chief Executive Officer of PSEG, will be

1 non-executive Chairman of the Board and a Director. Jim has indicated for  
2 some time that he intends to retire when he reaches age 65 in March 2007.  
3 Prior to Jim's retirement, he will chair Board of Directors' meetings and will  
4 provide us a wealth of experience and perspective on the New Jersey  
5 operations. After Jim's retirement, I will become Chairman of the Board and  
6 remain President Chief Executive Officer of EEG. Jim's Board position will  
7 continue to be filled, from the date of his retirement until at least three years  
8 after the Merger, by a director approved by the legacy PSEG Directors serving  
9 on the EEG Board of Directors.

## 11 II. THE PROPOSED MERGER

12 **Q. Please describe briefly the proposed Merger.**

13  
14 **A.** In December 2004, the Boards of Directors of Exelon and PSEG unanimously  
15 approved the Merger of PSEG into Exelon, subject to shareholder and  
16 regulatory approvals. The Merger would create the largest, and if we meet our  
17 expectations, the finest electric and gas utility in the United States. Under the  
18 agreed upon post-Merger corporate structure, PSE&G will become a subsidiary  
19 of Exelon Energy Delivery, LLC ("Exelon Energy Delivery"), a first tier  
20 subsidiary of Exelon and the immediate parent of Exelon's two existing

1 regulated public utility transmission and distribution companies, PECO Energy  
2 Company (“PECO”) and Commonwealth Edison Company (“ComEd”).

3  
4 **Q. What will happen at the shareholder level to effect the Merger?**

5  
6 **A.** The shareholders of PSEG must approve the Merger, and the shareholders of  
7 Exelon must approve the issuance of additional shares necessary to effect the  
8 Merger. Shareholder meetings for both Exelon and PSEG have tentatively  
9 been scheduled for mid-2005 to vote on the transaction. Upon consummation  
10 of the Merger after all regulatory and other approvals are obtained, each holder  
11 of PSEG common stock will receive 1.225 shares of Exelon common stock,  
12 with cash being paid in lieu of fractional shares.

13  
14 **Q. Please describe briefly the combined, post-Merger company.**

15  
16 **A.** The combined company will operate in the most competitive region of the  
17 nation, and in three states that have embraced retail competition. It will have a  
18 separate transmission and distribution utility operating in each of these states,  
19 and will provide service to over seven million retail electric customers and two  
20 million retail gas customers. Overall, we will serve over 18 million people, a  
21 responsibility that I welcome, but take very seriously indeed. Each of EEG’s  
22 utility subsidiaries will remain separate corporations with separate

1 headquarters located in their respective service areas: PSE&G in Newark,  
2 New Jersey, PECO in Philadelphia, Pennsylvania, and ComEd in Chicago,  
3 Illinois. Each will be adequately capitalized and fully subject to regulatory  
4 scrutiny.

5 Before the mitigation measures described below, EEG will also have  
6 approximately 52,000 Megawatts (“MW”) of generation, 40,000 MW of which  
7 are located principally within the centrally dispatched control area of PJM  
8 Interconnection, L.L.C. (“PJM”), which is the Federal Energy Regulatory  
9 Commission (“FERC”)-approved Regional Transmission Organization  
10 (“RTO”) for transmission systems covering all or parts of several states and the  
11 District of Columbia. The headquarters of Exelon Generation Company LLC  
12 (“Exelon Generation”) will move from Pennsylvania to Newark, New Jersey.  
13 The headquarters of the nuclear operation will move from the Chicago area to  
14 a site in southeastern Pennsylvania. This will place it in proximity to the  
15 Salem and Peach Bottom Generating Stations, which are presently co-owned  
16 by PSEG and Exelon, and Hope Creek, which is wholly owned by PSEG.

17



1 Mitchell, Senior Vice President, Treasurer and Business Unit Chief Financial  
2 Officer of Exelon, in his direct testimony.

3 **Financial Strength and Flexibility.** The Merger will provide greater  
4 financial strength and flexibility by creating a company with a stronger balance  
5 sheet. Thus, following the Merger, EEG will have approximately \$70 billion  
6 in assets, a market capitalization of approximately \$40 billion, annual revenues  
7 of approximately \$26 billion and annual net income of approximately \$2.6  
8 billion. These benefits and their direct consequences, in terms of enhancing  
9 access to capital at reasonable rates, are also explained by Mr. Mitchell.

10 **Commitment to High Quality Service; Sharing of Best Practices.**  
11 We are committed to maintaining the high quality service currently furnished  
12 by PSE&G. The Merger will allow our regulated energy distribution utilities  
13 to share best practices in transmission and distribution operations and customer  
14 service. Ralph Izzo will continue to serve as President and Chief Operating  
15 Officer of PSE&G after the Merger, helping to ensure the adoption of best  
16 practices in New Jersey and the continued provision of high quality service. In  
17 addition, the Merger will increase our ability to meet that commitment by  
18 ensuring that Exelon has the financial strength and flexibility to make the  
19 investments PSE&G, PECO and ComEd need to meet their service obligations.

1           **Synergies.** The Merger will create the opportunity to achieve  
2 meaningful cost savings not only through the sharing of best practices but also  
3 through the elimination of duplicative functions, improved operating  
4 efficiencies and supply chain benefits from improved sourcing. William  
5 Arndt, Exelon's Senior Vice President for Financial Operations, in his  
6 testimony, describes both the anticipated synergies and the costs that will have  
7 to be incurred to achieve those synergies.

8           **Commitment to Competition.** Exelon and PSE&G have been  
9 advocates of competition in retail and wholesale markets for both electricity  
10 and natural gas. The shared vision of Exelon and PSE&G is to continue to  
11 promote competitive retail and wholesale markets within New Jersey and  
12 throughout PJM. In addition, we anticipate that the knowledge and experience  
13 of each company will enhance the merged company's ability to promote  
14 competitive retail and wholesale markets, which in turn will continue to  
15 provide benefits for customers.

16           We also recognize that combining the generation assets of the two  
17 companies raises market concentration concerns unless properly addressed. To  
18 address those concerns, as part of our application to the FERC for approval of  
19 the Merger, we are proposing an unprecedented mitigation plan that eliminates  
20 any Merger-related competitive concerns that otherwise would be present. The

1 plan is to transfer control of over approximately 5,500 MW of capacity.  
2 Specifically, the plan includes a proposal to divest (i.e., sell to third parties)  
3 approximately 2,900 MW of mid merit and peaking generation. For baseload  
4 nuclear capacity, the plan includes a “virtual divestiture” proposal for 2,600  
5 MW of baseload capacity or, alternatively, a swap of capacity in PJM East for  
6 capacity outside of PJM. The virtual divestiture is described in detail in the  
7 companies’ Merger approval application being filed simultaneously at the  
8 FERC.

9 In addition to the benefits I have described above, we believe the  
10 Merger will provide greater opportunities for our employees and benefit the  
11 communities we serve, as I will explain at a later point in this testimony.

1                   **IV. EFFECTS OF THE MERGER ON PSE&G – CONTINUING**  
2                   **COMMITMENT TO HIGH QUALITY SERVICE AT REASONABLE RATES,**  
3                   **LOCAL PRESENCE AND AUTONOMY, AND SOUND CORPORATE**  
4                   **GOVERNANCE**

5                   **Q.     Please describe the principles that will guide the operation of EEG’s**  
6                   **transmission and distribution business after the Merger.**

7  
8                   **A.     As a company, we are committed to being the finest electric and gas utility in**  
9                   the United States. To achieve that goal, we are guided by three fundamental,  
10                  overarching principles. First, we must live up to all of our commitments.  
11                  Second, we must perform at world-class levels in all aspects of our business.  
12                  Third, we must build value through sound, disciplined management. These are  
13                  the principles that will continue to guide the post-Merger operation of all of  
14                  our utility businesses, including PSE&G. Obviously, we have a broad and  
15                  challenging mandate. However, we believe it can, and will, be realized  
16                  through our focus on three critical factors: (1) high quality service; (2) local  
17                  presence and decision making capability; and (3) maintaining sound corporate  
18                  governance policies, which assure that management understands what is  
19                  happening at the local level, provides the required corporate support and  
20                  delivers what it promises.

21

1 **Q. Please explain your corporate commitment to high quality service.**

2  
3 **A.** It is our fundamental belief that the success of Exelon today, and the success of  
4 EEG in the future, requires us to give the highest priority to assuring our local  
5 utility operations furnish outstanding utility service. Therefore, we must  
6 provide our utility subsidiaries the financial and human resources they need to  
7 maintain that level of service. Since its creation in 2000, Exelon has invested  
8 over \$3.5 billion in transmission and distribution improvements at both PECO  
9 and ComEd, even though rates are currently capped in both Pennsylvania and  
10 Illinois. We recognize that PSE&G has an outstanding record of performance  
11 in safety, customer service and reliability, and our record demonstrates our  
12 commitment to maintaining and enhancing that performance after the Merger.  
13 We are keenly aware that permitting the quality of service furnished by  
14 PSE&G or any of our utilities to diminish in any respect is inconsistent with  
15 our vision of being the finest electric and gas utility in the United States, is  
16 contrary to customers' interests, and could destroy shareholder value. We will  
17 not allow that to happen. Stated another way, we can build value for  
18 shareholders only if we preserve and enhance the quality and value of the  
19 service we furnish to our customers.

20

1 **Q. What impact will the Merger have on PSE&G's electric and gas rates?**

2  
3 **A.** PSE&G's rates and the terms and conditions of service in effect prior to the  
4 Merger will not change as a result of the Merger. Going forward, and after  
5 costs-to-achieve are incurred, the Merger will generate economies, some of  
6 which will accrue to the New Jersey jurisdictional regulated businesses of  
7 PSE&G. Those economies will help offset the rise in the cost of providing  
8 reliable regulated electric and gas distribution service and, thus, will, over  
9 time, result in lower rates than would otherwise be the case.

10  
11 **Q. Please explain your corporate commitment to local presence.**

12  
13 **A.** To achieve our goal of outstanding customer service and reliability, it is  
14 critically important that each of our utilities retain a local presence and an  
15 appropriate level of local decision making so that they can respond promptly  
16 and effectively to service-related matters and other issues that may arise within  
17 their respective service areas. Local presence also means that each utility will  
18 be an outstanding corporate citizen and will take a leadership role in the civic,  
19 cultural and charitable life of the communities it serves.

20 Exelon recognizes that PSEG, and its predecessor companies, have over  
21 a 100-year history of commitment to New Jersey and its communities. PSEG  
22 has been the mainstay of many community initiatives and has had an

1 exceptionally strong commitment to the civic, cultural and community life in  
2 the numerous communities it serves. I want to assure this Board that the  
3 Merger will not negatively impact that longstanding commitment to New  
4 Jersey and its communities. We will sustain PSEG's record of charitable and  
5 civic contributions, economic development and environmental commitment,  
6 just as we maintained the PECO and ComEd commitments when Unicom and  
7 PECO merged four years ago. Exelon is a strong supporter of numerous civic,  
8 cultural and community activities throughout our service territories. Exelon  
9 typically makes over \$12 million in charitable contributions annually through  
10 its various affiliates. In 2004, Exelon's charitable contributions totaled  
11 approximately \$17.9 million, including contributions in PECO's service  
12 territory of approximately \$7.4 million.

13  
14 **Q. How will the goal of local presence and decision-making be assured?**

15  
16 **A.** As I previously explained, after the Merger, PSE&G will remain a separate  
17 corporation and will keep its headquarters in Newark. Ralph Izzo will remain  
18 the President and Chief Operating Officer of PSE&G, and his office will  
19 continue to be located at 80 Park Plaza in Newark. Ralph will have day-to-day  
20 responsibility for the safe, efficient and effective operation of the electric and  
21 gas systems in New Jersey, and will have all necessary authority and resources

1 to ensure the continued provision of safe and adequate service. As has been  
2 my practice in Philadelphia, I will also be a frequent presence in Newark.  
3 Additionally, Exelon will assure that PSE&G has the necessary financial,  
4 managerial, back office, and field resources to conduct its business and make  
5 the investments needed to assure a continuing level of high quality service. As  
6 previously stated, we are also committed to maintaining PSE&G's community  
7 involvement, which is a topic I will address in detail at a later point.

8 In addition, steps have been taken to provide continuing local  
9 representation on the Exelon Board of Directors. Exelon's Board of Directors  
10 will be expanded from 12 to 18 members and the six new positions will be  
11 filled by former PSEG Directors, including Jim Ferland. The Agreement and  
12 Plan of Merger has protections built in so that PSEG Directors will continue to  
13 serve for at least three years following the Merger. As I previously explained,  
14 Jim Ferland will be the non-executive Chairman of the Board.

15  
16 **Q. Please explain generally the corporate governance policies of Exelon.**

17  
18 **A.** We believe it is essential that corporations have a robust corporate governance  
19 structure to assure that the managers of the business fulfill their fiduciary duty  
20 to shareholders, satisfy the company's legal requirements, and honor the

1 company's obligations – legal and otherwise – to employees, customers and  
2 the communities in which it operates.

3 Exelon has a governance structure that complies with applicable  
4 standards imposed by the Sarbanes-Oxley Act, the laws and regulations  
5 administered by the Securities and Exchange Commission ("SEC"), and the  
6 rules and listing requirements of the New York Stock Exchange ("NYSE"). I  
7 am the only company officer on the Exelon Board.

8 Exelon has independent Audit, Compensation and Governance  
9 Committees, as mandated by the listing requirements of the NYSE. Exelon's  
10 Board of Directors has adopted Corporate Governance Principles, and Exelon  
11 has adopted a Code of Business Conduct, both of which are consistent with  
12 applicable legal requirements. We view those standards as critically important  
13 to the management of the company.

14 I believe that Exelon's governance principles and business conduct are  
15 similar to those of PSEG. This tells me that we already share similar values,  
16 which is critical to the post-Merger integration of the companies. I have  
17 already seen similarities in corporate values and corporate cultures emerge in  
18 the interaction of our respective employees as they proceed with the efforts to  
19 make this Merger happen. The employees, management and Boards of both  
20 companies value honesty, creativity, commitment, accountability, quality of

1 performance and environmental stewardship. These common values are also  
2 key to achieving our vision of being the premier electric and gas utility in the  
3 United States.

4  
5 **Q. Please explain the corporate governance policies and procedures EEG will**  
6 **maintain to assure that management understands what is happening at the**  
7 **local level and delivers what it promises.**

8  
9 **A.** The Exelon Board has established operational oversight committees organized  
10 by functional area, which will continue after the Merger. The Exelon Energy  
11 Delivery Oversight Committee meets at least quarterly to review energy  
12 delivery operations in detail. Based upon that review, it reports directly to the  
13 full Board of Directors. With the addition of PSE&G, the Energy Delivery  
14 Oversight Committee will have the opportunity to compare operating  
15 performance across three local utilities, share best practices, and build upon the  
16 collective knowledge of the experienced management at each utility.

17 I also believe that, to meet our commitments, we must assure that the  
18 Board of Directors and senior management reflect the diversity of the areas we  
19 serve. Exelon's Board of Directors presently includes two women (including  
20 one Asian woman), one Hispanic and one African American. In my  
21 experience, the Board must also have a personal connection to the local  
22 operating areas of the company's utilities and other businesses. For that

1 reason, Exelon currently rotates Board meetings between Chicago and  
2 Philadelphia, and, following the Merger, EEG would include Newark in the  
3 rotation. Likewise, the Energy Delivery Oversight Committee meets at various  
4 field locations to see the operations first hand and meet the people responsible  
5 for running those operations. We will continue this practice following the  
6 Merger.

7  
8 **V. EFFECTS OF THE MERGER ON COMMUNITIES SERVED, THE**  
9 **ENVIRONMENT AND EMPLOYEES**

10 **Q. Earlier, you explained that community involvement was a key element in**  
11 **the corporate goal of maintaining a strong local presence. Please explain**  
12 **the level and degree of community involvement contemplated for PSE&G**  
13 **and EEG after the Merger.**

14  
15 **A.** EEG will continue a level of community and charitable involvement in New  
16 Jersey after the Merger at least as substantial as that of PSEG currently. The  
17 Merger Agreement provides that charitable commitments will continue at the  
18 current level for at least four years. I fully expect that charitable contributions  
19 at the same or higher levels will be an integral part of our New Jersey  
20 operations in the years ahead. For example, PSEG recently made a ten-year,  
21 \$5 million commitment to the new Children's Specialized Hospital to be built  
22 in New Brunswick, New Jersey. This is the kind of commitment that I believe

1 reflects sound corporate leadership on a community level and I will support  
2 that commitment.

3 It is important to point out that our commitment to leadership in the  
4 civic, cultural and charitable life of the communities where we do business is  
5 backed by a solid record of performance, which goes beyond monetary  
6 donations. Our efforts on behalf of education, neighborhood development, arts  
7 and culture and energy and the environment are described in the most recent  
8 issue of the periodic report we prepare, entitled *Energy for the Community –*  
9 *Corporate Citizenship Overview*. I am providing a copy of that report as  
10 Exhibit A to my testimony.

11  
12 **Q. Please explain Exelon's commitment to economic development within the**  
13 **communities it serves.**

14  
15 **A.** Again, continued support of economic development in New Jersey at least at  
16 PSE&G's existing level is consistent with our vision. We can only be  
17 successful if we serve a territory that is economically healthy. Therefore, it is  
18 in our economic and community interest to continue to support the economic  
19 development in this State. I also believe that it is important to support "smart"  
20 growth. The Board, with PSE&G's support, has already adopted regulations to  
21 incent development in the State's urban and underdeveloped areas, and we will  
22 continue to support these efforts after the Merger.

1 **Q. Please address Exelon's commitment to the environment.**

2  
3 **A.** Exelon, like PSEG, has a strong environmental commitment. We will continue  
4 the enviable environmental record PSEG has in New Jersey. We support the  
5 deployment of renewable energy resources and other Clean Energy Program  
6 initiatives. We will be supportive of projects and ideas that can meaningfully  
7 help to drive this and other environmental programs. PSEG and Exelon are  
8 both members of the Clean Energy Group, a coalition of utilities that support  
9 enactment of comprehensive clean air legislation by the Congress, including  
10 support for the enactment of so-called "4-P" legislation that would provide the  
11 Environmental Protection Agency ("EPA") authority to regulate sulphur  
12 dioxide, nitrogen oxide, mercury, and carbon dioxide emissions. We are also  
13 both partners in EPA's Climate Leaders Partnership, a voluntary industry-  
14 government partnership that encourages companies to develop long-term  
15 comprehensive climate change strategies. Partners set a corporate-wide  
16 greenhouse gas ("GHG") reduction goal and inventory their emissions to  
17 measure progress. PSEG has established a GHG reduction goal of 18% per  
18 kilowatt hour ("kWh") (excluding production from nuclear units) by 2008 over  
19 a 2000 base year. Exelon is slated to adopt its own goal this year.

20

1 **Q. What effect will the Merger have upon employees?**

2  
3 **A.** Following the Merger, we will consolidate certain positions, primarily in the  
4 managerial and administrative ranks, in order to achieve the efficiencies that  
5 can be gained by a corporate combination. We do not anticipate that any  
6 reductions will be made to field level employees in either the electric or natural  
7 gas delivery functions. With respect to non-field level positions, we intend to  
8 minimize the elimination of existing employees by focusing on attrition and  
9 the normal retirement process. Severance programs may also be utilized.  
10 Across both Exelon and PSEG, we project an overall reduction of about 5% in  
11 the combined workforce of approximately 28,000. The Merger will also  
12 provide employees with increased opportunities within the organization. In  
13 developing our employment plans, we will use a fair, geographically-neutral  
14 process to fill new or consolidated positions. In short, we will select the best  
15 people for the jobs regardless of their present location.

16  
17 **Q. How will the Merger create opportunities for employees within the**  
18 **combined company?**

19  
20 **A.** The new company will provide our employees a larger, stronger organization,  
21 a more secure employer and better opportunities for career development.  
22 Because of its larger size and expanded scope of operations, EEG will offer  
23 employees better training tools and more paths for advancement than either

1 Exelon or PSEG could provide separately. Additionally, Exelon is committed  
2 to the pursuit of diversity in its workforce because we firmly believe that  
3 inclusion, respect and fair treatment contribute to increased productivity and  
4 make our company stronger.

5  
6 **VI. CONCLUSION**

7 **Q. Please summarize the effects of the Merger as they relate to the joint**  
8 **request for approval of the Merger.**

9  
10 **A.** The Merger will create a company with the scale, scope, financial strength and  
11 operational resources (1) to provide high quality electric and gas utility service  
12 at reasonable rates in each of the jurisdictions in which its subsidiaries operate;  
13 (2) to be an active participant in the wholesale generation and power marketing  
14 business; (3) to attract and retain the finest quality employees to manage and  
15 operate its businesses; and (4) to continue the local presence and community  
16 support that is currently provided by PSE&G in New Jersey, by PECO in  
17 Southeastern Pennsylvania, and by ComEd in Northern Illinois. In summary,  
18 the Merger will create benefits for customers, employees, shareholders and the  
19 communities served by PSE&G, which could not otherwise be achieved.

20  
21 **Q. Does this conclude your direct testimony at this time?**

22  
23 **A.** Yes, it does.

ENERGY FOR THE COMMUNITY  
*Corporate Citizenship Overview*



## ENERGY FOR THE COMMUNITY

Powered by approximately 20,000 dedicated employees, Exelon Corporation is one of the largest utilities in the United States. Headquartered in Chicago, Exelon has approximately 5.1 million electric customers in northern Illinois and southeastern Pennsylvania and approximately 460,000 natural gas customers in the Philadelphia area as well as one of the industry's largest generation portfolios.

Our company has a strong tradition of community involvement—of committing our “Energy for the Community” to a wide range of educational, cultural, environmental, and community and neighborhood development programs. Over the last five years, we have donated more than \$55 million to organizations and institutions in the communities we serve and in which we work.

Our company is committed to strengthening the diverse communities in which we do business and maintaining and attracting a work force rich in diverse thoughts, ideas and backgrounds. Our Employee Network Groups (Asia-American Community for Exelon Success, Exelon African-American Members Association, Exelon Pride, Network of Exelon Women, and Organization of Latinos at Exelon), are an integral part of Exelon's diversity strategy. Externally, they work to strengthen corporate citizenship by building ties to the communities in which we operate.

Through our corporate citizenship efforts, we develop partnerships with not for profit organizations, and seek to encourage employee volunteer involvement to support the Company's strategic objectives.

**Dear Friends:**

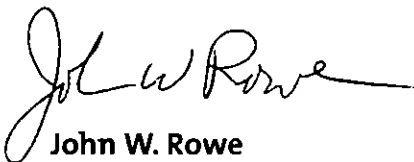
**It gives me great pride and pleasure to present you with Exelon's corporate citizenship brochure highlighting our commitment to the community.**

**As one of the nation's largest utilities, it's our business to make sure our customers and key constituents can depend on us to do more than keep the lights on. That's why we have nurtured a culture of community involvement at all levels of our organization. In addition to serving the community, these activities provide valuable experience and enhance morale and teamwork among our most important resource – our employees. Their personal commitment to community service is a great source of pride.**

**Our senior management team and other employees serve on numerous charitable boards throughout the Chicago and Philadelphia areas. Our generating stations also contribute at the local level in ways as individualized as the communities they serve. Through the company's Employee Network Groups, we're able to mirror the diversity of the communities we serve. Among the causes that benefit from our hands-on involvement are the arts, education, the environment and community development.**

**As chairman and CEO of Exelon, I am honored to serve our customers, shareholders, employees, community members and other stakeholders. I thank our community partners for allowing us to play such a significant role. We shall remain firmly committed. That's our promise; that's our way.**

**Sincerely,**

A handwritten signature in black ink that reads "John W. Rowe". The signature is written in a cursive, flowing style.

**John W. Rowe  
Chairman and CEO**

# ENERGY FOR EDUCATION

Our company has a long history of supporting education. We believe it is the foundation of a healthy community. Education is also the best tool for children and young adults to realize their full potential and have access to a range of career opportunities. Our investments in education are investments in the future of our communities and company. We support lifelong programs that encourage students to stay in school; promote math and science education through partnerships with area schools; enhance work force skills; and foster personal and professional development through scholarships, mentoring and internships. Below are a few highlights of our many educational initiatives.

## **FIRST Robotics**

To inspire the next generation of engineers and scientists, our company sponsored the FIRST Robotics Competition. This multinational program brings together professionals and young people to solve an engineering design problem in a competitive, hands-on environment. The FIRST Robotics Competition gives young people a chance to experience the exciting opportunities associated with careers in science, math and engineering. In addition to funding the FIRST program, we also support the Upper Darby High School Robotics team, and applaud their successes as winners of the prestigious Chairman's Award and several design awards.

## **Exelon Stay In School Program**

In partnership with the United Way, our company is piloting the Exelon/United Way Stay in School program to keep at-risk students in school. Beginning in the 2004-2005 school year, we will work with Chicago and Philadelphia-area communities to help reverse a disturbing trend in high school drop-out rates for African-American and Latino students. The desired outcome for Stay in School is very focused: a 100 percent high school graduation rate for program participants.

Stay in School will begin in the Chicago communities of Austin and Humboldt Park, North Philadelphia and the Philadelphia suburbs of Norristown and Chester. We are also working with the Chicago Park District to link this initiative with the Exelon Fellow environmental education program, especially with those projects in the Humboldt Park area.





### Chicago Public Schools Partnership

For many years, our company has supported the Chicago Public Schools (CPS).

As part of CPS's Futures Exchange program, we are the first company to underwrite participation in the Chicago Math and Science Initiative (CMSI). We sponsor Tanner Elementary, Piccolo Elementary, Audubon Elementary and Newberry Math & Science Academy with financial support, in-kind donations and employee volunteers.

The CMSI is a portfolio of programs that is transforming the way math and science are taught and supported throughout CPS – and that is helping more students become the engineers, scientists and mathematicians of tomorrow.

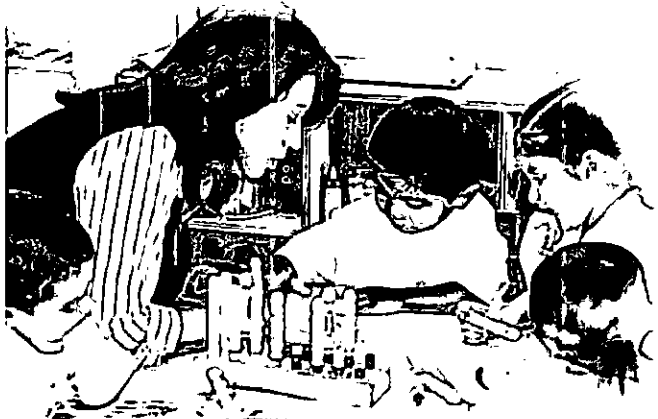
Additionally, by sponsoring the CPS Science Fair, we support 1,000 students in 28 high school science ComEd clubs that assist students in developing their ideas for science fair projects and research papers. These after-school clubs were designed to maintain students' interest in math and science throughout the school year.

### Philadelphia Academies

Among our most enduring grant relationships is the one we have with the Philadelphia Academy program, a partnership with the Philadelphia public school system designed to enhance academic and occupational skills for public school students.

Established in 1969 with our sponsorship of the first Academy of Applied and Electrical Science, the program now includes over 30 academies in 14 career areas at 20 of the city's high schools and two middle schools. Each school year, more than 8,000 students participate in an Academy program. Over the years, an average of 90% of graduates have been productively engaged in work or higher education, with well over half pursuing post-secondary education. With career focus that demonstrates the value of education to young people, the Academies' student attrition is much lower than the Philadelphia school-wide drop-out rate.

Since the outset, our employees have been actively involved at all levels: as board members, volunteers, mentors and professional development consultants.



### Matching Gifts for Education Program

The purpose of the Exelon Matching Gifts Program for Education is to encourage employee financial support for educational organizations. The Company will match one-for-one contributions made by eligible participants up to \$2000 per individual, per calendar year, for qualifying educational organizations.

Last year, the company made 802 matching gifts on behalf of 542 participating employees contributing \$242,000 to educational institutions.



# ENERGY FOR NEIGHBORHOOD DEVELOPMENT

To help strengthen communities and promote diversity, our company sponsors a variety of civic and cultural organizations, events, festivals and professional sports teams. We share business expertise and contribute financially through memberships in industry organizations, professional associations, local chambers of commerce and business organizations. We also support community-focused charitable organizations and promote employee volunteerism as well as executive involvement on not-for-profit community boards. We are proud to share with you a few examples of our efforts in the community.

## United Way

In partnership with our employees and retirees, our company has helped to provide community services and assistance for those in need by being an important long-term supporter of the United Way.

Our most recent United Way campaign was a resounding success. Of a total of \$5.1 million in contributions, employees and retirees gave over \$3 million and the company gave over \$2 million. These gifts were dispersed to over 600 United Way partner agencies to help those in need.

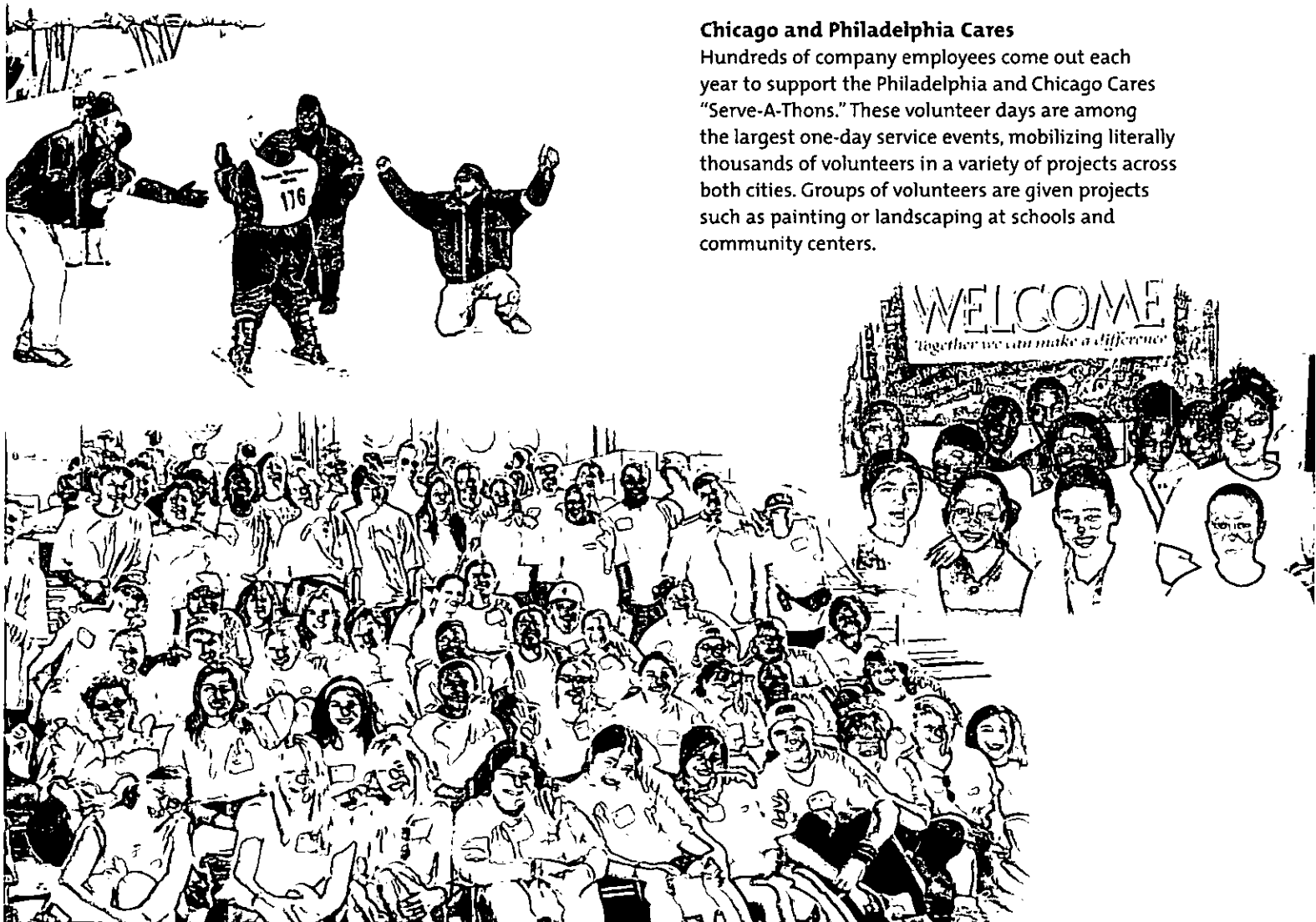
## PECO Hometown Heroes

Teaming with the National Football League's Philadelphia Eagles, we have been participating in the PECO Hometown Heroes program since 2001. The program recognizes individuals for their commitment to improving life in their communities.

Past recipients have been volunteer leaders in a range of grassroots activities, from feeding homebound individuals, to providing programs for at-risk youth, to helping arrange vacation trips for terminally ill patients and their families. Winners receive Eagles tickets and souvenirs, and a financial contribution from our company to support their causes.

## Chicago and Philadelphia Cares

Hundreds of company employees come out each year to support the Philadelphia and Chicago Cares "Serve-A-Thons." These volunteer days are among the largest one-day service events, mobilizing literally thousands of volunteers in a variety of projects across both cities. Groups of volunteers are given projects such as painting or landscaping at schools and community centers.





### **PECO Women's Empowerment Partnership**

Through the Women's Empowerment Partnership and the Mayor of Philadelphia's Office of Community Services Workwise Program, company employees continue to provide life-skills and mentoring services to women in the Delaware Valley. Through this partnership, we have also joined forces with the National Coalition of 100 Black Women to expand the benefits of mentoring to more women. Our employees provide guidance and support to improve participants' decision-making skills, self-confidence and the balance of family obligations and work responsibilities. Our commitment to helping people contribute productively to society and lead fulfilling careers and lives continues with the opening of the PECO Power Readiness lab, a state-of-the-art computer lab designed for job research and computer literacy. Our company will continue to support other similar projects throughout our service territory.

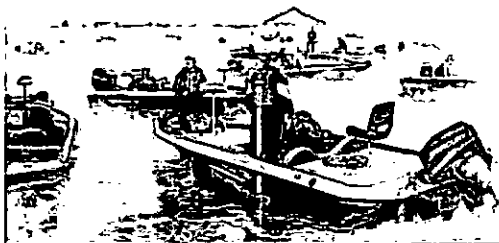
### **Fishing For A Cure**

Since its inaugural year, the Fishing for a Cure tournament, at Braidwood Lake adjacent to an Exelon generating station, has continued to grow in popularity. Each year, the tournament raises money for a new local charitable cause. Our most recent event raised more than \$13,000 for teen suicide prevention. Last year's tournament raised \$7,500 for the Cystic Fibrosis Foundation's Chicago Chapter.

Our company underwrites the costs for the tournament; therefore, 100 percent of the entry fees goes to the sponsored charity. Additional money is raised through raffles and silent auctions.

### **El Valor**

For the past 25 years, the company has partnered with El Valor, a community-based organization that works with 3,000 of Chicagoland's most needy families. El Valor was established more than 30 years ago with the goals of becoming a model of excellence for the inclusion of disabled people; a leader in early childhood development education for families in need; and the foremost U.S. organization for developing Latino leadership. El Valor is also among the nation's top 12 Hispanic-serving nonprofit organizations, and a partner in the White House initiative on Educational Excellence for Hispanic Americans. In addition to providing financial support and donating space for childcare programs, we have served the organization in a number of capacities, such as volunteering on the board of directors, assisting in management systems development and implementing innovative programs for the disabled.



### **Employee Volunteerism**

The company's volunteer program is an expression of our commitment to contribute time, skills and talent in the communities where employees live and work. Through "Energy For The Community", the Exelon Employee Volunteer Network, our employees develop leadership and teamwork skills, and put a personal face on our corporate citizenship activities. The program engages employees from all parts of the company, and recognizes and celebrates the importance of their efforts in building relationships with customers and constituents. From supporting company-sponsored events, serving as mentors, to helping at homeless shelters, our employees are out front in the community.



# ENERGY FOR ARTS & CULTURE

Supporting the social and cultural fabric of our communities is an essential component of our corporate citizenship program. Arts and cultural institutions are the hallmarks of world-class cities – attracting business, talented people and tourism. We are committed to supporting and nurturing these institutions. As part of our commitment to promoting diversity, we also dedicate significant resources to multicultural programs in Philadelphia and Chicago, as well as sponsor programs free to the public. This provides access to the arts for those who might not otherwise have the opportunity. We believe this helps develop new audiences and broadens access to the arts and culture for all citizens. Below are some examples of our range of activities in arts and culture.

## **Splendors of China's Forbidden City: The Glorious Reign of Emperor Qianlong**

Exelon served as the title sponsor of the Field Museum of Chicago's exhibit, Splendors of China's Forbidden City: The Glorious Reign of Emperor Qianlong. This tribute to the final flourishing of Imperial China and the man who guided its growth featured nearly 400 treasures borrowed from Beijing's Palace Museum, formerly called the Forbidden City. Most of the objects had never been seen outside of the palace compound.

Our Asian American group hosted 5th grade campers from the Chicago Park District for a day of Asian cultural activities such as a Chinese Lion Dance performance and a tour of the Forbidden City exhibit.

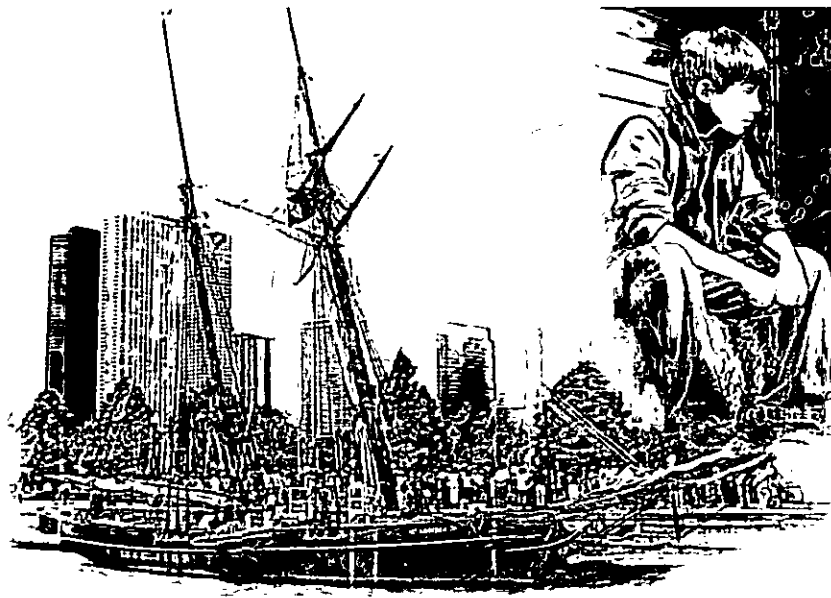
## **PECO Primate Reserve**

In partnership with the Philadelphia Zoo, our company sponsors the PECO Primate Reserve. The facility features spacious indoor and outdoor viewing areas where visitors can learn about and view gorillas, orangutans and other species. The Zoo recognized PECO President Denis O'Brien for the company's leadership in rebuilding the facility following a tragic fire, and for increasing public awareness of the value in preserving wildlife and protecting endangered species.

## **The Joffrey Ballet**

For several years, the company has supported one of Chicago's cultural gems and one of the world's premier ballet companies, the Joffrey Ballet. Since the ballet company moved to Chicago from New York, Exelon has been one of its key corporate supporters. Through our leadership, the company is helping the Joffrey with critical issues such as financial stabilization, increased board membership, and building a strong organizational structure that will provide a base from which the dance company will be able to grow.





An Exelon Company

### DuSable Museum

ComEd and the DuSable Museum of African American History, we sponsored the Freedom Schooner Amistad during Chicago's 2003 Tall Ships Festival. The Amistad is a re-production of the vessel La Amistad, which was the scene of an historic event that led to the first court ordered freeing of slaves in the United States. Through the sponsorship, thousands of people had the opportunity to tour the schooner at Chicago's Navy Pier to learn about this symbol of American history.

### GIANTS: African Dinosaurs

To help visitors learn valuable lessons about prehistoric times, ComEd, in partnership with the Chicago Park District, sponsored the exhibit GIANTS: African Dinosaurs at Chicago's Garfield Park Conservatory.

This dramatic exhibit, created by Project Exploration, featured gigantic skeleton replicas of dinosaurs – including the first flying reptile from Africa – and aligned with our strong commitment to education and science-based training. Hundreds of school groups throughout Chicagoland were treated to special educational programs and field trips to the Conservatory.



### Performing Arts Sponsorships

The company supports a number of theatres in the Chicago and Philadelphia areas which are committed to educational and community outreach. We partner with the People's Light and Theatre Company (Malvern, PA) to sponsor a Family Discovery Series production, which invites 3,300 family subscribers and 6,000 elementary and middle school students to experience and explore theatre together. We are also the official lighting sponsor for the Chicago Shakespeare Theatre and support Team Shakespeare, an educational outreach program that enables approximately 50,000 students a year to experience the works of the classic playwright.



# ENERGY FOR THE ENVIRONMENT

Exelon is deeply committed to improving the environment in which we all live and work, and to preserving it for generations to come. Everyone's quality of life depends on how well we care for our shared environment. Exelon supports organizations and initiatives that protect and improve the environment and preserve biodiversity. Our efforts focus on promoting environmental education, conservation and preservation; developing cleaner sources of energy; protecting endangered species; and beautifying neighborhoods. We've highlighted a few examples of our environmental initiatives below.

## TreeVitalize Program

In partnership with the Pennsylvania Department of Conservation and Natural Resources and other environmental groups, we are helping to reverse the negative effects of tree loss through our joint TreeVitalize program.

During a four-year period beginning in 2004, this program hopes to replace 5 million trees lost to development in the Philadelphia five-county region. This major tree-planting initiative will help reverse negative trends, such as lower air quality, increased storm water runoff and higher energy costs.

## Exelon Fellow

The Exelon Environmental Fellowship was created in 2002 under a unique private-public partnership between our company and the Chicago Park District to pioneer a new curriculum and teaching approach for Chicago Public School students in science and math. The goal is to establish a new experiential

approach to science while providing students with innovative and creative opportunities to study the environment around them and nurture their conservation skills.

