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February 27, 2007

VIA HAND DELIVERY

James J. McNulty
Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor North
PO Box 3265
Harrisburg, PA 17105-3265

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RE: Application of Duquesne Light Company for a Certificate of Public Convenience Under Section 1102(a)(3) of the Public Utility Code Approving the Acquisition of Duquesne Light Holding, Inc. by Merger - Docket No. A-110150F0035

Application of DQE Communications Network Services LLC for a Certificate of Public Convenience Under Section 1102(a)(3) of the Public Utility Code Approving the Acquisition of Duquesne Light Holding, Inc. by Merger - Docket No. A-311233F0002

Dear Secretary McNulty:

Enclosed, for filing, are two copies of the testimony and exhibits of Duquesne Light Company, DQE Holdings LLC, Office of Trial Staff, Office of Consumer Advocate, Office of Small Business Advocate, Duquesne Industrial Intervenors, Community Action Association of Pennsylvania, Strategic Energy, LLC/Retail Energy Supply Association and Citizen Power, Inc. in the above-referenced proceeding. The testimony and exhibits are being filed pursuant to Administrative Law Judge Robert P. Meehan's Order dated February 21, 2007, which admits this testimony and exhibits into the record.

13

Application of Duquesne Light Company
and DQE Communications Network Services

Docket Nos. A-110150F0035 and
A-311233F0002

Rebuttal Testimony of Duquesne Light Company

January 10, 2007

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Docket Nos. A-110150F0035 and A-311233F0002

REBUTTAL TESTIMONY OF DUQUESNE LIGHT COMPANY

Statement No. 1-R	Rebuttal Testimony of Morgan K. O'Brien
Statement No. 2-R	Rebuttal Testimony of Christopher J. Leslie
Statement No. 3-R	Rebuttal Testimony of Joseph G. Sauvage
Statement No. 4-R	Rebuttal Testimony of Frederick J. Eichenmiller
Statement No. 5-R	Rebuttal Testimony of Susan S. Betta
Statement No. 6-R	Rebuttal Testimony of Neil S. Fisher
Statement No. 7-R	Rebuttal Testimony of Michele Sandoe

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SECRETARY'S BUREAU

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Docket No. A-110150F0035

Docket No. A-311233F0002

**Duquesne Light Company
DQE Communications Network Services, LLC**

Statement No. 1R

REBUTTAL TESTIMONY OF MORGAN K. O'BRIEN

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DUQUESNE LIGHT COMPANY
REBUTTAL TESTIMONY OF MORGAN K. O'BRIEN

Q. Please state your name and business affiliation.

A. My name is Morgan K. O'Brien. I am President and Chief Executive Officer of Duquesne Light Company ("Duquesne Light").

Q. Did you previously submit direct testimony in this proceeding?

A. Yes. My direct testimony was submitted along with Duquesne Light's filing on September 6, 2006.

Q. What is the purpose of your rebuttal testimony?

A. I will respond to issues raised by various parties in their testimony by explaining:

- the reasons for Duquesne Light's decision to seek a strategic partner;
- why the Macquarie Consortium was selected as a strategic partner;
- the substantial benefits this transaction provides to Duquesne Light, its customers and the Pittsburgh region; and
- the reasons that certain conditions proposed by the Parties are unnecessary, unreasonable and unacceptable.

Q. Please summarize the key points of your rebuttal testimony.

A. Several parties contend *e.g.*, OCA, OTS and Citizen Power, that the merger of Duquesne Light Holdings, Inc. ("DLH") and DQE Holdings LLC ("DQE") will not produce substantial affirmative benefits. In particular, they argue that maintaining the headquarters, a management team and operations of Duquesne Light in Pittsburgh is not an affirmative benefit. This conclusion ignores the economic challenges facing the Pittsburgh region as well as the rapidly consolidating electric utility industry and the particularly vulnerable position of DLH and its principal subsidiary Duquesne Light. This merger, by maintaining management and operations in Pittsburgh, avoids the types

1 of significant job loss and loss of customer and community interaction that often occur
2 when a local utility is acquired by a multi-state utility operating company. I also will
3 explain why many of the conditions proposed by the Parties are based on erroneous
4 premises or assumptions about the merger, particularly as they relate to customer service
5 and reliability. Finally, I will address the purpose and affirmative benefits of our
6 proposed shareholder-funded economic development program.

7 **Q. What is the proper role of the DLH Board and the senior management team when**
8 **considering the major strategic issues facing the company?**

9 A. Duquesne Light's senior management team and DLH Board must anticipate the forces
10 that are driving change, both within the business and external to the business, and then
11 make decisions that are best for Duquesne Light's customers, communities, employees
12 and shareholders. In this regard, two key points should be emphasized. First, we need to
13 anticipate change, not just react to changes after they occur. Second, we need to consider
14 customer, employee, and community interests, not just shareholder interests.

15 **Q. Do the Parties properly recognize the need to anticipate change and act**
16 **accordingly?**

17 A. No, they do not. For example, some of the parties seem to argue that the decision to
18 undertake this transaction and thereby keep Duquesne Light in Pittsburgh can never be an
19 affirmative benefit because it simply preserves the status quo. I simply do not agree with
20 that position. Anticipating a threat to something of value – in this case a corporation that
21 is a major employer and contributor to the business and civic life of our community – and
22 taking steps to preserve that value constitutes a very real and substantial affirmative
23 benefit.

24 **Q. What external factors did the DLH Board consider when deciding to merge with**
25 **Macquarie?**

1 A. A number of general factors were considered, but two were of paramount importance.

2 First, the repeal of PUHCA in 2005 opened the door to accelerated consolidation within
3 the electric utility industry. Specifically, the repeal of PUHCA:

- 4 • Significantly reduced the regulatory impediments to multi-state utility systems
5 by eliminating, among other things, the requirement that utilities have
6 contiguous service areas; and
- 7 • Promoted consolidation of smaller utilities like Duquesne Light with other
8 larger utilities which have greater economies of scale and global capital
9 access.

10 Second, as I noted in my direct testimony, equity analysts believed that Duquesne Light
11 was an acquisition target due to its relatively small size and projected financial
12 performance. Specifically, we were concerned that a decline in DLH stock price in
13 relation to the underlying value of the shares made the company an acquisition target.

14 **Q. What internal factors did the DLH Board consider when deciding to merge with the**
15 **Macquarie Consortium?**

16 A. The primary internal factor was DLH's inability, on a going forward basis, to grow and
17 even sustain earnings per share, dividends, and share price. We undertook our "Back to
18 Basics" strategy to reduce business risk and to focus our capital and management
19 resources on our core electric business. Our customers have benefited through
20 infrastructure investments and improved reliability. However, one result of that strategy
21 has been to narrow and sharpen our business focus through disposal of unrelated
22 businesses, thereby narrowing the company's ability to generate earnings per share
23 growth, and placing pressure on the dividend and share price. As a focused electric
24 distribution company, the only growth opportunities are through expanding your service
25 territory by acquiring another electric distribution company or increasing the distribution
26 margin from your current customer base. The former is limited by your ability to access
27 capital as well as finding an electric distribution business which is willing to combine

1 their operations with yours. The latter is limited by how much capital you can put to
2 work within your service territory and by how much efficiency can be achieved without
3 impacting customer reliability and service.

4 **Q. Mr. O'Brien, please explain how these external and internal factors were evaluated**
5 **by the Board.**

6 A. As the President and CEO of Duquesne Light, I and my senior management team
7 continually evaluate Duquesne Light's current position in the industry, anticipate
8 emerging trends and then make decisions and recommendations to the DLH Board that
9 we believe are best for the customers, communities, employees, and shareholders we
10 serve.