## The Nature Conservancy

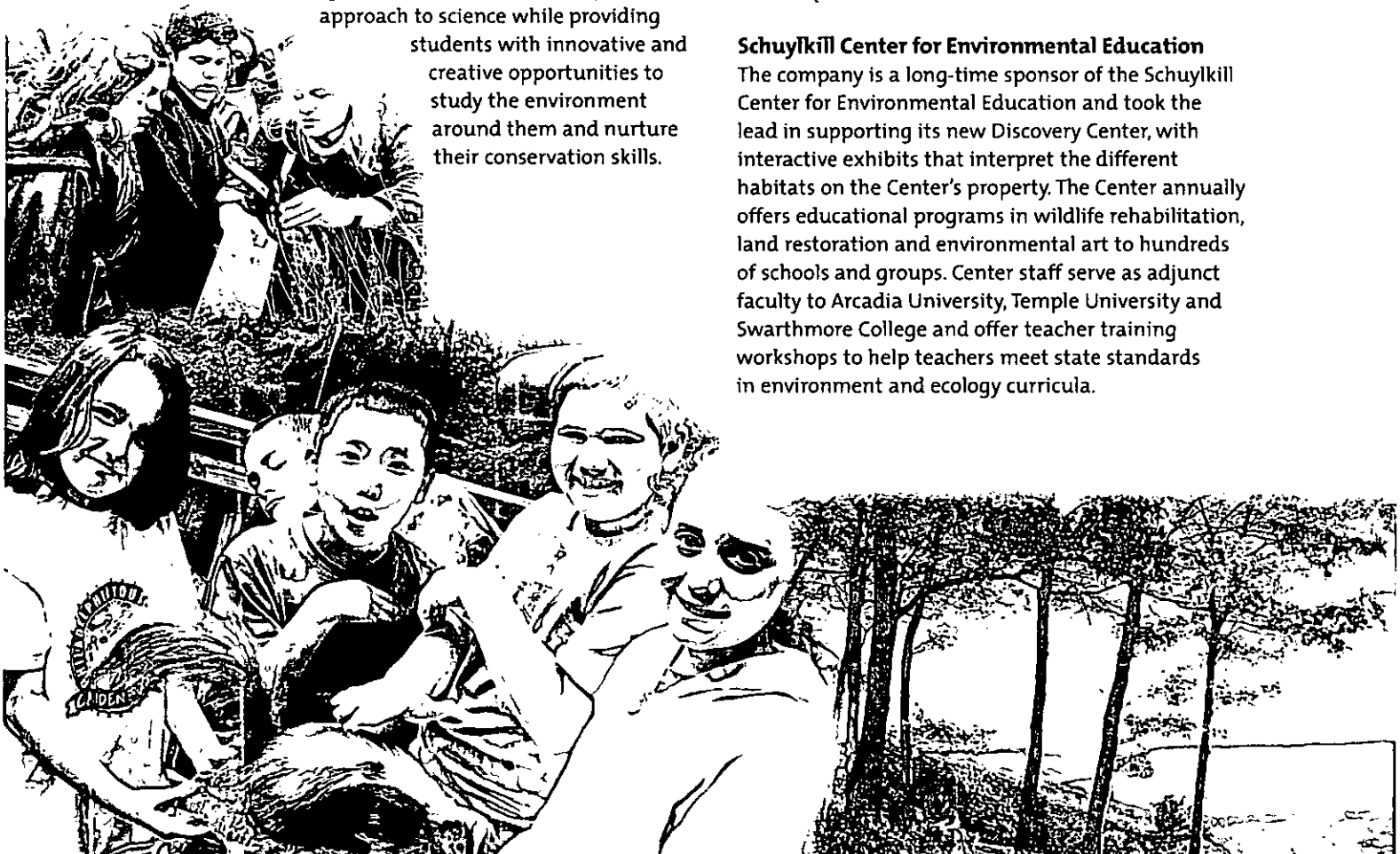
To help preserve water in Illinois and Pennsylvania, our company supports two key initiatives of The Nature Conservancy, an organization dedicated to "preserving the plants, animals and natural communities that represent the diversity of life on Earth by protecting the lands and waters they need to survive."

Our company is donating \$1 million over four years to restore and protect two challenged natural areas: Emiquon in central Illinois and the West Branch Wilderness in north central Pennsylvania.

Emiquon, a 7,000-acre wetland along the Illinois River, is one of the largest restoration efforts of its kind in the United States. The West Branch Wilderness area, a 3,000-acre tract of land on the Central Appalachian and the Allegheny Plateau eco-regions, is critical for the preservation of native species of plants and animals and contributes clean water to the Susquehanna River.

## Schuylkill Center for Environmental Education

The company is a long-time sponsor of the Schuylkill Center for Environmental Education and took the lead in supporting its new Discovery Center, with interactive exhibits that interpret the different habitats on the Center's property. The Center annually offers educational programs in wildlife rehabilitation, land restoration and environmental art to hundreds of schools and groups. Center staff serve as adjunct faculty to Arcadia University, Temple University and Swarthmore College and offer teacher training workshops to help teachers meet state standards in environment and ecology curricula.



# ENERGY TO REMAIN COMMITTED

We are proud that the company plays such an important role in our communities and in the lives of those we touch. While these results are reward enough, the company is also honored to have received formal recognition from many of our community partners. This recognition includes the following:

- The Spirit Award from the Chicago Urban League
- The Community Service Award from the Urban League of Philadelphia
- The Community Pillar Award for Volunteerism from the United Way
- The Leadership Summit and Diversity Award from Diversity Best Practices
- The Executive Leader Award from the Association of Fundraising Professionals
- The World of Difference Award from the Anti-Defamation League

The following is a representative list of nonprofits, not mentioned previously, with whom our company has worked on successful community partnerships. We value our relationships with all of our community partners and are not able to acknowledge all of them here.

## Energy for Education

- After School Matters
- Big Shoulders Fund
- Center for Adult & Experiential Learning
- Chicago State University
- Daniel Murphy Scholarship Foundation
- DePaul University
- Drexel University
- Free Library of Philadelphia
- Howard University
- Illinois Institute of Technology
- Junior Achievement of the Delaware Valley
- Merit School of Music
- Northwestern University
- Pennsylvania Statewide Latino Coalition
- Roosevelt University
- United Negro College Fund
- The University of Illinois at Chicago
- University of Chicago

## Energy for Arts and Culture

- Adler Planetarium
- African American Museum in Philadelphia
- Arden Theatre Company
- Arts and Business Council of Chicago and Greater Philadelphia
- The Black Ensemble Theatre
- Broadway in Philadelphia
- The Chicago Children's Museum
- The Chicago Historical Society
- Chicago Lyric Opera
- Chicago Symphony Orchestra
- The DuSable Museum of African-American History
- eta Creative Arts Foundation
- The Goodman Theater
- Greater Philadelphia Cultural Alliance
- The Institute of Puerto Rican Arts and Culture
- Lights of Liberty Show
- Lincoln Park Zoo
- The Lookingglass Theatre
- Main Line Arts Center's Children's Arts Festival
- Mann Center for the Performing Arts
- The Mexican Fine Arts Museum
- Painted Bride Arts Center
- Pennsylvania Ballet
- Ravinia Festival
- Shedd Aquarium
- Steppenwolf Theatre Company
- Taller Puertorriqueno
- Urban Gateway Center for Arts Education

## Energy for Neighborhood Development

- Access Living of Metropolitan Chicago
- Abraham Lincoln Centre
- The Aids Foundation
- Asian American Women's Coalition
- Big Brothers/Big Sisters Association of Philadelphia
- Boys and Girls Clubs
- Boy Scouts of America
- Chicago Community Trust
- Chicago Foundation for Women
- Chicago Urban League
- Chinese American Service League
- Dawn Staley Foundation
- Delaware Valley Habitat for Humanity
- Girl Scouts of America
- Greater Philadelphia Urban Affairs Coalition
- Hull House
- Metropolitan Family Services
- Partnership CDC
- Philadelphia Opportunities Industrialization Center
- Spanish Coalition for Jobs
- United States Hispanic Leadership Institute
- Urban Genesis "Crime and Drug Free That's Me" program with the Philadelphia District Attorney's Office
- Women's Business Development Center
- YMCA/YWCA

## Energy for the Environment

- Bucks County Audubon Society
- Chicago Park District
- Chicago Wilderness
- Fairmount Park Association
- Friends of the Parks
- Green Valleys Association
- Lower Merion Conservancy's Children's Earth Day Forest
- Openlands
- Peggy Notebaert Nature Museum
- Resources for the Future
- WXPN "Kid's Corner" environmental education programs



*Learn more about our  
commitment to corporate citizenship at  
[www.exeloncorp.com](http://www.exeloncorp.com).*

**Exelon**  SM

## CORPORATE CONTRIBUTIONS GUIDELINES

### Eligible Organizations

The company considers requests from organizations that are tax-exempt under sections 501(c)(3) of the U.S. Internal Revenue Code or other comparable tax-exempt organizations. Applicant organizations must also have offices primarily in the Exelon service areas in Illinois and Pennsylvania, or within a 25 mile radius of our generating stations.

### Ineligible Organizations

As a matter of policy, we do not accept requests from the following:

- Organizations and programs outside of the company's service area;
- Individuals;
- General operating endowments or memorials;
- Political, labor, fraternal, social or veterans organizations, or religious organizations or endeavors, unless the program benefits a large, non-denominational segment of the community;
- Medical programs;
- Organizations that discriminate for any reason;
- Fundraising events such as telethons;
- International organizations; or
- Advertising underwriting.

Due to the large number of requests we receive, the company will be unable to respond to grant status inquiries. If your request is under consideration, the company may ask for additional materials to support your request. Funding renewals are not automatic and cannot be guaranteed.

### Types of Grants

Grants are generally awarded for one year and do not necessarily imply a commitment for further support. However, the contributions committee will consider funding projects for longer periods of time – up to three years – with annual project updates.

## CORPORATE CONTRIBUTIONS GUIDELINES

### Application Process

The company accepts contribution requests from qualified organizations throughout the year. Our Corporate Citizenship Review Committee meets to review proposals on a bi-monthly basis, typically in February, April, June, August, October and December. Applicants will be notified in writing of the committee's decision within two weeks of the meeting. The process may include an on-site visit by a company representative.

All proposals should include the following information:

- Name and brief history of the organization;
- Primary contact, title, address, phone number, fax and current tax payer identification number;
- Letter verifying 501(c)3 status;
- List of current board members and their affiliations;
- Purpose and amount of grant being sought; and
- Major funding sources during the last year.

### Requests can be submitted to:

*For Exelon and ComEd:*  
Corporate Contributions Manager  
Exelon/ComEd  
440 South LaSalle, Suite 3300  
Chicago, IL 60605

*For PECO Energy:*  
Corporate Contributions Manager  
PECO Energy  
2301 Market Street S14-1  
Philadelphia, PA 19103

*For Exelon Generation:*  
Corporate Contributions Manager  
200 Exelon Way, Suite 340  
Kennett Square, PA, 19348

**STATE OF NEW JERSEY  
BOARD OF PUBLIC UTILITIES**

**In The Matter Of The Joint Petition Of  
Public Service Electric And Gas Company  
And Exelon Corporation  
For Approval Of A Change In Control Of  
Public Service Electric And Gas Company,  
And Related Authorizations**

**DIRECT  
TESTIMONY**

**OF**

**RALPH IZZO**

**JP-3**

**DIRECT TESTIMONY  
OF  
RALPH IZZO**

1  
2  
3  
4  
5  
6 **Q. Please state your name and your current position.**

7  
8 **A.** My name is Ralph Izzo, and I am the President and Chief Operating Officer  
9 (“COO”) of Public Service Electric and Gas Company (“PSE&G”).

10  
11 **Q. What is the purpose of your testimony?**

12  
13 **A.** My testimony describes how, following the proposed Merger of Public Service  
14 Enterprise Group Incorporated (“PSEG”) into Exelon Corporation (“Exelon”),  
15 PSE&G will continue to provide safe, adequate and reliable electric and gas  
16 service at reasonable rates. I will address the issue of how PSE&G will  
17 continue to be managed locally, including my role as President and COO of  
18 PSE&G after the Merger. Additionally, I will explain how, following  
19 consummation of the proposed Merger, PSE&G will continue to support the  
20 State’s energy objectives in, among others, the areas of energy efficiency,  
21 Smart Growth, low-income customer assistance and community involvement.

22

1 **Q. Please describe your professional background and community**  
2 **involvement.**

3 **A.** I was elected President and COO of PSE&G effective October 18, 2003. Prior  
4 to that time, I served as PSE&G's Senior Vice President – Utility Operations.

5 Since joining PSE&G in 1992, I have been elected to several senior  
6 executive positions of increasing responsibility within the PSEG family of  
7 companies, including Vice President – Appliance Service with PSE&G; Vice  
8 President - Corporate Planning for PSEG Services Corporation; Senior Vice  
9 President – Finance and Information Services with Energis Incorporated; and  
10 Vice President - Electric Ventures, PSE&G. In these capacities, I have  
11 developed broad experience in the areas of general management, strategic  
12 planning and finance.

13 Prior to joining PSE&G, I served as an American Physical Society  
14 Congressional Science Fellow, in the office of U.S. Senator Bill Bradley. I  
15 also served for four years as a senior policy advisor in the Office of New  
16 Jersey Governor Thomas H. Kean, specializing in energy, science and  
17 technology.

18 I began my career as a research scientist at the Princeton Plasma Physics  
19 Laboratory, and have published or presented over 35 papers related to my work  
20 in fusion energy. I received Bachelor of Science and Master of Science  
21 degrees in mechanical engineering, and a Doctor of Philosophy degree in

1 applied physics from Columbia University. In August 2002, I completed the  
2 requirements for a Master of Business Administration degree, with a  
3 concentration in finance from the Rutgers Graduate School of Management.

4 I am chairman of New Jersey After 3 Inc., and serve on the Board of  
5 Directors for the Electric Power Research Institute, the New Jersey Chamber of  
6 Commerce, the American Gas Association, the New Jersey Performing Arts  
7 Center and the New Jersey Utilities Association. I serve on the Board of  
8 Trustees for the Partnership for a Drug-Free New Jersey, Independent College  
9 Fund of New Jersey, and the New Jersey Network Foundation. I also serve as  
10 co-chair of the Drumthwacket Foundation, a member of the Rutgers Business  
11 School Board of Trustees, and electric utility sector chairman of the  
12 Infrastructure Advisory Committee in the Attorney General's Office of  
13 Counter-terrorism.

14  
15 **Q. Please describe the impact of the Merger on PSE&G's provision of safe**  
16 **and reliable service.**

17  
18 **A.** The Merger should enhance PSE&G's ability to render safe and reliable  
19 service as a result of local management having access to an energy delivery  
20 organization of a much larger scale and geographic scope.

21 After the Merger is consummated, utility operations at PSE&G will  
22 continue to be managed at the local level, that is, by PSE&G's New Jersey

1 management. I will continue as President and COO of PSE&G, having day-to-  
2 day responsibility for safe, adequate, efficient and effective operation by  
3 PSE&G of its electric and gas systems in New Jersey. I will have all necessary  
4 authority and resources to ensure the continued provision by PSE&G of safe  
5 and adequate service. In addition, by accessing the experience and skills  
6 available throughout the larger Exelon organization, PSE&G will be able to  
7 share “best practices” with Exelon’s other distribution utilities. This sharing of  
8 knowledge and experience should result in improved, more efficient and  
9 effective work practices throughout the Exelon organization, including here in  
10 New Jersey.

11 I can assure the Board that PSE&G’s commitment to customer and  
12 employee safety will remain of paramount importance. If a company can work  
13 safely, then its customers and the community at large are benefited. Following  
14 consummation of the Merger, PSE&G will continue to invest in the equipment,  
15 training, and staffing, and will continue to apply the management focus  
16 necessary, to maintain top safety and reliability performance into the future.  
17 Consistent with Exelon’s goals and objectives, we will strive to remain among  
18 the very best electric and gas delivery companies from a safety perspective. I  
19 note in this regard that PECO has an excellent track record of safety  
20 performance.

1 PSE&G's commitment to reliability is reflected in its hard work and  
2 documented results when benchmarked against its peers. Compared to utilities  
3 in the region, PSE&G's reliability indices ranked in the top and second quartile  
4 for the period 2000-2003. As with our safety commitments, this type of  
5 performance will continue to be PSE&G's goal post-Merger, and Exelon is  
6 committed to ensuring that sufficient financial and workforce resources are  
7 provided to maintain high service standards while appropriately managing  
8 costs.

9  
10 **Q. Please discuss further the financial and operational benefits to PSE&G's**  
11 **customers that will be derived from the Merger.**

12  
13 **A.** The proposed Merger will create a company with substantial resources and  
14 capabilities. The ability to leverage the capabilities of a larger organization is  
15 an exciting prospect for us and our customers. Among other things, Exelon  
16 brings to the table enhanced financial support that the increased scale and  
17 scope of a larger entity can provide.

18 The Merger creates a larger and more diverse electric and gas  
19 distribution base. This increased scale and scope and diversification is  
20 expected to maintain or improve service and reliability. The ability to share  
21 many best practices and systems, and draw upon the combined intellectual  
22 capital of the talent pool, will be particularly helpful in the areas of enhanced

1 systems and customer care, and should result in increased customer  
2 satisfaction. Sharing of best practices in the metering and new technologies  
3 arena will also bring new opportunities to our customers. The responsibility  
4 for day-to-day decision-making will remain with PSE&G. This will ensure  
5 that the service to our customers is not affected by the increased size of the  
6 company. However, the combined intellectual talent pool will provide  
7 improved problem solving capabilities and improved operations.

8  
9 **Q. How will the Merger impact PSE&G'S infrastructure investment plans?**

10  
11 **A.** While exploring all opportunities to improve efficiency and leverage the  
12 capabilities of the larger organization, PSE&G is committed to continuing to  
13 invest in and maintain its electric and gas distribution infrastructure in New  
14 Jersey. Investments will continue to be made in order to improve the long term  
15 performance of our electric and gas infrastructure.

16  
17 **Q. How will the Merger impact the cost of PSE&G's electric and gas  
18 distribution system operations?**

19  
20 **A.** As discussed in the testimony of William Arndt, Exelon's Senior Vice  
21 President, Financial Operations, the Merger will enable PSE&G to reduce the  
22 costs of its electric and gas delivery operations below what they otherwise  
23 would be absent the Merger. This reduction in PSE&G's future costs will

1 reduce the amount of any future rate relief required by the utility, thereby  
2 providing a direct benefit to customers. These savings will occur through  
3 some reductions of duplicative job functions, but will not adversely affect our  
4 field forces or our ability to perform operational or maintenance functions  
5 essential to providing high quality and safe delivery services. The Merger will  
6 also provide for more efficient purchasing of goods and services, which will  
7 inure to the benefit of PSE&G customers.

8  
9 **Q. What effects will the Merger have on PSE&G employees?**

10  
11 **A.** PSE&G has approximately 6400 employees, of whom approximately 5000 are  
12 union employees. Exelon has acknowledged that PSE&G will continue to  
13 recognize all of the unions currently representing our employees, and all  
14 existing collective bargaining agreements with those unions will continue to be  
15 honored. PSE&G's represented employees will have the same collective  
16 bargaining rights and protections after the Merger as they had before the  
17 Merger. A benefit of the Merger is that PSE&G employees will have more  
18 opportunities in a larger, more competitive company.

19 It is clear that to achieve synergies, positions must be eliminated. As  
20 Mr. Arndt explains in his testimony, utility field service personnel will not be  
21 affected by the Merger, and there will be no adverse impact on utility

1 reliability, customer service, or safety. The impact of the Merger on the  
2 employees of the utilities, including PSE&G, will be in the areas of business  
3 unit management and back-office support. We intend to accomplish as many  
4 reductions as we reasonably can through attrition and voluntary retirements.  
5 Severance programs may also be utilized. Consideration of staffing issues will  
6 be on-going through the coming months, and it will take time to be certain that  
7 all possibilities are examined and the appropriate staffing implemented  
8 following the Merger. I will work to ensure that these targeted reductions will  
9 be accomplished in a seamless fashion that does not adversely impact the  
10 service quality, reliability, safety or customer care standards that our customers  
11 expect and presently receive. In fact, our goal is to provide additional benefits  
12 to customers by implementing additional best practices that will result in  
13 system improvements.

14  
15 **Q. How will customer service levels be maintained following the Merger?**

16  
17 **A.** PSE&G customers have come to expect excellent customer service. Indeed,  
18 PSE&G's excellent service and high marks for customer satisfaction are an  
19 important aspect of PSE&G's value, and the incentives to maintain that level  
20 of service will only increase following consummation of the Merger.

1           It is important to remember that, through our service and call centers,  
2 we have over six million contacts with customers in a year. We emphasize  
3 First Contact Resolution for all customer requests received by telephone, in-  
4 person visits and customer premise visits. Our research has shown that  
5 customers want their problems solved during their initial contact with PSE&G.  
6 Exelon will add additional best practices and technology to enhance these  
7 customer contacts and services.

8  
9 **Q. How will the Merger affect competition?**

10  
11 **A. TO BE SUPPLEMENTED.** PSE&G considers the New Jersey Basic  
12 Generation Service (“BGS”) auction to be a success, and will continue to  
13 participate in it. We will also continue to support all the Board’s policies  
14

1 regarding open access and retail competition. In addition, PSE&G will  
2 continue to adhere fully to all New Jersey codes of conduct and affiliate  
3 standards.

4  
5 **Q. What impact will the Merger have on PSE&G's electric and gas rates?**

6  
7 **A.** PSE&G's rates and the terms and conditions of service in effect prior to the  
8 Merger will not change as a result of the Merger. Going forward, and after  
9 costs-to-achieve are incurred, the Merger will generate economies, some of  
10 which will accrue to the New Jersey jurisdictional regulated businesses of  
11 PSE&G. Those economies will help offset the rise in the cost of providing  
12 reliable regulated electric and gas distribution service.

13  
14 **Q. Will PSEG's historical support for community and charitable activities be**  
15 **continued following the Merger?**

16  
17 **A.** Yes. PSE&G has worked hard in the communities in our service territory, and  
18 our focus on our communities will continue. Exelon has pledged to sustain the  
19 level of community and charitable involvement of both PSEG and PSE&G in  
20 New Jersey to levels that are at least as substantial as those of PSEG currently.  
21 This commitment is not idle speculation; indeed it is in the Merger Agreement  
22 between the two companies. The Merger Agreement indicates that those levels  
23 will remain unchanged for at least four years. John Rowe has stated in his

1 testimony that he expects to continue the charitable commitment to New Jersey  
2 at the same or higher levels than have been committed to in the past. The  
3 strength of the combined company will, over the long term, bring enhanced  
4 benefits to the people of the state.

5  
6 **Q. Will the Merger affect PSE&G's involvement in economic development?**

7  
8 **A.** Our success is closely tied to the continued well-being of the towns and cities  
9 of New Jersey. The PSE&G service territory is a heavily populated  
10 commercial and industrial area that encompasses most of New Jersey's largest  
11 municipalities.

12 It has been, and will continue to be, in PSE&G's and its customers'  
13 economic interest for PSE&G to support economic development in our service  
14 territory. We will continue to support the Board's Smart Growth initiative to  
15 promote development in areas designated for growth. Exelon supports this  
16 philosophy and has pledged continued support of these community efforts.

17  
18 **Q. Will the Merger affect any currently existing customer assistance**  
19 **programs?**

20  
21 **A.** PSE&G and its customers participate in various assistance programs such as  
22 LIHEAP, Lifeline, Universal Service Fund and NJ Shares. We have partnered  
23 with Payment Assistance Agencies by having representatives work directly

1 with our customers. These efforts will continue in conjunction with the Board  
2 and the participating social service agencies.

3  
4 **Q. Will the Merger affect PSE&G's commitment to the environment?**

5  
6 **A.** As is indicated in John Rowe's testimony, Exelon, like PSEG, has a strong  
7 environmental commitment. Mr. Rowe has pledged to continue PSEG's strong  
8 environmental record in New Jersey. In addition, Exelon has endorsed the  
9 Board's renewable portfolio standards and continued compliance with the  
10 Clean Energy Program initiatives. PSEG and Exelon are both members of the  
11 Clean Energy Group, a coalition of utilities that support enactment of  
12 comprehensive clean air legislation by the Congress, including support for the  
13 enactment of so-called "4-P" legislation that would provide the Environmental  
14 Protection Agency ("EPA") authority to regulate sulphur dioxide, nitrogen  
15 oxide, mercury, and carbon dioxide emissions.

16  
17 **Q. What action are you requesting?**

18  
19 **A.** As President and COO of PSE&G, I believe that the Merger is an exciting  
20 opportunity, and the Board should approve the Merger request. PSE&G strives  
21 to meet customer expectations of safe, reliable service, and through the Merger  
22 we will be able to access better training tools, enhanced financial resources,

1 technologies and intellectual support to help us satisfy these expectations. I  
2 firmly believe that New Jersey will benefit from the Board's approval of this  
3 transaction.

4

5 **Q. Does this conclude your testimony at this time?**

6

7 **A. Yes, it does.**

**STATE OF NEW JERSEY  
BOARD OF PUBLIC UTILITIES**

**In The Matter Of The Joint Petition Of  
Public Service Electric And Gas Company  
And Exelon Corporation  
For Approval Of A Change In Control Of  
Public Service Electric And Gas Company,  
And Related Authorizations**

**DIRECT  
TESTIMONY**

**OF**

**J. BARRY MITCHELL**

**JP-4**

1  
2  
3  
4  
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6

**DIRECT TESTIMONY  
OF  
J. BARRY MITCHELL**

7  
8  
9  
10  
11

**I. INTRODUCTION AND QUALIFICATIONS**

12 **Q. Please state your name and business address.**

13  
14 **A.** My name is J. Barry Mitchell. My business address is Exelon Corporation, 10  
15 South Dearborn Street, 37th Floor, Chicago, Illinois 60680-5379.

16  
17 **Q. What positions do you hold at Exelon Corporation (“Exelon”)?**

18  
19 **A.** I am the Senior Vice President, Treasurer and Business Unit Chief Financial  
20 Officer of Exelon.

21  
22 **Q. Please summarize your professional background and your experience in  
the utility industry.**

23  
24 **A.** I joined PECO Energy Company (PECO) as an analyst in the finance  
25 department in 1971 and progressed through various positions in finance and  
26 corporate planning until I was named Vice President and Treasurer in  
December 1994. In October 2000, Exelon Corporation was created as a result  
of the merger between PECO and Unicom Corporation, and I was named Vice  
President and Treasurer of Exelon. In April 2002, I was named Senior Vice  
President and Treasurer, and in September 2003, I was also named Business

1 Unit Chief Financial Officer. I am responsible for Exelon's financing  
2 activities, cash management operations, pension and other investment trusts,  
3 project evaluations, internal audit, corporate financial controls and business  
4 unit finance operations.

5 I also serve on the board of Energy Insurance Mutual and the advisory  
6 board of the Factory Mutual Insurance Company. I was graduated from  
7 Lehigh University in 1970 with a bachelor's degree in business administration  
8 and an MBA in finance in 1971. I am also a 1987 graduate of the Executive  
9 Development Program at the Darden School of the University of Virginia.

10  
11 **Q. What is the purpose of your testimony in this proceeding?**

12  
13 **A.** The purpose of my testimony is to (1) discuss the financial impact on Public  
14 Service Electric and Gas Company ("PSE&G") of the Merger and describe  
15 Exelon policies with regard to the credit of its regulated subsidiaries; (2)  
16 describe the purchase accounting required as a result of the Merger and the  
17 need to establish regulatory assets and liabilities related to fair value  
18 adjustments to PSE&G's pension and other post-retirement benefit ("OPEB")  
19 obligations, debt obligations, Basic Generation Service ("BGS") auction  
20 contracts and the Basic Gas Supply Service (BGSS) contract; (3) support the  
21 pro forma financial documents submitted with the Joint Petition; and (4)

1 support the request for approval to add PSE&G as a party to the Exelon Utility  
2 Money Pool Agreement (“Money Pool Agreement”).

3  
4 **II. FINANCIAL CONDITION AND POLICIES FOLLOWING THE MERGER**

5 **Q. Will the Merger have any adverse financial effect upon PSE&G or upon**  
6 **PSE&G’s ability to serve its customers?**

7  
8 **A.** No. The Merger of Public Service Enterprise Group Incorporated (“PSEG”),  
9 the parent of PSE&G, with Exelon will not have any adverse financial effect  
10 upon PSE&G or upon its ability to serve its customers. This is based upon the  
11 following facts:

- 12 • PSE&G will continue to be viewed by its creditors as a separate, stand-  
13 alone company with its own corporate identity;
- 14 • PSE&G will maintain a capital structure that will be adequate to finance its  
15 capital needs and provide the funds that will be appropriate to maintain  
16 safe, adequate and reliable service to its customers;
- 17 • PSE&G will continue to issue and service debt and preferred securities on a  
18 stand-alone basis;
- 19 • PSE&G will maintain separate credit ratings for its securities;
- 20 • PSE&G will maintain strong investment-grade ratings for its senior secured  
21 securities.

1 **Q. What will be done to ensure that PSE&G continues to be viewed as a**  
2 **separate stand-alone company with its own corporate identity?**

3  
4 **A.** PSE&G will be a separate subsidiary of Exelon's first tier subsidiary Exelon  
5 Energy Delivery Company, LLC ("Exelon Energy Delivery"), just as PECO  
6 and Commonwealth Edison Company ("ComEd") are currently maintained as  
7 separate subsidiaries of Exelon Energy Delivery. Much like its fellow  
8 affiliates in Pennsylvania and Illinois, PSE&G will maintain its separate  
9 corporate existence and brand name, and all electric and gas services will be  
10 provided to its customers under that name. In addition, secured debt and  
11 preferred securities that need to be issued to finance the operations of PSE&G  
12 will continue to be issued under the name and legal entity of PSE&G. All  
13 existing debt and preferred stock of PSE&G will remain the legal obligations  
14 of PSE&G.

15  
16 **Q. How will PSE&G's capital structure be determined?**

17  
18 **A.** PSE&G will maintain its own capital structure to provide funding to maintain  
19 safe, adequate and reliable service to its customers. The determination of the  
20 appropriate capital structure is based upon a number of different factors  
21 including business risk, financial results, and projections of financial operating  
22 results and cash flows including incremental capital investments to maintain  
23 safe, adequate and reliable service. All of these factors are weighed and

1 viewed in light of the industry risk factors to arrive at appropriate debt and  
2 equity levels.

3  
4 **Q. How will PSE&G be financed?**

5  
6 **A.** PSE&G should be able to meet its capital expenditure requirements with  
7 internal sources. To the extent it requires external funding, PSE&G will  
8 maintain a financial profile to enable it to access external financial sources at  
9 reasonable terms. PSE&G will continue to issue its own debt and preferred  
10 securities on a stand-alone basis. PSE&G will also continue to maintain its  
11 own access to revolving credit facilities and its own commercial paper  
12 program. In addition, PSE&G will join the Exelon Money Pool Agreement,  
13 which provides an additional source of low-cost, short-term financing. I  
14 describe the Money Pool Agreement in Section IV of my testimony.

15  
16 **Q. How will PSE&G be rated by the credit rating agencies?**

17  
18 **A.** PSE&G will continue to have separate credit ratings for its securities, which  
19 are currently at the A- level for PSE&G's senior secured securities. It is  
20 expected that following the Merger, PSE&G's rating will benefit from being  
21 associated with a parent company with stronger, more diversified cash flows  
22 and a strong commitment to solid investment-grade ratings. The forecasted

1 values for the key quantitative credit measures for PSE&G are consistent with  
2 the company's A- rating for its senior secured securities. The strong, stable  
3 cash flows from the combined entity plus Exelon's commitment to a solid  
4 investment grade rating will be beneficial to PSE&G and its customers.  
5 Standard & Poors ("S&P") in undertaking an analysis of the PSEG-Exelon  
6 Merger stated: "If the announced merger with Exelon is consummated, the  
7 credit quality of PSEG and its subsidiaries should benefit from anticipated  
8 synergies and from the company's incorporation into a larger entity with a  
9 stronger credit profile." Moreover, S&P stated that "[b]ut for the merger  
10 transaction, the corporate credit ratings assigned to the Enterprise family of  
11 companies, other than PSEG Energy Holdings, would be lowered to 'BBB-'  
12 and the outlook would remain negative...."<sup>1</sup> Moody's also affirmed the  
13 PSE&G credit ratings following the merger announcement.<sup>2</sup>

14  
15 **Q. What is your view of PSE&G's ability to continue to obtain financing and**  
16 **attract capital at reasonable costs?**

17  
18 **A.** The prospects for PSE&G's continued ability to access the capital markets and  
19 secure financing at reasonable rates are excellent. Exelon is committed to

---

<sup>1</sup> Standard & Poor's Ratings Services, "Research Update: Public Service Enterprise Group's, Subs' Ratings Placed on Watch Developing After Merger News" (December 20, 2004).

<sup>2</sup> See Moody's Investors Services, "Moody's Affirms Ratings of Public Service Enterprise Group and Subsidiaries Following Announcement of Planned Merger with Exelon Corporation; Revises Outlook for Enterprise Group and PSEG Power to Stable from Negative" (December 20, 2004).

1 maintain financial ratios for PSE&G that will provide a solid investment grade  
2 rating. As John W. Rowe states in his direct testimony, Exelon is committed to  
3 maintaining and, where possible, enhancing the high-quality service currently  
4 furnished by PSE&G. We will meet that commitment by ensuring that  
5 PSE&G has the financial strength and flexibility to make the investments  
6 necessary to meet its service obligations and continue to provide safe, adequate  
7 and reliable service to its customers.

8  
9 **III. REGULATORY ACCOUNTING REQUIREMENTS**

10 **Q. Please describe the regulatory and accounting requirements that are**  
11 **implicated by the Merger.**

12  
13 **A.** The Merger transaction will be accounted for using the purchase method of  
14 accounting, which means that there will be a one-time adjustment of the assets  
15 and liabilities of PSEG at the Merger date to reflect their fair market value as  
16 of that date. Based on current market conditions, this will result in an increase  
17 in the balance sheet liabilities for (1) PSE&G's pension and OPEB plans to  
18 reflect previously unrecognized, or deferred, gains and losses, prior service  
19 costs, and transition obligations, and (2) PSE&G's third-party debt, including  
20 transitional trust notes to reflect their fair market values. Additionally, PSE&G  
21 will be required to recognize the fair value of its BGS and BGSS contracts,  
22 which based on current market conditions would create a balance sheet asset.

1 Because these adjustments do not affect the cash flow obligations of PSE&G,  
2 they should not impact the rate recovery mechanisms that have historically  
3 been utilized to recover pension and post-retirement obligations, long-term  
4 debt costs and purchased power costs on a historical cost basis. Regulatory  
5 assets should be recorded to offset the purchase accounting adjustments for the  
6 pension, OPEB and debt liabilities and a regulatory liability for the BGS and  
7 BGSS contracts, to maintain the current rate making recovery provisions for  
8 these costs.

9  
10 **Q. Please describe the purchase accounting adjustment to PSE&G's pension**  
11 **and OPEB liabilities that will occur at the Merger consummation.**

12  
13 **A.** Pension and OPEB expenses are recorded in accordance with SFAS 87 –  
14 Employers' Accounting for Pensions and SFAS 106 – Employers' Accounting  
15 for Postretirement Benefits other than Pensions, respectively, pursuant to  
16 which certain transition obligations, actuarial gains and losses, and market  
17 gains and losses are recognized in the financial statements over an extended  
18 period of time. Under SFAS 87 and SFAS 106, when the unrecognized  
19 pension and OPEB costs as of a given point in time become recognizable in  
20 future periods, they are reflected in the financial statements through an  
21 adjustment to the balance sheet liability offset by a corresponding adjustment  
22 to pension and OPEB expense. The resulting pension and OPEB expense has

1 historically, in turn, been reflected in customer rates. However, at the time of  
2 the Merger, in accordance with the required application of purchase  
3 accounting, these previously incurred but unrecognized costs will become  
4 recognized immediately as an increase in the balance sheet liability as of the  
5 Merger date. Absent the recording of a regulatory asset, the offset would be an  
6 increase in goodwill, rather than pension and OPEB expense.

7  
8 **Q. Please describe why a regulatory asset is required to recover the**  
9 **previously unrecognized pension and OPEB costs from customers.**

10  
11 **A.** The Board of Public Utilities (“Board”) historically has provided for recovery  
12 of these transition obligations and net actuarial and market losses as they  
13 became recognized in the financial statements. However, as I just described,  
14 the increase in the liability at the Merger date will be recorded during purchase  
15 accounting with an offsetting increase in goodwill. Because pension and  
16 OPEB expenses associated with these previously unrecognized losses will not  
17 be recognized in PSE&G’s future financial statements and because goodwill is  
18 not amortized, pension and OPEB expense will be lower in future periods than  
19 it would have been absent the Merger by the amount of the currently  
20 unrecognized transition costs and net actuarial and market losses. This  
21 potential expense reduction would not be reflective of changing demographics  
22 or economic factors used in determining plan expenses and would not be

1 reflective of a reduction in funding requirements. It would solely be due to the  
2 fact that purchase accounting accelerates the timing of the financial statement  
3 recognition of the transition obligations and market and actuarial losses.  
4 Accordingly, reflecting this lower level of pension and OPEB expense in  
5 setting rates would have the effect of inappropriately releasing customers of  
6 their obligation to pay for these amounts on a deferred basis consistent with  
7 present practice and would deprive PSE&G of a significant source of cash flow  
8 necessary to assure the plans will be adequately funded. The creation of a  
9 regulatory asset in accordance with the requirements of SFAS 71 "Accounting  
10 for the Effect of Certain Types of Regulation" is necessary to maintain  
11 PSE&G's current mechanism for recovery of the unrecognized and  
12 unrecovered amounts in future rate-setting processes.

13  
14 **Q. Did PSE&G record a regulatory asset for any unrecognized pension**  
15 **and/or OPEB liability at the time the pension and OPEB accounting**  
16 **requirements were implemented?**

17  
18 **A.** No. The net amount recognized for PSE&G pension and OPEB liabilities, in  
19 the absence of purchase accounting, only required footnote disclosure of the  
20 unrecognized amounts in the notes to the PSE&G financial statements.  
21 Purchase accounting, necessary at the time of the Merger, requires that all

1 assets and liabilities be restated at their fair value. That value must be  
2 recognized on the balance sheet.

3  
4 **Q. What are the implications of the creation of a regulatory asset in future**  
5 **rate-setting processes?**

6  
7 **A.** Recording a regulatory asset to offset the recognition of the previously  
8 unrecognized amounts simply maintains the status quo for rate-setting  
9 purposes. The approval and recording of a PSE&G regulatory asset ensures  
10 that plan expenses in future rate-setting proceedings will be in total identical to  
11 the amount that customers' rates would have supported had the Merger not  
12 taken place. In no event will PSE&G recover from customers pension and  
13 OPEB expenses pursuant to this treatment greater than the pension and OPEB  
14 expenses that would have been recorded in accordance with SFAS No. 87 and  
15 SFAS No. 106, absent this Merger.

16  
17 **Q. Please describe the impact of the application of purchase accounting to**  
18 **PSE&G's third-party debt.**

19  
20 **A.** PSE&G's third-party debt issuances, including transition bonds, will also be  
21 adjusted to reflect their fair market value as of the Merger closing date. Based  
22 on current market rates, we expect that the result will be an increase in the  
23 long-term debt obligations on PSE&G's balance sheet. This increased liability

1 will be amortized to income over the remaining term of each respective debt  
2 issuance, resulting in an effective interest rate that is consistent with market  
3 rates at the time of the Merger closing date, rather than the historical coupon  
4 rate.

5  
6 **Q. Why is it necessary to record a regulatory asset related to the fair value**  
7 **adjustment of the third-party debt?**

8  
9 **A.** The regulatory asset allows PSE&G to maintain current regulatory treatment of  
10 its third party debt. The fair value adjustment does not change the cash interest  
11 costs that PSE&G is obligated to pay - PSE&G will still be obligated to pay  
12 interest to bondholders and other creditors based on the historical cost of the  
13 debt. Consistent with the Board's past practice of cost-based ratemaking, the  
14 capital structure used for ratemaking purposes should reflect the historical cost  
15 and amounts of the third-party debt. In accordance with the requirements of  
16 SFAS 71, a regulatory asset will be recorded to offset the fair market value  
17 adjustment of the debt. When recorded, this regulatory asset will be amortized  
18 in an amount equal to the amortization of the fair market value adjustment to  
19 the liability. There will be no net income impact of these two amortizations as  
20 they offset each other.

21

1 **Q. Please describe the impact of the application of purchase accounting to**  
2 **PSE&G's BGS and BGSS contracts.**

3  
4 **A.** PSE&G's BGS and BGSS contracts will also be adjusted to reflect their fair  
5 market value as of the Merger closing date. Based on current market energy  
6 costs, we expect that the result will require the creation of an intangible asset  
7 on PSE&G's balance sheet. This intangible asset will be amortized over the  
8 remaining term of each respective contract, resulting in an effective purchased  
9 power rate that is consistent with market rates at the time of the Merger closing  
10 date, rather than the historical contractual rate.

11  
12 **Q. Why is it necessary to record a regulatory liability related to the fair value**  
13 **adjustment of the BGS & BGSS contracts?**

14  
15 **A.** The regulatory liability allows PSE&G to maintain current regulatory  
16 treatment of its BGS and BGSS contracts. The fair value adjustment does not  
17 change the cash energy costs that PSE&G is obligated to pay. PSE&G will  
18 still be obligated to pay suppliers for purchased electric and gas supply based  
19 on the contractual costs of the power. The operating costs for ratemaking  
20 purposes will continue to reflect the actual cost of the purchased power  
21 contracts. In accord with the requirements of SFAS 71, a regulatory liability  
22 will be recorded to offset the fair market value adjustment of the BGS and

1 BGSS contracts. The regulatory liability will be amortized in an amount equal  
2 to the amortization of the fair market value adjustment to the intangible asset.

3

4 **Q. What is the amount by category of the regulatory asset and liability that**  
5 **will be recorded?**

6

7 **A.** The fair market valuation of the assets and liabilities will occur at merger  
8 closing and, therefore, the exact amounts of the regulatory assets and liabilities  
9 will not be know until that time. Estimates based on fair market values as of  
10 September 30, 2004 are as follows:

11

12

13

	<u>Amount</u> (Millions)
<u>Regulatory Assets:</u>	

14

Unrecognized Pension and OPEB Liabilities	\$1,100
---	---------

15

Third Party Debt Obligations	\$ 350
------------------------------	--------

16

<u>Regulatory Liabilities:</u>	
--------------------------------	--

17

BGS/ BGSS Power Purchase Contract	\$ 750
-----------------------------------	--------

18

19 **Q. Will there be any goodwill reflected on PSE&G's financial statements in**  
20 **connection with the merger?**

21

22 **A.** Yes. In accordance with GAAP, the impacts of purchase accounting will be  
23 reflected on the PSEG subsidiary financial statements. It is currently estimated  
24 that approximately \$4,000 million of Goodwill will be recorded on PSE&G's

1 balance sheet, although this amount is preliminary and the ultimate amount  
2 recorded will be reflective of fair market valuations as of the merger closing  
3 date.

4  
5 **IV. PRO FORMA FINANCIAL DOCUMENTS**

6 **Q. Have you prepared any pro forma financial documents that represent the**  
7 **financial position of the merged corporation?**

8  
9 **A.** Yes. In accordance with the Board's requirements, we have included with this  
10 filing pro forma financial statements that reflect historical consolidated  
11 financial statements of the two parent companies, Exelon and PSEG, after  
12 giving effect to (1) the Merger using the purchase method of accounting with  
13 Exelon as the acquirer, and (2) Exelon's 2004 disposition of Boston  
14 Generating, LLC, a previously indirect wholly owned subsidiary. These pro  
15 forma financial statements have been attached to the Joint Petition as Exhibits  
16 JP-11.

17  
18 **Q. Did you have a pro forma balance sheet and income statement prepared**  
19 **for PSE&G?**

20  
21 **A.** Yes. The pro forma balance sheet and income statement have been prepared  
22 and are being provided as Exhibit JP-11 to the Joint Petition.

23

1                   **V. THE EXELON UTILITY MONEY POOL AGREEMENT**

2   **Q.    What is the purpose of the Money Pool Agreement?**

3  
4   **A.**The purpose of the Money Pool Agreement is to provide an additional short-  
5 term borrowing option to the utility subsidiaries of Exelon, including PSE&G,  
6 which will generally be more favorable to the borrowing participants than the  
7 cost of external borrowing. A copy of the Money Pool Agreement is attached  
8 to the Joint Petition as Exhibit JP-1G.

9  
10 **Q.    What are the sources of funds under the Money Pool Agreement?**

11 **A.**The funding under the Money Pool Agreement may be provided from internal  
12 and external funds; however, Exelon's practice has been to use only internal  
13 sources for money pool transactions. The source of internal funds are available  
14 funds from Exelon and its utility subsidiaries.

15  
16 **Q.    Are there restrictions that Exelon follows to insure that its utility**  
17 **subsidiaries are protected?**

18  
19 **A.**Yes. First, Exelon as a Pennsylvania corporation and a registered holding  
20 company under the Public Utility Holding Company Act of 1935 must file with  
21 and receive authorization from the SEC to implement the Money Pool  
22 Agreement. The aggregate amount of all loans requested by any party may not  
23 exceed the applicable borrowing limits set forth in applicable orders of the

1 SEC and other regulatory authorities, resolutions of the party's Board of  
2 Directors, the party's governing corporate documents, and agreements binding  
3 upon the party. In addition, Exelon may not borrow funds from the pool and,  
4 therefore, can only withdraw funds from the pool in amounts equal to what it  
5 has contributed.

6  
7 **Q. What will the Money Pool Agreement permit PSE&G to accomplish?**

8 **A.** PSE&G, like the other utility subsidiaries of Exelon, will be able to contribute  
9 surplus funds in the pool and have the right to borrow from the pool at rates  
10 equal to or lower than that available to it in the short-term market. PSE&G  
11 will be able to access the pool as a source of favorable short-term funding, if  
12 needed, for its utility operations.

13  
14 **Q. How are the interest charges and payments calculated?**

15 **A.** The interest rate payable to and by the participants will be the higher of (1) the  
16 rate for high-grade unsecured 30-day commercial paper, or (2) the daily yield  
17 on existing money market mutual funds utilized by the utility.

18

1 **Q. When are principal payments to be made on any borrowed funds?**

2 **A.** Borrowers will be required to repay the principal amount of the loan on  
3 demand and in any event within 365 days of the date of the loan. Prepayment  
4 may be made at any time without premium or penalty.

5

6 **Q. Does this conclude your testimony at this time?**

7 **A.** Yes, it does.

**STATE OF NEW JERSEY  
BOARD OF PUBLIC UTILITIES**

**In The Matter Of The Joint Petition Of  
Public Service Electric And Gas Company  
And Exelon Corporation  
For Approval Of A Change In Control Of  
Public Service Electric And Gas Company,  
And Related Authorizations**

**DIRECT  
TESTIMONY**

**OF**

**WILLIAM D. ARNDT**

**JP-5**

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1 **I. INTRODUCTION AND QUALIFICATIONS**

2 **Q. Please state your name and by whom you are employed.**

3 **A.** My name is William D. Arndt and I am the Senior Vice President, Financial  
4 Operations for Exelon Corporation. My business address is 10 S. Dearborn, 38<sup>th</sup>  
5 Floor, Chicago, Illinois 60603.

6 **Q. Would you briefly summarize your academic and professional background?**

7 **A.** I graduated from the U.S. Merchant Marine Academy with a Bachelor of  
8 Science degree in Marine Engineering in 1980. After working for two years as a  
9 licensed engineer aboard U.S merchant vessels, I began my professional career at  
10 General Electric Company (GE) where I remained until joining Exelon in 2001.  
11 During my tenure at GE, I held a number of operating, commercial and management  
12 positions within GE's nuclear energy business. My early responsibilities included  
13 field service engineering, project management, marketing and various customer  
14 relations and account leadership roles. My last five years at GE were at the executive  
15 level where I held global business leadership roles for two different divisions of GE  
16 Nuclear Energy in which my responsibilities included integration and leadership roles  
17 for two global joint ventures within GE's nuclear fuel business.

18 **Q. Please describe your current and previous roles within Exelon.**

19 **A.** As Senior Vice President, Financial Operations, I am currently responsible for  
20 leading the Business Unit financial organizations for Exelon Generation, Exelon

1 Energy Delivery, Exelon Enterprises, and Exelon Business Services. My  
2 responsibilities include strategic long-range planning, profit and loss forecasting and  
3 reporting, budgeting, financial variance analysis, cost management, business  
4 performance reporting and decision support, as well as leveraging economic  
5 synergies across these Business Units. I have also been responsible for managing our  
6 internal transformation program - The Exelon Way – from February 2003 through the  
7 present.

8 Prior to my current role, I was Senior Vice President, Business Operations for  
9 Exelon Generation, Enterprises and Services. My initial role at Exelon was Vice  
10 President, Business Operations for Exelon Nuclear with responsibility for the  
11 business planning, finance, supply chain and information technology functions across  
12 our nuclear business.

## 13 II. PURPOSE OF TESTIMONY

14 **Q. What is the purpose of your testimony?**

15 **A.** I am providing testimony on behalf of Exelon Corporation and Public Service  
16 Enterprise Group, Incorporated (the Companies) and their respective regulated utility  
17 operating companies, Public Service Electric & Gas Company (PSE&G); PECO  
18 Energy Company (PECO); and Commonwealth Edison Company (ComEd), to  
19 sponsor the identified merger-related synergies from the announced combination of  
20 the Companies. My testimony addresses the regulated cost savings from the merger  
21 and the costs-to-achieve those savings.

1           In this testimony I: (1) describe the process for identifying synergies from the  
2 merger of the Companies; (2) describe the synergies categories quantified by this  
3 process; (3) identify the specific areas where synergies are expected from the  
4 combination; (4) present the overall gross and net synergies to the regulated business  
5 over the relevant four-year time period; (5) describe the allocation process used to  
6 develop related savings distribution to the regulated business, the respective utility  
7 operating companies, and the business segments, i.e., electric and gas, transmission  
8 and distribution; and (6) affirm the reasonableness of the synergies presented.

9   **Q.   How is the remainder of your testimony organized?**

10  **A.**       My testimony is organized into the following sections:

- 11           - Summary of Testimony
- 12           - Approach to Synergies Identification
- 13           - Synergies Description and Quantification
- 14           - Costs-to-Achieve
- 15           - Pre-merger Initiatives
- 16           - Allocation of Savings

17  **Q.   Have you included any exhibits to your testimony?**

18  **A.**       Yes. EXHIBIT WDA-1 is a summary of my Exelon and prior work  
19 experience, EXHIBIT WDA-2 provides a four-year summary of the total net  
20 regulated business cost savings, EXHIBIT WDA-3 summarizes the total regulated  
21 business costs-to-achieve, EXHIBIT WDA-4 provides a before and after view of

1 corporate and shared services savings allocations to the regulated business, EXHIBIT  
2 WDA-5 summarizes a similar before and after view of costs-to-achieve allocations to  
3 the regulated business, and EXHIBIT WDA-6 provides an overall allocation of total  
4 regulated business cost savings and costs-to-achieve between the respective utility  
5 operating companies and business segments.

6 **III. SUMMARY OF TESTIMONY**

7 **Q. Please summarize your testimony.**

8 **A.** As I will discuss in the balance of my testimony, the merger is anticipated to  
9 result in costs below the levels that otherwise would have been achievable on a stand-  
10 alone basis for any of the utility operating companies. These savings in costs also will  
11 be realized without creating reliability risks or adverse impacts to the effective and  
12 safe delivery of service to customers.

13 The Companies have identified approximately \$155 million of estimated net  
14 O&M and capital carrying cost savings within or allocated to the regulated business  
15 over the four-year period 2006-2009. This net amount also reflects approximately  
16 \$358 million of out-of-pocket costs-to-achieve these savings, and approximately \$22  
17 million of planned cost constraint or reduction initiatives by the utility operating  
18 companies prior to the merger (pre-merger initiatives).

19 On an annual basis, net regulated business savings are expected to grow from  
20 a negative \$70 million in 2006 due to the high initial costs-to-achieve, to a positive  
21 savings level in excess of \$107 million by 2009 after the majority of costs-to-achieve

1 have been incurred. This savings level will generally continue on an ongoing basis.  
2 These identified savings, however, do not reflect other ongoing cost increases  
3 occurring within the overall business. Thus, the merger cost savings do not fully  
4 offset recurring cost escalation.

5 These identified total corporate and shared services savings before and after  
6 allocation to the regulated business are summarized on the following table.

7 **NET REGULATED SAVINGS**  
8 (\$ in Millions)

I. Gross Regulated Savings	2006	2007	2008	2009	Total
<b>A. Allocated Corporate</b>					
Corporate and Shared Services Staffing	\$29	\$37	\$44	\$47	\$157
Corporate and Administrative Programs	14	16	17	18	64
Information Technology	<u>14</u>	<u>17</u>	<u>23</u>	<u>24</u>	<u>78</u>
<b>Sub-Total Allocated Corporate</b>	<b>\$56</b>	<b>\$70</b>	<b>\$84</b>	<b>\$89</b>	<b>\$299</b>
<b>B. Utility</b>					
Support Staffing	\$14	\$37	\$40	\$44	\$135
Non-Labor	<u>16</u>	<u>25</u>	<u>28</u>	<u>32</u>	<u>101</u>
<b>Sub-Total Utility</b>	<b>\$30</b>	<b>\$62</b>	<b>\$69</b>	<b>\$76</b>	<b>\$236</b>
<b>Total Gross Regulated Savings</b>	<b>\$86</b>	<b>\$132</b>	<b>\$152</b>	<b>\$165</b>	<b>\$535</b>
<b>II. Regulated Cost-to-Achieve</b>	<b>\$(152)</b>	<b>\$(91)</b>	<b>\$(65)</b>	<b>\$(49)</b>	<b>\$(358)</b>
<b>III. Regulated Pre-Merger Initiatives</b>	<b>\$(3)</b>	<b>\$(5)</b>	<b>\$(6)</b>	<b>\$(8)</b>	<b>\$(22)</b>
<b>Net Regulated Savings</b>	<b>\$(70)</b>	<b>\$35</b>	<b>\$81</b>	<b>\$108</b>	<b>\$155</b>

9 The total identified corporate and shared services savings before allocation  
10 that were used to develop the above table are illustrated in EXHIBIT WDA-4.  
11 Through the remainder of my testimony, I will discuss the regulated business savings  
12 levels, by category.  
13

1           The identified synergies above reflect the net regulated business savings  
2 expected to result from the merger and were jointly developed by the Companies.

3           The cost savings that have been identified reflect my view of where and how  
4 operating synergies can be achieved for the regulated business. A structured process  
5 including officers and employees from each Company was utilized for synergies  
6 identification and quantification to guide management's evaluation and provide a  
7 basis for determining the potential benefits from the merger. I believe that this  
8 process effectively quantified a reasonable estimate of the savings that will be  
9 realized by the Companies.

10           The identified cost savings relate to the reduction or avoidance of costs from  
11 the consolidation of the separate corporate, shared services and utility operations  
12 support into single operating entities. The direct field service functions of the utility  
13 operating companies are not affected by the merger and no savings have been  
14 quantified in these areas.

15           Through consolidation, duplicative functions and positions can be eliminated  
16 and certain corporate costs, both O&M and capital, can similarly be reduced or  
17 avoided. In addition, expenditures for materials and third-party services can be  
18 reduced from more effective sourcing from suppliers and vendors, thus capturing  
19 economies of scale.

20           Related out-of-pocket costs-to-achieve these savings have also been identified  
21 and reflect the expenses that will be incurred in integrating the Companies to realize  
22 the savings and in processing the merger applications through the various Federal and

1 state regulatory agencies, among other required expenditure areas. These costs-to-  
2 achieve are necessary expenses incurred to attain the identified benefits from the  
3 merger.

4 The regulated business synergies estimate that has been prepared reflects only  
5 those savings that arise directly from the merger. The process we employed focused  
6 on savings that would not otherwise be attainable from management actions that  
7 either Company could have initiated on its own. In addition, we took deliberate  
8 efforts to avoid double-counting any potential savings that could relate to initiatives  
9 already underway or planned at either Company. Through this process we determined  
10 the level of cost initiatives already incorporated within those projections.

11 The identified regulated business savings reflect an allocation, where  
12 necessary, between regulated and non-regulated operations, and subsequently to the  
13 respective utility operating companies and the business segments. The total savings  
14 from corporate and shared services were split between the regulated and non-  
15 regulated businesses as they support both of these operational segments.

#### 16 IV. APPROACH TO SYNERGIES IDENTIFICATION

17  
18 **Q. Please describe in more detail the process that the Companies utilized for**  
19 **developing the overall synergies analysis.**

20 **A.** The Companies used a two-step process for synergies quantification. Prior to  
21 the announcement of the transaction, the Companies assembled a working group to  
22 focus on the identification and quantification of potential cost savings and costs-to-

1 achieve. I was responsible for the overall Exelon synergies team with the President of  
2 PSEG's Shared Services organization as my counterpart.

3 Post-announcement, I again led, with support from my PSEG counterpart, a  
4 focused effort to validate and refine the pre-announcement synergies and costs-to-  
5 achieve. This effort included a broader group than the original teams to identify any  
6 other factors that could affect synergies and that may not have been identified earlier.  
7 From this post-announcement effort, a refined synergies estimate was prepared which  
8 is the focus of my direct testimony.

9 **Q. How was the analysis conducted for the purpose of estimating available cost**  
10 **savings from the merger?**

11 **A.** Business unit focused teams were established by each Company to assess  
12 potential savings from the combination. The teams developed baseline data to  
13 compare starting cost and staffing levels. Assumptions were also developed about  
14 how the combined organizations would operate once the transaction was closed and  
15 the Companies could be aligned and integrated to produce savings from consolidation  
16 and / or the capture of economies of scale. With this data, the teams determined the  
17 level of going-forward staffing necessary to continue to provide high-quality service  
18 to either internal or external customers.

19 An underlying philosophy of this effort was that front-line field service  
20 positions would not be affected since the day-to-day work itself was not going to be  
21 impacted by the combination.

1           The teams also evaluated non-labor cost levels to identify elements that could  
2 be reduced from consolidation, wholly or partially avoided, absorbed through the  
3 larger entity, or reduced at the unit cost level from economies of scale.

4 **Q.    What period was used for the quantification of cost savings?**

5 **A.**           The savings were quantified for the regulated business over a four-year period  
6 from 2006-2009. This four-year period was utilized because it reflected the period  
7 during which a steady state of operations would be achieved, after which the savings  
8 will generally continue. For example, reductions in staffing will be sustained into  
9 future years since they relate to functions that are duplicative and related positions  
10 will be permanently eliminated.

11           Benefits from improved sourcing of materials will also continue into the  
12 future as increased volumes on a combined basis create opportunity to permanently  
13 reduce the unit and total costs of materials and services procured. Certain savings that  
14 relate to avoided technology projects in particular years are generally more event-  
15 driven, but will typically be replaced by other project expenditures from period-to-  
16 period.

17 **Q.    What assumptions were made about the organizational model to be in place for**  
18 **the combined Company?**

19 **A.**           The teams assumed that the current business unit based structure of Exelon  
20 would provide the future model for the combined organization. Essentially, separate

1 business units would exist for generation operations, transmission and distribution  
2 (T&D) operations (both electric and gas), shared services and the corporate functions.

3 Within the T&D business unit, which also includes the customer care  
4 functions, the individual utility operating companies were assumed to remain in place  
5 essentially as-is and to continue to focus on local service delivery. The T&D business  
6 unit management and operations support functions, e.g., technical services, however,  
7 were assumed to be consolidated across the three utility operating companies to  
8 leverage economies of scale without affecting local operations capability or focus.

9 The shared corporate and services functions were assessed together regardless  
10 of where the function actually resided.

11 **Q. Could the savings that have been quantified been achieved without the**  
12 **combination of the Companies?**

13 **A.** No. The teams identified and quantified cost savings that would only arise  
14 from the direct combination of the Companies and would not reflect reductions that  
15 could have been achieved on a stand-alone basis. For example, the consolidation of  
16 specific corporate functions, such as information technology, would not occur without  
17 the merger. Similarly, the ability to capture economies of scale would not be possible  
18 without the combination serving as the basis for joint planning, design and  
19 procurement.

20 Even though both Companies have been continuously focused on constraining  
21 or reducing costs, the cost savings that I am sponsoring do not duplicate these stand-

1 alone initiatives. In fact, I offset these savings to recognize the value of initiatives that  
2 are already contained within the high level, near term financial forecast of each of the  
3 Companies.

4 **Q. Were the costs-to-achieve the identified cost savings also identified during the**  
5 **analysis?**

6 **A.** Yes. As I will describe in more detail later in my testimony, out-of-pocket  
7 costs will be incurred to complete the merger, as well as integrate the Companies to  
8 support realization of the savings. These costs-to-achieve also only arise because of  
9 the merger and would not otherwise be incurred. Thus, internal costs associated with  
10 completing the merger would not be reflected in these amounts and are considered  
11 sunk-costs.

## 12 **V. SYNERGIES DESCRIPTION AND QUANTIFICATION**

### 13 **A. Summary**

14 **Q. What are the principal categories of cost savings that you have quantified?**

15 **A.** EXHIBIT WDA-2 indicates five primary categories of cost savings as  
16 described below, with the corporate and shared services staffing, corporate and  
17 administrative programs, and information technology areas assessed on an enterprise-  
18 wide basis and requiring allocation of total identified savings between the regulated  
19 and non-regulated businesses.

- 1       • Corporate and Shared Services Staffing – Position reductions related to  
2       redundancies associated with corporate management and business support  
3       functions that support the regulated and non-regulated businesses.
- 4       • Corporate and Administrative Programs – Reductions in non-labor programs and  
5       expenses, such as insurance and shareholder services, resulting from economies of  
6       scale and cost avoidance that support the regulated and non-regulated businesses.
- 7       • Information Technology – Reductions in hardware, software, projects, and  
8       operating costs associated with support of the regulated and non-regulated  
9       businesses, from consolidation of redundant technology and system platforms.
- 10      • Utility Support Staffing – Position reductions in utility business management and  
11      related support organizations from alignment and integration of functions.
- 12      • Utility Non-Labor – Aggregation and rationalization of materials and supplies  
13      volumes and services contracts to achieve greater sourcing economies plus  
14      improvements in bad debt expense from a combined billing platform.

15   **Q.    What level of gross and net regulated cost savings have been identified over the**  
16   **first four years after the merger?**

17   **A.**       Based on the overall operating philosophy and the approach to cost analysis I  
18   described earlier, approximately \$535 million of gross cost savings were quantified  
19   for the regulated business over the four-year period 2006-2009. The total amount of  
20   out-of-pocket costs-to-achieve related to these regulated business cost savings are

1 estimated at \$358 million over the first four years. Similarly, regulated business  
2 related pre-merger initiatives are estimated at approximately \$22 million.

3 The total estimated net regulated cost savings identified over the first four  
4 years after the merger, after being adjusted for costs-to-achieve and pre-merger  
5 initiatives, are approximately \$155 million.

### 6 **B. General Assumptions**

7 **Q. What general financial assumptions were utilized to support the quantification?**

8 **A.** Given the multi-year period used in the quantification of merger cost savings,  
9 several underlying assumptions were required for the determination of annual and  
10 recurring synergies, related to both O&M and capital. For the most part, the cost  
11 savings were estimated based on analysis of the budgeted 2005 expense levels. To  
12 reflect the continuing nature of the cost savings, specific escalation rates were then  
13 applied, by category, to determine the level of savings in subsequent years.

14 Other financial assumptions were utilized for fixed charge rates and for  
15 capitalization of costs. The fixed charge rate recognizes that a number of the cost  
16 savings areas include reduced or avoided capital related costs, which would then  
17 reduce the capital carrying costs of the utility operating companies. The fixed charge  
18 rate is used to quantify those impacts.

19 Certain expenditures in each of the business units are typically capitalized,  
20 rather than expensed, based on the type of cost incurred and the policies of the

1 business unit. Specific capitalization rates were reviewed and applied for each of the  
2 business units in the areas, where relevant, to recognize this accounting treatment.

3 **Q. Was a common escalation rate used for all savings categories?**

4 **A.** No, a single escalation rate could not be used for all cost savings categories,  
5 because certain cost components, e.g., salaries, escalate at different rates than others,  
6 e.g., benefits. An approximate 2.3% rate was used for general inflation. However, a  
7 higher rate of 3.8% was used for salaries to reflect existing contract arrangements and  
8 market requirements. This rate was then adjusted to reflect loadings for benefits and  
9 applicable taxes, which resulted in a blended salaries and benefits escalation rate of  
10 5.1%. The rates used reflect those developed for normal internal financial forecasting  
11 purposes.

12 **Q. How were fixed charge rates developed for the capital related savings**  
13 **components?**

14 **A.** A fixed charge rate was used in each year and applied to the capital-related  
15 expenditure reductions identified. The fixed charge rate, which covers depreciation  
16 and the pre-tax cost of capital, was determined for each of the utility operating  
17 companies. The fixed charge rates of each utility operating company were then  
18 blended to determine an overall rate for long-lived assets, such as plant-in-service,  
19 and for more rapidly recovered assets, such as information technology-related  
20 expenditures. The fixed charge rate for capital items other than information

1 technology was approximately 14.4%, while for information technology items it was  
2 approximately 32.1%, reflecting the more rapid (five year) depreciation period.

3 **C. Cost Savings Summary**

4 **1. Corporate & Shared Services Staffing**

5 **Q. What is the nature of the cost savings identified in the corporate staffing**  
6 **category?**

7 **A.** The Companies expect to consolidate the respective corporate management  
8 and related functions performed within each stand-alone company. This consolidation  
9 would allow for the execution of these corporate and administrative functions by a  
10 single entity and create cost savings from reduced staffing levels associated with  
11 these functions. This area captures the typical management functions of executive,  
12 *external relations, human resources, finance and accounting, information technology,*  
13 *communications, supply chain, and various other administrative support functions.*

14 These savings reflect those costs that can now either be achieved due to the  
15 avoidance of the need for certain positions which perform similar tasks or from the  
16 leveraging of existing positions to handle the workloads within the combined  
17 Company due to economies of scale.

18 **Q. How were the identified staffing reductions developed?**

19 **A.** After a comparative baseline was constructed, the current number of positions  
20 was reviewed to determine the level of necessary future positions to perform the  
21 required activities as a combined Company. Generally, it was assumed that there

1 would be full consolidation of these corporate and administrative functions and that  
2 duplication of functions and activities would be avoided.

3 The analysis assumed that the Companies would move to a common view of  
4 which functions would be performed within either the corporate management  
5 functions or the shared services business unit. For our purposes, it was assumed that  
6 significant consolidation would occur and that specific organization structures were  
7 not necessary for this analysis. In conducting the analysis, however, the nature of the  
8 activities performed; the requirement for proximate performance of related functions;  
9 the relative scale of the respective companies; and the relative stand-alone business  
10 models, were all considered.

11 **Q. What did you determine to be the level of comparable positions for the corporate  
12 management and shared services functions?**

13 **A.** For Exelon, approximately 1,626 positions were identified for the corporate  
14 and shared services areas, and 1,222 similar positions were identified for PSEG.  
15 These position totals capture currently filled and open positions, as both categories  
16 are affected by the merger.

17 A total of 528 corporate management and shared services position reductions  
18 were identified from the merger and the adoption of a consolidated operating model.  
19 These reductions represent the identified level of functional overlap and duplication  
20 that could be avoided through the creation of tightly integrated corporate management  
21 and shared services organizations.  
22

1 **Q. When are these position reductions assumed to occur?**

2 **A.** These position reductions are assumed to occur over several years as the  
3 related work can be consolidated and integrated. We have assumed that 313 positions  
4 can be reduced within the first year after close. Other reductions have been linked to  
5 anticipated system integration completion dates to reflect the timing of specific  
6 system cutovers. Of the total 528 position reductions in these corporate management  
7 and shared services areas, 119 would occur in the second year after the merger,  
8 another 71 in the third year, and 25 in the fourth year. All of the staffing reductions  
9 will occur within the four-year time period I have presented for savings  
10 quantification.

11 **Q. How were the actual position reduction cost savings calculated?**

12 **A.** Average salary levels were calculated by function and level and then applied  
13 to the identified position reductions in those respective areas. Benefit costs were also  
14 included in quantifying the cost savings associated with the identified position  
15 reductions. These benefits typically include health insurance, life insurance,  
16 employee investment plans, pension expense, accruals for retirement health benefits,  
17 incentives and bonuses, payroll taxes and others. A blended benefits loading rate  
18 of 37.5% was used to estimate average aggregate benefits cost.

19 **Q. Do any of the savings relate to costs that are capitalized?**

20 **A.** Yes. A certain portion of these savings reduce costs that are capitalized rather  
21 than expensed in the year incurred, reflecting the normal business practice of the

1 Companies. Capitalized amounts are recovered over the life of the asset to which  
2 these costs are assigned. A blended capitalization rate of approximately 1% was used  
3 for the corporate management and shared services areas, based on historical  
4 experience.

5 **Q. How were savings calculated related to these capitalized amounts?**

6 **A.** The fixed charge rates that I previously described were applied to the portion  
7 of savings allocated to capital to convert these savings to capital carrying costs that  
8 would be reduced.

9 **Q. What were the total regulated business savings estimated to result from**  
10 **corporate and shared services staffing consolidation?**

11 **A.** Cost savings for the corporate and shared services staffing reductions  
12 allocated to the regulated business are \$28.5 million in the first year, growing to  
13 \$47.5 million in the fourth year, resulting in average annual savings of \$39.2 million.

## 14 **2. Corporate and Administrative Programs**

15 **Q. What is the nature of corporate and administrative program cost savings?**

16 **A.** The merger allows for the reduction of non-labor costs that relate to these  
17 same corporate management or shared services functions that I described earlier.  
18 These costs can either be reduced or avoided as economies of scale can be leveraged,  
19 redundant costs will simply not be expended or lower amounts may be expended for  
20 similar activities from consolidation of stand-alone needs.

1 **Q. What specific areas were quantified in the corporate and administrative**  
2 **programs area?**

3 **A.** Savings were identified, quantified, and allocated to the regulated businesses  
4 over the four-year period. The following table shows the allocated cost savings to the  
5 regulated business, by category.

6 **CORPORATE AND ADMINISTRATIVE PROGRAMS**

7 (\$ in Millions)	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>Total</u>
8 Administrative and General Overhead	2.1	3.0	3.5	3.8	12.4
9 Advertising	0.9	0.9	0.9	0.9	3.6
10 Association Dues	0.1	0.1	0.1	0.1	0.5
11 Benefits Administration	1.4	1.5	1.6	1.8	6.3
12 Directors' Fees	0.2	0.2	0.2	0.2	0.8
13 Facilities	1.7	2.3	2.6	2.8	9.4
14 Insurance	2.1	2.1	2.2	2.2	8.5
15 Professional Services	4.2	4.4	4.7	4.9	18.3
16 Shareholder Services	1.1	1.1	1.1	1.2	4.5
17 Total Corporate and Admin. Programs	13.7	15.7	17.0	17.9	64.3

18 Each of the aforementioned categories is described below.

19 **a. Administrative and General Overhead**

20 **Q. How are administrative and general expenses affected by this merger?**

21 **A.** A variety of administrative expenses exist to support the day-to-day execution  
22 of work responsibilities by employees. These miscellaneous types of expense are  
23 generally characterized as overhead expenses and include training, postage,  
24 stationery, employee travel, transportation, and office supply expenses, among others.

1 These costs are generally variable with the total number of positions and change as  
2 the number of positions increase or decrease. As position reductions are achieved  
3 through the merger, these miscellaneous overhead expenses also are reduced.

4 **Q. How were estimated cost savings for this area quantified?**

5 **A.** Miscellaneous overhead expenses were identified in the synergies  
6 quantification process I described earlier, by category, by Company. The variable  
7 administrative and general costs for the Companies are incurred primarily by, or on  
8 behalf of, all employees. A \$16,363 loader was developed for application to each of  
9 the reduced positions to reflect these incidental support expenses that will no longer  
10 be incurred after the merger is completed. The estimated merger savings identified  
11 and allocated to the regulated business are \$2.1 million in the first year growing to  
12 \$3.8 million in the fourth year, resulting in an average annual savings of \$3.1 million.

13 **b. Advertising**

14 **Q. How are the advertising expenditures of the Companies affected by the merger?**

15 **A.** Both Companies maintain separate programs for advertising at the corporate  
16 level. After the merger is complete, the manner in which the Companies administer  
17 these programs will change with Exelon administering this program across the family  
18 of companies. Consolidation of each Company's agency spending and elimination of  
19 stand-alone advertising will enable cost savings to be achieved.

1 **Q. How were savings with respect to advertising expenditures quantified?**

2 **A.** The advertising and related expenditures of each Company were reviewed to  
3 identify categories of expenditures that could be avoided. As stated above, agency  
4 fees, campaign costs and general program consolidation will provide the opportunity  
5 for cost savings to be realized immediately. In this case, it is likely that corporate  
6 level PSEG expenditures will simply no longer be incurred, as all programs will be  
7 integrated at the Exelon enterprise level. The estimated cost savings for the regulated  
8 business in the advertising category are \$0.9 million in the each year, resulting in an  
9 average annual savings of \$0.9 million.

10 **c. Association Dues**

11 **Q. How are the regulated business association dues of the Companies affected by**  
12 **the merger?**

13 **A.** Both Companies incur dues for trade groups, such as the Edison Electric  
14 Institute (EEI) and the American Gas Association (AGA), which are calculated based  
15 on proscribed formulas. As a combined entity, these dues will be reduced after  
16 applying the formula to the combined two companies. The estimated cost savings for  
17 the regulated business in this category are \$0.1 million annually over the four years.

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**d. Benefits Administration**

**Q. How can cost savings be achieved in the area of benefits administration in this merger?**

**A.** Benefits administration savings typically arise from the consolidation of the benefits plan administrators, trustees, and related costs. This can occur even without the consolidation of the benefits plans themselves as these vendors are skilled at handling multiple plans and most companies today have more than a single plan across the business. These cost savings relate to the reduction in total administrative fees as a result of sourcing this support from fewer vendors.

**Q. What is the level of estimated regulated business benefits administration cost savings?**

**A.** The respective administrative fees paid by Exelon and PSEG to current vendors were reviewed to determine the baseline expenditures and the opportunity for plan management consolidation. The level of savings from improved sourcing of benefits administration allocated to the regulated business is estimated at \$1.4 million in the first year growing to \$1.8 million in the fourth year, resulting in an average annual savings of \$1.6 million.

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**e. Directors' Fees**

3

**Q. How are savings in directors' fees derived from this specific combination?**

4 **A.**

These reductions result from the reduced number of total directors in the combined Company compared to that of the separate Companies. The new board of the combined Company will be smaller than the total size of the two separate boards. The source of the savings is the reduced meeting and committee fees paid to directors as a result of these directors leaving the board, as well as the reduction in travel related costs from the fewer directors on the new board.

10

**Q. How were cost savings estimates in this category developed?**

11 **A.**

In this case, four directors will be reduced from the Companies as a result of the merger. Based on the average fees and expenses for directors at each Company, the total regulated business savings would amount to \$0.2 million in the first through fourth years, resulting in average annual savings of \$0.2 million.

15

**f. Facilities**

16

**Q. How are regulated business facilities cost savings created through the merger?**

17 **A.**

Cost savings arise from the number and geographic location of the various corporate and headquarters locations. Cost savings are possible from the lower square footage needed to be maintained after position reductions are worked through the existing space configuration.

20

1 **Q. What level of facilities savings was calculated from the merger?**

2 **A.** An average amount of square footage per employee was developed based on  
3 the actual configurations. We also assumed that the amount of freed-up space could  
4 be sub-let at the prevailing market rate to determine a blended sub-lease rate. Based  
5 on this approach, regulated business facilities savings were estimated at \$1.7 million  
6 in the first year growing to \$2.8 million in the fourth year resulting in average annual  
7 savings of \$2.4 million.

8 **g. Insurance**

9 **Q. Please describe how cost savings can be achieved from the merger in the area of**  
10 **insurance.**

11 **A.** A variety of insurance programs and coverages are established for the  
12 property, director and officer liability and excess casualty areas, among others, by the  
13 Companies. Each Company has independently defined its own risk philosophy,  
14 established its coverage levels, determined related deductibles and negotiated other  
15 terms and conditions of its insurance program. The combined Company will  
16 undertake these same activities across a broader asset base and a different loss profile.  
17 This view will result in lower insurance costs from a mix of program consolidation  
18 and redesign for the combined Company.

19 **Q. How were the savings in the area of insurance quantified in this merger?**

20 **A.** Savings on insurance premiums were determined across the various insurance  
21 program types through consultation with risk managers within each Company. The

1 ability to combine the insurance programs is estimated to result in approximately a  
2 10% to 20% reduction in premium levels, by type of insurance. We have estimated  
3 regulated business savings of \$2.1 million in the first year growing to \$2.2 million in  
4 the fourth year, resulting in average annual savings of \$2.1 million.

5 **h. Professional Services**

6 **Q. Please describe the nature of savings possible from the professional services**  
7 **area.**

8 **A.** The Companies utilize a variety of third-party advisors for skills and expertise  
9 beyond that available within either Company or to meet market or statutory  
10 requirements. These professional services functions include such areas as audit, tax,  
11 legal, and general management consulting and address similar areas within each  
12 Company.

13 **Q. How were savings in the area of professional services quantified?**

14 **A.** Savings were calculated by identifying and reviewing the expenditures for  
15 third-party vendors at each Company. Audit savings were based on reducing the total  
16 stand-alone costs of the Companies to a level reflecting the consolidated needs of the  
17 business. Legal and general consulting services were reduced from current levels to  
18 reflect the ability to combine internal and external resources more efficiently and  
19 effectively. The total savings resulting from these reductions for the regulated  
20 business is \$4.2 million in the first year growing to \$4.9 million in the fourth year,  
21 resulting in an average annual savings of \$4.6 million.

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**i. Shareholder Services**

**Q. How will the merger of the Companies impact the expenses incurred for shareholder services?**

**A.** In addition to the labor savings identified, cost savings are anticipated to result through the combination of transfer agents, the elimination of duplicative investor relations and a reduction in the total cost of processing transactions. Moreover, reductions are expected in combined non-labor shareholder services costs in common activities, such as proxy filings and registration costs, and from elimination of duplicate costs associated with annual meetings and annual reports.

**Q. What is the level of savings estimated and how was it calculated?**

**A.** The total estimated regulated business savings in the area of shareholder services based on the 2004 expenditures of each of the Companies is approximately \$1.1 million in the first year growing to \$1.2 million in the fourth year, resulting in an average annual savings of \$1.1 million.

**3. Information Technology (IT)**

**Q. Would you please describe how information technology savings are available to the Companies?**

**A.** The merger will result in a single IT organization, allowing stand-alone operations of both Companies to be fully integrated and the related operating and capital costs to be reduced. The opportunity to achieve these savings results from the rationalization and consolidation of underlying applications and standardization of

1 infrastructure including: data centers, servers, networks, telecommunications and  
2 workstations and elimination of duplicate projects. In essence, the merger will create  
3 a fully aligned and integrated IT organization that operates across the enterprise using  
4 consistent systems, networks, tools and methodologies.

5 **Q. How were the estimated savings in information technology developed?**

6 **A.** A specific team was chartered with members from each Company to focus on  
7 the IT area. This was done due to the complexity of the underlying decisions to be  
8 made and the potential level of IT savings. This team compiled stand-alone baselines  
9 to understand the current operating environments within each Company and the near-  
10 and long-term plans for the respective IT organizations. This team reviewed the  
11 stand-alone budgets of the Companies and inventoried the various applications in use.  
12 With this information, the team developed a preliminary view of how the respective  
13 IT organizations could be integrated in the future. Since the IT function serves the  
14 entire enterprise, it was analyzed as a total function with potential savings either  
15 directly assigned or allocated to the regulated business.

16 **Q. Are there particular information technology areas that are likely to provide**  
17 **significant savings contribution?**

18 **A.** Yes. PSEG and Exelon utilize different applications in many areas,  
19 particularly in the backbone applications areas for the finance, human resources and  
20 work management areas. For example, PSEG utilizes SAP for its backbone  
21 applications while Exelon uses a PeopleSoft platform. Only one of these platforms in

1 each area makes sense to carry forward as a combined Company. Consolidation into  
2 one system will avoid significant maintenance and upgrade expenditures.

3 Additionally, the customer billing platforms of each Company are different,  
4 with significant benefits available once a single system is selected for use across all of  
5 the utility operating companies. Aligning the billing systems of the Companies will  
6 not just benefit the IT organizations; the customer care function will also benefit as  
7 resources can be more effectively and productively employed across the enterprise.

8 Beyond these two specific applications, almost all other applications will be  
9 integrated to provide similar benefits. Similarly, almost all of the operating  
10 architecture can be standardized and consolidated to leverage the common system  
11 environment.

12 **Q. What are the components of the savings in the information technology area?**

13 **A.** Total IT function projected capital expenditures savings associated with the  
14 development of duplicative systems and future application development have been  
15 estimated at an average annual amount of \$18 million over the four-year period. The  
16 avoided annual cash flows have been converted to capital carrying costs using the  
17 fixed charge rate described earlier and assuming a five-year depreciable life, which  
18 reflects the planned amortization period for these investments. The level of savings in  
19 carrying costs related to IT capital expenditure avoidance for the regulated business is  
20 estimated at \$3.2 million in the first year growing to \$9.3 million in the fourth year,  
21 resulting in annual average carrying costs savings of \$6.4 million. These carrying

1 costs savings recognize that as future IT expenditures are avoided, future rates to  
2 customers to recover these costs would be lower.

3 The operating savings relate to the elimination of software leases and  
4 maintenance fees required to provide software support on personal computers. These  
5 savings also include benefits from the rationalization and consolidation of the  
6 Companies' two independent data centers and re-determination of the number of  
7 servers that will be required. The Companies will also be able to pursue the reduction  
8 of telecommunications expenditures for long distance, paging, cell phone and data  
9 transmission services from rationalizing enterprise needs and moving to a common  
10 provider. Operating cost savings over the four-year period for the regulated business  
11 are estimated at \$10.4 million in the first year growing to \$14.4 million in the fourth  
12 year, resulting in average annual savings of \$13.0 million.

#### 13 4. Utility Support Staffing

14 **Q. How are utility business operations affected by the proposed merger?**

15 **A.** As I stated earlier, we have made it clear that field service personnel will not  
16 be affected and there will be no adverse impact on utility reliability, customer service,  
17 or safety. The impact of the merger on the utilities relates to the areas of business unit  
18 management, back-office support, supply chain and bad debt expense. In these areas,  
19 duplication and overlap will be avoided, economies of scale will be captured and  
20 overall streamlining of the business unit will be pursued.

1 **Q. What is the nature of the expected impacts to these utility functions you just**  
2 **described?**

3 **A.** Exelon will be able to extend its operating model over the three utilities and  
4 reduce management personnel performing similar functions. These functions relate to  
5 business unit and functional leadership that would exist in parallel between Exelon  
6 and PSEG.

7 Similar impacts would also occur in the back-office support areas of  
8 transmission and distribution (T&D) operations. These areas would include functions,  
9 such as standards, engineering, and customer care activities related to customer  
10 accounting and billing system support. The integration of a common customer billing  
11 system will also enable the call centers to be aligned and staffing levels managed  
12 across time zones to levelize peak load requirements, resulting in resources being  
13 capable of handling overflow calls from any location.

14 The supply chain and bad debt savings areas related to utility operations are  
15 described more fully in the next section of my testimony. The supply chain savings  
16 deal with the opportunities that are available for improved sourcing from the  
17 consolidation of procurement programs across the three utilities. The bad debt savings  
18 relate to improved collecting processes and reduction of write-offs enabled by  
19 implementing a common billing system platform across the utility operating  
20 companies.

21

1 **Q. How were the impacts to the utility business unit determined?**

2 **A.** A team was chartered to focus on the opportunities to the T&D business  
3 through the merger. This group developed an initial staffing and cost baseline,  
4 determined the operating philosophy, constructed assumptions regarding how  
5 baseline staffing and cost baselines would be affected, and quantified the potential  
6 impacts.

7 This team addressed the technical services, safety and training, fleet, supply  
8 chain, customer care and business unit financial management functions. The team  
9 determined how the respective organizations could be brought together to improve  
10 the overall effectiveness of the business unit and drive out redundancies. This  
11 analysis occurred for both the electric and gas operating businesses.

12 **Q. What level of savings was quantified with respect to the utility business?**

13 **A.** The baseline level of staffing for Exelon in the T&D business unit was 8,364,  
14 and for PSE&G was 6,408. The identified staffing reductions in the utilities were 390  
15 positions, which represents 3% of the overall staffing base. The reductions above  
16 include opportunities that arise directly from the move to a common billing platform  
17 across the business by 2008. These resource reductions will improve the productivity  
18 of the call center resources across the three utility operating companies. The total  
19 level of labor savings in the T&D area was quantified at \$13.7 million in the first year  
20 growing to \$43.6 million in the fourth year, resulting in average annual savings of  
21 \$33.7 million.

22

1 **Q. Should any of the utility staffing be treated as capital savings?**

2 **A.** Yes. Approximately 40% of the T&D savings, excluding those relating to the  
3 combined billing platform, have been allocated to capital based on the estimated  
4 capitalization rate for all labor costs. The fixed charge rate previously described was  
5 applied to convert the capital cost reductions into capital carrying cost savings.

6 **5. Non-Labor**

7 **Q. Please discuss the nature of cost savings that can be created within the supply**  
8 **chain.**

9 **A.** Our regulated utilities incur significant investment requirements associated  
10 with corrective and preventative system maintenance, new business connections,  
11 capacity expansion, facility relocation, and system performance upgrades. Costs  
12 associated with fulfilling these requirements are typically reflected in the areas of  
13 materials and supplies and contract services expenditures.

14 The combination of the Companies enables a more effective and efficient  
15 sourcing of these materials and services needs. With respect to the purchase of  
16 materials and supplies, savings can be realized in the procurement of commodity  
17 items, consumable materials (e.g., conductors, wire, cable), and other equipment. In  
18 addition, standardization of system components such as meters, transformers, and  
19 poles can be achieved.

20 With respect to the procurement of services, particularly contract services  
21 such construction assistance, expenditures can be consolidated and contracted from

1 fewer sources. Cost savings are created by achieving a lower per unit cost for the  
2 service provided due to a broader contracting capability or the repackaging of work  
3 into more attractive options to the contractor. In addition, internal and external force  
4 utilization mix can be improved which can provide both unit cost and total cost  
5 benefits.

6 Within the utility back-office support areas, the Companies will be able to  
7 improve efficiencies in functions such as customer billing. Moving to a common  
8 billing system platform, for example, will enable more effective management of  
9 collections which will reduce bad debt expense.

10 **a. Materials and Supplies**

11 **Q. What level of merger cost savings was determined available from supply chain**  
12 **integration for materials and supplies?**

13 **A.** Annual T&D purchases for 2004 for Exelon were approximately \$329  
14 million, while for PSEG they were approximately \$129 million. These expenditure  
15 levels capture a mix of consumables, stock items and engineered items. The  
16 Companies will be able to improve how they source these items and the unit cost  
17 paid. They will also be able to reduce the overall level of total expenditures based on  
18 the standardization of specifications and the rationalization of maintenance  
19 philosophies and programs.

20 Based on the review of the detailed composition of the materials and supplies  
21 expenditures, the team estimated between 0.5% to 7.5% improvements to total

1 expenditure levels, by category, from improved sourcing. Total savings from pro-  
2 curement of materials and supplies were estimated at \$ 6.3 million in the first year  
3 growing to \$11.5 million in the fourth year, resulting in an average annual savings of  
4 \$8.9 million.

5 **Q. Should any of the materials and supplies savings be treated as capital savings?**

6 **A.** Yes. Approximately 69% of the materials and supplies savings has been  
7 assumed to be capital in nature based on the estimated capitalization rate for all  
8 materials and supplies. The fixed charge rate previously described was applied to  
9 convert the capital cost reductions into capital carrying cost savings.