11 Over the past several years, in response to the current competitive electric and
12 financial market environments, Duquesne Light determined that it would return to its
13 historic core business of being a utility company. This led to adoption of the "Back to
14 Basics" strategy described in my direct testimony. As a result, Duquesne Light divested
15 several non-core businesses and resolved a number of important legacy issues. These
16 actions reduced our business risk and further enhanced customer satisfaction and
17 shareholder value. However, as this process proceeded and the utility landscape changed,
18 we determined that it was not in our best interest for Duquesne Light to remain
19 independent.

20 As a result of these events, we concluded and the DLH Board concurred, that
21 Duquesne Light should consider aligning itself with a solid strategic partner like the
22 Macquarie Consortium, to secure Duquesne Light's financial future while at the same
23 time preserving our position as a Pittsburgh-based public utility.

24 **Q. Can you provide any more specific information regarding this analysis?**

1 A. Yes. As a result of the factors discussed above, Duquesne Light faced challenges in
2 maintaining current earnings levels and faced significant risks in funding future
3 investments which could provide for future earnings growth. In this regard, in response
4 to OCA Set I-31, we provided confidential information, presented to our Board, which
5 indicated that there were scenarios which DLH could face a potential dividend cut in the
6 future. The market for our stock also had a very negative outlook, as evidenced by the
7 fact that as of this past summer, approximately 12.7% of DLH's stock was sold "short,"
8 indicating that many investors expected a further decline in the stock price. As stated by
9 Mr. Joseph Sauvage of Lehman Brothers in his rebuttal testimony in this proceeding, the
10 percentage of DQE's outstanding shares sold "short" substantially exceeded the utility
11 average of 2.7%. The prospect of a dividend reduction was particularly troubling,
12 because of the resulting harm to Duquesne Light and its customers. A DLH dividend cut
13 would almost certainly have led to a substantial decline in the DLH stock price and could
14 have increased its existing vulnerability as a takeover target for other regional operating
15 companies. My direct testimony referenced a February 14, 2006 JP Morgan analysis,
16 which stated that DLH may be a perceived as an acquisition target, but noted that DLH's
17 current price level of \$17.51 made such an acquisition unlikely. However, between the
18 time of the JP Morgan analysis and announcement of the merger, DLH's stock price had
19 declined to \$15.67/share. Any additional downward pressure on our stock price, such as
20 a cut in its dividend, would have only further increased the likelihood of Duquesne Light
21 being acquired by another utility.
22
23

1 Q. **Did the DLH Board take all of these factors into consideration when weighing the**
2 **offer from the Macquarie Consortium?**

3 A. Yes. The DLH Board reviewed and considered a broad range of strategic alternatives
4 and through this process it became evident that in order to ensure that Duquesne Light
5 was able to continue to access capital on reasonable terms going forward and to remain a
6 Pittsburgh based utility, a strategic partner would be critical.

7 Q. **Why should the Commission be concerned about the possible acquisition of**
8 **Duquesne Light by a third party?**

9 A. Given the pressures for consolidation within the industry, the most likely acquirer would
10 be another electric utility. We do not, however, believe that selling Duquesne Light to
11 another utility would be in the best interest of our customers, our employees, or for
12 Pittsburgh.

13 As to the impact on our customers, Duquesne Light provides high quality service
14 to its customers. It achieves its service levels because of the quality of its business
15 processes and the dedication of its employees. To generate savings to produce returns
16 necessary to support a strategic acquisition, an electric utility acquiring DLH would bring
17 its own processes and systems to Duquesne Light. The exercise of combining the
18 processes and systems of two different companies, even though they are in the same
19 business, would place service levels at risk. I note that the proposed merger with
20 Macquarie will not have the effects that would be expected from an acquisition by a
21 typical regional operating company. While we will continue to seek to streamline and
22 make our operations more productive, we will not lose local management and employee
23 control over these operations.

24 As to the impact on Pittsburgh, loss of a corporate headquarters means that there
25 are fewer people to lead and support the institutions that contribute to the business, civic,

1 and cultural life of a metropolitan region. As those institutions are weakened, the
2 benefits that these institutions provide to people at all income levels decline. This would
3 impact Duquesne Light's low income customers by depleting the regions social agencies
4 of the Duquesne Light resources, namely its employees, which help fund and manage
5 many of these agencies as board members and volunteers. On a broader scale,
6 community events like Light Up Night, the Three Rivers Arts Festival, the Home and
7 Garden show and other Pittsburgh community events and traditions would be negatively
8 impacted by the loss of Duquesne Light's support both financially as well as the planning
9 and organizational resources that it provides for these types of events on an annual basis.

10 **Q. Do you agree with the assertion by other parties that maintaining the status quo**
11 **does not provide substantial affirmative benefits?**

12 A. No, I do not. Arguments that this transaction merely maintains the status quo simply
13 ignore the changing landscape of the utility business in the U.S. that I noted above.
14 Admittedly, this transaction does not fit the mold of the typical horizontal and/or strategic
15 merger. Past mergers often have presented the opportunity for significant "synergy"
16 savings, and the parties to those proceedings have requested that significant amounts of
17 these potential savings be allocated to customers. However, what is apparently forgotten
18 by the Parties in this proceeding is that such synergy savings come at a cost. Specifically,
19 in merger proceedings that involve two operating utilities, synergy savings are based on
20 the efficiencies to be realized by the consolidation of two companies. These
21 "efficiencies" typically result in a significant loss of jobs, the replacement and/or
22 relocation of senior management and the acquired company being subsumed into the
23 larger holding company corporate structure of a multi-state utility with a resulting loss of
24 local connection to the service territory. I believe there are a number of real examples of

1 utilities whose headquarters have left Pennsylvania to another state and whose
2 communities have been negatively impacted in a number of ways by those departures.
3 The Pittsburgh community still feels the loss of the CNG corporate headquarters when it
4 was acquired by Dominion, a Virginia headquartered company. Symbolic of that
5 significant loss to this community is the former CNG corporate headquarters, one of the
6 newest buildings in downtown Pittsburgh, sitting nearly vacant in the middle of the city.
7 CNG was a corporate citizen whose executives and employees were involved with
8 nearly all the same agencies and organizations that Duquesne Light is today. Those
9 vacancies by the CNG executives and employees were never replaced by Dominion. And
10 today, each of those local agencies and organizations have fewer resources than they did
11 before that transaction occurred.

12 As stated in our Application and supporting testimony, the value of retaining
13 Duquesne Light as a "local" public utility cannot be understated and without question
14 provides Duquesne Light, its customers and the communities we serve with a substantial
15 affirmative benefit. If Duquesne Light were to be acquired by another operating utility,
16 the adverse consequences to the Pittsburgh region would be profound, including reduced
17 employment opportunities, both at entry level (call center, administrative services), and at
18 middle and senior management levels. Further, the loss of a locally based electric utility
19 would likely result in reducing the leadership available to guide local non-profit
20 organizations important to region's quality of life as well as the loss of the company's
21 leadership position in regional economic development.