10 **b. Contract Services**

11 **Q. What is the nature of savings from contract services as a result of the merger**  
12 **and how were they quantified?**

13 **A.** Just as in consolidating materials and supplies volumes and rationalizing  
14 overall expenditure levels, the Companies will be able to gain economies of scale  
15 from the aggregation of related contract service providers such as general  
16 construction contractors.

17 Exelon's total T&D contract services for 2004 were \$ 497 million, while they  
18 were \$ 154 million for PSE&G. On a combined basis, the Companies should be able  
19 to achieve additional economies of scale and execute a revised sourcing strategy with  
20 contractors. Based on a detailed review of the contract services expenditures of both

1 companies, the team estimated a 1% to 4% improvement in unit costs, by category,  
2 from improved sourcing.

3 Some of the contract services savings should be considered as capital savings.  
4 A capitalization rate of 53%, based on the estimated blended rate for the Companies,  
5 was used to reflect the amount of contract services expenditures that are charged to  
6 capital. These savings amounts were then converted to capital carrying cost savings  
7 using the fixed charge rate. The total estimated savings from contract services was  
8 \$9.9 million in the first year growing to \$15.0 million in the fourth year, resulting in  
9 an annual average savings of \$12.4 million.

10 **c. Bad Debt Expense**

11 **Q. What is the nature of savings in bad debt expense as a result of the merger and**  
12 **what level was quantified?**

13 **A.** As described previously, the Companies' intend to align and integrate their  
14 stand-alone billing systems to realize efficiencies and capture economies from a  
15 single billing platform. These efficiencies include an improvement in the Companies'  
16 overall bad debt expense as the single platform will provide improved information on  
17 delinquent customer accounts and automate the collection process. Total savings are  
18 estimated at \$5.2 million in year two growing to \$5.5 million in year four resulting in  
19 an annual average savings of \$4.0 million over the four-year period.

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## VI. COSTS-TO-ACHIEVE

3 **Q.**

**What are costs-to-achieve and why are they incurred in this merger?**

4 **A.**

Costs-to-achieve are typically incurred in all mergers and relate to completing the transaction and combining the two entities to capture the identified cost savings. These costs-to-achieve include all of the costs associated with planning, prosecuting, integrating and closing a transaction and generally reflect contracted costs with third parties, commitments to employees and other incremental expenditures for effecting merger integration.

10

Costs-to-achieve reflect out-of-pocket cash payments and usually are one-time payouts incurred as a result of the merger. These expenditures generally are front-loaded and capture costs incurred leading up to an announcement, during the regulatory approval process and through the integration process. In some cases, these costs can be ongoing and relate to incremental, fixed expenditures, e.g., information technology seat licenses or capacity upgrades.

11

12

13 **Q.**

**Why is it appropriate to recognize each of these types of costs-to-achieve?**

14 **A.**

The completion of the merger is dependent upon three primary conditions: the ability to demonstrate to the respective Boards of Directors, shareholders and the financial community the merits of the proposed combination; the ability to demonstrate the benefits of the combination to all Federal and state regulatory agencies; and the ability to successfully integrate the Companies. The costs incurred

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1 are not avoidable, and are required to ensure that the merger receives approval by the  
2 Board of Directors of each company and by Federal and State regulatory agencies;  
3 employees leaving the Company are fairly treated; systems and infrastructure are  
4 converted and integrated to support operations; internal and external stakeholders  
5 receive adequate communications; and integration activities are thoroughly planned  
6 and conducted.

7 **Q. Was the process used for estimating costs-to-achieve consistent with that**  
8 **followed for cost savings?**

9 **A.** Yes. Where relevant, each team identified those types of out-of-pocket cost  
10 areas or levels that were anticipated to be required to integrate the respective business  
11 units.

12 **Q. What necessary level of out-of-pocket expenses has been estimated to merge the**  
13 **Companies?**

14 **A.** The regulated business costs-to-achieve are estimated at \$358 million over the  
15 four-year period 2006-2009. The expenses to be incurred over the first two years -  
16 2006 and 2007 - reflect approximately 68% of the total costs-to-achieve. The high  
17 proportion of costs in these years reflects the incurrence of costs related to merger  
18 approval, support for information technology readiness and the reduction in positions  
19 that occurs once the merger is closed and the Companies begin to operate on a  
20 combined basis.

1           The primary estimated regulated business costs-to-achieve relate to: severance  
2 (\$77 million), relocation (\$3 million), retention (\$4 million), systems integration  
3 (\$212 million), facilities integration (\$4 million), customer / supplier / employee  
4 education communication (\$6 million), regulatory and compliance processes (\$20  
5 million), transition (\$8 million), Directors' and Officers' liability coverage (\$4  
6 million), and transaction costs (\$21 million). The regulated business costs-to-achieve  
7 are summarized by year on EXHIBIT WDA-3.

8 **Q.    Would you please describe the nature of the severance and other employee**  
9 **related costs?**

10 **A.**Once the merger is approved, the organizations of the Companies will be able  
11 to be integrated and fewer positions will be required. Although the Companies intend  
12 to utilize attrition, controlled hiring, open positions, and other mechanisms to reduce  
13 total positions, more formal severance programs will also need to be utilized to  
14 achieve targeted staffing levels.

15           The costs-to-achieve for severance and employee related expenses actually  
16 capture several individual components: employee and executive severance costs,  
17 retention costs, and relocation costs. The severance costs are estimated based on the  
18 number of severance packages that would be needed to meet the expected workforce  
19 reductions. Additional severance related costs for payments to be made to employees  
20 in lieu of transfer, i.e., where employees elect to separate rather than move to a new  
21 job location, have also been estimated.

1           The estimated number of employees to whom severance payments will be  
2           made is 861 with separations occurring over the period from 2006 to 2009. This  
3           number is less than the total number of reduced positions as normal attrition and the  
4           open positions will be used to reduce the need for equivalent severance packages,  
5           where possible, within the Companies. Executive severance costs are also included in  
6           these amounts and reflect the required payments to departing officers and executives  
7           based on existing employment contracts in PSEG and estimated severances within  
8           Exelon. The total regulated business cost for the severance programs for employees in  
9           both Companies is estimated at \$77 million dollars and is primarily incurred in 2006  
10          and 2007.

11          For those employees that elect to move to a new location, relocation cost  
12          allowances will be extended to defray expenses associated with such moves.  
13          Employee retention payments, i.e., "stay payments", are also anticipated to be  
14          required to maintain needed employees and related skills in critical functions, e.g.,  
15          information technology and finance, through and beyond merger close. These  
16          payments reflect the extension of final separation dates where skills for critical  
17          activity completion is required or where the success of the merger and ability to  
18          produce the type and level of indicated benefits to customers could be threatened. The  
19          total retention and relocation payment amounts are estimated at \$7 million for the  
20          regulated business.

1 **Q. Please explain how the information technology costs-to-achieve was determined.**

2 **A.** Any merger requires significant effort and expense to align, convert and  
3 consolidate the underlying information systems of the entities involved. In this  
4 merger, each Company has an extensive number of applications and a well-  
5 established infrastructure in place to support its needs. Achieving the identified  
6 benefits from the merger due to duplication or overlap will require an extended effort  
7 to integrate the technology platforms of the Companies.

8 A team specifically focused on the assessment of information technology cost  
9 savings and related costs-to-achieve was chartered to preliminarily determine both  
10 opportunities and requirements. Given the differences in fundamental backbone  
11 platforms, i.e., PSEG uses SAP while Exelon is supported by PeopleSoft, significant  
12 expenditures will be incurred to bring the Companies to a single backbone system.  
13 Additionally, the customer billing systems of the Companies are different and will  
14 need to be integrated into a single billing system to simplify operations. Overall, the  
15 front-end regulated business technology integration costs are estimated at \$212  
16 million and position the Companies to attain the ongoing savings levels discussed  
17 herein.

18 The technology integration efforts will relate to reducing redundancy,  
19 integrating systems, aligning vendors, rationalizing infrastructure, defining necessary  
20 capacity, and linking databases, among other activities. Further, the  
21 telecommunications networks will be integrated through expanded

1 telecommunications capabilities. The related cost estimates cover third-party planning  
2 assistance, contract programming, hardware change-out and upgrading, seat license  
3 conversion, increased T-1 line capacity, and a number of other types of expenditures.  
4 The incurrence of these costs will provide the basis for realizing much of the cost  
5 savings potential that I have previously described. Without the integration of the  
6 information technology platforms of the two Companies, the ability to consolidate the  
7 Companies and operate in a seamless manner will not be achieved. The expenses  
8 associated with systems and communications integration are principally expected to  
9 be incurred in 2006 through 2008 but will carry through the full period to reflect  
10 additional hardware lease costs.

11 **Q. Can you describe the regulatory and compliance process costs-to-achieve related**  
12 **to the merger?**

13 **A.** Certain costs for assistance from professional service firms will be incurred  
14 for preparation and pursuit of necessary regulatory filings and related compliance  
15 requirements, such as those related to SEC, FERC, NRC and DOJ filings, as well as  
16 the merger approval cases filed before the state regulatory jurisdictions in New Jersey  
17 and Pennsylvania. These costs include professional services for legal, tax, accounting  
18 and consulting assistance associated with these filings related to market analyses,  
19 synergies and corporate restructuring, among other areas. These costs are necessary  
20 for the receipt of required regulatory approvals and the successful completion of the

1 merger. Regulatory process and compliance costs are estimated at \$20 million with  
2 respect to the regulated business.

3 **Q. Would you describe the estimated customer, supplier, and employee education**  
4 **communication costs-to-achieve?**

5 **A.** Communication expenses will be incurred as the Companies provide  
6 information about the merger to the various stakeholders that deal with the  
7 Companies. Mailings and informational brochures will be sent to customers,  
8 employees, retirees, suppliers, shareholders, rating agencies, and regulatory agencies  
9 to explain the specifics of the merger. Communications costs-to-achieve also include  
10 costs associated with implementing the new Company name and logo, e.g., signage  
11 across the business entities. These expenditures are estimated at \$6 million for the  
12 regulated business.

13 **Q. Please explain the transaction cost component.**

14 **A.** Transaction costs are necessary to secure the required internal approvals from  
15 the Boards of Directors and external approvals from the shareholders to pursue  
16 proposed transactions. These costs relate to fees for transaction structuring and  
17 valuation assistance, financial market analysis and fairness opinions. Transaction  
18 costs are not avoidable and typically are expended prior to the announcement of a  
19 merger. Transaction costs of \$21 million are allocated to the regulated business.

1 **Q. Are there additional costs-to-achieve beyond those you have described?**

2 **A.** Yes. Other costs that were attributed to the regulated business from the merger  
3 are transition costs (\$8 million); facilities integration (\$4 million); and D&O tail  
4 coverage (\$4 million). Transition costs include consulting fees for assistance with the  
5 integration of the Companies and expenses, such as travel for the transition teams.  
6 These costs will be incurred through and beyond closing of the merger. Additional  
7 facilities-related expenses are also necessary for addressing the space requirements of  
8 the Companies, e.g., restacking, refurbishment and leasehold improvements, and  
9 lease adjustment or cancellation. D&O tail liability coverage applies to directors and  
10 officers that will be leaving the Companies as a result of the merger.

11 **VII. PRE-MERGER INITIATIVES**

12 **Q. What are pre-merger initiatives and how were they determined?**

13 **A.** Each Company is separately planning on mitigating future cost increases on a  
14 stand-alone basis. To avoid double counting the quantified cost savings, I have  
15 determined the level and timing of any initiatives that had been planned prior to the  
16 announcement of the merger.

17 **Q. Once the baseline effect of these planned initiatives was established, what was  
18 the next step in your analysis?**

19 **A.** The merger savings were then specifically mapped to each of the business  
20 units to measure the relative impact of these savings. The merger savings related to

1 the corporate management and shared services areas have a much greater impact on  
2 baseline costs in those areas because of the extent of duplication that typically exists  
3 in those areas between the two Companies. The level of combined merger savings is  
4 only a small percentage of total O&M (approximately 6% in year four) for the  
5 combined Company because most of the costs associated with utility operations, i.e.,  
6 field service costs, are simply not affected. However, when the savings are mapped  
7 to business units, the corporate management and shared services merger savings have  
8 a higher than 6% impact on relevant baseline O&M costs, and consequently would  
9 have the potential for greater overlap with the separately identified merger cost  
10 savings in that area.

11 **Q. How were these observed ratios then used in the analysis of pre-merger**  
12 **initiatives?**

13 **A.** The calculated ratios were then applied against the estimated decline by each  
14 individual business unit. As an example, the calculated merger savings impact on  
15 corporate O&M was applied to the decline estimated for corporate O&M. This  
16 essentially suggests that any stand-alone cost reduction initiatives planned against  
17 corporate O&M would overlap in roughly the same percentage as the merger savings  
18 affecting the baseline level of costs. Stated another way, on a stand-alone basis, each  
19 of the Companies would mitigate future increases in costs that will occur in areas  
20 both affected and unaffected by the merger. Consequently, there is only a partial  
21 overlap between the merger cost savings and the stand-alone initiatives.

1 **Q. What impact did this analysis have on the level of regulated business merger cost**  
2 **savings?**

3 **A.** Based on this approach, I reduced the identified regulated business cost  
4 savings downward by \$3.3 million in the first year growing to a reduction of \$7.6  
5 million in the fourth year, resulting in an annual average reduction of \$5.6 million to  
6 reflect the potential overlap between the savings realized directly from the merger and  
7 the indicated forecast levels of O&M cost change.

8 **VIII. ALLOCATION PROCESS**

9 **Q. What is the purpose of this section of your testimony?**

10 **A.** Here, I describe how the total cost savings and costs-to-achieve have been  
11 allocated between the regulated and non-regulated businesses, respective utility  
12 operating companies and business segments. Since a large portion of the savings arise  
13 from the corporate and shared services businesses and relate to both regulated and  
14 non-regulated operations, they need to be allocated between these businesses to  
15 define the flow of benefits.

16 **Q. Please describe the approach used to allocate the corporate and shared services**  
17 **merger savings to the regulated and non-regulated businesses.**

18 **A.** The Companies used the corporate and shared services cost savings and  
19 related cost-to-achieve categories identified in EXHIBIT WDA-4 and EXHIBIT  
20 WDA-5 to this testimony as the basis from which to begin the allocation analysis.

1 **Q. Please elaborate on the allocation methodology that has been utilized.**

2 **A.** The allocation methodology used to allocate the merger savings employed a  
3 three-basis, four-tier allocation process that approximates the anticipated future cost  
4 structure of the combined Company. The three allocation bases used to assign  
5 savings, in order of precedence, are direct assignment, generally allocated or  
6 historically allocated. The first basis, direct assignment, represents savings that relate  
7 to operations that do not flow from corporate or shared service allocations; i.e., they  
8 were either savings from costs that are directly incurred in the utility operating  
9 companies, or savings from costs that are charged to utility operating companies on a  
10 direct assignment basis. The assignment of savings for this category was determined  
11 primarily through detailed analysis of the underlying costs charged for each type of  
12 savings. For example, reductions in direct business unit expenditures or business unit  
13 labor costs would be allocated directly to that business unit.

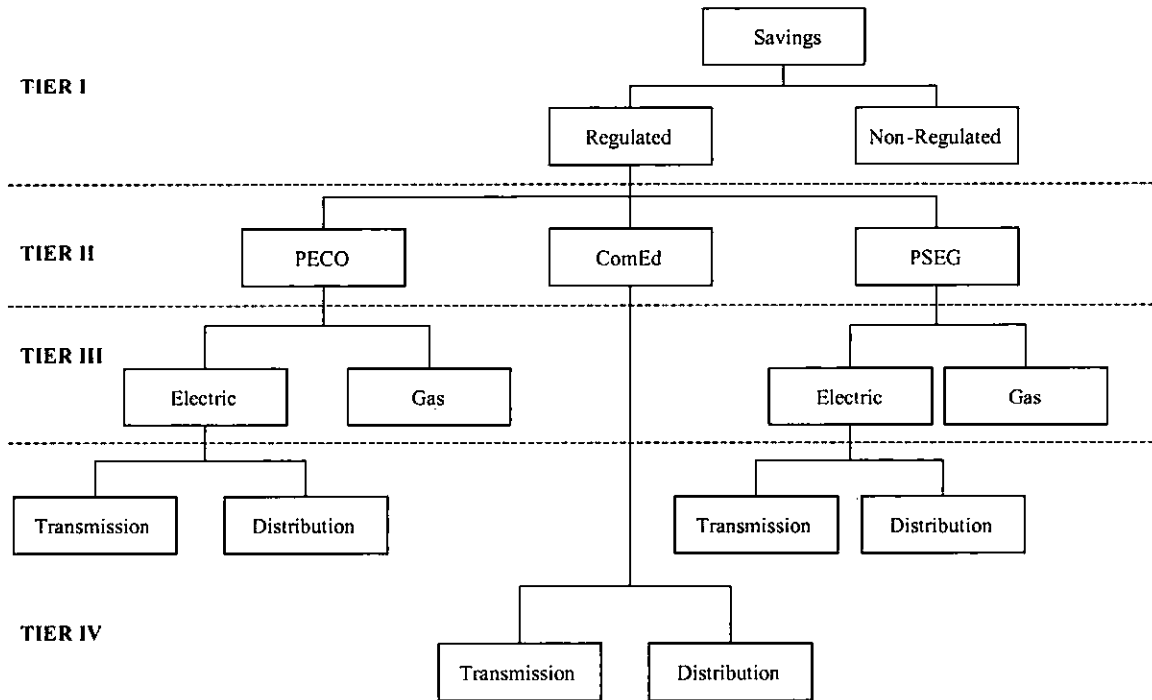
14 The second and third bases, generally allocated or historically allocated  
15 savings, represented all other savings. These savings resulted from costs almost  
16 exclusively incurred at the corporate level or in the service companies that could not  
17 be directly assigned. Generally allocated savings, utilized for tiers I and II discussed  
18 below, were assigned to each entity based upon that entity's anticipated non-fuel  
19 O&M costs as a percentage of the total merged Company's anticipated non-fuel O&M  
20 costs. This approach aligns estimated cost savings with the anticipated cost pools that  
21 are affected by the merger, thereby matching savings with costs. For example, the

1 savings resulting from a reduction in the costs of systems that support all elements of  
2 the Company, e.g., financial applications were allocated to the utility operating  
3 companies based upon their O&M weighting.

4 Historically allocated savings, utilized for tiers III and IV discussed below,  
5 were assigned to each entity based upon that entity's historical cost experience. For  
6 example, when looking at the composition of PECO's regulated O&M it has  
7 historically been comprised of approximately 83% electric and 17% gas respectively.  
8 This historical "split" was applied to the Pennsylvania Regulated savings in tier III to  
9 disaggregate it into their electric and gas components. Likewise, PECO's electric  
10 O&M has historically been comprised of approximately 7% transmission and 93%  
11 distribution respectively. This historical split was utilized in tier IV to disaggregate  
12 PECO's electric savings into their transmission and distribution components. A  
13 visual representation of the allocation methodology is shown below:

14

### SAVINGS ALLOCATION OVERVIEW



1

2 **Q. Were most savings directly assigned or allocated using allocation factors?**

3 **A.** Approximately sixty percent of the savings were directly assigned to either the  
4 "Regulated" or "Non-Regulated" categories of tier I, described below, with the  
5 remainder of the savings utilizing the weighted O&M or historical allocations. As the  
6 "Regulated" savings were further disaggregated through tiers II, III, and IV, the same  
7 allocation approach and methodology was employed, but a greater percentage of  
8 savings were allocated using the weighted O&M or historical allocations rather than  
9 direct allocation.

10

1 **Q. Please describe the first tier employed in the allocation of merger savings.**

2 **A.** The first tier separated the net cost savings into two categories. The first  
3 category, "Non-Regulated", represented all savings from costs incurred in the non-  
4 regulated utility operating companies, as well as those costs incurred in the corporate  
5 and shared services areas that were allocated to the non-regulated companies. The  
6 second category, "Regulated", included all savings from costs incurred in the  
7 regulated utility operating companies, as well as those costs incurred in the corporate  
8 and shared services areas that were allocated to the regulated companies. "Non-  
9 Regulated" and "Regulated" savings represent all savings resulting from the merger.  
10 In summary, the purpose of this first tier allocation was to segregate the identifiable  
11 non-regulated savings from the total savings before further disaggregating the  
12 regulated savings by jurisdiction and line of business.

13 **Q. Please describe the second tier of the allocation process.**

14 **A.** The "Regulated" savings category identified in the first tier was then further  
15 separated into the three jurisdictions where the combined Company will operate. The  
16 first jurisdiction, "Illinois", contained those savings related to costs directly incurred  
17 by, or allocated to, ComEd. The second jurisdiction, "New Jersey", contained those  
18 savings related to costs directly incurred by, or allocated to, PSE&G. The third  
19 jurisdiction, "Pennsylvania", contained those savings related to costs directly incurred  
20 by, or allocated to, PECO. The sum of the three jurisdictions represents all

1 "Regulated" savings and aligns the cost savings with all three utilities involved in the  
2 merger and the jurisdictional entities.

3 **Q. Please describe the third tier of allocation process?**

4 **A.** The third tier of the allocation process further disaggregated the jurisdictional  
5 savings from the "Pennsylvania" and "New Jersey" categories from tier two into their  
6 electric and gas line of business components using the previously discussed O&M  
7 weighting allocation. As the "Illinois" category is electric only, it was not further  
8 disaggregated at tier three. The sum of the Pennsylvania and New Jersey gas and  
9 Illinois, Pennsylvania and New Jersey electric components reflects all regulated  
10 savings.

11 **Q. Please describe the fourth tier of the allocation process?**

12 **A.** The fourth tier of the allocation focused on disaggregating the electric  
13 components identified in tier three, along with the "Illinois" component from tier two,  
14 into their transmission and distribution components using the same O&M weighting  
15 basis for development. The fourth tier represented the final level of savings  
16 disaggregation.

17 **Q. Were all types of savings treated similarly in the allocation process you have  
18 described?**

19 **A.** Yes. Each type of savings was analyzed to determine the appropriate  
20 allocation factor to use through an analysis of the underlying costs and the  
21 Companies' anticipated post-merger cost structure. This approach was used

1 consistently across all four tiers of the analysis. For the elements in the savings  
2 analysis making up the difference between gross savings and net savings, namely the  
3 costs-to-achieve, the allocations were calculated to have the costs follow the savings  
4 wherever possible. In other words, costs-to-achieve that could not be directly  
5 assigned were allocated on an O&M weighting or historical basis so that they  
6 followed allocated gross savings. For example, if 10% of the gross savings were  
7 allocated to the "Regulated-Illinois" category, then approximately 10% of the costs-  
8 to-achieve those savings were also allocated to the "Regulated-Illinois" category. This  
9 ensured that the savings and the costs necessary to create the savings were aligned.

10 **Q. Based on the allocation process you have described, what was the resulting**  
11 **breakdown of gross regulated business savings into the identified categories?**

12 **A.** The results of the allocation process, by tier, are shown on the following table  
13 for the four-year total gross regulated business savings.

14

**SUMMARY OF ALLOCATIONS**

**FOUR-YEAR TOTAL GROSS REGULATED SAVINGS**

(\$ millions)

Tier I	Percentage of Total Non-Fuel O&M	Total Four-Year Allocable Savings	Total Four-Year Direct Savings	Total Four-Year Savings
<b>Total Regulated</b>	<b>100%</b>	<b>\$299</b>	<b>\$236</b>	<b>\$535</b>
Tier II				
Illinois	37%	\$110	\$74	\$184
New Jersey	39%	\$116	\$97	\$213
Pennsylvania	24%	\$73	\$65	\$138
<b>Total</b>	<b>100%</b>	<b>\$299</b>	<b>\$236</b>	<b>\$535</b>
Tier III				
Illinois Electric	37%	\$110	\$74	\$184
New Jersey Gas	15%	\$44	\$30	\$74
New Jersey Electric	24%	\$72	\$67	\$139
Pennsylvania Gas	4%	\$12	\$10	\$22
Pennsylvania Electric	20%	\$61	\$55	\$116
<b>Total</b>	<b>100%</b>	<b>\$299</b>	<b>\$236</b>	<b>\$535</b>
Tier IV				
Illinois Transmission	3%	\$10	\$10	\$20
Illinois Distribution	34%	\$100	\$64	\$164
New Jersey Gas	15%	\$44	\$30	\$74
New Jersey Transmission	3%	\$9	\$13	\$22
New Jersey Distribution	21%	\$63	\$54	\$117
Pennsylvania Gas	4%	\$12	\$10	\$22
Pennsylvania Transmission	2%	\$4	\$5	\$9
Pennsylvania Distribution	18%	\$57	\$50	\$107
<b>Total</b>	<b>100%</b>	<b>\$299</b>	<b>\$236</b>	<b>\$535</b>

1 **Q. Have you also calculated these regulated business savings on any additional**  
2 **bases?**

3 **A.** Yes. The following table starts with gross regulated business savings. It then  
4 shows these savings on a net regulated business basis, i.e., after cost-to-achieve and  
5 pre-merger initiatives, for both the total four-year period and as an average annual  
6 amount over the four-year period.

7

**SUMMARY OF ALLOCATIONS**  
**FOUR-YEAR NET AND AVERAGE REGULATED SAVINGS**  
(\$ millions)

Tier I	Total Four-Year Savings	Total Costs-to-Achieve/Pre-Merger	Total Net Four-Year Savings	Average Net Four-Year Savings
<b>Total Regulated</b>	<b>\$535</b>	<b>\$380</b>	<b>\$155</b>	<b>\$39</b>
Tier II				
Illinois	\$184	\$141	\$43	\$11
New Jersey	\$213	\$147	\$66	\$16
Pennsylvania	\$138	\$92	\$46	\$12
<b>Total</b>	<b>\$535</b>	<b>\$380</b>	<b>\$155</b>	<b>\$39</b>
Tier III				
Illinois	\$184	\$141	\$43	\$11
New Jersey Gas	\$74	\$55	\$19	\$4
New Jersey Electric	\$139	\$92	\$47	\$12
Pennsylvania Gas	\$22	\$16	\$7	\$2
Pennsylvania Electric	\$116	\$76	\$39	\$10
<b>Total</b>	<b>\$535</b>	<b>\$380</b>	<b>\$155</b>	<b>\$39</b>
Tier IV				
Illinois Transmission	\$20	\$13	\$7	\$2
Illinois Distribution	\$164	\$128	\$36	\$9
New Jersey Gas	\$74	\$55	\$19	\$4
New Jersey Transmission	\$22	\$12	\$10	\$3
New Jersey Distribution	\$117	\$80	\$37	\$9
Pennsylvania Gas	\$22	\$16	\$7	\$2
Pennsylvania Transmission	\$9	\$5	\$4	\$1
Pennsylvania Distribution	\$107	\$71	\$35	\$9
<b>Total</b>	<b>\$535</b>	<b>\$380</b>	<b>\$155</b>	<b>\$39</b>

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1

**IX. CONCLUSION**

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

3 **A. Yes, it does.**

**William D. Arndt, Senior Vice President, Financial Operations, Exelon Corporation****Exelon Corporation****4/01-Present**

**Senior Vice President, Financial Operations, Exelon Corporation, 6/04-Present, Chicago, Illinois** – Responsible for leading the Business Unit financial organizations for Exelon: Generation, Exelon Energy Delivery, Exelon Enterprises, and Exelon Business Services. Responsibilities include strategic long-range planning, profit and loss forecasting and reporting, budgeting, financial variance analysis, cost management, business performance reporting and decision support, and leveraging economic synergies across these business units.

**Senior Vice President, Business Operations, Exelon Corporation, 2/03-5/04, Chicago, Illinois** – Led The Exelon Way, a restructuring of the corporation and transformation of how Exelon conducts business. Program's goal is to achieve sustainable business improvement while increasing cash flow from O&M and capital expense reduction by \$300M in 2004.

**Senior Vice President, Business Operations, Exelon Generation, Enterprises & Services, 5/02-3/03, Chicago, Illinois** – Selected by President to provide oversight for business management processes and strategic planning across Exelon's three unregulated Business Units, with focus on strengthening the depth and quality of financial talent and accomplishing organizational realignment to leverage economic synergies.

**Vice President, Business Operations, Exelon Nuclear, 4/01-5/02, Warrenville, Illinois** – Recruited to lead finance, business planning and performance monitoring / reporting organizations for largest nuclear operating company in the U.S, and AmerGen, an Exelon Nuclear joint venture with British Energy. Budget performance accountability for \$2 billion in operating costs and \$1 billion in capital expenditures, including fuel, across 17 operating plants and two corporate headquarters locations. Nuclear Supply Chain and Information Technology organizations added to scope 11/01.

**Global Nuclear Fuel, LLC (Joint Venture of GE, Hitachi & Toshiba) / GE Power Systems****4/98-4/01**

**Manager, Product Management, Wilmington, North Carolina** – Leader of \$300M global nuclear fuel manufacturing and engineering business responsible for all commercial activities and overall customer relations for Asia, Europe and the Americas. Accountable for orders, sales, project and contract management, marketing, pricing, the engineering and administration functional cost budget and strategic planning for the business. Sales and Marketing integration leader for the formation of Global Nuclear Fuel (GNF) on 1/1/00, a \$500M+ annual sales joint venture of GE, Hitachi and Toshiba. Chairman and President of GENUSA from 2/99 through 4/01, a GE joint venture with ENUSA (Spain) for nuclear fuel marketing and manufacturing operations in Europe.

**General Electric Company, GE Power Systems****2/82-4/98**

**Manager, Reactor Modifications, 1/96-4/98, San Jose, California** – Promoted to GE executive with profit and loss responsibility as leader of a global services business segment focused on developing and delivering major plant repair and replacement services for customers in Japan, Taiwan, Europe and the U.S.

**Account Manager, 1/90-12/95, Chattanooga, Tennessee; Baton Rouge, Louisiana; Oak Brook, Illinois** – Held account leadership roles of progressively increasing scope and size with responsibility for all commercial activities and overall customer relations between the business and assigned customers.

**Program Manager, Services Marketing, 2/89-2/90, San Jose, California** – Provided marketing support to analyze and segment the \$300M Plant Services business and develop a fix / sell / close strategy for its product lines. Performed market studies to evaluate key competitors and assess the viability of proposed development programs, commercial alliances and joint ventures.

**Commercial Programs, 1/87-2/90, Oak Brook, Illinois** – Developed account sales / marketing plans and prepared engineering / service proposals for Central Region's Account Managers.

**Project Manager & Field Service Engineer, 2/82-1/87, Darien, Illinois** – Project Manager and Lead Engineer with budget, schedule and quality accountability in support of maintenance outages, plant modifications and construction activities at U.S. power plants.

**Lykes Brothers Steamship Company / Keystone Tankships****7/80-1/82**

**Third Assistant Engineer, Marine Engineers Beneficial Association, District I** – Licensed operations and maintenance engineer aboard U.S. merchant vessels.

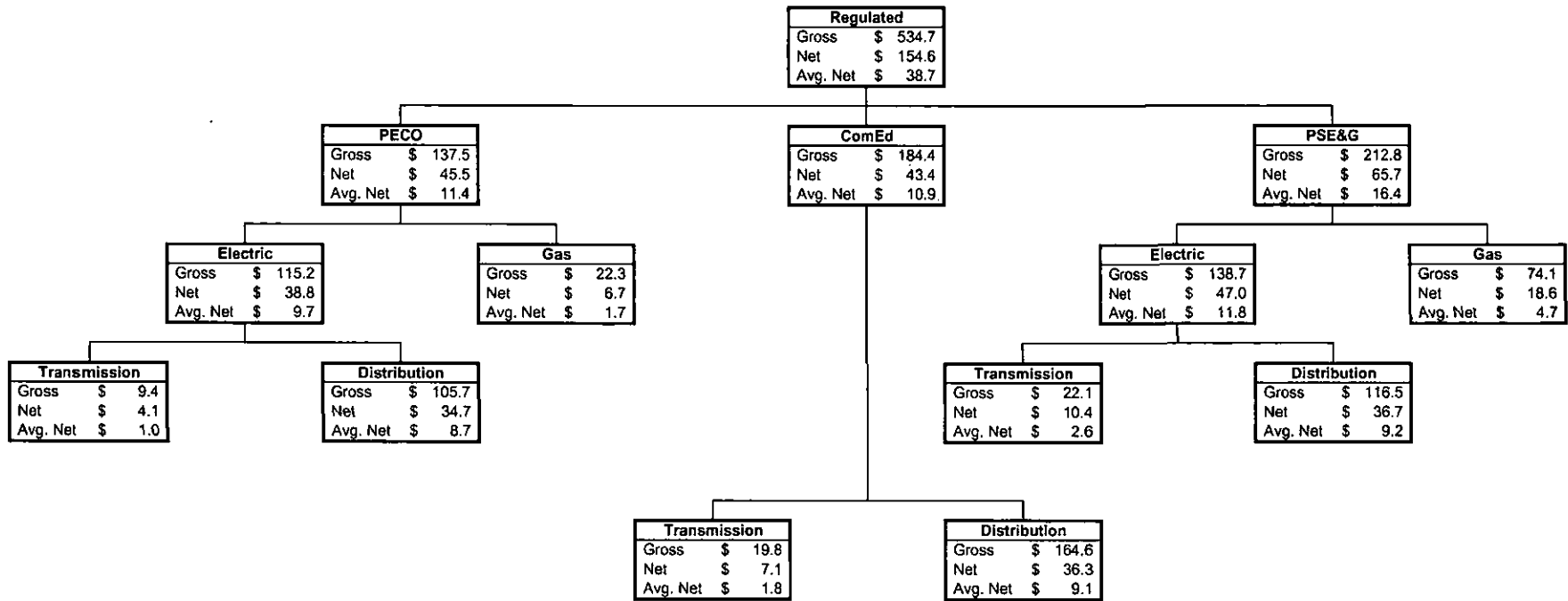
**Professional Education** - General Electric: Six Sigma Certified Green Belt; Global Business Manager's Course

**Education** - United States Merchant Marine Academy, Kings Point, New York, 1980, BS in Marine Engineering

**Military** - Lieutenant, U.S. Naval Reserve (Retired)

**Four Year Savings Allocation Detail**  
 (\$ in millions)

WDA Exhibit 6



**STATE OF NEW JERSEY  
BOARD OF PUBLIC UTILITIES**

**In The Matter Of The Joint Petition Of  
Public Service Electric And Gas Company  
And Exelon Corporation  
For Approval Of A Change In Control Of  
Public Service Electric And Gas Company,  
And Related Authorizations**

**DIRECT  
TESTIMONY**

**OF**

**PAMELA B. STROBEL**

**JP-7**

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**DIRECT TESTIMONY  
OF  
PAMELA B. STROBEL**

**I. INTRODUCTION AND QUALIFICATIONS**

**Q. State your name, title and business address.**

**A.** My name is Pamela B. Strobel. I am Executive Vice President and Chief Administrative Officer of Exelon Corporation (“Exelon”) and President of Exelon Business Services Company (“Exelon BSC”). My business address is 10 South Dearborn Street, Chicago, Illinois 60603.

**Q. Please summarize your professional background and experience.**

**A.** Prior to the Merger of PECO and Unicom, I was Executive Vice President of Unicom Corporation and its chief subsidiary, ComEd. In 1993 I joined ComEd as General Counsel. Before joining ComEd, I was a partner in the law firm of Sidley & Austin, which I joined in 1988. Prior to Sidley & Austin I practiced law for 11 years with the firm of Isham, Lincoln & Beale. I have played a broad corporate policy role with large customers and various regulatory and governmental officials.

I also serve on the Board of State Farm Mutual Automobile Insurance Company and Sabre Holdings. Sabre owns Travelocity.com and GetThere, the

1 world's leading provider of Web-based travel reservation systems for  
2 corporations and travel suppliers. I also serve on the Boards of Trustees of  
3 Rush University Medical Center, the Ravinia Festival Association, the  
4 Chicagoland Chamber of Commerce, Window to the World Communications,  
5 the Mid-Day Club, and I Chair the Board of The Joffrey Ballet. I am a  
6 Director of the Executives' Club of Chicago, the Chicago Network, and a  
7 member of the Forum of Executive Women, the Commercial Club of Chicago,  
8 the Economic Club of Chicago and the University Club of Chicago.

9 I received both my undergraduate and law degrees from the University  
10 of Illinois, where I was a Bronze Tablet (upper three percent) recipient and a  
11 member of the law review.

12 Throughout the years, I have been honored to receive numerous awards  
13 including the 2003 Association of Professional Fundraisers Award for  
14 Executive Leadership, the 2003 Myra Bradwell Award for Excellence in the  
15 Profession from the Women's Bar Association of Illinois, the 2002 Luminary  
16 Award from the Girl Scouts of Chicago, the Diversity 2000 Award from the  
17 Minority Corporate Counsel Association, the 1997 Women of Achievement  
18 Award from the Anti-Defamation League. In 1996, I was named one of the  
19 most distinguished alumnae of the University of Illinois College of Law. In  
20 2002, I was named to Fortune's 50 Most Powerful Women, received the

1 YWCA of Metropolitan Chicago's Outstanding Achievement Award in  
2 Business, and was inducted into Today's Chicago Woman Hall of Fame. In  
3 2004, I was named to Crain's Chicago Business' list of Chicago's 100 Most  
4 Influential Women and the Chicago Sun-Times' list of Top 10 Businesswomen  
5 in Chicago.

6  
7 **Q. What are your duties and responsibilities in your current job?**

8  
9 **A.** In my capacity as Chief Administrative Officer of Exelon, I provide strategic  
10 direction to Exelon BSC, Exelon Enterprises, Exelon Corporate  
11 Communications, and also serve on the Exelon Strategy & Policy Committee.  
12 In that role I help facilitate the strategic direction of the corporation. I am also  
13 President of Exelon BSC. Exelon BSC provides transactional, corporate and  
14 energy delivery shared services to the Exelon system companies in many areas  
15 as described in greater detail in this testimony.

16  
17 **II. PURPOSE AND SCOPE OF TESTIMONY**

18  
19 **Q. What is the purpose of your testimony?**

20  
21 **A.** I am providing this testimony in support of the request of Exelon and Public  
22 Service Electric and Gas Company ("PSE&G") that the New Jersey Board of  
23 Public Utilities (the "Board") approve as part of this Merger proceeding,

1 certain service agreements that will facilitate the sharing of certain functions,  
2 systems and services among the merged companies.

3  
4 **Q. What specific topics does your testimony address?**

5  
6 **A.** First, I will describe the specific agreements that will facilitate the sharing of  
7 services between the merged companies and for which we seek the Board's  
8 approval. Second, I describe those agreements and their purpose. Further, I  
9 describe the combination of Exelon BSC and PSEG Services Corporation  
10 ("PSEG Services") that will facilitate much of the sharing of services. For  
11 background purposes, I will describe Exelon BSC and the services that it  
12 currently provides to the Exelon system companies and provide a comparison  
13 with PSEG Services and the services it provides to PSE&G and its affiliates.  
14 My testimony also describes the services that the new combined service  
15 company will provide to PSE&G and its affiliates post-Merger. Perhaps most  
16 importantly, my testimony also sets forth our commitment to provide high  
17 quality advisory, professional, technical and other support services to PSE&G  
18 in accordance with all applicable New Jersey laws and regulations.

19  
20



1           accordance with the MSA include any such services that are appropriate, under  
2           applicable state law and Public Utility Holding Company Act of 1935  
3           (“PUHCA”), to be provided between the state regulated utility and its  
4           affiliates, including such services as emergency response services between  
5           operating utilities. In order to ensure that PSE&G is also positioned to engage  
6           in such appropriate affiliate interest transactions and to facilitate such  
7           efficiencies, the Joint Petitioners have also submitted a form of MSA for the  
8           Board’s approval.

9  
10       **Q.    Please describe in greater detail the GSA and Exelon BSC structure.**

11  
12       **A.    Exelon is a registered holding company under the PUHCA. One of Exelon’s**  
13           first tier subsidiaries is Exelon BSC, a company organized for the purpose of  
14           providing advisory, professional, technical and other services to the Exelon  
15           system companies. The organization, conduct of business and method of cost  
16           allocation at Exelon BSC are designed to meet the requirements of Section 13  
17           under PUHCA and the rules and regulations promulgated thereunder. Exelon  
18           BSC provides a wide array of services to the Exelon system companies in  
19           accordance with its GSA. Exelon BSC currently provides services to two state  
20           regulated public utilities, PECO and ComEd. As a result, its services to these  
21           entities and the charges for those services also conform to applicable state laws  
22           in Pennsylvania and Illinois.

1           Currently, Exelon BSC is divided into three functional groups  
2           (corporate services, transactional services, and energy delivery shared services)  
3           whose employees are housed in two business units — the Corporate and  
4           Transactional Functional Areas, and Energy Delivery Shared Services  
5           (“EDSS”). The following are general descriptions of each of the three groups.

- 6           • Corporate Functional Area. The Corporate Functional Area houses employees  
7           who provide corporate governance services, including executive management,  
8           human resources, security, finance (including treasury, accounting, tax, risk  
9           management, internal audit, investor relations and external reporting and  
10          planning), communications, governmental affairs, environmental affairs, and  
11          legal governance/corporate development (including corporate secretary  
12          functions).
  
- 13          • Transactional Functional Area. The Transactional Functional Area provides a  
14          variety of transactional shared services including information technology  
15          (“IT”), supply, support services, payroll, accounts payable, benefits  
16          administration, media and legal services. It is from this area of Exelon BSC  
17          that many enterprise-wide applications and infrastructure such as IT are  
18          centrally managed and business unit specific projects are provided.
  
- 19          • Energy Delivery Shared Services (“EDSS”). The EDSS Area generally  
20          provides services only to ComEd and PECO and includes executive and  
21          centralized management and direction for all utility operating functions. These  
22          services include utility financial planning and controller services, utility  
23          property management, energy acquisition, claims administration, quality  
24          assurance and performance improvement, environmental, safety, and industrial  
25          hygiene and training. EDSS also provides executive management and  
26          direction for Customer Service and marketing services; Technical Services  
27          (including engineering, work management, project and contract controls), and  
28          Transmission Operations and Planning Services. While the executive  
29          management and governance for each of these utility functions is performed  
30          out of Exelon BSC, to achieve efficiencies and ensure the sharing and  
31          standardization of best practices, the day-to-day field activities are generally

1 performed by employees who are dedicated specifically to either ComEd or  
2 PECO, and those resources are employees of the respective utility.

3 As of December 31, 2004, Exelon BSC had 2,012 employees, 463 of  
4 whom were EDSS employees.

5  
6 The specific services performed from time to time by Exelon BSC for  
7 the Exelon system companies within the general categories listed above are set  
8 out in a series of service level arrangements between Exelon BSC and the  
9 particular company taking a particular service. Where possible, costs are direct  
10 charged. For costs that cannot be direct charged, the principal allocation  
11 methodologies currently utilized by Exelon BSC include the Modified  
12 Massachusetts Formula, Headcount, and Expenditure Related.

13  
14 **Q. Please describe in greater detail the MSA.**

15  
16 **A.** The MSA recognizes that certain expertise to provide shared services remains  
17 embedded within the state regulated utilities. Where appropriate under  
18 PUHCA, and state law, the MSA allows the Exelon system companies to  
19 maximize efficiencies and achieve cost savings by having services provided by  
20 the least cost provider thereof whenever possible. A broad variety of services  
21 may be provided under the MSA, including emergency response services and  
22 other services for which the expertise to supply is embedded in an Exelon  
23 system company other than Exelon BSC. A party requesting services under  
24 the agreement shall pay the party providing those services the cost of those

1 services, except as otherwise directed or permitted by an appropriate regulatory  
2 authority, insofar as costs can reasonably be identified and related to the  
3 particular services in question or otherwise fairly and equitably allocated to  
4 such services. To the extent that PSE&G or any related competitive business  
5 segment of PSE&G, as defined in N.J.A.C. 14:4-5.2, is a participant in a  
6 particular transaction, the MSA expressly provides that the company  
7 requesting services shall pay to the providing company charges for services  
8 that comply with the Board's decisions, rules and regulations.

9  
10 **Q. Please describe the manner in which Exelon BSC charges the Exelon**  
11 **system companies for services.**

12  
13 **A.** As a registered holding company system, the Exelon system companies are  
14 subject to the affiliate transaction and cost-allocation rules of the SEC under  
15 PUHCA. Those rules generally provide that no service company (*i.e.*, Exelon  
16 BSC) may perform any service, or provide any goods to, any affiliate other  
17 than "at cost." Cost as defined in the Securities and Exchanged Commission's  
18 (SEC) rules is essentially fully distributed cost. *See* 17 CFR Secs 250.90 and  
19 250.91. These rules and cost allocation requirements are spelled out in  
20 Exelon's GSA, which is designed to be consistent with the SEC's cost  
21 allocation regulations. Direct charges are made for services where possible.  
22 Where costs cannot be directly charged or where it would be inappropriate to

1 charge in this manner, allocation methodologies are used depending upon the  
2 nature of the cost. Other elements of cost, including taxes, other overhead, and  
3 compensation for the use of debt capital are fairly and equitably allocated  
4 employing SEC reviewed allocation ratios. Exelon BSC funds its working  
5 capital needs via borrowings from the Exelon Utility Money Pool (“Money  
6 Pool Agreement”), as authorized by the SEC. (Holding Co. Act Release No.  
7 27830). Further details on the Money Pool Agreement are provided in the  
8 supporting testimony of J. Barry Mitchell, Exelon’s Senior Vice President,  
9 Treasurer and Business Unit Chief Financial Officer.

10  
11 **Q. In addition to the safeguards built into the GSA, please describe other**  
12 **mechanisms to ensure that no improper subsidization takes place between**  
13 **affiliates receiving services from Exelon BSC**

14  
15 **A.** In addition to the SEC rules restricting service charges to cost, as described  
16 above, each Exelon affiliate maintains separate books, accounts and records in  
17 accordance with generally accepted accounting principles (“GAAP”) and with  
18 the provisions of applicable state laws. These separate books, accounts and  
19 records facilitate the auditing of costs that are attributable to a particular  
20 affiliate. This same practice, which is in use today by PSE&G and PSEG  
21 Services, will be followed for PSE&G post-Merger. Finally, Exelon BSC  
22 maintains its books, accounts and records in accordance with the SEC’s

1 Uniform System of Accounts for Mutual Service Companies and Subsidiary  
2 Service Companies, 17 CFR Part 256. I believe these requirements are  
3 adequate to ensure that there is no improper subsidization.

4 **Q. What regulatory approvals were received in connection with this existing**  
5 **Exelon shared services structure?**

6  
7 **A.** Exelon BSC's structure, its form of GSA and allocation methodologies, were  
8 initially approved by the SEC at the time of the Unicom/PECO Merger (See  
9 Holding Co. Act Release No. 35-27256), subject to continuing reporting,  
10 supervision and audit of service company activities. In addition to being  
11 scrutinized by the SEC, the GSA was approved by the Pennsylvania Public  
12 Utility Commission ("PAPUC") and by the Illinois Commerce Commission  
13 ("ICC").

14  
15 **Q. Please describe the current service company structure at PSEG.**

16  
17 **A.** It is my understanding, based upon my review of the existing PSEG Services  
18 Agreement, that PSE&G currently receives a broad array of corporate support,  
19 managerial and administrative services from PSEG Services. These services  
20 are provided pursuant to a Service Agreement approved by the Board. *In The*  
21 *Matter Of Petition Of Public Service Electric And Gas Company For Approval*  
22 *Of A Service Agreement With PSEG Services Corporation And Transfer Of*

1        *Assets*, Docket No. EM00040253, OAL Docket No. PUC 1187-03, April 22,  
2        2004. PSEG Services likewise offers these services to PSE&G's affiliates  
3        pursuant to the same form Service Agreement.

4                The PSEG Service Agreement provides that PSEG Services will charge  
5        PSE&G and its affiliates for services rendered in a manner that ensures that all  
6        costs of doing business are compensated. All of the services rendered by  
7        PSEG Services are charged using a fully allocated cost methodology. Direct  
8        charges are made for services where possible. Where costs cannot be directly  
9        charged or where it would be inappropriate to charge in this manner, allocation  
10       methodologies are used depending upon the nature of the cost. The principal  
11       allocation methodologies currently utilized by PSEG Services include the  
12       Modified Massachusetts Formula and Headcount. These cost  
13       assignment/allocation methodologies are reviewed periodically as deemed  
14       appropriate by the operating companies receiving the services and PSEG  
15       Services.

16               The Service Agreement also requires each operating company receiving  
17       services to contribute to a working capital fund on an as needed basis. PSEG  
18       Services uses this working capital fund to make payments for all costs incurred  
19       in providing its services and in discharging its responsibilities under the  
20       Service Agreement. Each operating company, including PSE&G, currently

1 funds the working capital fund and to the extent that there is a material excess  
2 or a deficiency in the working fund, the contributing operating companies  
3 receive, or are charged, interest at PSEG Services' borrowing rate.

4  
5 **Q. Are there significant differences in the types of services offered or the**  
6 **methodology used to charge for those services between Exelon BSC and**  
7 **PSEG Services?**

8  
9 **A.** No. While there are some differences in the services provided by Exelon BSC  
10 and PSEG Services, in general, the major categories of available services are  
11 similar. Also, there are some differences in particular allocation  
12 methodologies employed by Exelon BSC and PSEG Services. The general  
13 framework, however, of the service company agreements and the policies and  
14 principles that are used to provide those services are substantially similar.

15 I believe there are three key drivers of the differences that do exist:

- 16
- 17 • First, Exelon BSC serves the needs of both PECO and ComEd and is in  
18 a position to offer the benefits of centralizing certain support functions  
19 that are unique to these types of businesses. The services offered by the  
20 Energy Delivery Shared Services Group of Exelon BSC to PECO and  
21 ComEd create efficiencies and allow best practices to be shared in  
22 support services provided to these state regulated utility companies.  
PSEG Services currently serves only one electric and gas distribution

1 and transmission company, PSE&G. As a result, many of the types of  
2 services offered by the EDSS Group of Exelon BSC simply did not  
3 make sense for the current PSEG Services structure as they would have  
4 only benefited one entity. For example, Exelon BSC provides executive  
5 management and direction over customer billing and payment  
6 processing, whereas PSE&G retained these functions.

7 • Second, as described above, Exelon BSC is subject to the jurisdiction of  
8 the SEC and PSEG Services is not. The SEC regulates and audits the  
9 services and charges that are offered by Exelon BSC. The primary  
10 focus of the SEC's rules is to ensure that services are rendered at cost  
11 and are fairly and equitably allocated. This same principle has been  
12 followed by PSEG Services; however, the allocation methodologies  
13 reviewed by the SEC for use by Exelon BSC differ in some respects  
14 from those used by PSEG Services.

15 • Third, there are differences between which services are offered from the  
16 service companies versus which services are provided by employees or  
17 systems embedded in the operating companies. For example, the  
18 Exelon operating companies retain certain services such as company-  
19 specific HR, Communications, and IT, whereas at PSEG these services

1           are provided by PSEG Services and the costs are directly charged back  
2           to the benefiting company.

3           These differences will be evaluated and worked through during the  
4           integration process. At the end of that process, there may be a decision to  
5           functionally move certain employees currently embedded in PSE&G to Exelon  
6           BSC and to functionally move some PSEG Services employees back to  
7           PSE&G to provide the services consistently across all companies. In any  
8           event, the two agreements for which the Joint Petitioners are seeking approval  
9           will support the structure regardless of these details by ensuring that two cost-  
10          based service agreements are in place to provide services whether from Exelon  
11          BSC or PSE&G.

12  
13 **Q.    What is the anticipated structure for the service company and the service**  
14 **company arrangements post Merger?**

15 **A.**As described in the Petition, as part of the Merger transaction the activities of  
16          PSEG Services will be combined with those of Exelon BSC. As part of this  
17          combination, PSEG Services will sell and transfer its assets and rights to  
18          Exelon BSC. Exelon BSC will continue to provide the types of services that it  
19          currently offers and will render such services to the expanded Exelon system of  
20          companies including PSE&G. Services will be rendered at cost, fairly and  
21          equitably allocated pursuant to the GSA approved by the SEC, the PAPUC, the

1 ICC and at the conclusion of this proceeding - the Board. Exelon BSC will use  
2 direct charges to the extent practicable. Other elements of cost, including  
3 taxes, other overhead, and compensation for the use of debt capital shall be  
4 fairly and equitably allocated employing SEC compliant allocation ratios.  
5

6 **Q. Will this new structure significantly affect any of the services that PSE&G**  
7 **is currently receiving from PSEG Services?**

8  
9 **A.** No. I am not aware of any basis upon which to believe that the types of  
10 services that PSE&G is receiving currently from PSEG Services or through  
11 embedded services within PSE&G will be significantly affected. Rather, it is  
12 my expectation that as a result of synergies and the sharing of best practices  
13 that will result from the combination of PSEG Services and Exelon BSC that  
14 the value of the services that PSE&G receives will be improved. As noted  
15 above, there may be changes in which entity provides the service, such as  
16 services currently performed in PSEG Services being moved back to PSE&G  
17 or having certain functions performed by PSE&G moved to Exelon BSC post  
18 closing. To the extent these changes are made, I do not expect any significant  
19 change in the level or quality of service being provided to PSE&G.  
20

1 **Q. Will the combination of the service companies increase the price that**  
2 **PSE&G currently pays for these corporate support services?**

3  
4 **A.** While as yet there have been no detailed comparative reviews of the pricing of  
5 specific services of the two service companies, the combination of PSEG  
6 Services and Exelon BSC is not expected to increase the cost of providing  
7 services. There will be a transition period during which the combination of  
8 systems and functions is being implemented, which may entail higher costs for  
9 this transition period. Once that transition period is completed, the  
10 combination of the service organizations and centralization of many services  
11 will be the source of significant synergies. As identified in the testimony of  
12 William D. Arndt, it is through the reduction of duplicative functions and the  
13 integration of resources and systems, such as a common customer billing  
14 system, that many of the benefits of the Merger will be created.

15  
16 **Q. Will the combination of the service companies result in any decrease of**  
17 **authority or jurisdiction by the New Jersey Board?**

18  
19 **A.** No. Exelon BSC will comply with all applicable state laws and regulations,  
20 including New Jersey. Exelon BSC is committed to provide high quality  
21 support services to all of the Exelon system companies and will continue such  
22 commitment after the Merger in a manner that is in accordance with all  
23 applicable New Jersey laws and regulations.

1

2 **Q. Please describe the regulatory framework that the Exelon BSC will be**  
3 **subject to post-Merger.**

4

5 **A.** Exelon BSC is and will continue to be regulated by the SEC. As Exelon BSC  
6 will provide services to state regulated public utilities such as PSE&G, PECO  
7 and ComEd, those services and the related charges will continue to be subject  
8 to applicable state laws and regulations.

9

10 **Q. Please describe the methodologies that the service company will use to**  
11 **charge PSE&G.**

12

13 **A.** As discussed earlier in my testimony, Exelon BSC will use direct charges to  
14 the extent practicable. Other elements of cost, including taxes, and other  
15 overhead, shall be fairly and equitably allocated employing SEC compliant  
16 allocation ratios. The ratios are set forth in the GSA which is an exhibit to the  
17 Petition.

18

19 **Q. Will PSE&G be required to take services from Exelon BSC?**

20

21 **A.** In accordance with the GSA, Exelon BSC agrees to provide services only at  
22 such times and for such period and in such manner as an Exelon system  
23 company may from time to time request. The only exception to this policy is  
24 with respect to "Corporate Governance Services" as defined in Section 7 of the

1 GSA. Corporate governance consists of those activities and services  
2 reasonably determined to be necessary for the lawful and effective  
3 management of Exelon system businesses.

4  
5 **Q. Will the Board have access to the books and records of the combined**  
6 **service companies?**

7  
8 **A.** The records of Exelon BSC will be maintained in accordance with 17 C.F.R.  
9 §257.1. In accordance with the GSA and SEC regulations, all records must be  
10 retained for no less than seven years following a transaction. Exelon  
11 recognizes that the Board, under its authority pursuant to the Electric Discount  
12 and Energy Competition Act, has the right to audit PSE&G's affiliate  
13 relationships every two years. Exelon further recognizes that as part of that  
14 audit, the Board may request access to the books and records of Exelon BSC  
15 and its affiliates, which pertain to services that they provide to PSE&G.  
16 Exelon BSC commits to providing access to books and records to the full  
17 extent required by New Jersey law.

18

1 **Q. Can you summarize the approvals you are seeking from the Board in**  
2 **regard to the service agreements you have discussed in your testimony?**

3

4 **A.** Yes. Exelon and PSE&G request approval of the following agreements, each  
5 of which is attached to the Petition, that PSE&G will become a signatory to  
6 upon consummation of the merger:

- 7       • General Services Agreement  
8       • Mutual Services Agreement

9

10 **Q. Does this conclude your prepared direct testimony?**

11 **A.** Yes.

A-110550F0160

As filed with the Securities and Exchange Commission on March 15, 2005 File No. 70-10294

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM U-1  
APPLICATION-DECLARATION  
UNDER  
THE PUBLIC UTILITY HOLDING COMPANY ACT OF 1935**

**Exelon Corporation**  
(and the Subsidiaries listed on the  
Signature Page hereto)  
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37<sup>th</sup> Floor  
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**Public Service**  
**Enterprise Group Incorporated**  
(on behalf of the Subsidiaries listed on  
the Signature Page hereto)  
80 Park Plaza  
Newark, New Jersey 07102

(Name of companies filing this statement and address of principal executive office)

**Exelon Corporation**

(Name of top registered holding company)

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## Item 1. Description of Proposed Transaction

### A. Introduction.

In this Form U-1 application/declaration (this "Application"), Applicants are seeking approval pursuant to Sections 6(a), 7, 8, 9, 10, 12, 13, 32 and 33 of the Public Utility Holding Company Act of 1935 (the "Act") and the rules thereunder to engage in various transactions related to the merger of Exelon Corporation ("Exelon") and Public Service Enterprise Group Incorporated ("PSEG"), as described more fully herein.<sup>1</sup>

On December 20, 2004, Exelon and PSEG, an electric and gas utility holding company that claims exemption from registration pursuant to Rule 2 under Section 3(a)(1) of the Act, entered into an Agreement and Plan of Merger (the "Merger Agreement").<sup>2</sup> Pursuant to the terms of the Merger Agreement, PSEG will merge into Exelon (the "Merger"), thereby ending the separate corporate existence of PSEG. Each PSEG shareholder will be entitled to receive 1.225 shares of Exelon common stock for each PSEG share held and cash in lieu of any fraction of an Exelon share that a PSEG shareholder would have otherwise been entitled to receive. Exelon common stock will be unaffected by the Merger, with each issued and outstanding share remaining outstanding following the Merger as a share in the surviving company. Upon completion of the Merger, Exelon will change its name to Exelon Electric & Gas Corporation.<sup>3</sup>

As the surviving company in the Merger, Exelon will remain the ultimate corporate parent of PECO Energy Company ("PECO") and Commonwealth Edison Company ("ComEd") and the other Exelon subsidiaries and become the ultimate corporate parent of Public Service Electric and Gas Company ("PSE&G"), a public utility company under the Act, and the other PSEG subsidiaries.

Exelon will continue to be a registered public utility holding company under the Act, and ComEd, PECO and PSE&G will continue to be operating franchised utility companies. Exelon will remain headquartered in Chicago but will also have energy trading and nuclear headquarters in southeastern Pennsylvania and generation headquarters in Newark, New Jersey. PSE&G will remain headquartered in Newark. PECO will remain headquartered in Philadelphia and ComEd will remain headquartered in Chicago.

The Merger is subject to a number of usual and customary conditions precedent, including receipt by the parties of required state and federal regulatory approvals and filing of pre-merger notification statements under the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended ("HSR Act"), and the expiration or termination of the statutory waiting period thereunder. (See Item 4 - Regulatory Approvals.) The boards of directors of Exelon and PSEG have approved the proposed Merger, which will also require approval of the issuance of shares of common stock by Exelon required by the Merger Agreement by the shareholders of Exelon and approval of the Merger by the shareholders of PSEG.

In addition to the changes resulting from the Merger Agreement, the Applicants intend to revise their corporate structure (the "Exelon Generation Restructuring"). Although their plans are not yet completely finalized, the Applicants currently propose to implement the following changes, subject to approval, as required, by the Securities and Exchange Commission (the "Commission"). After obtaining

---

<sup>1</sup> The Applicants are Exelon and its Subsidiaries listed on the Signature Page hereto, and PSEG and its Subsidiaries listed on the Signature Page hereto, and such other direct and indirect subsidiary companies that Exelon may hereinafter form or acquire in accordance with a Commission order or otherwise in accordance with the Act or a rule promulgated thereunder.

<sup>2</sup> A copy of the Merger Agreement was filed with the Commission by Exelon with a Current Report on Form 8-K on December 21, 2004. The Merger Agreement is incorporated herein by reference. The description of the Merger Agreement herein is qualified in its entirety by reference to the full text of the Merger Agreement.

<sup>3</sup> As appropriate in the context, the term "Exelon" refers variously to Exelon Corporation pre-Merger and to Exelon Electric & Gas Corporation post-Merger.

necessary approvals and third party consents, PSEG Power LLC ("PSEG Power") and its direct subsidiaries PSEG Nuclear LLC ("PSEG Nuclear"), PSEG Fossil LLC ("PSEG Fossil") and PSEG Energy Resources & Trade LLC ("PSEG ER&T") will all cease to exist as separate entities and will become part of Exelon Generation Company, LLC ("Exelon Generation"). The business functions of each of these former PSEG entities will become a part of the respective Exelon Generation business unit. It is anticipated that the subsidiaries owned by these PSEG entities will be retained as direct subsidiaries of Exelon Generation.

Also in connection with the Merger, PSE&G will become a direct subsidiary of Exelon Energy Delivery Company, LLC ("Delivery").<sup>4</sup> The current subsidiaries of PSE&G will remain intact. PSEG Energy Holdings LLC ("PSEG Holdings") will become a subsidiary of Exelon, as the successor to PSEG. The current subsidiaries of PSEG Holdings will remain intact. PSEG Services Corporation ("PSEG Services") will sell all of its assets to Exelon Business Services Company ("Exelon BSC"), change its name, and remain as a non-energy subsidiary. Exelon BSC will be the sole "service company" of Exelon.

A summary diagram depicting Exelon's proposed post-Merger corporate structure is filed herewith as Exhibit G-1. Diagrams depicting the existing corporate structure of the Exelon system as well as the PSEG system are filed herewith as Exhibits G-2 and G-3, respectively.

Exelon and PSEG have proposed a plan to mitigate any generation market concentration concerns resulting from the Merger, which calls for Exelon to divest certain generation capacity.<sup>5</sup> The sale of this generation capacity will occur as soon as possible within 18 months following close of the Merger. Approval of the Commission will be required for the disposition of this generation capacity because, as a result of the Exelon Generation Restructuring, this generation capacity will be owned by Exelon Generation, a public utility under the Act. The disposition of generation capacity owed by Exelon Generation is referred to as the "Generation Divestiture."<sup>6</sup>

In addition to authorization of the Merger, the Exelon Generation Restructuring, and the Generation Divestiture, Applicants are requesting certain related approvals, including:

1. Authorizations related to service company and other affiliate transactions.
2. Issuance by Exelon of common stock in connection with the Merger and employee and director compensation plans as described below.
3. Authorization to the extent required of the consolidation (or replacement in lieu of consolidation) of existing indebtedness and obligations of PSEG and its subsidiaries as obligations of Exelon or its subsidiaries as a result of the Merger.
4. Necessary modifications to Exelon's existing omnibus financing authority granted by order of April 1, 2004 in Holding Company Act Release No. 27830 (the "2004 Financing Order").

Applicants request that the Commission issue a final order granting the requested authority without an evidentiary hearing, as expeditiously as feasible, but no later than December 15, 2005.

---

<sup>4</sup> This will be accomplished through a contribution of the common stock of PSE&G held by Exelon immediately following the Merger to Delivery or other appropriate corporate transaction.

<sup>5</sup> The mitigation plan also proposes to transfer control of the output of a portion of Exelon's baseload nuclear generating capacity, which transfer is not jurisdictional under the Act.

<sup>6</sup> The Exelon Generation Restructuring and Generation Divestiture will require regulatory approvals in addition to those from the Commission as described elsewhere herein.

B. Description of Exelon and Its Subsidiaries

1. Exelon, Generally

Exelon was incorporated in Pennsylvania in February 1999. On October 20, 2000, Exelon became the ultimate parent corporation for PECO and ComEd, and registered pursuant to Section 5 of the Act.

Exelon, through its subsidiaries, operates in three business segments - Delivery, Generation and Enterprises - as described below. In addition to Exelon's three business segments, Exelon BSC, a subsidiary of Exelon, provides Exelon and its subsidiaries with financial, human resources, legal, information technology, supply management and corporate governance services, as well as direction and management of shared functions for Delivery.

Delivery. Exelon's energy delivery business consists of the purchase and sale of electricity and distribution and transmission services by ComEd in northern Illinois and by PECO in southeastern Pennsylvania and the purchase and sale of natural gas and distribution services by PECO in the Pennsylvania counties surrounding the City of Philadelphia.

Generation. Exelon's generation business consists of the owned and contracted for electric generating facilities and energy marketing operations of Exelon Generation, a 49.5% interest in two power stations in Mexico, and the competitive retail sales business of Exelon Energy Company.

Enterprises. Exelon's enterprise business consists primarily of the remaining infrastructure and electrical contracting services of Exelon Enterprises Company, LLC ("Enterprises") and other investments weighted towards the communications and energy services industries. Exelon plans to divest or wind-down the remaining assets of Enterprises during 2005.

2. The Exelon Utility Subsidiaries

Exelon indirectly owns all of the issued and outstanding membership interests of Exelon Generation, all the issued and outstanding common stock of PECO and substantially all of the issued and outstanding common stock of ComEd,<sup>7</sup> and ComEd owns all the issued and outstanding common stock of Commonwealth Edison Company of Indiana, Inc. (the "Indiana Company") (together, the "Exelon Utility Subsidiaries").

PECO is engaged principally in the purchase, transmission, distribution and sale of electricity to residential, commercial and industrial customers in southeastern Pennsylvania and in the purchase, distribution and sale of natural gas to residential, commercial and industrial customers in the Pennsylvania counties surrounding the City of Philadelphia. PECO is subject to extensive regulation by the Pennsylvania Public Utility Commission ("PAPUC") as to electric and gas rates, the issuances of certain securities and certain other aspects of PECO's operations. PECO is also subject to regulation by the Federal Energy Regulatory Commission ("FERC") as to transmission rates, gas pipelines and certain other aspects of its business.

PECO's retail service territory covers approximately 2,100 square miles in southeastern Pennsylvania. PECO provides electric delivery service in an area of approximately 2,000 square miles, with a population of approximately 3.8 million, including 1.5 million in the City of Philadelphia. Natural gas service is supplied in an approximately 1,900 square mile area in southeastern Pennsylvania adjacent to

---

<sup>7</sup> In connection with the conversion of warrants and convertible preferred stock that were outstanding prior to the 2000 merger of Unicom Corporation with PECO Energy Corp., a small number of shares of common stock of ComEd (about 0.1% of the total outstanding) are not owned by Exelon but are held by third parties. See *Exelon Corporation, Holding Co. Act Release No. 27256*, note 4 (Oct. 19, 2000) (the "2000 Merger Order").

Philadelphia, with a population of approximately 2.3 million. PECO delivers electricity to approximately 1.5 million customers and natural gas to approximately 460,000 customers.

ComEd is engaged principally in the purchase, transmission, distribution and sale of electricity to a diverse base of residential, commercial, industrial and wholesale customers in northern Illinois. ComEd is subject to extensive regulation by the Illinois Commerce Commission ("ICC") as to rates, the issuance of certain securities, and certain other aspects of ComEd's operations. ComEd is also subject to regulation by the FERC as to transmission rates and certain other aspects of its business.

ComEd's retail service territory has an area of approximately 11,300 square miles and an estimated population of eight million. The service territory includes the City of Chicago, an area of about 225 square miles with an estimated population of three million. ComEd has approximately 3.7 million customers.

Electric utility restructuring legislation was adopted in Pennsylvania in December 1996 and in Illinois in December 1997. Both Illinois and Pennsylvania permit competition by alternative generation suppliers for retail generation supply while transmission and distribution service remains fully regulated. Both states, through their regulatory agencies, established a phased approach for allowing customers to choose an alternative electric generation supplier, required rate reductions and imposed caps on rates during a transition period, and allowed the collection of competitive transition charges from customers to recover costs that might not otherwise be recovered in a competitive market.

Effective as of January 1, 2001, Exelon effected a restructuring that involved the transfer of the electric generating assets of ComEd and PECO to Exelon Generation, a Pennsylvania limited liability company and a public utility company engaged in the generation, sale and purchase of electricity in Pennsylvania, Illinois and elsewhere and also engaged in the trading of other energy and energy-related commodities and development and ownership of exempt wholesale generators ("EWGs").

PJM Interconnection, L.L.C. ("PJM") is the independent system operator and the FERC-approved Regional Transmission Organization ("RTO") for the Mid-Atlantic and a portion of the Midwest. PJM is the transmission provider under, and the administrator of, the PJM Open Access Transmission Tariff, operates the PJM Interchange Energy Market and Capacity Credit Markets, and conducts the day-to-day operations of the bulk power system of the PJM region. ComEd's and PECO's transmission systems are currently under the control of PJM and, by order dated October 28, 2004 (Holding Co. Act Release No. 27904) (the "PJM Order"), the Commission found that the electric utility properties of the Exelon system satisfy the interconnection requirement of Section 2(a)(29)(A) of the Act by reason of PJM's operational control of the transmission assets of ComEd and PECO.<sup>8</sup>

Each of ComEd and PECO is a public utility company within the meaning of the Act. ComEd is also a holding company exempt from registration pursuant to Section 3(a)(1) of the Act, by reason of its ownership of the Indiana Company, which is a fourth public utility company subsidiary, with no retail operations. Delivery is an intermediate registered holding company and a first-tier subsidiary of Exelon. Delivery owns all of the issued and outstanding common stock of PECO and substantially all of the issued and outstanding common stock of ComEd. *See* Note 7.

Exelon Generation is also an electric utility company within the meaning of the Act. Exelon Generation is a wholly owned subsidiary of Exelon Ventures Company, LLC ("Ventures"), which is an intermediate registered holding company and a first tier subsidiary of Exelon. Ventures and Delivery are

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<sup>8</sup> In the 2000 Merger Order approving the formation of Exelon, the Commission had found that the electric utility operations of Exelon constituted a single, integrated electric utility system, and that the gas utility operations of Exelon constituted a single, integrated gas utility system that was a permissible "additional" system under the standards of Section 2(a)(11) of the Act. The findings of the 2000 Merger Order were based in part on a certain 100 MW firm west-to-east transmission contract path (the "Contract Path"). The PJM Order found that PJM's operational control of the transmission assets of ComEd and PECO obviated the need for the Contract Path.

referred to herein as the "Other Registered Holding Companies." None of the Other Registered Holding Companies has securities outstanding in the hands of the public.

3. Direct Non-Utility Subsidiaries of Exelon

Exelon has direct wholly owned non-utility subsidiaries (in addition to its direct, wholly owned registered holding company subsidiaries, Ventures and Delivery), as follows:

Exelon BSC, a service company, provides administrative, management and technical services to Exelon and its associate companies;

Exelon Investment Holdings, LLC, an Illinois limited liability company, is a holding company for tax-advantaged housing transactions;

UII, LLC, an Illinois limited liability company, is engaged in a like-kind exchange transaction pursuant to which a portion of the proceeds from the sale of ComEd's fossil generating stations was invested in passive generating station leases with entities unrelated to Exelon. The generating stations were leased back to such entities as part of the transaction.<sup>9</sup>

Exelon has the following additional direct subsidiaries: Unicom Assurance Company, Ltd., an inactive captive insurance company, Exelon Capital Trust I, an inactive finance company, Exelon Capital Trust II, an inactive finance company and Exelon Capital Trust III, an inactive finance company.

4. Capitalization of Exelon

The total authorized shares of capital stock of Exelon consist of (i) 1,200,000,000 shares of common stock, no par value and (ii) 100,000,000 shares of preferred stock, no par value.<sup>10</sup> At the close of business on December 31, 2004, 664,187,996 shares of Exelon common stock were outstanding, and no shares of Exelon preferred stock were issued and outstanding. In addition, at that date (i) 2,499,865 shares of common stock were held by Exelon in its treasury, (ii) 25,205,285 shares of common stock were reserved for issuance pursuant to outstanding options to purchase common stock granted under Exelon's Long-Term Incentive Plan, Exelon's Amended and Restated Long-Term Incentive Plan, as amended, and Exelon's 1998 Stock Option Plan (together with Exelon's Directors' Stock Unit Plan, the "Exelon Stock Incentive Plans"), (iii) 14,777,078 shares of common stock were reserved for the grant of additional awards under the Exelon Stock Incentive Plans, (iv) 7,000,000 shares of common stock were reserved for issuance pursuant to the Dividend Reinvestment and Stock Purchase Plan, (v) 624,495 shares of common stock were reserved for issuance pursuant to outstanding performance shares, (vi) 216,000 shares of common stock were reserved for issuance pursuant to outstanding units under Exelon's Directors' Stock Unit Plan, (vii) 5,357,745 shares of common stock were reserved for issuance under Exelon's Employee Stock Purchase Plan, (viii) 1,060,053 shares of common stock were reserved for issuance pursuant to outstanding restricted shares (shares of common stock subject to forfeiture) and (ix) 1,336,516 shares of common stock were reserved for issuance pursuant to outstanding deferred shares (shares of common stock the issuance of which has been deferred pursuant to Exelon's Deferred Compensation Plan).

As of December 31, 2004, Exelon's capitalization on a consolidated basis was as follows:

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<sup>9</sup> Unicom Investment, Inc., an Illinois corporation, was reorganized as an Illinois limited liability company, UII, LLC on November 10, 2004.

<sup>10</sup> In connection with the proposed Merger, Exelon is seeking approval to amend its Amended and Restated Articles of Incorporation to increase its authorized common stock to 2,000,000,000 shares. See File No. 70-10291. That filing also seeks approval for solicitation of proxies in connection with the Merger and certain employee and director plan changes.

**EXELON CORPORATION**  
**CONDENSED CONSOLIDATED CAPITAL STRUCTURE**

(Dollars in Millions)  
As of December 31, 2004

**Consolidated Capitalization**

	<b>Amount</b>	<b>Capital Structure Percentage</b>
Common Equity (includes Retained Earnings of \$3,353)	\$9,423	40.79%
Minority Interest	42	0.18%
Preferred and Preference Stock	632	2.74%
Securitization Obligations	4,797	20.76%
Long-Term Debt	7,292	31.56%
Current Maturities of Long-Term Debt	427	1.85%
Total Long-Term Debt	7,719	33.41%
Short-Term Debt	490	2.12%
Total Capital Structure	<u>\$23,103</u>	<u>100.00%</u>

Additional information regarding Exelon and its subsidiary companies is set forth in the following documents, each of which has been previously filed with the Commission and is incorporated herein by reference:

(i) Annual Report on Form 10-K of Exelon (Commission File No. 1-16169), ComEd (Commission File No. 1-1839), PECO (Commission File No. 1-1401) and Exelon Generation (Commission File Number No. 333-85496) for the fiscal year ended December 31, 2004, filed with the Commission on February 23, 2005;

(ii) The following Current Reports on Form 8-K of Exelon (Commission File No. 1-16169):

<u>Description</u>	<u>Filing Date</u>
Current report, items 1.01 and 2.03	3/08/05
Current report, item 8.01	3/07/05
Current report, item 5.02	2/25/05
Current report, item 5.02	2/22/05
Current report, items 8.01 and 9.01	2/04/05
Current report, item 2.01	2/01/05
Current report, items 1.01 and 5.02	1/28/05
Current report, items 2.02, 7.01 and 9.01	1/25/05;

(iii) Annual Report on Form USS for the fiscal year ended December 31, 2003, filed with the Commission on April 30, 2004; and

(iv) Registration Statement on Form S-4, filed with the Commission on February 10, 2005 (File No. 333-122074).

C. Description of PSEG and Its Subsidiaries.

1. PSEG, Generally.

PSEG was incorporated under the laws of the State of New Jersey in 1985 and is an exempt public utility holding company. PSEG, through its subsidiaries, operates in three business segments - Delivery, Generation and Enterprises, as described below. In addition to PSEG's three business segments, PSEG Services, a subsidiary of PSEG, provides PSEG and its subsidiaries with financial, human resources, legal, information technology, supply management and corporate governance services.

Delivery – PSEG's domestic energy delivery business consists of the transmission and distribution of electric energy and gas in New Jersey through PSE&G.

Generation – PSEG's generation businesses consist of the owned and contracted for electric generation facilities and energy marketing operations of the PSEG Power subsidiaries and the PSEG Global L.L.C. ("PSEG Global") subsidiaries. PSEG Power has three principal direct wholly owned subsidiaries: PSEG Nuclear, PSEG Fossil and PSEG ER&T. The PSEG Power generation portfolio consists of approximately 14,607 MW of generation in the Northeast and Midwest. PSEG Global has equity ownership interests in approximately 2,404 MW of generation in North America. All the generation assets in the PSEG system are held by PSEG subsidiaries with EWG or FUCO status under the Act or qualifying facility ("QF") status under the Public Utility Regulatory Policies Act of 1978, as amended ("PURPA").

Enterprises – PSEG's enterprise businesses consist primarily of (1) investments in energy-related financial transactions, leveraged leases, operating leases, leveraged buyout funds, marketable securities and a demand-side management business and (2) investments in international generation and delivery businesses qualified as EWGs and foreign utility companies through PSEG Resources L.L.C. ("PSEG Resources") and through PSEG Global.

2. The PSEG Utility Subsidiary.

PSE&G is a public utility company within the meaning of the Act and is the only utility subsidiary of PSEG. PSEG directly owns all of the issued and outstanding common stock of PSE&G.

PSE&G is an electric and gas utility company engaged principally in the transmission and distribution of electric energy and gas in New Jersey. PSE&G is subject to extensive regulation by the New Jersey Board of Public Utilities ("NJBPU") as to electric and gas rates, the issuance of securities and certain other aspects of PSE&G's operations. PSE&G is also subject to regulation by the FERC as to electric transmission rates and certain other aspects of its business.

PSE&G's retail service territory covers a corridor of approximately 2,600 square miles running diagonally across New Jersey from Bergen County in the northeast to an area below the city of Camden in the southwest with a population of approximately 5.5 million. PSE&G provides service to approximately 2.0 million electric customers and approximately 1.6 million gas customers.

PSE&G does not own or operate any electric generation facilities. PSE&G, pursuant to an order of the NJBPU issued under the provisions of the New Jersey Electric Discount and Energy Competition Act ("EDECA"), transferred all of its electric generation facilities, plant, equipment and wholesale power trading contracts to its affiliate PSEG ER&T in August 2000. Also, pursuant to an NJBPU order, PSE&G transferred its gas supply business, including its inventories and supply contracts, to a subsidiary of PSEG Power in May 2002. PSE&G continues to own and operate its electric transmission and electric and gas distribution business. PSE&G has transferred operational control over its electric transmission facilities to PJM.

All electric and gas customers in New Jersey have the ability to choose an electric energy and/or gas supplier. For those retail electric customers located in New Jersey who do not choose a competitive

electric supplier, New Jersey's Electric Distribution Companies ("EDCs"), including PSE&G, provide basic generation service ("BGS") or provider of last resort service ("POLR"). The EDCs satisfy their BGS obligations through a competitive state-wide annual auction. PSE&G's affiliate PSEG ER&T, has historically been a successful participant in these auctions and serves several EDCs including PSE&G.

For those retail gas customers located in New Jersey who do not choose a competitive natural gas supplier, New Jersey's gas distribution companies, including PSE&G, provide basic gas supply service ("BGSS") or POLR. PSE&G has entered into a full requirements contract through 2007 with PSEG ER&T to meet the supply requirements of PSE&G's gas customers.<sup>11</sup> PSEG ER&T charges PSE&G for the gas commodity costs, which PSE&G recovers from its customers. Any difference between rates charged by PSEG ER&T under the BGSS contract and rates charged to PSE&G's customers are deferred and collected or refunded through future adjustments in retail rates.

PSE&G's natural gas facilities consist entirely of local gas distribution facilities in the State of New Jersey and neither PSE&G nor any other PSEG company owns any interstate natural gas facilities subject to the Natural Gas Act.

### 3. Direct Non-Utility Subsidiaries of PSEG.

PSEG has three direct wholly owned non-utility subsidiaries, PSEG Power, PSEG Holdings and PSEG Services:

PSEG Power - PSEG Power has three principal direct wholly owned subsidiaries: PSEG Nuclear, which owns and operates nuclear generating stations; PSEG Fossil, which develops, owns and operates domestic fossil generating stations and other non-nuclear generating stations; and PSEG ER&T, which markets the capacity and production of PSEG Fossil's and PSEG Nuclear's stations, manages the commodity price risks and market risks related to generation and markets electricity, capacity, ancillary services and natural gas products on a wholesale basis. PSEG Power also provides specialized maintenance, repair and plant engineering services on energy-related electro-mechanical equipment to its affiliates.

PSEG Nuclear is an EWG and has an ownership interest in five nuclear generating units and operates three of them: the Salem Nuclear Generating Station, Units 1 and 2, located in New Jersey, each owned 57.41% by PSEG Nuclear and 42.59% by Exelon Generation; and the Hope Creek Nuclear Generating Station, located in New Jersey, which is 100% owned by PSEG Nuclear. Exelon Generation operates the Peach Bottom Atomic Power Station Units 2 and 3, located in Pennsylvania, each of which is 50% owned by PSEG Nuclear and 50% by Exelon Generation. PSEG Nuclear is subject to regulation by the FERC as to its wholesale electric sales and certain other aspects of its business. All of PSEG Nuclear's generation assets are located in PJM. As explained below, it is contemplated that PSEG Nuclear will be merged into Exelon Generation.

PSEG Fossil is an EWG and has direct interests in 12 generating stations in New Jersey and two in Pennsylvania. PSEG Fossil, together with Jersey Central Power and Light Company, is a co-licensee of the Yards Creek Pumped Storage Project, which has a FERC hydroelectric license (Project 2309). All of PSEG Fossil's directly owned generating assets are located in PJM. PSEG Fossil has certain subsidiaries, that are also EWGs, that own generating stations in Connecticut, New York, Indiana and Ohio. PSEG Fossil is subject to regulation by the FERC as to its wholesale electric sales and certain other aspects of its business. As explained below, it is contemplated that PSEG Fossil will be merged into Exelon Generation and the subsidiaries owned by PSEG Fossil will be retained as direct subsidiaries of Exelon Generation.

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<sup>11</sup> The BGSS contract continues year to year thereafter unless terminated by either party consistent with its terms.

PSEG ER&T conducts energy trading operations and does not own any utility assets. PSEG ER&T is subject to regulation by the FERC as to its wholesale electric sales and certain other aspects of its business. As explained below, it is contemplated that PSEG ER&T will be merged into Exelon Generation.

PSEG Holdings - PSEG Holdings has two principal subsidiaries: PSEG Resources, which invests primarily in energy-related, financial transactions, and PSEG Global, which invests in international generation and delivery businesses qualified as EWGs and FUCOs and domestic generation qualified as EWGs and QFs.<sup>12</sup>

PSEG Resources has investments in energy-related financial transactions and assets including leveraged leases, operating leases, leveraged buyout funds, limited partnerships and marketable securities. PSEG Resources also engages in demand side management services in New Jersey through its subsidiaries.

PSEG Global, through various subsidiaries qualified as FUCOs and EWGs, has investments in electric generation, transmission and distribution facilities in selected international markets and through various subsidiaries qualified as EWGs and QFs, has investments in electric generation in selected domestic markets. PSEG Global's domestic generation assets are located in California, Pennsylvania, Texas, New Hampshire and Hawaii.

PSEG Services is a non-utility service company. As explained below, it is contemplated that PSEG Services will sell all of its assets to Exelon BSC, change its name, and remain as a subsidiary.

4. Capitalization of PSEG.

**PUBLIC SERVICE ENTERPRISE GROUP INCORPORATED  
CONDENSED CONSOLIDATED CAPITAL STRUCTURE**

(Dollars in Millions)  
As of December 31, 2004

**Consolidated Capitalization**

	Amount	Capital Structure Percentage
Common Equity (includes Retained Earnings of \$2,425)	\$5,739	29.03%
Preferred and Preference Stock	1,281	6.48%
Securitization Obligations	2,085	10.55%
Long-Term Debt	9,785	49.50%
Current Maturities of Long-Term Debt	240	1.21%
Total Long-Term Debt	<u>10,025</u>	<u>50.71%</u>
Short-Term Debt	<u>638</u>	<u>3.23%</u>
Total Capital Structure	<u>\$19,768</u>	<u>100.00%</u>

\* \* \* \* \*

<sup>12</sup> Neither PSEG Holdings nor any of its subsidiaries is a public utility company for purposes of the 1935 Act. PSEG Holdings and its subsidiaries are more fully described in Exhibit G-7.

Additional information regarding PSEG and its subsidiary companies is set forth in the following documents, each of which has been previously filed with the Commission and is incorporated herein by reference:

(i) Annual Report on Form 10-K of PSEG (Commission File No. 001-09120), PSE&G (Commission File No. 001-00973), PSEG Power (Commission File No. 001-49614), PSEG Holdings (Commission File No. 000-32503) for the fiscal year ended December 31, 2004, filed with the Commission on March 1, 2005;

(ii) The following Current Reports on Form 8-K of PSEG (Commission File No. 001-09120):

<u>Description</u>	<u>Filing Date</u>
Current report, items 8.01 and 9.01	2/04/05
Current report, items 2.02, 8.01 and 9.01	2/03/05
Current report, items 1.01 and 9.01	1/24/05;

(iii) Annual Report on Form U-3A-2 of PSEG for the fiscal year ended December 31, 2004, filed with the Commission on March 1, 2005; and

(iv) Registration Statement on Form S-4, filed with the Commission on February 10, 2005 (File No. 333-122074).

#### D. Principal Terms of the Merger Agreement

The Merger Agreement provides for a business combination whereby PSEG will be merged with and into Exelon, with Exelon surviving. At the effective time of and as a result of the Merger, (i) each outstanding share of PSEG common stock will be converted into the right to receive 1.225 shares of Exelon common stock (the "Exchange Ratio") and (ii) each share of Exelon common stock will remain outstanding. All outstanding PSEG stock options will be converted into options to purchase the number of shares of Exelon common stock determined by multiplying (a) the number of shares of PSEG common stock subject to such stock option immediately prior to the effective time by (b) the Exchange Ratio, at an exercise price per share of Exelon common stock equal to the exercise price per share of PSEG common stock under such stock option immediately prior to the effective time divided by the Exchange Ratio.