22 **Q. While the proposed transaction may not provide the synergy savings typically**
23 **identified in merger proceedings, will it still provide substantial affirmative**
24 **benefits?**

25 **A.** Without question. While this transaction is somewhat different from past merger

1 proceedings, it fully satisfies the affirmative benefits test used in Pennsylvania to
2 evaluate merger transactions. Specifically, the proposed merger between DHL and DQE
3 provides the following benefits:

- 4 • It retains Duquesne Light as a Pittsburgh-based operating utility that will continue
5 to provide safe, reliable and efficient utility service to the Pittsburgh region.
- 6 • It is consistent with recent Pennsylvania Public Utility Commission decisions that
7 have recognized the significant benefits of Pennsylvania-based utility operations
8 and job retention. The proposed transaction avoids the type of job losses and
9 relocation of senior management that are typical in more "traditional" mergers
10 which will sustain the benefits to the Pittsburgh region that Duquesne Light now
11 provides such as:
 - 12 ○ Employment opportunities at all levels
 - 13 ○ Contributions to the region in terms of charitable dollars and leadership
- 14 • While certain members of the Macquarie Consortium reside outside of the U.S.,
15 DQE, DLH and Duquesne Light will continue to be U.S. companies.
- 16 • The Macquarie Consortium represents a strategic partner that is making a long-
17 term investment in a well-run and well-maintained, stable business. It does not
18 seek to interfere with the day-to-day operation of an electric distribution
19 company. As a result, the job of operating Duquesne Light, providing continuous
20 and efficient utility service to our customers and maintaining an active role as a
21 good corporate citizen, will continue to rest with me, my senior management team
22 and the hard working employees at Duquesne Light.

23 **Q. Are there other benefits to be realized by the approval of the proposed transaction?**

24 **A.** Yes. The transaction will: (1) increase Duquesne Light's access to a greater amount of

1 capital on more reasonable terms; (2) provide the Duquesne Light senior management
2 team the opportunity to access best practices used by other utilities and infrastructure
3 companies affiliated with Macquarie Consortium and Macquarie Bank; and (3) provide
4 our service area with an economic development program aimed at meeting a critical
5 regional need to attract new business and encourage the expansion of existing businesses.

6 **Q. Mr. Kahal contends that the benefits of increased access to capital have not been**
7 **demonstrated. Do you agree?**

8 A. No. Absent approval of the proposed transaction, it is not clear that DLH and Duquesne
9 Light can continue to raise equity on reasonable terms given the business risks facing the
10 Company which I discussed above. This transaction will provide DLH and Duquesne
11 Light with a stable equity base provided by a group of investors who want to continue to
12 invest more equity as it is needed in the future. Those investments will be judged based
13 upon the ability to produce long-term cash flows coincident with the life of the assets to
14 be constructed, and not based primarily on quarterly or annual earnings estimates. This
15 stable equity base coupled with the Macquarie Consortium's access to global debt
16 markets will significantly improve Duquesne Light's liability to fund further capital
17 expenditures. This is clearly an affirmative benefit from the transaction.

18 Duquesne Light has historically been able to access capital markets to finance
19 capital projects, but this access is no longer assured. In today's consolidating utility
20 industry, Duquesne Light is rapidly moving from a mid-sized regional utility to a smaller
21 local utility. This reality will adversely affect our ability to access capital markets on
22 reasonable terms. Absent approval of the proposed transaction, Duquesne Light's cost of
23 capital will clearly increase to the detriment of customers. Specifically, the cost of
24 capital for companies the size of Duquesne Light clearly includes a small company

1 premium. The cost of this premium would inevitably result in higher rates to customers.

2 **Q. Can you elaborate on the potential benefits?**

3 A. This transaction, among other things, is designed to remedy Duquesne Light's access to
4 capital, and the results already are apparent. For example, two members of the
5 Macquarie Consortium have already invested \$141 million in newly issued DLH equity,
6 which paved the way for the acquisition of a minority interest in Keystone and
7 Conemaugh generation stations.

8 **Q. Mr. Kahal argues that the Petitioners have not substantiated the benefits associated**
9 **with the best practices available through Macquarie Consortium. Do you agree?**

10 A. No. Mr. Kahal's argument presumes that the proposed transaction should be evaluated as
11 if it were a merger among operating utilities with a plan to consolidate operational
12 processes. This is not an accurate evaluation of the transaction. Macquarie does not plan
13 to combine Duquesne Light's operational processes with those of any other utility.
14 Instead, Duquesne Light's future association with the utilities affiliated with other
15 members of the Macquarie Consortium will provide our management with access to the
16 processes that they use, and vice-versa. This exchange of processes will add value to
17 Duquesne Light, but will not place service delivery at risk. Accordingly, this represents a
18 substantial affirmative benefit.

19 **Q. Would you like to address some of the recommended conditions Parties have**
20 **requested the Commission adopt prior to approving the proposed transaction?**

21 A. Yes. For the reasons set forth above the transaction, as proposed, clearly provides
22 affirmative benefits to customers. However, DLH and Duquesne Light are willing to
23 respond to reasonable concerns raised by other parties with constructive and workable
24 solutions. We provide a list of the specific commitments in my attached Exhibit MKO-2.

1 However, in some circumstances the parties have recommended conditions that are
2 unacceptable to DLH and Duquesne Light.

3 **Q. Some Parties have raised concerns about the proposed economic development**
4 **program. Are these concerns valid?**

5 A. In its testimony, RESA states that the proposed economic development program would
6 require eligible commercial and industrial customers to take at least the discounted
7 portion of their generation service from Duquesne, thus impeding customer choice. To
8 address the concerns raised by RESA, this program will be implemented in a
9 competitively neutral fashion. That is, eligibility for participation in the Economic
10 Development Program will not be contingent upon the customer purchasing energy from
11 either Duquesne Light or Duquesne Light Energy. This will enable customers to realize
12 the benefits to be garnered from the Economic Development Program regardless of their
13 retail electric supplier ensures that this program benefits our customers while not placing
14 any retail electric supplier at a competitive disadvantage.

15 **Q. OCA Witness Kahal suggests that the proposed corporate governance structure of**
16 **DLH raises concerns and recommends changes to this structure. Do you agree?**
17

18 A. No, I do not. As set forth in my Exhibit No. MKO-3, which provides our interrogatory
19 response to OCA Set III-16, DLH and its subsidiaries, including Duquesne Light, will be
20 owned by DQE which will be governed by its Board of Directors (the "Board"). The
21 Board will consist of the six investors constituting the Macquarie Consortium along with
22 myself as CEO of DLH and Duquesne Light. This Board will be supported by the
23 Management Committee¹ which includes representatives of the three largest investors
24 and the DLH senior management team. The Management Committee is the primary

¹ The Management Committee will be chaired by the Chief Executive Officer of Duquesne Light. Other members will include key members of the senior management team of Duquesne Light and representatives of the three members of the Consortium with the largest interest (DUET, MIP, and IFM).

1 forum for the senior management team and certain Consortium representatives to discuss
2 substantive matters facing the business as well as to assess progress against previously
3 agreed to business plans. The Management Committee will meet monthly and report and
4 make recommendations to the Board.

5 The Management Committee's specific responsibilities will be as follows:

- 6 • Provide input to management in connection with its preparation of the
7 annual operating and capital budgets and long-term business plans.
- 8 • Review performance against business plans and budgets.
- 9 • Review the financial statements prior to submission to the Board for
10 formal approval.
- 11 • Review management accounts and performance reports prior to
12 submission to the Board.
- 13 • Evaluate and implement compliance and risk mitigation measures.
- 14 • Oversee regulatory strategy.
- 15 • Review management initiatives.

16 Because the senior management team of Duquesne Light, as well as myself, live
17 in the Pittsburgh region, this structure ensures that an important community perspective
18 will be represented when the Board and the Management Committee deliberate the major
19 issues facing Duquesne Light and the affiliated companies in the group.

20 I should also note that I have received and executed a contract to remain as CEO
21 of DLH and Duquesne Light. In that role, I will participate in all decisions affecting
22 Duquesne Light, including approval of business plans, capital expenditure plans,
23 regulatory actions, and other actions affecting the future of the business and the quality of

1 service rendered by Duquesne Light. Another important benefit of the transaction is the
2 maintenance of the senior management team and corporate headquarters of Duquesne
3 Light in Pittsburgh.