Following the effective time of the Merger, the surviving corporation, which will be renamed Exelon Electric & Gas Corporation, will have an eighteen-member board of directors, which will include twelve Exelon directors and six new members nominated by PSEG. John W. Rowe, the current Chairman, President and Chief Executive Officer of Exelon, will become the President and Chief Executive Officer of the surviving corporation. E. James Ferland, the current Chairman, President and Chief Executive Officer of PSEG, will become the non-executive Chairman of the Board of the surviving corporation until his retirement on March 31, 2007, at which time Mr. Rowe will become Chairman of the surviving corporation.

Exelon and PSEG have made customary representations, warranties and covenants in the Merger Agreement, including, among others, covenants (i) by PSEG not to (a) solicit proposals relating to alternative business combination transactions or (b) subject to certain exceptions, enter into discussions concerning alternative business combination transactions, (ii) by Exelon and PSEG to cause shareholder meetings to be held to consider approval of the Merger and related transactions, (iii) subject to PSEG's right to terminate the Merger Agreement to accept a superior proposal (as described in the Merger Agreement), for the board of directors of PSEG to recommend adoption and approval by PSEG's shareholders of the Merger Agreement and related transactions and (iv) for the board of directors of Exelon to recommend approval by Exelon's shareholders of the issuance of shares of Exelon contemplated by the Merger Agreement subject to Exelon's board of directors' right to change its recommendation as required by its fiduciary duties.

Consummation of the Merger is subject to various customary conditions, including the requisite approval by the shareholders of Exelon and PSEG, respectively, no legal impediment to the Merger, the receipt of required regulatory approvals, the absence of a material adverse effect on Exelon, PSEG or, prospectively, the surviving corporation and the absence of certain specified burdensome actions as a

condition to the regulatory approvals for the Merger. The Merger Agreement contains certain termination rights for both Exelon and PSEG, and further provides that, upon termination of the Merger Agreement, a termination fee may be payable under specified circumstances including (i) if Exelon enters into a definitive agreement to be acquired, it must pay PSEG a termination fee of \$400 million plus PSEG's transaction expenses up to \$40 million, (ii) if Exelon's board of directors changes its recommendation, it must pay PSEG's transactions expenses up to \$40 million and (iii) if PSEG's board of directors changes its recommendation or if PSEG enters into a definitive agreement for a superior proposal to be acquired it must pay Exelon a termination fee of \$400 million plus Exelon's transaction expenses up to \$40 million.

E. Accounting Treatment for the Merger

The Merger will be accounted for as a purchase by Exelon under accounting principles generally accepted in the United States. Under the purchase method of accounting, the assets and liabilities of PSEG will be recorded, as of completion of the Merger, at their respective fair values and added to those of Exelon. The reported financial condition and results of operations of Exelon issued after completion of the Merger will reflect PSEG's balances and results after completion of the Merger, but will not be restated retroactively to reflect the historical financial position or results of operations of PSEG. Following completion of the Merger, the earnings of the combined company will reflect purchase accounting adjustments, including changes to amortization and depreciation expense for acquired assets.

F. Operation of the Combined System Post-Merger

Following the Merger, ComEd, PECO and PSE&G (the "Retail Utility Subsidiaries") will all be subsidiaries of Delivery and will operate their respective electric distribution systems, and PECO and PSE&G will operate their respective gas distribution systems. The electric transmission systems of the Retail Utility Subsidiaries together with the Indiana Company will be interconnected through and subject to the functional control of a single operator, PJM. The Retail Utility Subsidiaries, the Indiana Company and Exelon Generation are referred to herein as the "Utility Subsidiaries."

A more detailed description of Exelon's plans to integrate PSEG's operations with those of its existing subsidiaries is set forth in Item 3.B.4.b, below.

G. Exelon Generation Restructuring

After obtaining any appropriate third-party consents, including consents of certain PSEG Power debt holders to certain amendments of PSEG Power debt agreements, the Applicants will undertake the Exelon Generation Restructuring such that PSEG Power and its direct subsidiaries PSEG Nuclear, PSEG Fossil and PSEG ER&T will all cease to exist as separate entities and will become part of Exelon Generation. The business functions of these former PSEG entities will become a part of their respective Exelon Generation business unit. The subsidiaries owned by these PSEG entities will be retained as direct subsidiaries of Exelon Generation, which will continue to be an electric utility company for purposes of the Act. It is contemplated that the Exelon Generation Restructuring will take place contemporaneously with the closing of the Merger. See Exhibits G-1, G-2 and G-3 hereto for diagrams of the pre-Merger and post-Merger corporate structures.

It is anticipated that the current subsidiaries of PSEG Fossil that own and/or operate electric generation facilities will remain subsidiaries of Exelon Generation as EWGs. The Exelon Generation Restructuring will not result in any new "public utility" subsidiary of Exelon Generation.

Applicants seek such approval as may be required for the Exelon Generation Restructuring.<sup>13</sup>

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<sup>13</sup> Approvals related to the Exelon Generation Restructuring have been sought in the pending FERC Merger filing. A determination will be requested from the New Jersey Department of Environmental Protection ("NJDEP") that the Industrial Site Recovery Act ("ISRA") does not apply to the Merger and its related corporate reorganizations including the Generation Restructuring. Filings will also

#### H. Generation Divestiture

The proposed Merger will increase the total capacity of generation resources owned or controlled by Exelon. To ensure that the combined company does not have market power in any relevant market, Exelon and PSEG have proposed a comprehensive market power mitigation plan designed to address in full FERC's requirements for competitive markets. As part of the plan, the companies have proposed the Generation Divestiture -- to divest a number of coal, mid-merit, and peaking generating plants and transfer control of the output of a portion of their baseload nuclear generating capacity.

The Applicants propose to divest 1,000 MW of peaking capacity and 1,900 MW of mid-merit capacity, including at least 550 MW of coal capacity which (when combined with the proposed nuclear baseload mitigation discussed below) should fully mitigate the market concentration in all geographic markets.<sup>14</sup> The divestiture will occur either through a swap of assets with owners of generation located outside of PJM or through an outright sale of generating facilities or units within facilities. No more than half of this capacity, i.e. 1,450 MW, will be sold to a single purchaser. In addition, no capacity will be sold to a market participant with a greater than 5% share of installed capacity in either PJM East or Expanded PJM.<sup>15</sup> Furthermore, no more than 25% of this amount of capacity, i.e., 725 MW, will be sold in the aggregate to market participants with 3% - 5% of the total installed capacity in either the PJM East or the Expanded PJM markets.

Rather than divest their nuclear baseload units, the Applicants have proposed to FERC to implement a "virtual divestiture" whereby they will divest themselves, through sales of long-term firm energy rights, of 2,600 MW of nuclear generating capacity in PJM East. Such "virtual divestiture" will take the form of FERC jurisdictional wholesale power transactions and will not constitute the disposition of "utility assets" within the meaning of the Act, therefore, no approval by the Commission is required for the virtual divestiture.<sup>16</sup>

The Applicants have not yet identified the specific assets that they intend to divest. However, they recognize that the FERC needs to be assured that the divested generation will be located in PJM East to ensure that FERC market concentration criteria will be met. Applicants also understand that the Commission will need to approve any dispositions of "utility assets" associated with the Generation Divestiture. As a result, filed herewith as Exhibit G-4 is a list of generation facilities that will be considered for divestiture. Applicants seek Commission approval to dispose of any of the facilities identified on Exhibit G-4.

The Applicants proposed to FERC that they be given 18 months following the closing of the Merger to complete the proposed Generation Divestiture. The Applicants intend to complete the divestiture more quickly, but 18 months may be necessary to conduct a sales process, negotiate all necessary agreements and obtain all necessary regulatory approvals.

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be made with the Connecticut Siting Council and the Connecticut Department of Environmental Protection with respect to the implications of the Merger and the Generation Restructuring to the generating stations located in Connecticut and owned by a subsidiary of PSEG Fossil.

<sup>14</sup> The Department of Justice will also review potential market power issues associated with the Merger.

<sup>15</sup> "PJM East" is the eastern portion of PJM Pre-2004, on the eastern side of transmission constraints that limit the amount of energy that can be transferred from generation in the western part of PJM Pre-2004. "PJM Pre-2004" is the original PJM Mid-Atlantic market before PJM was expanded, plus Allegheny Energy. "Expanded PJM" consists of all the geographic markets that constitute the PJM RTO. More detail regarding these terms can be found in the Application for approval of the Merger filed with FERC included as Exhibit D-1 hereto.

<sup>16</sup> For further description of the virtual divestiture see Item 3.B.7.b below.

Implementation of the proposed mitigation measures, including the Generation Divestiture, will be subject to review by various regulators, including the FERC.<sup>17</sup> None of the proposed mitigation, including the Generation Divestiture, would affect the integration of the combined electric utility operations for purposes of the Act.

Applicants seek such approval as may be required for the Generation Divestiture and authorization to complete the Generation Divestiture during the period of 18 months following consummation of the Merger.

I. Affiliate Transactions

1. Service Company Transactions

Under the 2000 Merger Order, the Commission authorized Exelon to organize and capitalize Exelon BSC as a service company subsidiary, found that Exelon BSC was so organized and conducted, or to be conducted, as to meet the requirements of section 13(b) of the Act with respect to reasonable assurance of efficient and economical performance of services or construction or sale of goods for the benefit of associate companies, at cost fairly and equitably allocated among them (or as permitted by Rule 90), and authorized Exelon BSC to provide ComEd, PECO and other companies in the Exelon system with administrative, management, engineering, construction, environmental, and other support services pursuant to a General Services Agreement.<sup>18</sup>

The 2000 Merger Order directed Exelon to file a post-effective amendment in File No. 70-9645 describing its accounting systems and cost allocation methodologies and requesting a supplemental order of the Commission. On October 1, 2001, Exelon filed Amendment No. 5 (Second Post-Effective) in File No. 70-9645.<sup>19</sup> Thereafter, on October 31, 2003, Exelon submitted a 60-day letter that, as supplemented, described certain proposed changes in allocation methods for "corporate governance costs," and the reorganization of Energy Delivery Shared Services, a business unit of Exelon BSC that would begin to provide new services to ComEd and PECO effective January 1, 2004.<sup>20</sup>

In connection with the Merger, PSEG Services will sell all of its assets to Exelon BSC, change its name and remain as a subsidiary. Post-Merger, Exelon BSC intends to add the former PSEG companies as client companies under the General Services Agreement and will provide to the new client companies the same administrative, management, and technical services that it now provides to Exelon system companies, utilizing the same work order procedures and the same methods of allocating costs that are specified in the

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<sup>17</sup> Approvals related to the Generation Divestiture have been sought in the pending FERC Merger filing. Authorizations will be sought from the NJDEP pursuant to ISRA for generating stations in New Jersey that are transferred as part of the Generation Divestiture pursuant to the mitigation plan.

<sup>18</sup> The form of General Services Agreement was filed as Exhibit B-2 to Amendment No. 3 in File No. 70-9645.

<sup>19</sup> A copy of the Exelon Business Service Company Associate Transaction Procedures Manual (the "Manual") dated October 1, 2001 was filed as Exhibit B-2.1 in File No. 70-9645. A revised copy of the Manual, which incorporated changes requested by the Commission, was provided to the Commission Staff in August of 2003. No supplemental order was ever issued, although Exelon has fully complied with the requirement to file the post-effective amendment. Therefore, Exelon requests, to the extent the Commission deems it necessary to make additional findings with respect to Exelon BSC, that it make those findings in the instant proceeding.

<sup>20</sup> Under the 2000 Merger Order, Exelon BSC is required to give written notice to the Commission at least 60 days prior to implementing any change in the type and character of the companies receiving services, the methods of allocating costs to associate companies, or the scope or character of services to be rendered.

General Services Agreement.<sup>21</sup> In connection with the Transaction, certain employees of PSEG Services may be transferred to and become employees of Exelon BSC, which will be the sole subsidiary service company for the Exelon system.

Exelon requests that the Commission find, to the extent required, that following the transactions described herein, Exelon BSC will continue to be organized and conducted in a manner to meet the requirements of Section 13(b) of the Act. Recognizing that it will take some time for conversion to Exelon BSC platforms of the work order procedures, cost capture and allocation processes of the portion of Exelon BSC that was formerly PSEG Services, Applicants request authority to delay the full implementation of all services and systems relative to the new PSEG clients for a period not longer than one year after the date of the consummation of the Merger.

2. Other Inter-Company Goods and Services At Cost

(a) Incidental Services

The 2000 Merger Order recognized that ComEd, PECO and Exelon Generation may provide services incidental to their utility businesses, such as infrastructure services and storm outage emergency repairs, to one another and other associate companies in accordance with rules 87, 90 and 91. In accordance with these rules also, a utility may provide certain goods, through a leasing arrangement or otherwise, to one or more associate companies, and may use certain assets for the benefit of one or more associate companies. Following the Merger, PSE&G also may provide these incidental services to, or receive these incidental services from, the other Exelon companies. PSE&G also may provide goods, through a leasing arrangement or otherwise, to one or more associate companies, and may use certain assets for the benefit of one or more associate companies.

(b) Services Required for the Efficient Operation of Exelon Generation's Businesses

Under the 2000 Merger Order, the Commission authorized Exelon Generation and any future subsidiary of Exelon Generation and AmerGen Energy Company, LLC ("AmerGen") to provide services at cost to each other as required for the efficient operation of the Exelon system generating facilities. Although Exelon Generation is an "electric utility company" under the Act, it is not subject to state rate regulation and has no "captive" customers. Following the Merger, as is the case now, Exelon Generation will own and operate generating facilities, engage in energy marketing and trading, and invest in and own exempt wholesale generators, intermediate companies and other permitted investments such as Rule 58 energy-related companies, all of which are operated as an integral part of its system generating facilities. Accordingly, Exelon Generation proposes that post-Merger it, and all of its current and future subsidiaries, including the former PSEG subsidiaries, will provide services at cost to each other as required for the efficient operation of Exelon Generation's businesses.

(c) Services at the Interface between Generation and Transmission and Distribution

Under the 2000 Merger Order, the Commission authorized Exelon Generation to render and receive services at cost from ComEd and PECO related to the interface -- primarily switchyard facilities -- between the generation function of Exelon Generation and the transmission and distribution functions of ComEd and PECO. Applicants request authorization for ComEd, PECO, PSE&G, Exelon Generation and its subsidiaries to render and receive the same types of services at cost, among each other following the Merger.

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<sup>21</sup> Exelon and PSE&G are seeking approval of the General Services Agreement from the NJBPU. Following the Merger, Exelon BSC may file with the Commission 60-day letters regarding changes in allocation factors or other changes.

(d) Exelon Generation Services in Connection with Supply of Electricity and Natural Gas

1. Background

a. Scheduling Coordination Agreements. PSE&G is obligated to purchase electricity from certain QFs pursuant to PURPA, is obligated to purchase electricity from certain EWGs under restructured former PURPA contracts, and receives an allocation of hydroelectric power from the St. Lawrence Power Project. Pursuant to a stipulation filed at the NJBPU, PSE&G is obligated to resell this power at wholesale into the PJM spot market. As PSE&G owns no generation and engages in no other wholesale energy transactions, it relies upon its affiliate PSEG ER&T to schedule these transactions on its behalf and to submit bids for capacity as directed by PSE&G. PSEG ER&T also fulfills certain billing and accounting functions with respect to such energy and capacity. These services are provided under two agreements (“Scheduling Coordination Agreements”) pursuant to which PSE&G receives the full PJM market value for the electricity. PSE&G either (i) pays PSEG ER&T a cost-based fee, or (ii) enables PSEG ER&T to receive a credit from PJM for capacity from the purchases described above against any emergency power it would otherwise have to pay for under the PJM Open Access Transmission Tariff. The Scheduling Coordination Agreements will be assumed by Exelon Generation by operation of law.

b. BGSS Gas Contract. PSEG ER&T provides full-requirements gas supply service to PSE&G pursuant to a contract approved by the NJBPU for the purpose of satisfying all of PSE&G’s retail gas service obligations (“BGSS Gas Contract”). As part of the transaction approved by the NJBPU, PSEG ER&T assumed the PSE&G entitlements under most of its gas transportation and storage contracts with interstate pipelines. In a few cases, the entitlements remained with PSE&G and PSEG ER&T administers the contracts as PSE&G’s agent. The BGSS Gas Contract will be assumed by Exelon Generation by operation of law.

2. Exelon Generation Services in Connection with Supply of Electricity and Natural Gas.

Under the 2000 Merger Order, the Commission authorized Exelon Generation to provide, at cost, supply planning services and assistance to ComEd and PECO and to assist the utilities in obtaining energy supply resources from unaffiliated sellers, in each case in connection with the utility’s unbundled retail sales and/or wholesale sales, to the extent that energy supply is not provided by Exelon Generation. The Retail Utility Subsidiaries might require assistance from Exelon Generation with respect to the procurement process for the procurement of energy for the utilities’ bundled as well as unbundled retail sales. For this reason, and also to allow Exelon Generation to provide any jurisdictional services currently provided by PSEG ER&T pursuant to the Scheduling Coordination Agreements and the BGSS Gas Contract, the Applicants request that the authorization obtained in the 2000 Merger Order be modified not only to include PSE&G, but also to relate to the Retail Utility Subsidiaries’ bundled retail sales, as well as unbundled retail sales and/or wholesale sales, of both electricity and natural gas. Thus, the Applicants request that the Commission authorize Exelon Generation to provide, at cost, supply planning services and assistance to the Retail Utility Subsidiaries and to assist the utilities in obtaining, or disposing of, energy supply resources from unaffiliated sellers, in each case in connection with the Retail Utility Subsidiaries’ bundled and unbundled retail sales and/or wholesale sales, to the extent that energy supply is not provided by Exelon Generation.<sup>22</sup>

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<sup>22</sup> The described services will be provided at cost, with the exception of some services under the Scheduling Coordination Agreements, which provide, as an alternate mechanism for PSE&G to compensate PSEG ER&T (Exelon Generation after the Exelon Generation Restructuring) for scheduling coordination services, for PSEG ER&T to receive a credit from PJM for capacity, all as described above.

(e) Modification of Intercompany Services Authorized by the 2000 Merger Order

ComEd currently provides to and receives from affiliates certain services in accordance with an Affiliated Interests Agreement ("ComEd AIA") approved by the ICC. PECO's form of Mutual Services Agreement ("PECO MSA") under which PECO provides and receives certain services from affiliates has been approved by the PAPUC.<sup>23</sup> In connection with the Merger, PSE&G plans to enter into a Mutual Services Agreement (the "PSE&G MSA") to govern affiliated interest transactions between PSE&G and its affiliates other than Exelon BSC as service provider.<sup>24</sup> Such transactions would be executed at cost, consistent with Rules 90 and 91.

The 2000 Merger Order approved, as part of the filing in File No. 70-9645, Exhibit B-3.3 (Part B), which listed then existing arrangements under the ComEd AIA, the PECO MSA, or individual contracts pursuant to which ComEd and PECO received or rendered services at other than cost. Those arrangements or contracts have all either concluded, or are being conducted currently at cost. Such Exhibit B-3.3 (Part A) listed those services expected to be provided by one Exelon (non-service) company to another company at cost. These services are reported in a semi-annual report of affiliate transactions. The report for the first six months of the year is filed under a Rule 24 certificate at the time of the filing of Exelon's Rule 24 certificate for the second quarter. The report for the second six months of the year is filed as an attachment to Exelon BSC's Report on Form U-13-60. Exelon proposes to modify the service providers and recipients under the types of services so described in the 2000 Merger Order so that each of ComEd, PECO, PSE&G and Exelon Generation may provide, at cost, the listed services to associate companies in the new Exelon system under the same conditions as currently apply to the Exelon system companies.<sup>25</sup>

In addition to the services authorized to be provided and received as described in such Exhibit B-3.3 as contemplated by the 2000 Merger Order, as modified herein, Applicants request authorization for the following additional services to be provided at cost. These services will also be subject to the aforementioned reporting requirements.

- a) PowerLabs Services to ComEd, PECO and PSE&G. Exelon Generation was authorized to provide Instrument Calibration services to PECO in Exhibit B-3.3. Since the time of the 2000 Merger Order, the department of Exelon Generation that performed those services has been placed in a separate first-tier Rule 58 subsidiary of Exelon Generation. The new company, which is called Exelon PowerLabs, LLC ("PowerLabs"), provides Instrument Calibration services at cost to Exelon Generation under the authority in the 2000 Merger Order permitting Exelon Generation and any future subsidiary of Exelon Generation to provide services at cost to each other as required for the efficient operation of the Exelon system generating facilities. PowerLabs also provides Instrument Calibration services at cost, pursuant to Rule 87(b)(1), to Exelon BSC, which passes them through, at cost, to ComEd and PECO. Applicants request that PowerLabs be authorized to provide Instrument Calibration and other technical services, at cost, directly to ComEd, PECO and PSE&G, in addition to Exelon Generation.
- b) Energy Efficiency Audit Services by the Retail Utility Subsidiaries to Other Exelon Companies. ComEd Technical Services performs site efficiency assessments, which review

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<sup>23</sup> The ComEd AIA and PECO MSA were filed as Exhibits B-3.1 and B-3.2, respectively, in File No. 70-9645.

<sup>24</sup> Exelon and PSE&G are seeking approval of the PSE&G MSA from the NJBPU. The PSEG MSA is filed as Exhibit B-4 hereto.

<sup>25</sup> Such services as described on Exhibit B-3.3 include: services provided by the Retail Utility Subsidiaries: regulatory and legislative services, call center, central mail, fleet services, real estate and facilities, distribution technical services, telephone overflow coverage, strategic marketing and sourcing, installation and maintenance of substation equipment, purchase of materials and logistics, metering equipment and rubber goods, customer services rep emergency training, environmental and lab services, training for electrical and fire; and services provided by Exelon Generation: instrument calibration, operation of Richmond Frequency Converters and synchronous condenser maintenance.

current energy use profiles and identify cost-savings opportunities ("Energy Efficiency Audit Services"). ComEd has provided a small volume of these services at cost to Exelon Generation and PECO under Rules 87, 90 and 91, as services incidental to its utility business. In anticipation that the volume of these services may grow over time, may be provided by the other Retail Utility Subsidiaries and may be useful to other Exelon system companies, the Applicants request the Retail Utility Subsidiaries be authorized to provide Energy Efficiency Audit Services to other companies in the Exelon system at cost.

- c) **Exelon Generation Maintenance, Repair and Plant Engineering Services.** PSEG Power provides a range of specialized maintenance, repair and plant engineering services on energy-related electro-mechanical equipment. PSEG Power provides these services to PSEG Fossil and its EWG subsidiaries, as well as to PSEG Nuclear, PSE&G and PSEG Services. PSEG Power charges its affiliates a blended hourly rate that recovers the fully allocated cost of providing these services. PSEG Power charges PSE&G approximately \$3.4 million on an annual basis for the services it provides to PSE&G. PSEG Power charges PSEG Fossil's EWG subsidiaries approximately \$150,000 on an annual basis for the services it provides to these entities. After the Exelon Generation Restructuring, PSEG Power will be part of Exelon Generation. Thus, Applicants request authorization for Exelon Generation to provide these services, at cost, to other Exelon companies, including, but not limited to, PSE&G, Exelon BSC, ComEd and PECO.
- d) **Peak Shaving Services.** To facilitate PSEG ER&T's provision of BGSS to PSE&G, PSE&G provides a peaking natural gas supply to PSEG ER&T from three Liquefied Propane Air ("LPA") Plants and one Liquefied Natural Gas ("LNG") Plant. The LPA and LNG peaking supplies are economical alternatives to gas supply contracts for very short periods of time. PSE&G charges PSEG ER&T for all labor, material and other costs that are required to operate and maintain the facilities along with a carrying cost for the return on and depreciation of the investment. PECO may enter into similar arrangements with Exelon Generation regarding similar gas peak facilities owned by it. Applicants request authorization for PSE&G to provide these peak shaving services to Exelon Generation, as successor to PSEG ER&T and for PECO to provide similar peak shaving services to Exelon Generation, in the event PECO enters into similar arrangements with Exelon Generation.

J. Issuance of Common Stock in the Merger

Exelon requests approval to issue that number of shares of its common stock necessary to comply with its obligations under the Merger Agreement. Exelon expects that it will issue approximately 341 million shares of common stock to the former holders of PSEG common stock in the Merger. This includes approximately 14 million shares of common stock, or options on its common stock, Exelon will be required to issue at the consummation of the Merger to satisfy the obligations under various PSEG stock option and employee benefit plans.

Upon completion of the Merger, each outstanding option to purchase shares of PSEG common stock will be assumed by Exelon and substituted with an option to purchase shares of Exelon common stock, exercisable on generally the same terms and conditions that applied before the Merger. The number of shares of Exelon common stock subject to the substitute Exelon stock option will equal the number of shares of PSEG common stock subject to the PSEG stock option immediately prior to completion of the Merger, multiplied by the exchange ratio, rounded down to the nearest whole share. The per share exercise price of each substitute Exelon stock option will equal the exercise price of the PSEG stock option immediately prior to completion of the Merger divided by the exchange ratio, rounded up to the nearest whole cent. In addition, upon completion of the Merger, Exelon will assume all PSEG equity-based awards and substitute them with equity-based awards with respect to shares of Exelon common stock on generally the same terms and conditions that applied before completion of the Merger. The number of shares of Exelon common stock issuable under those awards, and the exercise prices for those awards, will be adjusted to take into account the exchange ratio (1.225) in the Merger.

K. PSEG Indebtedness Assumed

As a consequence of the Merger and the Exelon Generation Restructuring, all the existing consolidated indebtedness of PSEG will become consolidated indebtedness of Exelon. As the surviving entity in the Merger, Exelon will become the successor obligor on all outstanding indebtedness directly issued by PSEG. Further, subject to receipt of the appropriate consents, upon the Exelon Generation Restructuring, indebtedness and obligations of PSEG Power, PSEG Nuclear, PSEG Fossil and PSEG ER&T will become obligations of Exelon Generation. Prior to the closing of the Merger, PSEG Power's debt holders will be solicited for consent to amendments to certain of its existing debt instruments to reflect the changes in credit profile and other circumstances that will result from the assumption by Exelon Generation of PSEG Power indebtedness.<sup>26</sup>

Exelon will not legally assume or become successor obligor on any outstanding indebtedness of PSEG system companies, except (as noted above) for PSEG indebtedness for which Exelon is successor obligor. Exelon may issue guaranties on behalf of former PSEG system companies subject to the limitations on guaranties contained in the 2004 Financing Order, modified as described below. Likewise, except for the obligations of PSEG Power, PSEG Nuclear, PSEG Fossil and PSEG ER&T for which Exelon Generation becomes successor obligor in the Generation Restructuring, Exelon Generation will not legally assume any outstanding indebtedness of any PSEG system company. Exelon Generation may issue guaranties on behalf of former PSEG system companies subject to the limitations on guaranties contained in the 2004 Financing Order, modified as described below.

Filed herewith as Exhibit G-5 are descriptions of all outstanding indebtedness and obligations of PSEG that are expected to become consolidated indebtedness of Exelon following the Merger.<sup>27</sup> Filed as Exhibit G-6 is a description of all existing inter-company guaranties in the PSEG system that will remain in place following the Merger.<sup>28</sup>

Applicants seek approval to the extent required for the consolidation of indebtedness, or in the case of Exelon and Exelon Generation, becoming the successor obligor under the indebtedness, and continuation of inter-company guaranties, as described above. Applicants further request authority to continue existing financing arrangements, guarantees and hedging arrangements, as well as any transactions undertaken to extend the terms of or replace, refund or refinance existing obligations and the issuance of new obligations in exchange for existing obligations, provided in each case that the issuing entity's total capitalization is not increased as a result of such financing transaction except as permitted by the 2004 Financing Order modified as discussed below.

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<sup>26</sup> For purposes of the Securities Act of 1933, the assumption by Exelon Generation of the obligations of PSEG Power which have been the subject of changed terms by reason of the consent solicitation may be considered the offering of new securities by Exelon Generation that requires registration on an S-4 Registration Statement. However, as a matter of corporate law, the intention is that Exelon Generation will become the successor obligor on the obligations, as amended, by operation of law in the Exelon Generation Restructuring.

<sup>27</sup> Applicants will update this exhibit to reflect changes that may occur prior to the issuance of an order in this proceeding.

<sup>28</sup> In addition, Exelon will increase its consolidated indebtedness by approximately \$3.2 billion as a result of the outstanding consolidated obligations of PSEG Holdings, the non-utility subsidiary of PSEG which will become a first tier subsidiary of Exelon. These obligations are included in the calculations of the pro forma post-Merger capitalization of Exelon. All such obligations would have been exempt from the requirement of Commission approval under Rule 52(b) if issued by a subsidiary of a registered holding company so no approval for their assumption is sought in this proceeding.

L. Modifications to 2004 Financing Order

1. The 2004 Financing Order

On April 1, 2004, Exelon received approval from the Commission in the 2004 Financing Order (Docket No. 70-10189) to engage in certain financing transactions. The 2004 Financing Order authorized, through April 15, 2007, certain financing transactions, including the issuance of common stock, preferred securities, equity-linked securities, long-term debt and short-term debt in an aggregate amount not to exceed \$8.0 billion above the amount outstanding for Exelon and Exelon Generation at December 31, 2003, with no separate sublimit for short-term debt.<sup>29</sup> The 2004 Financing Order also authorized the use of up to \$4 billion of the proceeds of financings for investments in EWGs and FUCOs, and reserved jurisdiction over a request to use an additional \$3 billion of the proceeds of financings for investments in EWGs and FUCOs.

Because the 2004 Financing Order did not contemplate a transaction of the magnitude of the current Merger, Exelon is requesting, as noted in Item 1. J. above, approval for the issuance of its common stock in the Merger and related to stock options and employee plans. In addition, certain modifications to the 2004 Financing Order are necessary to accommodate the addition of the PSEG system into the Exelon system. Except for the issuance of common stock in the Merger and the specific modifications listed below, however, Exelon is not seeking any changes to the approvals granted in the 2004 Financing Order.

In particular, Exelon is not proposing to increase the authorized amount of new financing it will be permitted above the existing authorized \$8 billion. As noted in the 2004 Financing Order: "Applicants state that [the \$8 billion External Limit] does not include the refunding or replacement of securities where capitalization is not increased from that in place at [a specified date]. Applicants state that any refunding or replacement of securities where capitalization is not increased from that in place at [the specified date] will be through the issuance of securities of the type authorized in [the 2004 Financing Order]." Applicants request that the base level of capitalization, against which the authorized increase of \$8 billion will be measured, will be adjusted to be the pro forma capitalization of Exelon or Exelon Generation, as the case may be, as of the date of consummation of the Merger and Exelon Generation Restructuring.

Exelon proposes that the 2004 Financing Order will remain in full force and effect except to the extent expressly modified by the Commission's order in this matter. Except as specifically modified herein, all parameters, restrictions and conditions imposed in the 2004 Financing Order will remain in effect.

2. Requested Modifications or Extensions of 2004 Financing Order<sup>30</sup>

Applicants seek approval for the following modifications to the 2004 Financing Order:

- i. The definition of "Utility Subsidiaries" under the 2004 Financing Order be amended to include PSE&G, and the definition of "Nonutility Subsidiaries" be amended to include all non-utility subsidiary companies of PSEG.<sup>31</sup>

<sup>29</sup> The 2004 Financing Order replaced the approval granted by the Commission in Docket No. 70-9693 to engage in certain financing transactions pursuant to orders dated November 2, 2000 (Holding Co. Act Release No. 35-27266) and December 8, 2000 (Holding Co. Act Release No. 35-27296) (collectively, the "2000 Orders") that expired on March 31, 2004. The 2000 Orders had authorized up to \$4.0 billion of financing.

<sup>30</sup> Capitalized terms used in this Item 1.L. and not otherwise defined herein shall have the meanings assigned to such terms in the 2004 Financing Order.

<sup>31</sup> The authority under the 2004 Financing Order, as it relates to non-utilities, applies to "all other direct and indirect subsidiaries that Exelon may hereinafter form or acquire in accordance with a Commission order or otherwise in accordance with the Act or a rule promulgated thereunder." By

- ii. The Utility Money Pool authority be amended to permit: (a) PSE&G to become a participant in the Utility Money Pool, with a participation limit for borrowing of \$1 billion, and (b) Exelon Generation to borrow up to \$1.5 billion (an increase from \$1 billion) at any one time outstanding from the Utility Money Pool.<sup>32</sup>
- iii. To authorize the establishment of a Nonutility Money Pool.<sup>33</sup>
- iv. To add authority, to the extent not exempt under Rule 52, for PSE&G to enter into Hedge Instruments and Anticipatory Hedges of the same type and under the same conditions as authorized under the 2004 Financing Order.
- v. To add authority for Exelon to enter into guarantees to or on behalf of the PSEG companies, and PSE&G to enter into Non-Exempt Utility Guarantees, all under the terms and conditions authorized under the 2004 Financing Order.
- vi. To increase to \$8 billion (from the current \$6 billion) the aggregate authority for Exelon and Exelon Generation to issue guaranties.
- vii. To add authority for PSE&G to pay dividends out of capital to the extent of PSE&G's retained earnings immediately prior to the Merger where such retained earnings are transferred to paid in capital in accordance with purchase accounting.
- viii. To add authority for Delivery to pay dividends out of capital to the extent of PSE&G's retained earnings immediately prior to the Merger where such retained earnings are transferred to paid in capital in accordance with purchase accounting.
- ix. To add authority for Exelon Generation to pay dividends out of capital to the extent of the retained earnings of PSEG Power, PSEG Nuclear, PSEG Fossil and PSEG ER&T immediately prior to the Merger where such retained earnings are transferred to paid in capital in accordance with purchase accounting.
- x. To add authority for Ventures to pay dividends out of capital to the extent of the retained earnings of (A) PSEG Power, PSEG Nuclear, PSEG Fossil and PSEG ER&T immediately prior to the Merger where such retained earnings are transferred to paid in capital in accordance with purchase accounting and (B) PSEG Holdings immediately prior to the Merger where such retained earnings are transferred to paid in capital in

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extending the authorizations of the 2004 Financing Order to the new, former PSEG, non-utility subsidiaries acquired in the Merger, such subsidiaries will be authorized, in each case subject to the restrictions and conditions of the 2004 Financing Order, inter alia to: (i) create and enter into transactions with Financing Subsidiaries, (ii) issue intra-system advances and guarantees, to the extent not exempt pursuant to Rules 45(b) and 52, to or on behalf of other Non-Utility Subsidiaries and others, (iii) benefit from the issuance by Exelon of guaranties approved by the 2004 Financing Order, (iv) participate in the Nonutility Money Pool, subject to the release of jurisdiction over the formation of the Nonutility Money Pool as specified in the 2004 Financing Order, (v) pay dividends out of capital or unearned surplus, (vi) enter into Non-Exempt Non-Utility Guaranties (as defined in the 2004 Financing Order), and (vii) change the par value, or change between par value and no-par stock, or change the form of such equity from common stock to limited partnership or limited liability company interests or similar instruments, or from such instruments to common stock, without additional Commission approval.

<sup>32</sup> The 2004 Financing Order authorized Unicom Investments, Inc. to participate in the Utility Money Pool as a lender only. Unicom Investments, Inc. has been reorganized and is now UII, LLC.

<sup>33</sup> The Commission reserved jurisdiction over the establishment of a Nonutility Money Pool in the 2004 Financing Order.

accordance with purchase accounting in the event PSEG Holdings becomes a subsidiary of Ventures rather than a direct subsidiary of Exelon.<sup>34</sup>

- xi. To increase Exelon's authority to pay dividends out of capital by the amount of PSEG's retained earnings immediately prior to the Merger where such retained earnings are transferred to paid in capital in accordance with purchase accounting.<sup>35</sup>
- xii. To add authority for Exelon, Exelon Generation, Ventures, Delivery and PSE&G to declare and pay dividends out of current earnings before any deduction resulting from impairment of goodwill or other intangibles recognized as a result of the Merger.<sup>36</sup>
- xiii. To increase to 75 million shares (from 42 million shares approved by the 2004 Financing Order) the number of shares of Exelon common stock that may be issued, following the Merger, under Exelon's dividend reinvestment plan, employee stock ownership plan, certain incentive compensation plans and certain other employee benefit plans, including PSEG plans assumed as part of the Merger, as described below (collectively, the "Plans").
- xiv. To increase the amount of financing proceeds that may be used for investments in EWGs and FUCOs such that "aggregate investment" within the meaning of Rule 53 does not exceed \$8.0 billion (an increase from \$4 billion currently authorized).<sup>37</sup>
- xv. To provide that the base capitalization against which the limit of additional financing of \$8 billion authorized in the 2004 Financing Order is measured shall be the pro forma capitalization of Exelon or Exelon Generation as the case may be, as of the date of consummation of the Merger and the Exelon Generation Restructuring. Financial information given herein as to the pro forma effect of the Merger is as of the date indicated and is illustrative only of the actual opening balance sheet of Exelon post-Merger that will be used for this purpose. As required under the 2004 Financing Order, all financing where capitalization is not increased from that in place at the Merger date will be through the issuance of securities of the type authorized in the 2004 Financing Order, modified as described herein, and subject to the Financing Parameters (as defined in the 2004 Financing Order).<sup>38</sup>

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<sup>34</sup> Such dividend authority is requested in the event that Exelon were to do an internal restructuring to move PSEG Holdings, a non-utility subsidiary to be a subsidiary of Ventures rather than as a direct first tier subsidiary of Exelon as is contemplated to be the structure immediately following the Merger. No further approval under the Act would be required for such a restructuring for PSEG Holdings under the authorization granted in Holding Co. Act Release No. 27545 (June 27, 2002).

<sup>35</sup> This new approval will not affect the authority of ComEd and Exelon to pay dividends out of capital up to \$500 million as approved in the 2004 Financing Order.

<sup>36</sup> Applicants ask the Commission to reserve jurisdiction over this request pending completion of the record.

<sup>37</sup> In the 2004 Financing Order, the Commission authorized up to \$4 billion in File No. 70-10189.

<sup>38</sup> The capitalization base for Exelon and Exelon Generation, respectively, will be measured according to the balance sheet prepared to reflect consummation of the Merger, by taking the post-Merger outstanding common stock or membership interests (excluding retained earnings), preferred and preference securities, long-term debt, short-term debt, current portion of long-term debt and securitization obligations, as applicable, of Exelon and Exelon Generation. Increases in capitalization through securities issuances of Exelon and Exelon Generation, as the case may be, will count towards the \$8 billion limit; but increases in consolidated capitalization resulting from exempt securities issuances (such as issuances of state commission approved securities by the Retail Utility Subsidiaries) and increases to retained earnings will

- xvi. To add authority for Exelon Generation to engage in tax-exempt financing pursuant to sale or lease transactions of its utility assets as described below.
- xvii. To amend the expiration of the authority granted in the 2004 Financing Order so that "Authorization Period" shall mean the period ending the later of (A) April 15, 2009 or (B) the 15th day of the month that is 40 months following the month in which the order in this matter is entered (an extension from April 15, 2007).

3. Parameters for Financing Authorization.

The proposed financing transactions will be subject to the Financing Parameters, as set forth in the 2004 Financing Order, without modification. Accordingly the limits on effective cost of money on financings, maturity, issuance expense and use of proceeds shall be unchanged. The 30% common equity condition shall apply to PSE&G as a "Utility Subsidiary."<sup>39</sup> The 30% Condition will be unchanged for Exelon, ComEd, PECO and Exelon Generation. Finally, the Investment Grade Condition (as defined in the 2004 Financing Order) will apply to PSE&G to the extent it requires Commission approval for any securities issuance.<sup>40</sup>

4. Filing of Certificates of Notification

Exelon currently files quarterly reports in connection with the 2004 Financing Order. Applicants propose to continue to file Rule 24 certificates containing the information required by the 2004 Financing Order for the post-Merger Exelon system, including equivalent information relating to former PSEG system subsidiaries.

5. Increase in Shares for Plans; New and Adopted Plans

The 2004 Financing Order authorized Exelon to issue and/or acquire in open market transactions, or by some other method which complies with applicable law and Commission interpretations then in effect, up to 42 million shares of Exelon common stock (adjusted for a stock split) under Exelon's dividend reinvestment plan, employee stock ownership plan, certain incentive compensation plans and certain other employee benefit plans. Such issuances are in addition to common stock that may be issued under the general financing authorization of \$8 billion. Exelon proposes to increase the number of shares authorized for this purpose to 75 million to accommodate two new Exelon plans and the former PSEG plans that will become Exelon's responsibility following the Merger. Exelon stock will be used, following the Merger, to satisfy requirements under the PSEG plans to provide common stock. These plans are summarized below.

Exelon Corporation 2006 Long-Term Incentive Plan

The purpose of the Exelon Corporation 2006 Long-Term Incentive Plan (the "Incentive Plan") is to encourage designated key employees of Exelon and its subsidiaries to contribute materially to the growth of the company, thereby benefiting Exelon's shareholders. The Incentive Plan authorizes the following types of grants singly, in combination or in tandem: non-qualified stock options, incentive stock options,

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not reduce available financing. Retirement or redemption of securities or reductions in equity through stock buybacks by Exelon or Exelon Generation, as the case may be, in each case with available funds will correspondingly increase available financing.

<sup>39</sup> Under the 2004 Financing Order, the consequence of failing to satisfy the 30% Condition when required is that the Applicant issuer would not be authorized to issue securities in a transaction subject to Commission approval except for securities which would result in an increase in such common equity percentages.

<sup>40</sup> PSE&G receives approval from the NJPBU for all of its securities issuances, both long-term and short-term and, therefore, is not seeking Commission approval for any exempt securities issuances hereunder.

stock appreciation rights, restricted stock and restricted stock units, including performance share awards and performance units.<sup>41</sup>

#### Exelon Corporation Employee Stock Purchase Plan For Unincorporated Subsidiaries

The purposes of the Exelon Corporation Employee Stock Purchase Plan For Unincorporated Subsidiaries (the "Purchase Plan") are to provide employees of participating subsidiaries added incentive to remain employed and promote Exelon's best interests by permitting these employees to purchase shares of Exelon common stock at below-market prices through payroll deductions on substantially the same basis as employees who participate in Exelon's qualified employee stock purchase plan.<sup>42</sup>

#### Public Service Enterprise Group Incentive Plans

The purposes of the Public Service Enterprise Group Incorporated 1989 Long-Term Incentive Plan (the "1989 Plan"), the Public Service Enterprise Group Incorporated 2001 Long-Term Incentive Plan (the "2001 Plan"), and the Public Service Enterprise Group Incorporated 2004 Long-Term Incentive Plan (the "2004 Plan," and together with the 1989 Plan and 2001 Plan, the "PSEG Incentive Plans") are to promote the growth and profitability of the company and its subsidiaries by enabling them to attract and retain the best available personnel for positions of substantial responsibility; to motivate participants, by means of appropriate incentives, to achieve long-range goals; to provide incentive compensation opportunities that are competitive with those of other similar companies; and to align participants' interests with those of the company's shareholders and thereby promote the long-term financial interest of the company and its subsidiaries, including the growth in value of the company's equity and enhancement of long-term shareholder return. Outstanding, unexercised award grants under the 1989 Plan and the 2001 Plan are nonqualified stock options. Award grants under the 2004 Plan may be stock options, stock appreciation rights, restricted stock, stock units, performance shares, cash awards or any combination thereof.<sup>43</sup>

Public Service Enterprise Group Incorporated Stock Plan for Outside Directors (the "Directors' Plan")<sup>44</sup>

The Directors' Plan provides annual grants (currently, 1,000 shares) of restricted stock to outside directors for service on PSEG's Board of Directors. These shares of restricted stock vest upon the director's retirement from the Board following his/her 70th birthday.