4 In addition, the senior management team of Duquesne Light will remain in
5 Pittsburgh, will provide input to the Board via the Management Committee, and will be
6 responsible for implementing the business plans and providing the necessary levels of
7 service. These individuals will have direct management authority over the business and
8 will continue to control the allocation of resources within the business. The senior
9 management team and the employees that report to them currently are the primary
10 contact with customers and the community. The senior management team and their
11 employees will continue to be active participants in the communities in Duquesne Light's
12 service territory and thereby will have first hand knowledge of the needs of the customers
13 and communities we serve.

14 Retaining Duquesne Light and its operations in the Pittsburgh region also secures
15 one of the region's leading corporate citizens. Duquesne Light and its employees are
16 committed community partners supporting a wide array of community activities designed
17 to strengthen the economic and cultural vitality of its service territory. In 2005, Duquesne
18 Light's employees provided 5,797 person hours of voluntary service.

19 **Q. Please respond to Mr. Kahal's recommendation that the DQE Board be expanded to**
20 **include four outside directors and that at least two these outside directors reside in**
21 **the Duquesne Light service area?**

22 **A.** While I appreciate and share the Office of Consumer Advocate's interest in making sure
23 that the needs and interests of the local community continue to be considered by the
24 Board after approval of the merger, Mr. Kahal's specific recommendation is unnecessary
25 and inappropriate.

1 As noted above, the DLH Board's decision to select the Macquarie Consortium as
2 its strategic partner was based, in part, on its determination to keep Duquesne Light as a
3 locally based and operated utility. However, the proposed Board of DLH will properly
4 be comprised of members of the Macquarie Consortium as they will become the sole
5 shareholders of DLH. This is fully consistent with the board composition of other
6 privately-owned companies.

7 However, the Macquarie Consortium is acutely aware of the importance of
8 maintaining a strong local connection in the footprint of the regulated entities that it
9 acquires both in assessing operational decisions as well as serving as a strong corporate
10 citizen. To that end, as the President and CEO of Duquesne Light and a resident of
11 Pittsburgh, I will serve as a voting member of the Board and will ensure that the Board is
12 cognizant of all relevant matters of import to Pittsburgh and its surrounding communities.
13 I believe that having the CEO and the senior management team in Pittsburgh is critical to
14 the impact the company has in the community. But even more important than location is
15 having a CEO and senior management team who are committed to the region and
16 engaged in its development. As an example, I would note that my predecessor as CEO
17 was located in Pittsburgh and worked with a board of directors who were mainly business
18 people from the Pittsburgh area. This CEO convinced the board to move the company's
19 headquarters from Pittsburgh and also convinced the board it was in the company's best
20 interest to be less involved in the Pittsburgh community. This was a key strategic
21 decision the company adopted following the divestiture of its generation assets and its
22 subsequent diversification into the water and propane businesses. As a committed
23 Pittsburgher, my team subsequently convinced this board to re-engage ourselves with the

1 Pittsburgh community as a critical part of our Back to Basics strategy.

2 Duquesne Light and its employees have become an integral part of the
3 communities in which we serve and will continue in this role after this transaction is
4 approved. It is through Duquesne Light and its employees that the interests of our
5 customers and our communities will be communicated to the Board. Expanding the
6 Board to include local Pittsburgh business people and the costs associated with such an
7 expansion are unnecessary to protect the company's local commitment and therefore
8 should not be adopted.

9 **Q. Mr. Kahal suggests that there is a significant risk that the proposed transaction may**
10 **result in the loss of Duquesne Light personnel to other ventures of the Macquarie**
11 **Consortium. Do you agree that this is a legitimate concern?**

12 A. No, I do not. As I mentioned previously, one of the substantial affirmative benefits of
13 this transaction is maintaining Duquesne Light as a locally based and operated utility.
14 The concern raised by Mr. Kahal is not relevant to this proposed transaction. As set forth
15 in Mr. Leslie's rebuttal testimony, the Macquarie Consortium does not believe that it is
16 beneficial to run infrastructure business like Duquesne Light with an externally located
17 management team. For this reason, the Macquarie Consortium seeks businesses that have
18 strong, locally based management teams and retains them. Therefore, as Duquesne Light
19 will continue to be headquartered in Pittsburgh and operated by a Pittsburgh based
20 senior management team as it is today, a key personnel retention plan is unnecessary.

21 **Q. The OSBA is concerned that Duquesne Light has not committed to completing its**
22 **Infrastructure Improvement Program. Will Duquesne Light make such a**
23 **commitment?**

24 A. Yes. We have worked diligently over the past several years to ensure that Duquesne
25 Light continues to provide the levels of service and reliability that our customers have
26 come to expect by making significant capital investment in our transmission and

1 distribution system. Our commitment to provide high quality service to our customers
2 will remain after approval of this transaction, and we will commit to complete our \$530
3 million distribution and transmission infrastructure improvement plan for 2005-2007.

4 We have completed approximately \$377 million as of December 31, 2006, and the
5 remainder will be completed by the end of 2007.

6 **Q. Witnesses for the OCA and OSBA recommend that the Commission condition its**
7 **approval of the merger upon Duquesne Light's acceptance of specific performance**
8 **standards related to reliability and customer service quality. Do you have any**
9 **comments on these proposals?**

10 **A.** Yes, I do. As part of Duquesne Light's "Back to Basics" strategy, we have made
11 significant investments in our existing infrastructure and in new technologies to enhance
12 the service we provide to our customers. These investments have resulted in Duquesne
13 Light becoming one of the best performing utilities in Pennsylvania in both customer
14 service quality and providing reliable service. We are extremely proud of the work of our
15 employees to translate these investments into providing exceptional service to our
16 customers.

17 Duquesne Light's successes in these areas are demonstrated, in part, through the
18 existing Commission reporting requirements as to reliability and customer service
19 quality. The Commission has set via regulation, individual reliability performance
20 benchmarks and standards for all Pennsylvania electric distribution companies ("EDC").
21 These regulations ensure that the Commission is able to monitor each EDC's service
22 reliability annually and to compare it to past historic performance. While the
23 Commission does not have regulations relative to these issues, public utilities like
24 Duquesne Light report regularly to the Commission's Bureau of Consumer Services
25 which reviews our performance and reports on them annually. The Commission's 2005

1 Reliability Report supports Duquesne Light's successful "Back to Basics" strategy.
2 Indeed, Ms. Alexander acknowledges that "Duquesne Light's reliability and service
3 quality performance ranks among the highest level of all Pennsylvania EDCs in most
4 categories." OCA St. 2, p. 18, ln. 16-17.

5 As I stated in my Direct Testimony, Duquesne Light is a well-run public utility
6 and as noted by Ms. Alexander, our customer service is at the highest levels in
7 Pennsylvania. While Duquesne Light and the Macquarie Consortium are committed to
8 continuing to provide excellent service, to use our current performance levels as a
9 baseline with a financial penalty for any decline is unnecessary and would penalize
10 Duquesne Light for its past exemplary service. I also must take issue with Ms.
11 Alexander's assertion that our level of performance may decline due to the merger with
12 Macquarie. Duquesne Light sought a strategic partner like the Macquarie Consortium so
13 that its customers would continue to receive service from a local EDC whose employees
14 are committed to those we serve.

15 **Q. Do you agree with the assertions of Ms. Alexander that absent service compensation**
16 **dollars, Duquesne Light will not have an incentive to avoid deterioration in service**
17 **due to the merger?**

18 **A.** No, I do not. Again, Duquesne Light sought a strategic partner like the Macquarie
19 Consortium to ensure that Pittsburgh would continue to receive service from a local EDC
20 that is committed to those we serve. To my knowledge, no other utility in Pennsylvania
21 is currently required to pay customers for a reduction in performance levels. It is clearly
22 inappropriate to impose such a condition on DLC, particularly where our service is better
23 than most other Pennsylvania EDCs.