Public Service Enterprise Group Incorporated Directors' Compensation Program (the "Directors' Compensation Program")<sup>45</sup>

Under the Directors' Compensation Program, one-half of each outside director's annual retainer (the total amount of which is currently \$50,000) is paid in shares of PSEG common stock.

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<sup>41</sup> The Incentive Plan is incorporated by reference to Annex H to Exelon's Registration Statement on Form S-4 filed February 10, 2005 in File No. 333-122704, which is included as Exhibit C hereto.

<sup>42</sup> The Purchase Plan is incorporated by reference to Annex I to Exelon's Registration Statement on Form S-4 filed February 10, 2005 in File No. 333-122704, which is included as Exhibit C hereto.

<sup>43</sup> The 1989 Plan is incorporated by reference to Exhibit 10 to the PSEG Quarterly Report on Form 10-Q for the quarter ended September 30, 2002, File No. 001-09120. The 2001 Plan is incorporated by reference to Exhibit 10a(7) to the PSEG Annual Report on Form 10-K for the year ended December 31, 2000, File No. 001-09120. The 2004 Plan is incorporated by reference to Exhibit 10a(21) to the PSEG Annual Report on Form 10-K for the year ended December 31, 2003, File No. 001-09120.

<sup>44</sup> The Directors' Plan is incorporated by reference to Exhibit 10a(17) to the PSEG Annual Report on Form 10-K for the year ended December 31, 2002, File No. 001-09120.

<sup>45</sup> The Directors' Compensation Program is incorporated by reference to Exhibit 10a(20) to the PSEG Annual Report on Form 10-K for the year ended December 31, 2002, File No. 001-09120.

Public Service Enterprise Group Incorporated Deferred Compensation Program for Directors (the "Directors' Deferred Plan")<sup>46</sup>

PSEG outside directors who elect to defer a portion of their fees under the Directors' Deferred Plan may elect to have all or a portion of the amounts deferred treated as if they were invested in PSEG common stock ("Phantom Stock"). Any shares distributed under the Directors' Deferred Plan are purchased on the open market for that purpose.

Public Service Enterprise Group Incorporated Employee Stock Purchase Plan (the "ESPP")<sup>47</sup>

The ESPP allows all employees of PSEG and its participating subsidiaries to purchase shares of PSEG common stock through payroll deduction at a 5% discount from market price.

#### 6. Nonutility Money Pool

In the 2004 Financing Order, the Commission noted that Exelon requested authority to establish the Nonutility Money Pool to be operated on the same terms and conditions as the Utility Money Pool, except that Exelon funds made available to the Money Pools would be made available to the Utility Money Pool first to the extent it is operated and needed and thereafter to the Nonutility Money Pool. None of the Utility Subsidiaries will be a participant in the Nonutility Money Pool, and no loans through the Nonutility Money Pool can be made to, and no borrowings through the Nonutility Money Pool can be made by, Exelon, Ventures or Delivery.<sup>48</sup>

Furthermore, other Non-Utility Subsidiaries (i.e., Non-Utility Subsidiaries that are not currently anticipated to participate in the Non-Utility Money Pool and such that are acquired or formed in the future, collectively, "Other Non-Utility Subsidiaries") may lend funds to and borrow from the Non-Utility Money Pool, when established, without the need for additional authority from the Commission.<sup>49</sup>

#### 7. Exelon Generation Tax-Exempt Financing

Exelon Generation may be able to incur lower financing costs by taking advantage of tax-exempt financing where a governmental entity, such as a county or a state authority or agency, issues securities and lends the proceeds to Exelon Generation or where Exelon Generation sells or leases an undivided interest in one or more of its generating facilities and related assets to the governmental entity and leases back or purchases the assets and operates such assets as before. Exelon Generation's payments to the governmental entity under such arrangements will provide payments of principal, interest and any other amounts due under the bonds issued by the governmental entity. In connection with such transactions, Exelon Generation seeks approval for the sale, lease or other transfer and lease back, purchase or other operating arrangement of generating and related assets that constitute utility assets under the Act. Such sale, lease or other transfer and lease back, purchase or other operation arrangement would be solely for financing purposes and would not affect the operation of the assets. This request does not seek to increase the amount of authorized financing and any financing under this authority would have to come within the

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<sup>46</sup> The Directors' Deferred Plan is incorporated by reference to Exhibit 10a(1) to the PSEG Annual Report on Form 10-K for the year ended December 31, 1999, File No. 001-09120.

<sup>47</sup> The ESPP is incorporated by reference to the PSEG Registration Statement on Form S-8, No. 333-106330 filed on June 20, 2003.

<sup>48</sup> To the extent necessary, Applicants request that the Commission release jurisdiction over the formation of the Nonutility Money Pool.

<sup>49</sup> See *NiSource, Inc.*, Holding Co. Act Release No. 27789 (December 30, 2003).

limits approved in the 2004 Financing Order, as it may be modified herein, but is solely to cover the technical disposition and acquisition of utility assets that is involved in this type of financing.<sup>50</sup>

8. Pro Forma Financial Information

Exelon is a financially sound company, and following the Merger will remain sound, with investment grade ratings from major rating agencies. The Exelon system's ratings as of December 31, 2004 from Standard & Poor's Corporation ("S&P"), Moody's Investors Service ("Moody's") and Fitch Investors Service, Inc. ("Fitch"), as well as the ratings of PSE&G at that date, are set forth in the following table. Exelon expects that following the Merger, it will maintain investment grade ratings at Exelon and each of the Utility Subsidiaries with respect to each type of obligation rated.<sup>51</sup>

Company and type of rating	S&P	Moody's	Fitch
<u>Exelon</u>			
• Corporate	A-	NR	NR
• Unsecured	BBB+	Baa2	BBB+
• Commercial Paper	A-2	P-2	F2
<u>ComEd</u>			
• Corporate	A-	NR	NR
• Secured	A-	A3	A-
• Unsecured	BBB+	Baa1	BBB+
• Preferred Stock/ Trust Securities	BBB	Baa3	BBB
• Commercial Paper	A-2	P-2	F2
• Transitional Trust Notes <sup>52</sup>	AAA	Aaa	AAA

<sup>50</sup> The Commission has approved this type of financing on numerous occasions. E.g., *Appalachian Power Co., Holding Co.* Act Release No. 27283 (November 27, 2000).

<sup>51</sup> The Indiana Company was created for historical reasons and does not currently have any publicly issued securities or securities ratings.

<sup>52</sup> These are obligations of a special purpose subsidiary of ComEd.

Company and type of rating	S&P	Moody's	Fitch
<u>PECO</u>			
• Corporate	A-	NR	NR
• Secured	A-	A2	A
• Unsecured	BBB+	A3	A-
• Preferred Stock	BBB	Baa2	BBB+
• Trust Securities	BBB	Baa1	BBB+
• Commercial Paper	A-2	P-1	F1
• Transitional Trust Notes <sup>53</sup>	AAA	Aaa	AAA
<u>Exelon Generation</u>			
• Corporate	A-	Baa1	--
• Unsecured	A-	Baa1	BBB+
• Commercial Paper	A-2	P-2	F2
<u>PSE&amp;G</u>			
• Corporate	BBB	NR	NR
• Secured	A-	A3	A
• Unsecured	BBB-	Baa1	A-
• Preferred Stock	BB+	Baa3	BBB+
• Commercial Paper	A-3	P-2	F-2
• PSE&G Transition Funding Notes	AAA	Aaa	AAA

NR=not rated

Exelon also has a sound capital structure. At September 30, 2004, Exelon's consolidated common equity as a percentage of consolidated capitalization was 40.18%.<sup>54</sup> Details regarding Exelon's consolidated capitalization are shown in the table in Item 1.B.4. above. Following the Merger, Exelon will

<sup>53</sup> These are obligations of a special purpose subsidiary of PECO.

<sup>54</sup> Consolidated capitalization includes securitization obligations. If securitization obligations were excluded in the calculation, Exelon's equity component of consolidated capitalization would be 50.10% at September 30, 2004.

continue to have sound capitalization. The following shows the pro forma post-Merger Exelon consolidated capitalization as of September 30, 2004.

**EXELON CORPORATION**  
**PRO FORMA CONDENSED CONSOLIDATED CAPITAL STRUCTURE**  
(Dollars in Millions)  
As of September 30, 2004

	Exelon		Post-Merger Pro Forma	
	Amount	Capital Structure Percentage	Amount	Capital Structure Percentage
Common Equity (includes Retained Earnings of \$3,256)	\$9,546	40.18%	\$22,189	42.89%
Minority Interest	53	0.22%	53	0.10%
Preferred and Preference Stock	632	2.66%	1,913	3.70%
Securitization Obligations	4,978	20.95%	7,449	14.40%
Long-Term Debt	7,814	32.89%	18,250	35.27%
Current Maturities of Long-Term Debt	410	1.73%	901	1.74%
Total Long-Term Debt	8,224	34.62%	19,151	37.01%
Short-Term Debt	325	1.37%	985	1.90%
Total Capital Structure	<u>\$23,758</u>	<u>100.00%</u>	<u>\$51,740</u>	<u>100.00%</u>

As part of the Exelon Generation Restructuring, PSEG Power, PSEG Nuclear, PSEG Fossil and PSEG ER&T will become a part of Exelon Generation, which will continue to have a strong capitalization following those transactions. As a result of the accounting for the Merger, however, the retained earnings of the PSEG subsidiaries combining with Exelon Generation will be eliminated. Accordingly, as noted above, Applicants request that Exelon Generation be authorized to pay dividends out of capital to the extent of the pre-Merger retained earnings of PSEG Power, PSEG Nuclear, PSEG Fossil and PSEG ER&T.

The following shows the pro forma post-Merger Exelon Generation consolidated capitalization as of September 30, 2004.

**EXELON GENERATION  
PRO FORMA CONDENSED CONSOLIDATED CAPITAL STRUCTURE**

(Dollars in Millions)  
As of September 30, 2004

	Exelon Generation		Post-Merger Pro Forma	
	Amount	Capital Structure Percentage	Amount	Capital Structure Percentage
Common Equity (includes Undistributed Earnings of \$1,031)	\$3,330	56.54%	\$10,222	62.12%
Minority Interest	55	0.93%	55	0.33%
Long-Term Debt	2,444	41.49%	6,083	36.97%
Current Maturities of Long-Term Debt	61	1.04%	95	0.58%
Total Long-Term Debt	2,505	42.53	6,178	37.55%
Short-Term Debt				
Total Capital Structure	<u>\$5,890</u>	<u>100.00%</u>	<u>\$16,455</u>	<u>100.00%</u>

PSE&G has a sound capital structure, with capitalization at December 31, 2004 as follows:

**PUBLIC SERVICE ELECTRIC AND GAS COMPANY  
CONDENSED CONSOLIDATED CAPITAL STRUCTURE**

(Dollars in Millions)  
As of December 31, 2004

**Consolidated Capitalization**

	Amount	Capital Structure Percentage
Common Equity (includes Retained Earnings of \$656)	\$2,700	33.61%
Preferred and Preference Stock	80	1.00%
Securitization Obligations	2,085	25.96%
Long-Term Debt	2,938	36.57%
Current Maturities of Long-Term Debt	125	1.56%
Total Long-Term Debt	3,063	38.13%
Short-Term Debt	105	1.30%
Total Capital Structure	<u>\$8,033</u>	<u>100.00%</u>

The following shows the pro forma post-Merger PSE&G consolidated capitalization as of September 30, 2004.

**PUBLIC SERVICE ELECTRIC AND GAS COMPANY**  
**PRO FORMA CONDENSED CONSOLIDATED CAPITAL STRUCTURE**  
(Dollars in Millions)  
As of September 30, 2004

	PSE&G		Post-Merger Pro Forma	
	Amount	Capital Structure Percentage	Amount	Capital Structure Percentage
Common Equity (includes Retained Earnings of \$592)	\$2,637	31.85%	\$6,000	50.04%
Preferred and Preference Stock	80	0.97%	80	0.67%
Securitization	2,124	25.65%	2,299	19.17%
Long-Term Debt	2,936	35.46%	3,053	25.46%
Current Maturities of Long-Term Debt	218	2.63%	273	2.28%
Total Long-Term Debt	3,154	38.09%	3,326	27.74%
Short-Term Debt	285	3.44%	285	2.38%
Total Capital Structure	<u>\$8,280</u>	<u>100.00%</u>	<u>\$11,990</u>	<u>100.00%</u>

**Item 2. Fees, Commissions And Expenses.**

The fees, commissions and expenses to be paid or incurred, directly or indirectly, in connection with the Merger, including the solicitation of proxies, registration of securities of Exelon under the Securities Act of 1933, and other related matters, are estimated to be approximately \$70 million, as discussed in Item 3.B.2.

**Item 3. Applicable Statutory Provisions.**

**A. Applicable Provisions.**

Sections 6(a), 7, 8, 9, 10, 12, 13, 32 and 33 of the Act and the rules thereunder are considered applicable to the proposed transactions.

To the extent that the proposed transactions are considered by the Commission to require authorizations, exemption or approval under any section of the Act or the rules and regulations thereunder other than those set forth above, request for such authorization, exemption or approval is hereby made.

**B. Section 10 of the Act.**

Section 10(b) provides that, if the requirements of Section 10(f) are satisfied, the Commission shall approve an acquisition under Section 9(a) unless the Commission finds that:

(i) such acquisition will tend towards interlocking relations or the concentration of control of public utility companies, of a kind or to an extent detrimental to the public interest or the interests of investors or consumers;

(ii) in case of the acquisition of securities or utility assets, the consideration, including all fees, commissions, and other remuneration, to whomsoever paid, to be given, directly or indirectly, in connection with such acquisition is not reasonable or does not bear a fair relation to the sums invested in or the earning capacity of the utility assets to be acquired or the utility assets underlying the securities to be acquired; or

(iii) such acquisition will unduly complicate the capital structure of the holding-company system of the applicant or will be detrimental to the public interest or the interests of investors or consumers or the proper functioning of such holding-company system.

Section 10(c) of the Act provides that, notwithstanding the provisions of Section 10(b), the Commission shall not approve:

(i) an acquisition of securities or utility assets, or of any other interest, which is unlawful under the provisions of Section 8 or is detrimental to the carrying out of the provisions of Section 11; or

(ii) the acquisition of securities or utility assets of a public utility or holding company unless the Commission finds that such acquisition will serve the public interest by tending towards the economical and the efficient development of an integrated public utility system.

As set forth more fully below, the Merger complies with all of the applicable provisions of Section 10 of the Act and should be approved by the Commission.

1. Section 10(b)(1).

The standards of Section 10(b)(1) are satisfied because the proposed Merger will not “tend towards interlocking relations or the concentration of control of public utility companies, of a kind or to an extent detrimental to the public interest or the interests of investors or consumers.” By its nature, any merger results in new links between previously unrelated companies. The Commission has recognized, however, that such interlocking relationships are permissible in the interest of efficiencies and economies. See *Northeast Utilities*, 50 S.E.C. 427, 443 (1990), *as modified*, 50 S.E.C. 511 (1991), *aff’d sub nom. City of Holyoke v. SEC*, 972 F.2d 358 (D.C. Cir. 1992) (finding that interlocking relationships are necessary to integrate the two merging entities). The links that will be established as a result of the Merger are not the types of interlocking relationships targeted by Section 10(b)(1), which was primarily aimed at preventing uneconomical combinations.<sup>55</sup> In contrast, the Merger will achieve various operating synergies. Among other things, the PSEG subsidiaries will enter into contractual arrangements with other Exelon system companies under which various administrative and management services will be provided. Because substantial benefits will accrue to the public, investors and consumers from the affiliation of Exelon and PSEG, whatever interlocking relationships may arise from the combination are not detrimental.

Under the Section 10(b)(1) concentration of control test, the Commission “considers various factors, including the size of the resulting system and the competitive effects of the acquisition.” *Entergy Corp., Holding Co.* Act Release No. 25952 (Dec. 17, 1993), *request for reconsideration denied*, Holding Co. Act Release No. 26037 (Apr. 28, 1994), *remanded sub nom. Cajun Elec. Power Coop. Inc. v. SEC*, 1994 WL 704047 (D.C. Cir. Nov. 16, 1994) *on remand*, *Entergy Corp., Holding Co.* Act Release No. 26410 (Nov. 17, 1995) (citations omitted). These factors are discussed below.

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<sup>55</sup> See Section 1(b)(4) of the Act (finding that the public interest and interests of consumers and investors are adversely affected “when the growth and extension of holding companies bears no relation to the economy of management and operation or the integration and coordination of related operating properties . . .”).

(a) Size.

As the Commission has recognized, Section 10(b)(1) does not “impose any precise limits on holding company growth.” *American Electric Power Company, Inc.*, 46 S.E.C. 1299, 1307 (1978) (“*AEP*”). The Commission has rejected a mechanical size analysis under Section 10(b)(1) in favor of assessing the size of the resulting system as it relates to the efficiencies and economies that can be achieved through the integration and coordination of the new system’s utility operations. *Entergy, supra* (rejecting “conclusory assertions that the combined systems would be too large to satisfy [Section 10(b)(1)]” and finding that merger created a “large system, but not one that exceeds the economies of scale of current electrical generation and transmission technology.”). Section 10(b)(1) allows the Commission to “exercise its best judgment as to the maximum size of a holding company in a particular area, considering the state of the art and the area or region affected.” *AEP, supra*. The Merger will not create a “huge, complex and irrational system” but, rather, will afford the opportunity to achieve economies of scale and efficiencies for the benefit of investors and consumers.

If approved, Exelon will serve approximately 7 million electric customers and 2 million gas customers located primarily in three states. As of September 30, 2004, the combined consolidated assets of Exelon and PSEG totaled approximately \$81 billion and, for the nine months ended September 30, 2004, combined consolidated operating revenues totaled approximately \$19 billion. As of December 31, 2004, the combined owned generating capacity of Exelon and PSEG was approximately 40,363 MW.

The following table shows Exelon’s relative size as compared to other registered systems in terms of assets, operating revenues and customers:<sup>56</sup>

<u>System</u>	<u>Total Assets (\$ Millions)</u>	<u>Operating Revenues (\$ Millions)</u>	<u>U.S. Electric Customers (Thousands)</u>
E.ON AG	140,897	58,405	1,208
National Grid Transco plc	57,021	12,531	3,750
Dominion Resources Inc.	44,186	12,078	3,900
American Electric Power Co. Inc.	36,743	14,545	5,013
Southern Company	35,045	11,251	4,136
Exelon (pro forma)	<u>80,865</u>	<u>25,863</u> <sup>57</sup>	<u>7,300</u>

In *AEP*, the Commission noted that, although the framers of the Act were concerned about “the evils of bigness, they were also aware that the combination of isolated local utilities into an integrated system afforded opportunities for economies of scale, the elimination of duplicate facilities and activities, the sharing of production capacity and reserves and generally more efficient operations... [and] [t]hey wished to preserve these opportunities.” *AEP*, 46 S.E.C. at 1309. By virtue of the Merger, Exelon will be in a position to realize precisely these types of benefits. Among other things, the Merger is expected to yield operating cost savings, corporate and administrative savings and purchasing savings, among others. These expected economies and efficiencies from the combined utility operations are described in greater detail in Item 3.B.5 below.

(b) Concentration of Control.

<sup>56</sup> Data derived from U.S. Securities and Exchange Commission, Financial and Corporate Report, *Holding Companies Registered under the Public Utility Holding Company Act of 1935 as of June 1, 2004* (data provided is as of December 31, 2003); Exelon data from Unaudited Pro Forma Combined Condensed Financial Statements included in S-4 Registration Statement filed as Exhibit C hereto.

<sup>57</sup> Nine months ended September 30, 2004, Post-Merger Pro Forma annualized.

The Commission's analysis under Section 10(b)(1) also includes a consideration of federal antitrust policies.

The proposed Merger will increase the total capacity of generation resources owned or controlled by Exelon. To ensure that the combined company does not have market power in any relevant market, Exelon and PSEG have proposed a comprehensive market power mitigation plan designed to address in full FERC's requirements for competitive markets. As part of the plan, the companies have proposed the Generation Divestiture as described in Item 1.H above.

The potential competitive concerns will be considered by other regulators, including the FERC and the Department of Justice. Pursuant to the HSR Act, Exelon and PSEG are required to file with the Antitrust Division Premerger Notification and Report Forms. See 16 C.F.R. Parts 801 through 803. The HSR Act prohibits consummation of the Merger until the statutory waiting period has expired or been terminated. Similarly, the Merger cannot proceed unless and until the FERC has approved the Merger, which will include review of potential competitive concerns pursuant to its authority under Section 203 of the Federal Power Act.

In these circumstances, the Commission has found, and the courts have agreed, that it is appropriate for the Commission to look to the FERC's expertise in operating issues, in determining that the standards of Section 10(b)(1) are met. In this regard, the Court of Appeals for the D.C. Circuit has found:

[W]hen the SEC and another regulatory agency both have jurisdiction over a particular transaction, the SEC may "watchfully defer[]" to the proceedings held before - and the result reached by - that other agency.

*Madison Gas & Electric Co. v. SEC*, 168 F.3d 1337, 1341-42 (D.C. 1999), citing *City of Holyoke Gas & Electric Department v. SEC*, 972 F.2d 358 (D.C. Cir. 1992) (dismissing challenge to order approving merger that asserted Commission could not rely on FERC and state review of competitive effects). Consistent with the foregoing, the Division in its 1995 Report on the Regulation of Public Utility Holding Companies (the "1995 Report") recommended that "the SEC avoid duplicative review of acquisitions and, where possible, defer to the work of other regulators in reviewing acquisitions." 1995 Report at 66.

2. Section 10(b)(2).

Section 10(b)(2) of the Act precludes approval of an acquisition if the consideration to be paid in connection with the Merger, including all fees, commissions and other remuneration, is "not reasonable or does not bear a fair relation to the sums invested in or the earning capacity of the utility assets to be acquired or the utility assets underlying the securities to be acquired." The Commission has found "persuasive evidence" that the standards of Section 10(b)(2) are satisfied where, as here, the agreed upon consideration for an acquisition is the result of arms-length negotiations between the managements of the companies involved, supported by an opinion of a financial advisor. See *Entergy Corp.*, 51 S.E.C. 869, 879 (1993); *Southern Company, Holding Co.* Act Release No. 24579 (Feb. 12, 1988).

The consideration paid in the Merger is reasonable for several reasons.

First, the former PSEG shareholders will hold about 32% and the Exelon shareholders will hold approximately 68% of the shares of Exelon following the Merger.

Second, as explained in the joint proxy statement/prospectus (included in Exhibit C hereto) (the "Joint Proxy Statement"), the historical price data for Exelon and PSEG common stock provide support for the consideration of 1.225 shares of Exelon common stock for each share of PSEG common stock.

Third, the merger consideration is the product of extensive and vigorous arm's-length negotiations between Exelon and PSEG. These negotiations were preceded by extensive due diligence, analysis and evaluation of the assets, liabilities and business prospects of each of the respective companies. This process is described in "Background of the Merger" in the Joint Proxy Statement. As recognized by the

Commission in Ohio Power Co., Holding Co. Act Release No. 16753 (June 8, 1970), prices arrived at through arms-length negotiations are particularly persuasive evidence that Section 10(b)(2) is satisfied.

Fourth, nationally recognized independent investment bankers have reviewed extensive information concerning Exelon and PSEG, analyzed the merger consideration employing a variety of valuation methodologies, and ultimately opined that the merger consideration is fair to the respective holders of Exelon common stock and PSEG common stock. The investment bankers' analyses are described in detail and their opinions are included in full in the Joint Proxy Statement. The assistance of independent consultants in setting consideration has been recognized by the Commission as evidence that the requirements of Section 10(b)(2) have been met.

Finally, submitting the share issuance for approval by the Exelon shareholders and the Merger for approval by the PSEG shareholders will provide additional assurance that the prices paid are reasonable.

Another consideration under Section 10(b)(2) is the overall fees, commissions and expenses to be incurred in connection with the Merger. Exelon believes that the Merger costs will be reasonable and fair in light of the size and complexity of the proposed Merger, and that the anticipated benefits of the Merger to the public, investors and consumers. *See, e.g., Entergy Corp.*, 51 S.E.C. at 881, n. 63 (fees and expenses of \$38 million, representing approximately 2% of the value of the consideration paid to the shareholders of Gulf States Utilities); *Northeast Utilities*, Holding Co. Act Release No. 25548 (June 3, 1992) (fees and expenses of approximately 2% of the value of the assets to be acquired); and *American Electric Power Company, Inc.*, Holding Company Act Release No. 27186 (June 14, 2000) at n. 40 (total fees, commissions and expenses of approximately \$72.7 million, representing 1.1% of the value of the total consideration paid by American Electric Power to the shareholders of Central and South West Corp.).

The total expenses of the Merger are approximately \$70 million (\$41 million for Exelon and \$29 million for PSEG) which constitute about one half of one percent of the value of the consideration paid by Exelon in the Merger.<sup>58</sup>

Pursuant to an engagement letter dated October 26, 2004, Exelon has agreed to pay JPMorgan a fee of \$15 million in consideration for its services as financial advisor, \$5 million of which was paid following the public announcement of the execution of the Merger Agreement, \$5 million of which is payable upon approval of the issuance of shares of Exelon common stock as contemplated by the Merger Agreement by Exelon shareholders and \$5 million of which is payable upon completion of the Merger. Pursuant to an engagement letter dated November 5, 2004, Exelon has agreed to pay Lehman Brothers a fee of \$15 million in consideration for its services as financial advisor, \$5 million of which was due upon the public announcement of the execution of the Merger Agreement, \$5 million of which is payable upon approval of the issuance of shares of Exelon common stock as contemplated by the Merger Agreement by Exelon shareholders and \$5 million of which is payable upon completion of the Merger.

Pursuant to an engagement letter dated November 8, 2004, PSEG has agreed to pay Morgan Stanley a fee of \$20 million in consideration for its services as financial advisor, \$5 million of which was paid following the public announcement of the execution of the Merger Agreement, \$5 million of which is payable upon PSEG shareholder approval of the Merger Agreement and \$10 million of which is payable upon completion of the Merger.

### 3. Section 10(b)(3).

Section 10(b)(3) requires the Commission to determine whether the Merger will "unduly complicate the capital structure" or be "detrimental to the public interest or the interest of investors or consumers or the proper functioning" of the Exelon system.

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<sup>58</sup> The value of the consideration, \$12,629 million, is taken from the pro forma financial statements in the Joint Proxy Statement.

The capital structure of the Exelon system will not change materially as a result of the Merger. In the Merger, Exelon will acquire 100% of the issued and outstanding common stock of PSE&G. Hence, the Merger will not create any publicly-held minority stock interest in the voting securities of any public utility company. The outstanding debt securities and preferred stock of PSE&G will also remain as outstanding obligations of PSE&G and will not be recourse to Exelon or any other company in the Exelon system.

The capital structures of Exelon and PSEG and the pro forma consolidated capital structure of Exelon are set forth in Item 1 hereof.

As those tables show, Exelon's pro forma consolidated common equity to total capitalization ratio of 42.89% will comfortably exceed the "traditionally acceptable 30% level." See *Northeast Utilities*, 50 S.E.C. at 440, n. 47. Common equity as a percentage of capitalization of each of the Utility Subsidiaries, other than PECO, is and will remain well over 30%.<sup>59</sup>

Section 10(b)(3) also requires the Commission to determine whether the proposed combination will be detrimental to the public interest, the interests of investors or consumers or the proper functioning of the combined Exelon system. The proposed combination of Exelon and PSEG is entirely consistent with the proper functioning of a registered holding company system. Exelon's and PSEG's electric utility operations are contiguous and interconnected and will be operated as a single interconnected and coordinated electric utility system following the Merger. Likewise, Exelon's existing gas utility operations and PSE&G's gas operations, which serve Pennsylvania and New Jersey, will be an integrated gas utility system as described *infra* following the Merger.

The Merger will result in substantial, and otherwise unavailable, savings and benefits to the public and to consumers and investors of both companies. Moreover, the Merger is subject to review by the PAPUC and the NJBPU, as well as the FERC, and notice has been given to the ICC, all of which ensures that the interests of customers will be adequately protected. For these reasons, Exelon believes that the Merger will be in the public interest and the interest of investors and consumers and will not be detrimental to the proper functioning of the resulting holding company system.

4. Section 10(c)(1).

(a) The Merger Will be Lawful Under Section 8.

Section 10(c)(1) first requires that the Merger be lawful under Section 8. That section was intended to prevent holding companies, by the use of separate subsidiaries, from circumventing state restrictions on common ownership of gas and electric operations. The Merger will not result in any new situation of common ownership of so-called "combination" systems within a given state. PSE&G already provides electric and gas service in overlapping areas of New Jersey. Moreover, the NJBPU has jurisdiction over the Merger. Accordingly, the Merger does not raise any issue under Section 8.

(b) The Merger Will Not be Detrimental to Carrying Out the Provisions of Section 11.

Section 10(c)(1) also requires that the Merger not be "detrimental to the carrying out of the provisions of section 11." Section 11(b)(1), in turn, directs the Commission generally to limit a registered holding company "to a single integrated public utility system," either electric or gas. An exception to this requirement, as discussed below, is provided in Section 11(b)(1)(A) - (C) (the "ABC clauses"), which

<sup>59</sup> As noted in the 2004 Financing Order, PECO has common equity of less than 30% when including securitization and the effects of a "receivable contribution" (as described in File No. 70-10189) but Exelon anticipates that PECO's common equity ratio will continue to improve and that PECO will reach a level of common equity of at least 30% of capitalization by December 31, 2010 (at which time all securitization bonds are expected to be retired and therefore will not be a consideration in the calculation). At December 31, 2004, PECO's common equity was 21% of total capitalization calculated in accordance with GAAP and was 66% excluding securitization and the effects of the receivable contribution.

permits a registered holding company to retain one or more additional (i.e., secondary) integrated public utility systems if the system satisfies the criteria of the ABC clauses.

In the 2000 Merger Order, the Commission determined that Exelon's primary system, comprised of the electric utility facilities of ComEd and PECO, constitutes an integrated electric utility system; and that the gas utility properties of PECO constitute an integrated gas utility system that is retainable under the standards of the ABC clauses. At issue in this proceeding is whether Exelon's acquisition of PSE&G, which operates as both an electric and gas utility in New Jersey, will result in a system that is "detrimental to the carrying out of the provisions of section 11."

As explained more fully below, the combination of the electric utility operations of the Utility Subsidiaries will result in a single, integrated electric utility system. In addition, the combination of PSE&G's gas utility properties with those of PECO will comprise an integrated gas utility system that may be retained by Exelon as an additional system under the ABC clauses of Section 11(b)(1).

These standards are addressed below.

(i) Integration of Electric Operations.

The threshold question is whether the electric utility properties of the Utility Subsidiaries will form a single "integrated public utility system," which, as applied to electric utility companies, is defined in Section 2(a)(29)(A) to mean:

a system consisting of one or more units of generating plants and/or transmission lines and/or distributing facilities, whose utility assets, whether owned by one or more electric utility companies, are physically interconnected or capable of physical interconnection and which under normal conditions may be economically operated as a single interconnected and coordinated system confined in its operations to a single area or region, in one or more States, not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management, efficient operation, and the effectiveness of regulation.

The Commission has interpreted this provision to establish four separate requirements for integration, as applied to an electric system: physical interconnection; coordination; limitation to a single area or region; and no impairment of localized management, efficient operation, and the effectiveness of regulation. See *National Rural Electric Cooperative Association v. Securities and Exchange Commission*, 276 F.3d 609 at 611 (D.C. Cir. 2002). The combined electric utility operations will satisfy each of these tests.

A. Interconnection

The first requirement for an integrated electric utility system is that the electric generation and/or transmission and/or distribution facilities comprising the system be "physically interconnected or capable of physical interconnection." As found by the Commission in the PJM Order, "electric properties within PJM are physically interconnected through PJM." In addition, the electric facilities and retail service areas of PSE&G and the Exelon Utility Subsidiaries are adjacent and their facilities are interconnected at numerous points (*see* Exhibit E-1). Under traditional analysis, this fact alone satisfies the interconnection requirement. *See e.g., Energy East*, Holding Company Act Release No. 27546 (June 27, 2002).

B. Coordination.

Historically, the Commission has interpreted the requirement that an integrated electric system be economically operated under normal conditions as a single interconnected and coordinated system "to refer to the physical operation of utility assets as a system in which, among other things, the generation and/or flow of current within the system may be centrally controlled and allocated as need or economy directs." *See, e.g., Conectiv, Inc.*, Holding Co. Act Release No. 26832 (Feb. 25, 1998), citing *The North American Company*, 11 S.E.C. 194, 242 (1942), *aff'd*, 133 F.2d 148 (2d Cir. 1943), *aff'd on constitutional issues*, 327 U.S. 686 (1946). The Commission has noted that, through this standard, "Congress intended that the utility

properties be so connected and operated that there is coordination among all parts, and that those parts bear an integral operating relationship to one another." See *Cities Service Co.*, 14 S.E.C. 28 at 55 (1943). Traditionally, the most obvious indicia of "coordinated operations" was the ability to jointly dispatch all system generating units automatically on an economic basis in order to achieve the lowest overall cost of electricity. As noted in the PJM Order, the facilities of PJM members are subject to the control of a single operator, PJM: "As the single control operator, PJM exercises functional control, including centralized dispatch of generation, over a contiguous, interconnected electric transmission system that encompasses the operations of its members, including PECO and ComEd." Of course, PSE&G is also a member of PJM and accordingly the analysis of the PJM Order applies equally to the post-Merger Exelon system.

Under Section 2(a)(29)(A), the Commission must also find that the resulting interconnected and coordinated system may be "economically operated." This calls for a determination that coordinated operation of the combined company's facilities is likely to produce economies and efficiencies. The question of whether a combined system will be economically operated under Section 10(c)(2) and Section 2(a)(29)(A) was addressed by the U.S. Court of Appeals in *Madison Gas and Electric Company v. SEC*, 168 F.3d 1337 (D.C. Cir. 1999). In that case, the court determined that in analyzing whether a system will be economically coordinated, the focus must be on whether the acquisition "as a whole" will "tend toward efficiency and economy." *Id.* at 1341. As discussed below, the Merger will meet this standard.

In short, all aspects of the combined system will be centrally directed and efficiently planned and coordinated. As with other utility combinations approved by the Commission, the combined system will be capable of being economically operated as a single interconnected and coordinated system as demonstrated by the variety of means through which its operations will be coordinated and the efficiencies and economies expected to be realized by the proposed Merger.

#### C. Single Area or Region.

As required by Section 2(a)(29)(A), the electric utility operations of Exelon following the Merger will be confined to a "single area or region in one or more States," all within PJM. See, e.g., *Pepero Holding, Inc.*, Holding Co. Act Release No. 27553 (July 24, 2002) ("the high degree of operational coordination and energy trading that occurs within the PJM RTO demonstrate that the mid-Atlantic U.S. is a single area or region in both operational and economic terms"). The Commission should find, based on the PJM Order and the facts presented herein, that the territories of ComEd, PECO and PSE&G also constitute a "single area or region in both operational and economic terms."

#### D. Size.

The final clause of Section 2(a)(29)(A) requires the Commission to look to the size of the combined system (considering the state of the art and the area or region affected) and its effect upon localized management, efficient operation, and the effectiveness of regulation. In the instant matter, these standards are easily met. The size of the Exelon electric system will not impair the advantages of localized management, efficient operation or the effectiveness of regulation. Instead, the proposed Merger will actually increase the efficiency of operations.

**Localized Management** -- Although PSE&G will necessarily come under new holding company management as a result of the Merger, it will continue to exist as a separate legal entity. PSE&G will continue to be headquartered in Newark, and the utility will continue to operate through regional offices with local service centers and line crews available to respond to customers' needs.

This operational structure, which is similar to that currently in place at ComEd and PECO, will permit the local, district and regional management teams of PSE&G to budget for operation of the electric distribution system and to schedule work forces in order to provide the same (or better) quality of service to customers of PSE&G. In short, PSE&G will continue to be managed on a day-to-day basis at a local level, particularly in areas that must be responsive to local needs. Accordingly, the advantages of localized management will not be impaired.

Efficient Operation -- As discussed below in the analysis of Section 10(c)(2), the Merger will result in greater economies and efficiencies. Operations will be more efficiently performed on a centralized basis because of economies of scale, standardized operating and maintenance practices and closer coordination of system-wide matters.

Effective Regulation -- The Merger will not impair the effectiveness of regulation at either the state or federal level. PSE&G will continue to be regulated by the NJBPU with respect to retail rates, service, securities issuances and other matters, and by FERC with respect to interstate electric sales for resale and transmission services.

(ii) Integration of Gas Operations.

The gas utility properties of PSE&G, when added to those owned by PECO, will form an "integrated gas utility system," which is defined in Section 2(a)(29)(B) to mean:

a system consisting of one or more gas utility companies which are so located and related that substantial economies may be effectuated by being operated as a single coordinated system confined in its operations to a single area or region, in one or more States, not so large as to impair (considering the state of the art and the area or region affected) the advantages of localized management, efficient operation, and the effectiveness of regulation: provided, that gas utility companies deriving natural gas from a common source of supply may be deemed to be included in a single area or region.

Thus, the definition of an integrated gas utility system has three distinct parts, each of which will be satisfied in this case.

A. Coordination.

In order to find coordination among the gas utility companies in the same holding company system, the Commission has historically focused primarily on the operating economies that may be effectuated through coordinated management of gas supply portfolios (i.e., gas purchase arrangements, transportation agreements, and storage assets), the access of the gas utility companies in the same holding company system to common market and supply-area hubs, the functional merger of separate gas supply departments under common management, and sharing of data management software systems. See *NIPSCO Industries, Inc.*, 53 S.E.C. 1296 at 1306-1309 (1999); *New Century Enterprises, Inc.*, Holding Co. Act Release No. 27212 (Aug. 16, 2000).

As discussed further in Item 2.B.5, below, Applicants state that the Merger will produce significant benefits to the public, investors and consumers. Applicants expect that the Merger will enable them to take advantage of future strategic opportunities in the increasingly competitive and rapidly evolving markets for energy and energy services in the United States. In particular, Applicants believe that the combined companies will be better positioned to take advantage of operating economies and efficiencies. Although PECO and PSE&G will continue to conduct their gas distribution operations through their respective corporate entities, and do not currently plan to combine gas supply operations, the systems nonetheless will be operated as a single coordinated system.

In 2004, Exelon BSC reorganized and expanded its Energy Delivery Shared Services ("EDSS") business unit. EDSS now houses employees who provide executive or centralized management services to ComEd and PECO (but not to Exelon, Exelon Generation or Enterprises), or whose duties include performing work on both ComEd and PECO projects. At that time, each of the major operating areas of the utilities assumed a new consolidated structure, with a single management team overseeing both ComEd and PECO functions. This structure focuses on the standardization of electric utility processes across both companies and the achievement of synergies through consolidation of common functions. Numerous operational and administrative and general functions overseen by EDSS management are applied at PECO across both electric and gas operations. These include policies and practices, training and methods, contractor and supply management, call center dispatch, financial planning and accounting services,

construction services and vehicle services, among others. Applicants expect that post-Merger, this model will be expanded to include PSE&G's gas as well as electric utility operations. Thus, EDSS will house employees who will perform work on behalf of both the PECO and the PSE&G gas systems. In this way, EDSS will coordinate the management of the two gas systems in areas such as executive services, asset management, customer service and marketing services, support services and business operations. With respect to business operations, as the PSE&G and PECO gas systems share many common features, (e.g. percentage of cast iron, steel and plastic pipes that make up the infrastructure) coordination can also be achieved by the use of common Supervisory Control and Data Acquisition ("SCADA") approaches and monitoring of pressures and flows at all of the points at which PSE&G and PECO take gas off the interstate pipeline systems; the use of common system design standards and criteria, the development of common material specifications to improve procurement processes and reduce costs and sharing of best work practices and the use of a common work management system. Further, PSE&G and PECO's systems are both subject to the same federal standards with respect to construction, operation and maintenance which results in opportunities for further coordination and efficiencies.

With regard to natural gas service itself, a significant amount of the gas distributed by PECO and PSE&G is purchased from the same supply basins in Texas and Louisiana, and is transported on the Texas Eastern and Transcontinental pipelines, and is stored in common storage areas owned by those and other pipelines (e.g. Dominion, Equitrans). These common portfolio resources should bring long-term benefits to the companies' customers. Moreover, as the dynamics and structure of the natural gas industry continue to change, the marketplace will create even more options for the companies to create value through coordination of their respective gas supply portfolios.<sup>60</sup>

**B. Single Area or Region.**

The combined gas system of PECO and PSE&G will also be confined to a single area or region in New Jersey and southeastern Pennsylvania.

**C. Size.**

For the same reasons given above in connection with the discussion of impacts of the Merger on the combined electric system, localized management, efficient operation, and the effectiveness of regulation will not be impaired by the resulting size of the integrated gas utility system.

**(iii) Retention of Combined Gas System.**

As indicated, under the "ABC clauses" of Section 11(b)(1), a registered holding company can own "one or more" additional integrated public utility systems if certain conditions are met. Specifically, the Commission must find that (A) the additional system "cannot be operated as an independent system without the loss of substantial economies which can be secured by the retention of control by such holding company of such system," (B) the additional system is located in one state or adjoining states, and (C) the combination of systems under the control of a single holding company is "not so large . . . as to impair the advantages of localized management, efficient operation, or the effectiveness of regulation."

**A. Loss of Economies.**

Clause A requires a showing that each additional integrated system (in this case, the integrated gas utility system formed by combining the operations of PECO and PSE&G) cannot be operated as an independent system without the loss of substantial economies which can be secured by the retention of control by a holding company of such system. Historically, the Commission has considered four ratios as a "guide" to determining whether lost economies would be "substantial" under Section 11(b)(1)(A). Specifically, the Commission has considered the estimated loss of economies expressed in terms of the ratio of increased expenses to the system's total operating revenues, operating revenue deductions, gross

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<sup>60</sup> Although PSEG ER&T currently procures the natural gas supply and manages pipeline capacity and gas storage services for the PSE&G gas system, and PECO performs these functions itself, as noted above, the source of supply, pipelines and location of storage for the two systems overlap to a large extent.

income and net income. See *Engineers Public Service Co.*, 12 SEC 41 (1942), *rev'd on other grounds and remanded*, 138 F. 2d 936 (DC Cir. 1943), *vacated as moot*, 332 US 788 (1947) ("*Engineers*"), and *New England Electric System*, 41 S.E.C. 888, 893 - 899 (1964). In *Engineers*, the Commission suggested that cost increases resulting in a 6.78% loss of operating revenues, a 9.72% increase in operating revenue deductions, a 25.44% loss of gross income, and 42.46% loss of net income would afford an "impressive basis for finding a loss of substantial economies" associated with a divestiture. 12 SEC at 59. More recently, the Commission has indicated that it will no longer require a comparison of resulting loss ratios to those in earlier cases. See *CP&L Energy, Inc., Holding Co.* Act Release No. 27284 (Nov. 27, 2000), fn. 40.