24 **Q. Some parties question the lack of identified "best practices" in the Application, is**
25 **that concern warranted?**

1 A. No, as Ms. Alexander points out, Duquesne Light currently provides extremely high
2 levels of service. There is always room for improvement, but it should not be a concern
3 that we have not yet identified how to improve on our existing high level of service. As
4 noted above, Duquesne Light has already benefited from the Macquarie Consortium's
5 ability to access capital in the investment relative to Keystone and Conemaugh.
6 However, identifying and implementing "best practices" in other areas of our business
7 will obviously require more study and analysis. Any "best practices" identified in this
8 area are more likely to be seen as we proceed to new initiatives and as technology
9 improves. Requiring Duquesne Light to specifically identify "best practices" now is
10 unrealistic and, based on our existing service levels, unwarranted.

11 **Q. Witnesses for the OCA and OSBA have stated that the Commission should require**
12 **that Duquesne Light agree to refrain from seeking a distribution rate increase for**
13 **specified time periods. Do you agree?**

14 A. Again, in my opinion the transaction as proposed provides substantial affirmative benefits
15 to merit its approval absent any conditions. However, Duquesne Light is willing to
16 accept a provision that there would be no further distribution rate increase for a two-year
17 period ending December 31, 2008, recognizing the lack of the typical synergy savings in
18 this transaction and as a sign of our obligation to continue to provide high levels of
19 service.

20 **Q. Mr. O'Brien, is Duquesne Light willing to accept Mr. Kahal's recommendation that**
21 **Duquesne Light provide periodic reporting on the status of the merger?**

22 A. I do not believe that additional reporting is necessary beyond our existing Commission
23 reporting requirements. However, should the Commission deem additional reporting be
24 necessary to monitor the merger, Duquesne Light will submit such reports.

25 **Q. Is Duquesne Light willing to accept Ms. Alexander's recommendation that the**
26 **Commission require Duquesne Light to fund the five new Stay Warm Programs**

1 identified in Duquesne Light's recent base rate case for the period of the
2 distribution rate increase stay out period.

3 A. In part. As noted above, Duquesne Light is willing to agree to not seek a distribution rate
4 increase that would become effective after full suspension before December 31, 2008.

5 Further, as explained in the rebuttal testimony of Michele Sandoe, Duquesne Light will
6 confirm its long-term commitment to universal service programs, including the
7 continuation of Stay Warm Programs, as needed.

8 **Q. Mr. O'Brien, is Duquesne Light willing to accept the OCA recommendation that**
9 **Duquesne Light be required not to seek to recover the transaction costs and**
10 **premium associated with merger via state distribution or FERC transmission rates**
11 **and agree not to seek recovery of any increase in the Pennsylvania Capital Stock**
12 **Tax resulting from the Merger?**

13 As noted in Mr. Leslie's testimony, Duquesne Light will commit to exclude from
14 distribution rates any costs directly associated with the proposed transaction and will not
15 seek to recover any increase in its Capital Stock Tax obligations resulting solely from the
16 Merger. However, we do not believe that it is appropriate to condition the proposed
17 transaction with an exclusion of costs that may be properly recovered by Duquesne Light
18 in its FERC jurisdictional rates.

19 **Q. Mr. O'Brien would you like to offer any closing observations?**

20 A. Yes. The DLH Board and the senior management team are continually evaluating our
21 operations to identify means by which to improve our operational and financial status and
22 to continue to improve service to our customers and the communities we serve. This
23 evaluation resulted in our successful "Back to Basics" strategy which has yielded
24 significant benefits. The "Back to Basics" strategy required that the DLH Board and
25 senior management team to view ourselves with a critical eye inward at our current
26 operations and processes as well as to identify where we stand amongst the other utilities
27 in our region. While this strategy has been successful, external changes made it clear to

1 us that proactive measures were required to maintain our position as the hometown
2 electric distribution company of Pittsburgh and surrounding communities.

3 The Merger with the Macquarie Consortium benefits our customers by
4 maintaining our local senior management team and dedicated employees, while at the
5 same time, providing us substantially improved access to capital to provide the service
6 our customers need and expect. In my opinion, the Commission should consider these
7 important matters and benefits when reviewing this Merger. We submit that this Merger
8 is a vital, proactive step by Duquesne Light that will result in significant benefits for
9 Duquesne Light, its customers and the communities we serve. The transaction will
10 maintain our operations and our employees in Pittsburgh. In addition, this Merger will
11 provide Duquesne Light with owners that are committed to its operational and financial
12 success over the long-term and with capital to ensure that we are successful in our
13 continuing to provide Pittsburgh and the surrounding communities with safe, reliable and
14 efficient electric service.

Universal Service

1. Duquesne will convene a collaborative of local representatives of low income groups, community based organizations and the Office of Consumer Advocate to discuss proposed changes to universal service programs within current funding levels. The collaborative will include a representative of CAAP and a representative from the Pennsylvania weatherization network providers.

2. Duquesne will increase the number of customers served under its Smart Comfort (LIURP) program from 2,250 customers per year to 3,000 customers per year and, on approval from the Commission's Bureau of Consumer Services, target the additional 750 visits to customers with incomes between 150% and 200% of the federal poverty level.

Service Quality and Reliability

For the reasons expressed in the testimony of Mr. Eichenmiller, Duquesne Light does not believe that additional service quality and reliability standards are necessary. However, if the Commission deems additional standards to be necessary to monitor changes in service:

1. Duquesne Light will provide a report to the Commission if in a one year calendar period of 2007-2009 its SAIFI and SAIDI metrics both fall below the three year standards established by the Commission of 1.29 and 153, respectively. The report will identify the reasons for the variance and identify any management actions Duquesne Light intends to undertake.

2. Duquesne Light will also provide a report to the Commission if, in any calendar year period of 2007-2009:

- The percent calls answered within 30 seconds falls below 75%;
- The average busy out rate is above 2%; or
- The average call abandonment rate is above 4%.

The report will identify the reasons for the variance and identify any management actions Duquesne Light intends to undertake.

Economic Development Program

Duquesne Light will establish a competitively neutral economic development program to attract and support expanding Pennsylvania industrial employers by offering a flat 50 MW block (7 days by 24 hours) of energy consumed at the new facility at a \$3 per MWh discount below market to commercial/industrial customers on Schedules HVPS and L that intend to add new load or that expand their existing load by at least 10 MW and create two new full time employment positions per MW of new load. To accomplish competitive neutrality, Duquesne Light will not condition the discount upon the customer's obtaining energy under the provider of last resort service or purchase of energy from an affiliate of Duquesne Light.

Reporting

Should the Commission deem additional reporting be necessary to monitor the merger, Duquesne Light will submit annual reports on the merger during the distribution rate stay-out period.

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RESPONSES TO OFFICE OF CONSUMER ADVOCATE SET III

16 At page 10 of Mr. Leslie's testimony he states that the Board of Directors of DQE Holdings will be the six representatives from the Macquarie funds:

- (a) Please confirm that this is the intended governance structure;
- (b) Does this mean that no current director or manager of Duquesne Light or Duquesne Holdings will be a Director of DQE Holdings? If so, please explain why this is appropriate, given that "the sole purpose [of this Board] is to supervise the operations of DLH and Duquesne Light." (Leslie, page 11)

RESPONSE:

DQE Holdings LLC ("Holdings") and its subsidiaries will be governed through:

- The board of directors of Holdings LLC (the "Board"),
- A management committee consisting of senior management of DLC, certain representatives of the Members of the Consortium, and the Asset Manager (the "Management Committee"),
- The audit committee of Holdings and its subsidiaries ("Audit Committee"),
- The Chief Executive Officer of Holdings and its subsidiaries along with the senior management of such companies, and
- One person who will support the financial reporting activities and otherwise assist the Management Committee (the "Asset Manager").

This structure will provide Holdings LLC and DLC with access to substantial expertise in utility management, a global management perspective, and knowledge of the local circumstances and markets facing DLC. The structure also appropriately balances the interests among the customers and communities served by DLC and its shareholders.

The Board

The Board will provide strategic direction for DQE Holdings LLC and its subsidiaries and will fulfill the legal requirements of the boards all of the subsidiaries of Holdings, including DLC. Accordingly, the Board will perform the following functions:

- review and approve long term business plans,
- review and approve annual capital and operating budgets,
- review and approve financial statements,
- establish accounting, financial reporting and internal control policies,
- Appoint the independent auditor,

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- establish risk management policies, and
- review and approve transactions outside the normal course of business of Holdings and its subsidiaries, such as material acquisitions, divestitures, financings, etc.

The Board shall also appoint, evaluate and compensate the Chief Executive Officer and Chief Financial Officer. The Chief Executive Officer shall report to the Board and the Chief Financial Officer shall report to the Chief Executive Officer.

The Board will meet quarterly unless more frequent meetings are required. Regular quarterly meetings will take place in Pittsburgh (preferably) or elsewhere in the United States. Special meetings may be held telephonically.

The following shall be members of the Board:

- The Chief Executive Officer of DLC,
- Each Member of the Consortium with a 10% or more interest in the Consortium may select one member of the Board for each 10% interest in the Consortium, up to a maximum of two members,
- Each Member of the Consortium with less than 10% interest may combine its interest with other such Members and appoint one Board member for each 10% of shares held.

Accordingly, as of the closing, it is expected that the Board will consist of six members including the Chief Executive Officer of DLC, one member representing each of MIP, DUET, IFM, MFSS, and one member representing both MTAA and State Super. The Board shall elect the chair from among its Members; it is currently expected that the Chair shall be the CEO of MIP.

In the aggregate, the Members of the Board will provide Holdings and its subsidiaries, including DLC, with both global and Pennsylvania market-specific expertise in utility management and operations, plus broad executive level experience necessary to properly guide the businesses of Holdings, including DLC.

Management Committee

The Management Committee is the primary forum for the executive management and certain Consortium representatives to discuss substantive matters facing the business as well as to assess progress against previously agreed business plans. The Management Committee will not have any decision-making authority but will report and make recommendations to the Board. The Management Committee will meet monthly.

The Management Committee will be chaired by the Chief Executive Officer of DLC. Other members will include key members of the senior management team of DLC and representatives of the three members of the Consortium with the largest interest (DUET, MIP, and IFM).

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The Management Committee's specific responsibilities will be as follows:

- Provide input to the management in connection with its preparation of the annual operating and capital budgets and long term business plans.
- Review performance against business plans and budgets.
- Review the financial statements prior to submission to the Board for formal approval.
- Review management accounts and performance reports prior to submission to the Board.
- Evaluate and implement compliance and risk mitigation measures.
- Oversee regulatory strategy.
- Review management initiatives.

Audit Committee

The Board will appoint an Audit Committee comprised of Members of the Board. The Audit Committee will recommend accounting policies for approval by the Board, will oversee the accounting and financial reporting processes of Holdings and its subsidiaries, will recommend the appointment of the independent auditor to the Board and will oversee the independent auditor's preparation of its report on the financial statements and processes to the Board. The Audit Committee will also oversee the internal auditor.

Senior Management of DLC

The senior management team of DLC, under the direction of the Chief Executive Officer of DLC, shall have authority and responsibility for the development and implementation of the business plans of Holdings and its subsidiaries, including DLC. Accordingly, the team's primary responsibilities include:

- Anticipating the needs of the customers and communities served by DLC and assuring that the facilities and organizational resources are available to serve those needs,
- Implementing the management and operational processes, systems and controls necessary to meet the needs of Holdings' customers, employees, and investors,
- Maintaining the relationships with customers, communities, regulatory bodies, and others to assure that needs of important constituencies are satisfied, and
- Delivering the service levels, operational metrics and financial performance levels required of the business and/or set forth in its business plans.

The Chief Executive Officer shall report to the Board and the senior team shall report to the Chief Executive Officer.

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Asset Manager

The primary responsibilities of the Asset Manager will be to support the activities of the Management Committee. The Asset Manager will be an employee of Macquarie and will be based in New York City. The Asset Manager's primary contact at the Company will be the Chief Financial Officer. The Asset Manager will work with the Chief Financial Officer to develop financial and operational reports which meet the needs of the Management Committee and perform analyses of such reports as required for the Management Committee to understand the progress of the business against its plans and budgets. The Asset Manager will also keep the minutes of the Management Committee.

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Docket No. A-110150F0035

Docket No. A-311233F0002

**Duquesne Light Company
DQE Communications Network Services, LLC**

Statement No. 2R

REBUTTAL TESTIMONY OF CHRISTOPHER J. LESLIE

1 Q. Please state your name and business address.

2 A. My name is Christopher J. Leslie and my business address is Level 22, 125 West 55th
3 Street, New York, New York, 10019.

4 Q. By who and in what capacity are you employed?

5 A. I am the Chief Executive Officer of Macquarie Infrastructure Partners and Executive
6 Director of both Macquarie Investment Management (USA) Inc. and Macquarie
7 Holdings (USA) Inc., which are members of the Macquarie Group ("Macquarie"). I also
8 serve as Chairman of DQE Holdings LLC.

9 Q. Have you previously submitted direct testimony in this proceeding?

10 A. Yes, I submitted direct testimony designated as DQE Holdings LLC Statement 2 on
11 September 6, 2006.

12 Q. What is the purpose of your rebuttal testimony?

13 A. I will respond to several contentions raised by the various parties in this proceeding:

14 1. That the proposed merger between DQE Holdings LLC ("DQE") and DLH
15 Holdings, Inc. ("DLH") does not provide affirmative benefits to customers
16 ("Merger");

17 2. That the Merger represents the acquisition of DLH and Duquesne Light Company
18 ("Duquesne Light") by a private equity fund that may seek to maximize cash
19 withdrawals from DLH and Duquesne Light at the expense of the obligation of
20 Duquesne Light to provide high quality service to its customers;

21 3. That the transaction is predicated on Duquesne Light expanding the number of
22 Provider of Last Resort Service ("POLR" or "Default Service") customers and the

1 number of customers served by Duquesne Light Energy ("DLE") and the
2 profitability of those businesses; and

3 4. That substantial conditions should be imposed on the approval of the Merger as a
4 result of these false conclusions.

5 **Q. Please summarize your response to the contentions and proposals raised by the**
6 **Parties to this proceeding.**

7 A: The fundamental message I want to convey is the Macquarie Consortium understands
8 and is committed to the regulatory compact. The Macquarie Consortium is investing in
9 utility assets because the members are seeking a long-term investment with a steady cash
10 stream to meet the long-term expectations of their investors, principally pension funds.
11 The Macquarie Consortium brings its world-wide expertise in investing in infrastructure,
12 which by its nature is a long-term proposition. Such investments require long-term
13 commitments to customer service and reliability and a long-term commitment to the
14 communities served by the infrastructure assets. It would simply be bad business for the
15 Macquarie Consortium to attempt to maximize cash flow from DLH to the detriment of
16 customer service quality, reliability and growth of the business.