In its early decisions, the Commission considered the increases in operational expenses that were anticipated upon divestiture, but also took into account, as offsetting benefits, the significant competitive advantages that were perceived to flow from a separation of gas and electric operations. The Commission's assumption was that a combination of gas and electric operations is typically disadvantageous to the gas operations and, hence, the public interest and the interests of investors and consumers would be benefited by a separation of gas from the electric operations. In more recent cases, however, the Commission has recognized that the historical ratios may not provide an adequate indication of the substantial loss of economies that may occur by forcing a separation of electric and gas. Specifically, beginning with its decision in *New Century Energies, Inc.*, 53 S.E.C. 54 (1997), the Commission took notice of the changing circumstances in today's electric and gas industries, notably the increasing convergence of the electric and gas industries. The Commission concluded that, "in these circumstances, separation of gas and electric businesses may cause the separated entities to be weaker competitors than they would be together. This factor adds to the quantifiable loss of economies caused by increased costs." 53 S.E.C. at 76. This view was repeated in subsequent cases, including the 2000 Merger Order and *WPL Holdings, Inc.*, 53 S.E.C. 501 (1997). The Commission has also recognized that revenue enhancement opportunities and other benefits likely to be realized from a "convergence" merger would be diminished or lost if the Commission forced a divestiture of the additional system. See *SCANA Corp., Holding Co.* Act Release No. 27133 (Feb. 9, 2000); and *Northeast Utilities, Holding Co.* Act Release No. 27127 (Jan. 31, 2000).

The Commission in the 2000 Merger Order found that the PECO gas utility operations constituted a permissible additional integrated public utility system.

The Applicants are preparing a study that analyzes the lost economies that the combined gas utility operations would suffer if Exelon could not retain them (the "Gas Study").<sup>61</sup> Among other things, divestiture of the gas operations would cause consumers to forfeit the cost-saving benefits that they may obtain from Exelon's ability to offer a complete package of energy products and services.

The 2000 Merger Order noted the Commission's policy determination that "significant economies and competitive advantages inure in the ownership of both gas and electric operations."<sup>62</sup> Besides the loss of these inherent economies, other substantial economies would be lost by the separation of the gas operations from the Exelon electric system. These lost economies would include decreased efficiencies from separate meter reading, meter testing and billing operations; expenses for duplicative customer service operations; plus a loss of savings due to the inability to exploit synergies in areas such as facilities maintenance, emergency work coordination and other administrative operations. A final consideration is that the electric and gas operations of PSE&G have long been under its control. The Merger will not alter the status quo with respect to these operations.<sup>63</sup> Further, the Merger will be subject to review by the PAPUC, which has jurisdiction over PECO, and the NJBPU, which has jurisdiction over PSE&G.

#### B. Same State or Adjoining States.

<sup>61</sup> See Exhibit G-9 hereto.

<sup>62</sup> 2000 Merger Order, citing *WPL Holdings, Inc., Holding Co.* Act Release No. 26856 (Apr. 14, 1998), *aff'd, Madison Gas and Electric Co. v. SEC*, 972 F.2d 358 (D.C. Cir. 1992); *TUC Holding Co., Holding Co.* Act Release No. 26749 (Aug. 1, 1997); and *New Century Energies, Inc.*, 53 S.E.C. 54 (1997).

<sup>63</sup> See *New Century Energies, Inc.*, 53 S.E.C. 54 (1997).

The proposed Merger does not raise any issue under Section 11(b)(1)(B) of the Act, as the gas utility properties are located and operate exclusively in adjoining states, Pennsylvania and New Jersey. Thus, the requirement that each additional system be located in one State or adjoining States is satisfied.

C. Size.

Further, retention of the combined gas utility business does not raise any issues under Section 11(b)(1)(C) of the Act. The combination of both electric and gas utility systems under the control of a single holding company will be “not so large . . . as to impair the advantages of localized management, efficient operation, or the effectiveness of regulation.” As the Commission has recognized, the determinative consideration is not size alone or size in an absolute sense, either big or small, but size in relation to its effect, if any, non-localized management, efficient operation and effective regulation. From these perspectives, it is clear that the continued ownership of the combined gas system by Exelon is not too large.

As of December 31, 2004, and giving effect to the Merger, the combined gas utility operations would represent only about 11% of Exelon’s post-Merger gross utility plant, and only about 14% of Exelon’s post-Merger net operating revenues.

The local operations of PSE&G will continue to be handled from PSE&G’s local operations centers, with supplemental support provided by other Exelon system companies with personnel and other resources in close proximity. Thus, the advantages of localized management will be preserved.

(iv) Retention of PSEG’s Non-Utility Interests.

Section 11(b)(1) permits a registered holding company to retain “such other businesses as are reasonably incidental, or economically necessary or appropriate, to the operations of [an] integrated public utility system.” The Commission has historically interpreted this provision to require an operating or “functional” relationship between the non-utility activity and the system’s core utility business. *See, e.g. Michigan Consolidated Gas Co.*, 44 S.E.C. 361 (1970), *aff’d*, 444 F.2d 913 (D.C. Cir. 1971); *United Light and Railways Co.*, 35 S.E.C. 516 (1954); *CSW Credit, Inc.*, 51 S.E.C. 984 (Mar. 2, 1994); and *Jersey Central Power and Light Co.*, Holding Co. Act Release No. 24348 (Mar. 18, 1987).

In addition, the Commission has permitted new registered holding companies to retain passive investments which, although not meeting the functional relationship test, could nevertheless be acquired under the standards of Section 9(c)(3) of the Act.

Exhibit G-7 lists and describes those non-utility businesses conducted by PSEG and its subsidiary companies. As a result of the Merger, those non-utility businesses and interests will become businesses and interests of Exelon. Except as discussed below, these non-utility interests are fully retainable by Exelon under the Act.

In previous matters, including the 2000 Merger Order, the Commission determined it was appropriate to exclude from the computation of “aggregate investment” for purposes of Rule 58 investments made at a time the company was not part of a registered holding company system.<sup>64</sup> *See also New Century Energies, supra.* In this matter as well, Applicants ask the Commission to confirm that pre-existing investments by PSEG and its subsidiaries in “energy-related companies” prior to the effective date of Rule 58 will not count in the calculation of the 15% limitation for purposes of the safe harbor under Rule 58.

(v) Post-Merger Corporate Structure: The Intermediate Holding Company

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<sup>64</sup> Safe harbor under Rule 58 is available so long as, among other things, a registered holding company’s “aggregate investment” in “energy-related companies” does not exceed 15% of the consolidated capitalization of the registered holding company.

Section 11(b)(2) of the Act requires the Commission to ensure that “the corporate structure or continued existence of any company in the holding company system does not unduly or unnecessarily complicate the structure, or unfairly or inequitably distribute voting power among security holders, of the holding company system.” Section 11(b)(2) also directs the Commission to require each registered system company “to take such action as the Commission shall find necessary in order that such holding company shall cease to be a holding company with respect to each of its subsidiary companies which itself has a subsidiary company which is a holding company,” in other words, to eliminate “great-grandfather” holding companies.

Post-Merger, there will be one instance of a “great-grandfather” holding company, the continued existence of which the Commission approved in the 2000 Merger Order. Exelon, through Delivery, owns substantially all of the outstanding common stock of ComEd (*see* note 7) which, in turn, is a holding company for the Indiana Company. The Indiana Company has no retail customers and owns only transmission facilities with a depreciated book value at December 31, 2004 of only \$7.4 million. The operation of the Indiana Company’s transmission facilities is subject to the control of PJM. Accordingly, the Indiana Company has virtually no business operations with outside third parties. As noted in the 2000 Merger Order:

We do not believe in any event that the proposed corporate structure of the Exelon system implicates the abuses that section 11(b)(2) of the Act was intended to prevent. These abuses, facilitated by the pyramiding of holding company groups, involved the diffusion of control and the creation of different classes of debt or stock with unequal voting rights. Those abuses are not at issue in this matter.

With respect to the Delivery chain, only the presence of the Indiana Company raises an issue under section 11(b)(2). The Indiana Company has no retail customers and holds only a very small amount of transmission assets directly related to the distribution business of ComEd. . . . [T]he Indiana Company has been in existence for decades and federal and state regulators have perceived no abuses in the arrangement.

We think that it is appropriate to “look through” the intermediate holding companies (or to treat them as a single company) for purposes of the analysis under section 11(b)(2) of the Act. Accordingly, we do not find it necessary to require the elimination of the intermediate holding companies to ensure that the corporate structure of the Exelon system or continued existence of any system company “does not unduly or unnecessarily complicate the structure” of the Exelon system.

5. Section 10(c)(2).

The Merger will “serve the public interest by tending toward the economical and efficient development of an integrated public utility system,” and therefore will satisfy the requirements of Section 10(c)(2) of the Act.

The proposed Merger will create the nation’s premier utility company, with over seven million electric customers and two million gas customers in three states. By sharing resources and best practices, the proposed Merger will enhance operations across the Exelon system and strengthen Exelon’s ability post-Merger to provide cost-effective, safe and reliable service. The Merger will result in numerous economies and efficiencies within the meaning of the Act:

- Increased Scale and Scope; Diversification. The combined company will have increased scale and scope in both energy delivery and generation. In addition, the combined company is expected to have greater diversification and balance in its energy delivery business and generation portfolio. This increased scale, scope and diversification is expected to result in improved service and reliability. With

respect to the energy delivery business, the combined company will have three urban utility franchises with service areas encompassing more than 18 million people. The combined company also will have a large gas distribution portfolio to complement its electric distribution business. The combined generation portfolio will be more balanced in terms of geography, fuel mix, dispatch and load-servicing capacity.

- Commitment to Competition. Exelon and PSEG have been staunch advocates for competitive retail and wholesale markets in electricity and gas. This shared vision will allow the new company to be even more active in the promotion of competitive markets and the development of energy-related services. In addition, New Jersey, Pennsylvania and Illinois all have passed legislation bringing competition to the electric industry, and are in varying phases of the transition to full competition. The regulatory knowledge and experience of each company will enhance the merged company's ability to manage the transition to competition for the benefit of both customers and shareholders.
- Improved Nuclear Operations. Given Exelon's strong, successful performance in running the nation's largest nuclear fleet, the Applicants expect to realize improved stability, higher capacity utilization rates and lower costs from combining nuclear operations under one management. Higher capacity utilization rates means that the Applicants would be producing more energy from their nuclear fleet that can be sold in the wholesale markets, which should have a procompetitive effect in the wholesale energy markets located in the PJM region where the Applicants are located. This in turn should be beneficial to the Applicants' retail customers as well as to retail customers throughout the PJM region. Increasing nuclear output will have a small but significant tendency to lower wholesale prices. This is because increasing the amount of energy at "the bottom of the stack" will in at least some hours lower the PJM marginal cost. All else being equal, therefore, this should lower Locational Marginal Prices ("LMP"), particularly in PJM East.
- Anticipated Financial Strength and Flexibility. The diversification of the energy delivery and generation portfolios of the combined company should result in a more stable cash flow, with approximately half of the combined company's earnings and cash flow coming from the three regulated utilities and approximately half coming from the unregulated generation business.
- Sharing of Best Practices. The Merger will combine companies with complementary areas of expertise; Exelon's expertise in generation operations and PSEG's expertise in transmission and distribution operations.
- Substantial Synergies. Exelon and PSEG have estimated synergies from the Merger to be approximately \$400 million pre-tax in the first full year after closing, growing to approximately \$500 million pre-tax annually in the second full year, excluding out-of-pocket costs to achieve and transaction costs. Approximately 85% of these synergies are cost related and 15% are based on increased production at PSEG's nuclear plants. These cost savings and productivity improvements will result from a consolidation of the proven capabilities of both companies, including implementing certain practices and processes that have been successful in achieving cost reductions since the 2000 merger of Unicom and PECO. Savings are expected to come from the elimination of duplicative activities in corporate and administrative operations, marketing and trading operations, as well as fossil, nuclear and utility management functions; improved operating efficiencies in nuclear operations; efficiencies and savings generated from consolidation of corporate programs and information technology platforms; and supply chain benefits realized from improved sourcing efficiencies.

Although some of the anticipated economies and efficiencies will be fully realized only in the longer term, they are properly considered in determining whether the standards of Section 10(c)(2) have been met. *See AEP*, 46 S.E.C. at 1320 - 1321. Some potential benefits cannot be precisely estimated; nevertheless, they too are entitled to be considered. As the Commission has observed, "[s]pecific dollar forecasts of future savings are not necessarily required; a demonstrated potential for economies will suffice even when these are not precisely quantifiable." *Centerior Energy Corp.*, 49 S.E.C. at 480.

6. Section 10(f).

Section 10(f) provides that:

The Commission shall not approve any acquisition as to which an application is made under this section unless it appears to the satisfaction of the Commission that such State laws as may apply in respect of such acquisition have been complied with, except where the Commission finds that compliance with such State laws would be detrimental to the carrying out of the provisions of section 11.

As previously indicated, the Merger is subject to review by or notice to each of the affected state regulators.

C. Rules 53 and 54.

The 2004 Financing Order authorizes Exelon to engage in financings for the purposes of investing in EWGs and FUCOs so long as the aggregate investment in EWGs and FUCOs does not exceed \$4 billion. The 2004 Financing Order reserves jurisdiction over a request to engage in an additional \$3 billion in EWG and FUCO-related financing transactions. Exelon requests the Commission authorize it to engage in financings post-Merger for the purposes of investing in EWGs and FUCOs so long as the aggregate investment in EWGs and FUCOs does not exceed \$8.0 billion.

In support of this request, Exelon presents the following:

1. Rule 53 Generally

Under Rule 53(a), the Commission shall not make certain specified findings under Sections 7 and 12 in connection with a proposal by a holding company to issue securities for the purpose of acquiring the securities of or other interest in an EWG, or to guarantee the securities of an EWG, if each of the conditions in paragraphs (a)(1) through (a)(4) thereof are met, provided that none of the conditions specified in paragraphs (b)(1) through (b)(3) of Rule 53 exists.

As of December 31, 2004, the consolidated amount of Exelon's aggregate investment in EWGs and FUCOs (as that term is defined in Rule 53) was \$2.2 billion, which is in excess of 50% of Exelon's average consolidated retained earnings (calculated as required by Rule 53) of \$3.0 billion as of that date. As a result of the sale of Sithe Energies, Inc. ("Sithe") on January 31, 2005, Exelon's aggregate investment in EWGs decreased to approximately \$1.4 billion. In the 2004 Financing Order, the Commission authorized Exelon to enter into financing transactions in respect of an "aggregate investment" in EWGs and FUCOs of up to \$4 billion and reserved jurisdiction over the remainder of Exelon's \$7.0 billion request. It is anticipated that, as a result of the Merger, Exelon's aggregate investment in EWGs and FUCOs will be approximately \$6.5 billion.<sup>65</sup> Accordingly, Exelon requests that the Commission approve an aggregate investment limit of \$8.0 billion.

Exelon satisfies all of the requirements of Rule 53(a) except for clause (1) thereof. None of the conditions specified in Rule 53(b) is, or is expected to be, applicable.<sup>66</sup> For the reasons that follow, the proposed increased aggregate investment:

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<sup>65</sup> This amount is premised upon the successful execution of the Exelon Generation Restructuring, but not the Generation Divestiture described in Item 1.H.

<sup>66</sup> Exelon represents that it will remain in compliance with the requirements of Rule 53(a), other than Rule 53(a)(1), at all times through the Authorization Period. Exelon will file a post-effective amendment in to this Application/Declaration in the event that one of the circumstances described in Rule 53(b) should occur during the period through the end of the Authorization Period.

- (1) Will not have a substantial adverse impact upon the financial integrity of the registered holding company system; and
- (2) Will not have an adverse impact on any utility subsidiary of the registered holding company, or its customers, or on the ability of State commissions to protect such subsidiary or customers.

Rule 53(c).

As described in Item 1.L.5, because of the accounting for the Merger under GAAP, the retained earnings of Exelon post-Merger will be less than the combined retained earnings balances of Exelon and PSEG prior to the Merger. The Commission has considered similar situations in which previously significant amounts of retained earnings were eliminated.<sup>67</sup> Write-offs reducing retained earnings have been caused by unrecovered stranded costs, disposition of generating assets, the purchase accounting required in certain mergers and other factors.<sup>68</sup> The Commission has recognized that these are extraordinary events and, while retained earnings have been reduced, the changes causing such reduction have not adversely affected the fundamental financial strength of the holding company system. In this matter there can be no question that Exelon currently is, and post-Merger will be, a financially sound holding company with significant equity.

## 2. EWG and FUCO Earnings and Losses

With regard to capitalization, since December 31, 2000, there has been no material adverse impact on Exelon's consolidated capitalization resulting from Exelon's investments in EWGs and FUCOs. Exelon's common equity ratio has remained above 30% since 2000.

December 31,	Common Equity Ratio (%)
2000	31.3
2001	35.0
2002	32.1
2003	34.9
2004	40.8

These ratios are within acceptable industry ranges. The proposed transactions will not have any material adverse impact on capitalization.

In the aggregate, Exelon's EWG and FUCO investments have been profitable for all annual periods ending December 31, 2000 through December 31, 2002 and for the quarter ended June 30, 2003. While in 2003 Exelon recorded losses of \$1.2 billion (\$729 million net of income tax) in connection with

<sup>67</sup> See, e.g., *FirstEnergy Corp.*, Holding Co. Act Release No. 27459 (Oct. 29, 2001), *Connectiv, Inc.*, Holding Co. Act Release No. 27111 (Dec. 14, 1999).

<sup>68</sup> In *FirstEnergy*, *supra*, the subject merger eliminated the acquired company's retained earnings, and in *Connectiv*, *supra*, retained earnings were affected by write-offs resulting from de-regulation legislation and previous merger eliminating acquired company's retained earnings). See also *Northeast Utilities*, Holding Co. Act Release No. 27147 (March 7, 2000) (restructuring legislation, asset divestitures and securitization resulted in EWG investments in excess of 50% of retained earnings).

two of its EWG investments, Exelon New England Holdings Company ("EBG") and Sithe Energies, Inc. ("Sithe"), Exelon has since transferred the ownership of EBG to EBG's lenders (on May 25, 2004, recognizing a net gain of \$85 million) and disposed of Sithe on January 31, 2005 (see discussion below). Excluding the losses at these two companies, for which substantially all required write-offs have been taken, Exelon's remaining EWGs were profitable in 2003. For the twelve months ending December 31, 2004, Exelon's EWGs have been, in the aggregate, profitable. For information on EWG earnings, please see item 5a of Exelon's quarterly filed Rule 24 certificates.

On November 25, 2003, Exelon Generation, Reservoir Capital Group ("Reservoir") and Sithe completed a series of transactions resulting in Exelon Generation and Reservoir each indirectly owning a 50% interest in Sithe (Exelon Generation owned 49.9% prior to November 25, 2003).

Both Exelon Generation's and Reservoir's 50% interests in Sithe were subject to put and call options. On September 29, 2004, Exelon Generation exercised its call option and entered into an agreement to acquire Reservoir's 50% interest in Sithe for \$97 million. On November 1, 2004, Exelon Generation entered into an agreement to sell Sithe to Dynegy Inc. ("Dynegy") for \$135 million in cash.

On January 31, 2005, subsidiaries of Exelon Generation completed a series of transactions that resulted in Exelon Generation's exit from its investment in Sithe. Specifically, subsidiaries of Exelon Generation closed on the acquisition of Reservoir's 50% interest in Sithe and the sale of 100% of Sithe to Dynegy. Prior to closing on the sale to Dynegy, subsidiaries of Exelon Generation received from Sithe approximately \$65 million in cash distributions. As a result of the sale, Exelon deconsolidated from its balance sheet approximately \$820 million of debt and was released from approximately \$125 million of credit support. Additionally, Exelon issued certain guarantees to Dynegy that will be taken into account in the final determination of the gain or loss on sale.

On October 13, 2004, Sithe transferred all of the shares of Sithe International, Inc. and its subsidiaries to a subsidiary of Exelon Generation in exchange for the cancellation of a \$92 million note and accrued interest. Sithe International, through its subsidiaries, had a 49.5% interest in two Mexican business trusts that own the Termoeléctrica del Golfo ("TEG") and Termoeléctrica Peñoles ("TEP") power stations, two 230 MW petcoke-fired generating facilities in Tamuín, Mexico that commenced commercial operations in the second quarter of 2004. Both the TEG and TEP power stations are EWGs.

### 3. Risk Analysis and Mitigation.

Exelon has a comprehensive risk analysis and mitigation process in place.<sup>69</sup>

All of Exelon's investments in EWGs and FUCOs are segregated from ComEd and PECO, and in the future will remain segregated from ComEd, PECO and PSE&G. Any losses that may be incurred by such EWGs and FUCOs would have no effect on the rates of the Retail Utility Subsidiaries. Exelon represents that it will not seek recovery through higher rates from the Retail Utility Subsidiaries' utility customers in order to compensate Exelon for any possible losses that it or any Subsidiary may sustain on the investment in EWGs or FUCOs or for any inadequate returns on such investments.

### 4. Financial Ratios.

Growth in Retained Earnings. Both Exelon and PSEG have had significant increases in retained earnings over the past four years. Since the 2000 Merger, Exelon's retained earnings have grown from \$334 million to \$3,353 million, an increase of 935%. Also during this period, PSEG's retained earnings have increased by 66%, from \$1,459 million to \$2,425 million.

<sup>69</sup> This process was described in detail in Amendment No. 4 in File No. 70-9693, filed December 5, 2000. Exelon is aware of proposed Rule 55, which would codify the Commission's practice of requiring holding companies to institute a risk management process. See Holding Co. Act Release No. 27342 (Feb. 7, 2001). Exelon will comply with the requirements of Rule 55 if it is adopted.

Financial Ratios. Exelon's requested \$8.0 billion aggregate investment in EWGs and FUCOs would represent a conservative and reasonable commitment of Exelon capital for a company the size of Exelon post-Merger. For example, investments of this amount would be equal to only approximately:

15.5% of Exelon's pro-forma total consolidated capitalization (\$51.7 billion),<sup>70</sup>

24.5% of pro forma consolidated utility plant and equipment (\$32.7 billion),

9.9% of pro forma total consolidated assets (\$80.9 billion), and

18.1% of the pro forma market value of Exelon's outstanding common stock (\$44.3 billion).<sup>71</sup>

These percentages are substantially better than the comparable figures relied on by the Commission in approving Exelon's aggregate investment in the 2004 Financing Order. Based on Exelon's financial condition at December 31, 2003, a \$7.0 billion aggregate investment in EWGs and FUCOs would have represented 28.7% of consolidated capitalization, 38.6% of consolidated utility plant, 16.7% of consolidated assets and 32.1% of market value of Exelon common stock. Accordingly, the calculations show that Exelon should be authorized to invest the proceeds of financings in EWGs and FUCOs as requested.

#### 5. State Commissions.

The PAPUC has previously advised the Commission that Exelon's proposed aggregate investment of up to \$7.0 billion in EWGs and FUCOs would not adversely affect the state commission's ability to continue to assure adequate protection of utility customers and ratepayers, and the ICC has previously advised the Commission that Exelon's proposed aggregate investment of up to \$5.5 billion in EWGs and FUCOs would not adversely affect the state commission's ability to continue to assure adequate protection of utility customers and ratepayers. Exelon and PSE&G have asked the NJBPU to advise the Commission that Exelon's proposed aggregate investment of up to \$7.0 billion in EWGs and FUCOs would not adversely affect the state commission's ability to continue to assure adequate protection of utility customers and ratepayers. Exelon plans to seek any necessary confirmation from each state commission regarding its request contained herein for an increase in aggregate investment authority.

#### 6. Rule 54.

Rule 54 provides that, in determining whether to approve the issue or sale of any securities for purposes other than the acquisition of any EWG or FUCO or other transactions unrelated to EWGs or FUCOs, the Commission shall not consider the effect of the capitalization or earnings of subsidiaries of a registered holding company that are EWGs or FUCOs if the requirements of Rule 53(a), (b) and (c) are satisfied. As described above in detail, Exelon may not be in compliance with all of the provisions of the Rule 53 safe harbor post-Merger. Exelon believes that, for the reasons set out above, the Commission should approve the increased limit on aggregate investment. For those same reasons, Exelon requests the Commission to make no adverse findings under Rule 54 in connection with the approvals sought herein for other purposes.

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<sup>70</sup> This calculation of capitalization includes securitization obligations.

<sup>71</sup> The market value of Exelon common stock is calculated based on the pro forma number of shares of Exelon common stock to be outstanding immediately following the Merger assuming conversion of PSEG common stock, times the closing stock price of Exelon common stock at December 31, 2004 of \$44.07 per share.

#### Item 4. Regulatory Approvals.

##### New Jersey Board of Public Utilities

As a utility in the State of New Jersey, PSE&G is subject to the jurisdiction of the NJBPU. Under Section 48:2-51.1 of New Jersey's public utility law, the NJBPU's approval is required in connection with the indirect transfer of the capital stock of PSE&G resulting from the Merger. In considering the Merger, the NJBPU is required to evaluate the impact of the Merger in four areas: competition, the rates of ratepayers affected by the Merger, the employees of the affected public utility, and the provision of safe and adequate utility service at just and reasonable rates.

On February 4, 2005, Exelon and PSE&G made the initial filing of their joint application with the NJBPU for approval of the indirect transfer of the capital stock of PSE&G resulting from the Merger. While New Jersey law does not specify a timetable for completion of the NJBPU's review, Exelon and PSE&G have asked that the NJBPU handle the matter on an expedited basis.

In addition, while not required by law to complete the Merger, Exelon and PSEG have made it a condition to the Merger that PSE&G receive an order from the NJBPU allowing PSE&G to defer certain pension and other post-retirement benefit expenses that will be recognized in connection with the purchase accounting treatment of the Merger, and providing that PSE&G's rate recovery of pension and other post-retirement benefits will be calculated consistently with recovery of such amounts in the absence of the Merger.<sup>72</sup> On February 4, 2005, Exelon and PSE&G made the initial filing of their joint application with the NJBPU to obtain the order.<sup>73</sup>

##### New Jersey Department of Environmental Protection

Subsidiaries of PSEG own facilities in New Jersey that are industrial establishments as defined in ISRA. The parties intend to file their application with NJDEP for a letter of non-applicability under ISRA with respect to the Merger, the Generation Restructuring and Merger related corporate restructurings during the first quarter of 2005.<sup>74</sup>

##### New York Public Service Commission

As an owner of generation facilities in the State of New York, a subsidiary of PSEG Power is subject to the jurisdiction of the New York Public Service Commission ("NYPSC"). Under Section 70 of the New York Public Service Law, the NYPSC's written consent is required in connection with the indirect transfer of ownership interests in such subsidiary of PSEG Power in connection with the Merger. Under Section 70 of the New York Public Service Law, the NYPSC must determine whether the Merger is in the public interest. The parties intend to file their application for approval with the NYPSC during the first quarter of 2005.<sup>75</sup>

##### Pennsylvania Public Utility Commission

PECO and PSE&G are subject to the jurisdiction of the PAPUC. The issuance to each of PECO and PSE&G of a certificate of public convenience and necessity by the PAPUC may be required as a result

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<sup>72</sup> For a description of this matter, see "Risk Factors—Risks Relating to the Merger—The combined company may be unable to obtain permission from the NJBPU to recover PSE&G's pension and other post-retirement benefit expenses, which could have an adverse effect on its cash flow and results of operations" in the Registration Statement on Form S-4 filed as Exhibit C hereto.

<sup>73</sup> See Exhibit D-2 hereto.

<sup>74</sup> See Exhibit D-5 hereto.

<sup>75</sup> See Exhibit D-6 hereto.

of the indirect transfer of the capital stock of PSE&G in connection with the Merger under Chapters 11, 22 and 28 of the Public Utility Code of Pennsylvania. The standard for approval is whether the transaction is necessary and proper for the service, accommodation, convenience or safety of the public. This standard has been applied by the PAPUC to require that applicants demonstrate that the transaction will affirmatively promote the service, accommodation, convenience or safety of the public in some substantial way. In addition, under provisions enacted as part of Pennsylvania's electric and natural gas restructuring legislation, the PAPUC must consider:

- whether a proposed transaction is likely to result in anticompetitive or discriminatory conduct, including the unlawful exercise of market power, which would prevent retail electric or natural gas customers in Pennsylvania from obtaining the benefits of a properly functioning and workable competitive retail electric or natural gas market; and
- the effect of the proposed transaction on the natural gas distribution company employees and authorized collective bargaining agreement.

On February 4, 2005, PECO and PSE&G made the initial filing of their joint application for approval by the PAPUC under the Public Utility Code of Pennsylvania or a determination that Chapters 11, 22 and 28 are not applicable to the Merger.<sup>76</sup> While the Public Utility Code of Pennsylvania does not specify a timetable for completion of the PAPUC's review, PECO and PSE&G have asked that the PAPUC handle the matter on an expedited basis.

Illinois Commerce Commission ComEd has filed a notice with respect to the Merger with the ICC. Formal approval of the Merger by the ICC is not required.<sup>77</sup>

Connecticut As the owner of generation stations in the State of Connecticut, PSEG Power Connecticut LLC, an indirect subsidiary of PSEG Power, is subject to the jurisdiction of the Connecticut Siting Council ("CSC") under Connecticut public utility laws and the Connecticut Department of Environmental Protection ("CDEP") under Connecticut environmental law. The indirect transfer of the ownership interests in these entities may require the approval of the CDEP and will require the approval of the CSC. The parties filed their application with the CSC on March 3, 2005 and intend to file their application for approval with the CDEP during the first quarter of 2005.<sup>78</sup>

#### Nuclear Regulatory Commission ("NRC")

PSEG Power holds a NRC operating license for its Salem and Hope Creek nuclear generating facilities. This license authorizes PSEG Power to own and/or operate its nuclear generating facilities. The Atomic Energy Act provides that a license may not be transferred or, in any manner disposed of, directly or indirectly, through transfer of control of any license unless the NRC finds that the transfer complies with the Atomic Energy Act and consents to the transfer. Therefore, the consent of the NRC is required for the transfer of control pursuant to the Merger of the license held by PSEG Power. The NRC will consent to the transfer if it determines that:

- the proposed transferee is qualified to be the holder of the license; and
- the transfer of the license is otherwise consistent with applicable provisions of laws, regulations and orders of the NRC.

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<sup>76</sup> See Exhibit D-4 hereto.

<sup>77</sup> See Exhibit D-3 hereto.

<sup>78</sup> See Exhibit D-7 hereto.

The parties have filed applications with the NRC.<sup>79</sup>

#### Federal Energy Regulatory Commission

Each of Exelon and PSEG has public utility subsidiaries subject to the jurisdictions of FERC under the Federal Power Act. Section 203 of the Federal Power Act provides that no public utility may sell or otherwise dispose of its jurisdictional facilities, directly or indirectly merge or consolidate its facilities with those of any other person, or acquire any security of any other public utility, without first having obtained authorization from FERC.

FERC has stated that, in analyzing a merger under Section 203, it will evaluate the following criteria:

- the effect of the merger on competition in wholesale electric power markets, utilizing an initial screening approach derived from the Department of Justice/Federal Trade Commission-Initial Merger Guidelines to determine if a merger will result in an increase in an applicant's market power;
- the effect of the merger on the applicants' FERC jurisdictional ratepayers; and
- the effect of the merger on state and federal regulation of the applicants.

On February 4, 2005 Exelon and PSEG made the initial filing of their application for approval with FERC. Included in the filing was the parties' market concentration mitigation plan.<sup>80</sup> The market concentration mitigation plan contemplates (1) the divestiture of fossil fuel generating facilities with 2,900 MW of generating capacity and (2) the transfer of control of 2,600 MW of baseload nuclear capacity through either long-term firm baseload energy sales contracts or an annual auction. Exelon and PSEG have not offered to divest any nuclear generating facilities and do not anticipate doing so.

In addition, while not required by the Federal Power Act, Exelon and PSEG have made it a condition to completion of the Merger that FERC approve under Section 205 of the Federal Power Act the sale by the public utility subsidiaries of the combined company of wholesale power and related services at market-based rates.

#### Antitrust

Under the provisions of the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, the Merger cannot be completed until both Exelon and PSEG file a notification of the proposed transaction with the Antitrust Division of the United States Department of Justice and the Federal Trade Commission ("FTC") and the specified waiting periods have expired or been terminated. The parties have been informed that the Antitrust Division will review the case and the FTC will not.

At any time before the Merger is completed, the Antitrust Division could challenge or seek to block the Merger under the antitrust laws, as it deems necessary or desirable in the public interest. Other competition promoting agencies with jurisdiction over the Merger could also initiate action to challenge or block the Merger. In addition, in some jurisdictions, a competitor, customer or other third party could initiate a private action under the antitrust laws challenging or seeking to enjoin the Merger, before or after it is completed. Based upon an examination of information available relating to the businesses in which the companies are engaged, Exelon and PSEG believe, with the market concentration mitigation plan they have proposed, that completion of the Merger will not violate United States or applicable foreign antitrust laws.

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<sup>79</sup> See Exhibits D-8, D-9 and D-10 hereto.

<sup>80</sup> See Exhibit D-1 hereto.

The Merger may also be subject to review by the governmental authorities of various other jurisdictions under the antitrust laws of those jurisdictions.

#### Federal Communications Commission

The Federal Communications Commission ("FCC") must approve the transfer of control of telecommunications permits or licenses. The Communications Act of 1934 prohibits the transfer, assignment or disposal in any manner of any license, or any rights thereunder, to any person without authorization from the FCC. PSEG's subsidiaries hold telecommunications licenses and, together with the appropriate subsidiaries of Exelon, will seek the necessary approvals from the FCC for the assignment of or transfer of control over such licenses in connection with the Merger. Under the Communications Act, the FCC will approve a transfer of control if it serves the public interest, convenience, and necessity.

#### Private Letter Ruling of the Internal Revenue Service

United States Treasury Regulations generally provide for the nonrecognition of gain or loss for United States federal income tax purposes with respect to the transfer of certain decommissioning trust funds maintained by nuclear power plant owners in connection with the transfer of an interest in a nuclear power plant. The precise application of these Treasury Regulations in the context of the Merger, however, is not free from doubt. Therefore, Exelon and PSEG have agreed to seek a ruling from the Internal Revenue Service confirming that no gain or loss will be recognized for United States federal income tax purposes with respect to the transfer of PSEG's decommissioning trust funds as a result of the Merger.

Except as stated above, no state or federal regulatory agency other than the Commission under the Act has jurisdiction over the proposed Merger.

#### NJBPU Approval Regarding PSE&G Securities Issuances

The NJBPU has authority under N.J.S.A. 48:3-7, N.J.S.A. 48:3-9 and N.J.S.A. 14:1-5,9 to approve the issuance of securities by PSE&G. PSE&G, a New Jersey corporation, obtains approval from the NJBPU for all of its securities issuances, including both long-term and short-term debt securities. Its existing approvals include authority to issue up to \$750 million of short-term debt through January 2, 2007 (Order of Approval, Docket No. EF04101117 (December 2, 2004)). Further, PSE&G has authority to issue various long-term debt securities in an amount not to exceed \$525 million through December 31, 2005. (Order of Approval, Docket No. EF03121003 (April 28, 2004)). Accordingly, PSE&G is not seeking any approval from the Commission for the issuance of exempt securities, but will rely on Rule 52(a).

PSE&G has pending an application with the NJBPU seeking approval in connection with the issuance of up to \$150 million of securitization obligations under N.J.S.A. 48:3-57. If the application is approved, the NJBPU would authorize a transition bond charge which amounts would be sold by PSE&G to a special purpose Financing Subsidiary in connection with the securitization financing. Because PSE&G will be covered by the general authorizations applicable to the Exelon system approving formation and activities of Financing Subsidiaries and entering into servicing agreements at "market rates" in compliance with rating agency requirements, PSE&G will need no further approval from the Commission for the proposed \$150 million securitization financing.

#### **Item 5. Procedure.**

The Commission is respectfully requested to publish the requisite notice under Rule 23 with respect to this Application as soon as possible, such notice to specify a date by which comments must be entered and such date being the date when an order of the Commission granting and permitting this Application to become effective may be entered by the Commission. The Applicants request that the Commission's order be issued as soon as the rules allow, and that there should not be a 30-day waiting period between issuance of the Commission's order and the date on which the order is to become effective. The Applicants hereby waive a recommended decision by a hearing officer or any other responsible officer

of the Commission and consent that the Division of Investment Management may assist in the preparation of the Commission's decision and/or order, unless the Division opposes the matters proposed herein.

**Item 6. Exhibits And Financial Statements.**

A. Exhibits.

- A-1 Amended and Restated Articles of Incorporation of Exelon (incorporated by reference to Exhibit 3.1 to Exelon's Registration Statement on Form S-4, filed May 15, 2000 (File No. 333-37082))
- A-2 Amendment to Amended and Restated Articles of Incorporation of Exelon (incorporated by reference to Exhibit 3.1 to Exelon's Quarterly Report on Form 10-Q for the quarter ended June 30, 2004, filed July 28, 2004 (File No. 001-16169))
- A-3 Form of Amendment to Amended and Restated Articles of Incorporation of Exelon, (incorporated by reference to Exhibit 4.1 to Exelon's Registration Statement on Form S-4, filed February 10, 2005 (File No. 333-122074))
- B-1 Agreement and Plan of Merger between Exelon and PSEG, dated as of December 20, 2004 (incorporated by reference to Exhibit 2.1 to Current Report on Form 8-K, filed December 21, 2004 (File No. 001-16169))
- B-2 Exelon Indenture (incorporated by reference to Exhibit 4.1 to Exelon's Registration Statement on Form S-3, filed March 27, 2001 (File No. 333-57540))
- B-3 Exelon Generation Indenture (incorporated by reference to Exhibit 4.1 to Exelon's Registration Statement on Form S-4, filed April 4, 2002 (File No. 333-85496))
- B-4 Form of PSEG Mutual Services Agreement
- B-5 Description of Exelon Service Providers and existing agreements under State approved affiliated interest requirements (incorporated by reference to Exhibit B-3.3 to Exelon's Application on Form U-1, filed October 18, 2000 (File No. 70-09645))
- C Exelon's Registration Statement on Form S-4, filed February 10, 2005, including the Joint Proxy Statement and Prospectus of Exelon and PSEG (File No. 333-122074) (incorporated by reference)
- D-1 Joint Application of Exelon and PSEG to the FERC regarding Merger, filed February 4, 2005 (excluding exhibits and testimony, which Applicant will supply upon request of the Commission)
- D-2 Joint Petition of Exelon and PSE&G to the NJBPU for Approval of a Change in Control of PSE&G, and Related Authorizations, filed February 4, 2005 (excluding exhibits and testimony, which Applicants will supply upon request of the Commission)
- D-3 ComEd's Notice of Holding Company Merger to the ICC, filed February 4, 2005 (excluding exhibits and attachments, which Applicants will supply upon request of the Commission)
- D-4 Joint Application of PECO and PSE&G to PAPUC for Approval of the Merger of

- PSEG with and into Exelon, filed February 4, 2005 (excluding exhibits and testimony, which Applicants will supply upon request of the Commission)
- D-5 Joint Application of Exelon and PSEG with NJDEP for Letter of Non-Applicability under ISRA (to be filed by amendment)
  - D-6 Joint Application of Exelon and PSEG to NYPSC for Approval of Indirect Transfer of Ownership Interests (to be filed by amendment)
  - D-7 Joint Request of PSEG Power Connecticut, LLC and Exelon Corporation to CSC for Approval of Transfer of Certificate of Environmental Compatibility and Public Need, filed March 3, 2005 (excluding exhibits and testimony, which Applicants will supply upon request of the Commission)
  - D-8 Application of PSEG Nuclear LLC to NRC for Proposed License Transfer and Conforming License Amendments Relating to the Merger of PSEG and Exelon (excluding exhibits and testimony, which Applicants will supply upon request of the Commission)
  - D-9 Application of Exelon Generation to NRC for Approval of License Transfers (excluding exhibits and testimony, which Applicants will supply upon request of the Commission)
  - D-10 Application of AmerGen to NRC for Approval of Indirect License Transfers (excluding exhibits and testimony, which Applicants will supply upon request of the Commission)
  - E-1 Map of combined transmission systems of Exelon and PSEG (to be filed by amendment)
  - E-2 Map of combined gas service territory of Exelon and PSEG (to be filed by amendment)
  - F Opinions of counsel (to be filed by amendment)
  - G-1 Diagram of Exelon's Post-Merger Corporate Structure
  - G-2 Diagram of Existing Corporate Structure of Exelon System
  - G-3 Diagram of Existing Corporate Structure of PSEG System
  - G-4 List of Generation Facilities Subject to Divestiture
  - G-5 Description of all outstanding indebtedness and obligations of PSEG
  - G-6 Description of all inter-company guaranties in PSEG system
  - G-7 Analysis of Non-Utility Interests of PSEG
  - G-8 Analysis of the Economic Impact of a Divestiture of the Gas Operations of PECO Energy Company (incorporated by reference to Exhibit J-1 to Exelon's Application on Form U-1, filed March 16, 2000 (File No. 70-09645))
  - G-9 Analysis of the Economic Impact of a Divestiture of the Gas Operations of PECO and PSE&G (to be filed by amendment)
  - H Proposed Form of Notice

B. Financial Statements.

- FS-1 Consolidated Balance Sheet of Exelon as of December 31, 2004 (incorporated by reference to Exelon's Annual Report on Form 10-K for the year ended December 31, 2004, filed February 23, 2005 (File No. 1-16169))
- FS-2 Consolidated Statement of Income of Exelon for the year ended December 31, 2004 (incorporated by reference to Exelon's Annual Report on Form 10-K for the year ended December 31, 2004, filed February 23, 2005 (File No. 1-16169))
- FS-3 Consolidated Balance Sheet of PSEG as of December 31, 2004 (incorporated by reference to PSEG's Annual Report on Form 10-K for the year ended December 31, 2004, filed February 28, 2005 (File No. 1-09120))
- FS-4 Consolidated Statement of Operations of PSEG for the year ended December 31, 2004 (incorporated by reference to PSEG's Annual Report on Form 10-K for the year ended December 31, 2004, filed February 28, 2005 (File No. 1-09120))

**Item 7. Information as to Environmental Effects**

The proposed transaction involves neither a "major federal action" nor "significantly affects the quality of the human environment" as those terms are used in Section 102(2)(C) of the National Environmental Policy Act, 42 U.S.C. Sec. 4321 et seq. No federal agency is preparing an environmental impact statement with respect to this matter.

SIGNATURES

Pursuant to the requirements of the Public Utility Holding Company Act of 1935, each of the undersigned companies has duly caused this amended Application/Declaration to be signed on its behalf by the undersigned thereunto duly authorized.

Date: March 15, 2005

**Public Service Enterprise Group Incorporated**

**Public Service Electric and Gas Company\***  
**PSEG Power LLC\***  
**PSEG Energy Holdings LLC\***  
**PSEG Service Corporation**  
80 Park Plaza  
Newark, New Jersey 07102

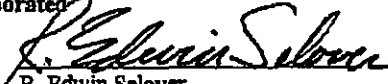
\* Including one or more subsidiaries

**Exelon Corporation**

**Commonwealth Edison Company\***  
**Exelon Energy Delivery Company, LLC\***  
**Exelon Business Services Company\***  
**Exelon Ventures, LLC\***  
10 South Dearborn Street  
37<sup>th</sup> Floor  
Chicago, Illinois 60603  
**PECO Energy Company\***  
2301 Market Street  
Philadelphia, Pennsylvania 19101  
**Exelon Generation Company, LLC\***  
300 Exelon Way  
Kennett Square, Pennsylvania 19348

\* Including one or more subsidiaries

By Public Service Enterprise Group  
Incorporated

By:   
Name: R. Edwin Selover  
Title: Senior Vice President and General  
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80 Park Plaza  
Newark, New Jersey 07102

By Exelon Corporation

By: \_\_\_\_\_  
Name: Elizabeth A. Moler  
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