17 Some of the contentions and proposals of the Parties appear to stem from a
18 misunderstanding and mistrust of the intent of what several parties refer to as "foreign
19 buyers" or "private equity funds." However, these assertions mischaracterize the
20 Merger, and as I and other rebuttal witnesses will explain, the Merger will provide
21 substantial benefits to Duquesne Light's customers and the communities it serves.

22 **Q. What is inaccurate about the characterizations by other Party's witnesses?**

1 A. First, it is inaccurate to characterize this transaction as an acquisition by a "private equity
2 fund". Private equity funds, as typically defined, acquire underperforming businesses,
3 improve and streamline business operations, often with attendant significant job
4 reductions, and then sell such businesses in a relatively short period of time to obtain a
5 profit on their investment. They also often interject new management teams to run the
6 business. This is different from the business model of infrastructure investors, and it is
7 not what the Macquarie Consortium intends to do in this investment. As we have
8 explained, infrastructure investors look to acquire quality well-performing businesses
9 with strong management teams that are likely to continue to perform at high levels for the
10 long time horizons over which they seek to invest. Long-term infrastructure investors, do
11 not base their investment decisions on plans to fix, then sell or "flip" such business to
12 obtain a "quick" profit. This type of investing by the consortium members was
13 evidenced by our response to Duquesne Industrial Intervenors Set II-3 attached as
14 Exhibit CJL-3. As a result, this transaction serves to align long-term infrastructure
15 investors with long-term infrastructure assets. The investment proposition is based on a
16 long-term view of the performance of the business, and as such will only be successful if
17 service quality, reliability and the needs of the community are continuously addressed.

18 Similarly, several parties characterize this transaction as an acquisition by a
19 foreign buyer. While it is true that certain Australian pension funds will become
20 shareholders, I note that the business will also include substantial investments from U.S.
21 and Canadian pension funds that invest through Macquarie managed vehicles. The fund
22 that I am CEO of, *Macquarie Infrastructure Partners*, as an example has raised the
23 majority of its funds from North American investors. Furthermore, from an investor

1 perspective, DQE Holdings LLC will be managed from Macquarie's offices in New York
2 City. More importantly, the business will not be run from New York or Australia, it will
3 be run from the DLH corporate headquarters in Pittsburgh, by a Pittsburgh based senior
4 management team, as it is today.

5 **Q. Please elaborate on the management of DLH and Duquesne Light.**

6 A. As I explained previously, the Macquarie Consortium understands and recognizes that
7 infrastructure investments will only be successful if they continuously respond to the
8 needs of the consumers and the communities they serve. It is not possible to adequately
9 monitor such service and the needs of the community and identify opportunities for
10 further investment, unless the people that run the business are aligned with the
11 community and are locally based. For this reason, the investors in the Macquarie
12 Consortium do not believe that it is beneficial to run infrastructure businesses,
13 particularly a utility business, with an externally located management team. To the
14 contrary, we target businesses that have strong, locally based management teams and
15 seek to retain them. This is precisely what is being done in this transaction.

16 **Q. Is it appropriate or necessary to adopt OCA's recommendation that persons**
17 **"independent" of the investor group be placed on the Board of DLH?**

18 A. No, it is neither appropriate nor necessary. As I explained, we will maintain the
19 management team in Pittsburgh to operate the business. It is currently, and will continue
20 to be, the management team's duty to anticipate and respond to the needs of customers
21 and the communities that Duquesne Light serves. Further, the CEO will be a member of
22 the board, and will also chair the management committee which will meet monthly and
23 consist of representatives of both the senior management team and the three largest

1 members of the Macquarie Consortium. As a result, the investors and the Board will
2 have regular forums to receive input directly from the CEO and other members of the
3 Pittsburgh based senior management team on the needs of the community.

4 I also note that placing persons on the Board that have "independence" from the
5 shareholders raises concerns about who such persons would represent or owe any
6 obligations to if not the investors in the business. This would be in stark contrast to a
7 publicly listed company board, where the independent directors are appointed to
8 represent and protect the interests of shareholders.

9 As I have noted previously, the shareholder representatives clearly understand
10 that it is essential to balance the interests of customers and communities with those of
11 shareholders if an infrastructure investment is to succeed. I believe this has already been
12 evidenced by our proposal of an economic development plan that will be funded by the
13 shareholders. This was a plan that was proposed to the investor group by the current
14 management team as addressing the real need to generate economic and employment
15 growth in Duquesne Light's service territory. While this program will create a cost to the
16 investors in the short run, we believe that promoting economic growth in Pittsburgh will
17 benefit the community, which will benefit the investors in the long run.

18 **Q. Will there be ongoing services provided to Duquesne Light from other utilities
19 managed by Macquarie?**

20 **A.** No, it is our intention to continue the management team, and they will run the business
21 and obtain outside services as they are needed from those persons best qualified to
22 provide those services.

1 It is possible that as a major operating initiative is considered or undertaken, that
2 employees at other utilities or entities managed by Macquarie with experience in the
3 sector could provide valuable assistance. And as such, Duquesne Light's senior
4 management team will have access to the management of other utility investments of the
5 members of the Macquarie Consortium. In any such instance where there will be costs
6 incurred by Duquesne Light, an appropriate filing would be made concerning the
7 provision of such services. Since the Pennsylvania Public Utility Commission has
8 authority to review and must approve contracts for services provided by employees of
9 entities affiliated with Duquesne Light before the services are provided, and since no
10 major initiative or service is currently planned, OCA's proposal that the Commission
11 delay approval of the merger until it has received and approved an affiliate contract is not
12 reasonable and should be rejected.

13 **Q. Please summarize the benefits of the Merger.**

14 **A.** There are three principal benefits of the transaction in addition to the aforementioned
15 economic development plan and access to Macquarie Consortium's utility expertise. The
16 first is maintaining the headquarters of Duquesne Light and the senior management team
17 in Pittsburgh. The rebuttal of other witnesses addresses the real possibility that a
18 multistate utility would acquire Duquesne Light, and the likely attendant loss of jobs and
19 loss of customer and community contact that would result. As explained above and in
20 other rebuttal testimony, this transaction will provide assurance that the headquarters and
21 management will remain in Pittsburgh.

22 The second major benefit to this transaction is that DLH and Duquesne Light will
23 have increased access to capital as a result of the Merger. Increased access to capital will

1 over time lead to a lower cost of capital. As to equity capital, the members of the
2 Macquarie Consortium have large and growing pools of equity to invest and are actively
3 seeking additional opportunities to invest that equity in infrastructure. As to debt capital,
4 the members of the Macquarie Consortium, and Macquarie in particular as one of the
5 largest borrowers globally of infrastructure and utility debt, have worldwide access to
6 debt capital and can access capital on market leading terms, even under difficult market
7 conditions. This cannot be said for Duquesne Light, which is a small company and seeks
8 to raise a relatively small amount of capital only periodically as compared to Macquarie's
9 continuing interactions with capital markets.

10 The third principal benefit is interrelated with the first two. The Merger will
11 allow DLH and Duquesne Light to continue to proceed with its "Back to Basics"
12 strategy. This was an important point in our early discussions with Mr. O'Brien. On a
13 stand alone basis, the "Back to Basics" strategy would have made DLH smaller and
14 likely would have reduced earnings growth, both of which would likely have been looked
15 at unfavorably by the public markets, which in turn would put negative pressure on
16 DLH's stock price and only increase the likelihood that DLH would be acquired,
17 potentially under terms that would not benefit customers and community over the long
18 term. The Macquarie Consortium brings access to global capital markets and investors
19 that are very interested in investing capital in Duquesne Light's core electric utility
20 business.

21 Finally, as I noted previously, the economic development program provides both
22 affirmative benefits to customers and the community, and demonstrates the investor's

1 commitment over the long-term to Duquesne Light, its customers and the community that
2 it serves.

3 **Q. What are the implications of the transaction on Duquesne Light's plans for POLR**
4 **service and Duquesne Light Energy's activities as an Electric Generation Supplier?**

5 A. We have not entered into this transaction with any plan to either increase or diminish
6 Duquesne Light's provision of POLR service or DLE's retail activities, however we did
7 make certain assumptions about expected diminishing profitability of providing POLR
8 service. In this regard, I want to respond to testimony by Retail Energy Supply
9 Association ("RESA") and Strategic Energy LLC ("Strategic") that the Merger is
10 predicated on some expansion of these activities. These "assumptions" by RESA and
11 Strategic are not correct. We provided in discovery a highly confidential analysis that
12 was performed by NERA for the Macquarie Consortium that discussed in detail the risks
13 associated with supplying the power as well as future regulatory risks associated with the
14 profitability of these services. It is attached to the RESA and Strategic testimony. This is
15 the analysis on the POLR business that the Consortium members used to evaluate the
16 transaction, and it confirms that RESA and Strategic are simply incorrect to contend that
17 the transaction is predicated on an expansion of POLR service and increased POLR
18 profits. In fact, quite the opposite is true. In the operating forecasts used by the
19 Macquarie Consortium to evaluate and raise financing for the transaction, we used
20 expected load forecasts provided by Duquesne for our analysis, however we assumed that
21 POLR profits would be significantly reduced moving from POLR III to POLR IV in
22 2008, and further reduced moving to POLR V in 2011. As to DLE, the Macquarie
23 Consortium viewed DLE as a small piece of the overall transaction from a value

1 perspective, and that type of business would not be a typical investment for the members
2 of the Macquarie Consortium. However, we understand that DLE was created in
3 response to certain market demands, and as such we are currently expecting to continue
4 its operations. However, to be clear, there was no material expansion of DLE's
5 operations or profitability assumed in our evaluation of this transaction. In fact, the
6 Macquarie Consortium assumed for purposes of the acquisition analysis that DLE's
7 operating profit would decline from current levels before stabilizing and growing
8 approximately at the rate of load growth in Duquesne's service territory. In support of
9 this testimony, I have provided as Exhibit CJL-4 a highly confidential page from the Debt
10 Information Memorandum which includes the forecast revenue and earnings before
11 interest, tax, depreciation and amortization ("EBITDA") for DLE (Light Energy) and
12 Duquesne Power (Power) that were used by debt and equity investors to evaluate the
13 transaction.

14 **Q. How do you respond specifically to the conditions of approval requested by the**
15 **Parties to this proceeding?**

16 **A.** As a general matter, we believe that most of the conditions are based on a possible
17 misunderstanding of our approach to investment in utility and infrastructure assets.
18 However, we also acknowledge that this is a new type of arrangement and that lack of
19 familiarity understandably generates concern and caution, particularly on behalf of those
20 parties who are charged with representing customer interests. For these reasons, we are
21 willing to accept conditions with regard to the transaction. For the convenience of the
22 Parties, the Administrative Law Judge and the Commission, we have set forth all of the
23 conditions we can accept in a consolidated exhibit designated Ex. No. CJL-5.

1 Mr. O'Brien will address conditions related to service and competition matters and I will
2 address financial conditions. I note that we offer these conditions as further
3 demonstration of our commitment to customers and community which Duquesne Light
4 serves.

5 **Q. What financial conditions are acceptable?**

6 A. A number of parties have raised matters and proposed conditions that could be viewed as
7 financial conditions, particularly OTS Witness Deardoff, OCA Witness Kahal and OSBA
8 Witness Kalcic. We respond to such proposed conditions as follows, with the specifics of
9 the commitment specified in Exhibit CJL-5.

10 OSBA Witness Kalcic requests that the planned 2005-2007 infrastructure
11 improvement plan be completed as scheduled. We will commit to do so.

12 OCA witness Kahal and OSBA witness Kalcic argue that a distribution rate-
13 freeze through December 31, 2010 is necessary to establish affirmative benefit. While
14 we do not agree with the assertion, we will agree not to increase distribution rates prior to
15 January 1, 2009, absent substantial changes in regulation or federal tax policy.

16 OTS Witness Deardoff and OCA Witness Kahal request conditions prohibiting
17 loans to affiliates, guaranteeing any debt of affiliates and pledging the assets of Duquesne
18 Light to provide credit support. These conditions are acceptable unless Duquesne Light
19 obtains approval from the Commission.

20 OTS Witness Deardoff, OCA Witness Kahal and OSBA Witness Kalcic request
21 certain conditions that the transaction will not increase capital costs. We will accept a
22 condition that states that Duquesne Light will not request a capital structure for
23 ratemaking purposes in future rate proceedings which is outside of a reasonable range of

1 that used by comparable companies and that Duquesne Light will not claim increased
2 debt costs resulting from a downgrade of Duquesne Light resulting from the merger for
3 three years following the closing. Beyond three years, the effects of this merger on bond
4 ratings will be difficult if not impossible to identify.

5 In conjunction with the above, we will also accept a condition as requested by
6 OTS Witness Deardoff that Duquesne Light will maintain debt held by investors not
7 affiliated with Duquesne Light or its affiliates, unless the Commission authorizes to the
8 contrary.

9 In response to conditions requested by several Parties, we agree to maintain
10 reasonable accounting controls and pricing protocols governing transactions between
11 Duquesne Light and its affiliates. Upon written request, DLH and its subsidiaries will
12 provide the Commission, the OTS, OCA and OSBA reasonable access to the books and
13 records, officials and staff of DLH and its subsidiaries in Pittsburgh, Pennsylvania,
14 subject to such companies' traditional rights to object to discovery.

15 Also, as requested by OTS Witness Deardoff, DLH and its subsidiaries, including
16 Duquesne Light, will provide to OTS, OCA and OSBA access in connection with rate
17 proceedings, upon request, of presentations given by DLH and its subsidiaries to
18 common stock, bond, or rating analysts. Such material will be accorded confidential
19 treatment.

20 In response to OTS Witness Deardoff's request, Duquesne Light's long term debt
21 ratio as a percent of total capitalization shall not exceed 60% during the 3 years following
22 the closing. I note that additional long-term debt issuances are subject to prior filing and

1 registration of a Securities Certificate by the PA PUC and projected capital structure
2 information would be included in such filings.

3 **Q. OTS Witness Deardoff also requests that the Commission require certain**
4 **notifications to the Commission related to dividends.**

5 A. Dividends are already reported in annual reports to the Pennsylvania PUC. OTS Witness
6 Deardoff has not provided any compelling reason why further limitations or notices
7 should be required. Further, the condition that the long-term debt ratio not exceed 60%
8 without Commission approval would be an effective limitation on dividends because
9 dividends in excess of growth in retained earnings would cause the equity ratio to decline
10 and the debt ratio to increase.

11 **Q. Do you believe that this Merger benefits customers, the Pittsburgh area and the**
12 **Commonwealth?**

13 A. Yes, I strongly believe that to be the case. We believe that the Merger aligns the long
14 term business plans and capital requirements of Duquesne Light with investors that have
15 global access to capital and are actively looking for opportunities to invest that capital for
16 the long term. This will free Duquesne Light from the need to focus on producing
17 quarterly earnings that, under the current structure, are necessary to maintain access to
18 capital markets. The new structure supports DLH's ability to divest non-regulated assets
19 and continue its Back to Basics Strategy that focuses on delivering high quality electric
20 service to its customers, and provides access to the management of other utilities owned
21 by the Macquarie Consortium for the exchange of best practices. Finally, the Merger will
22 benefit the customers and the Pittsburgh region by maintaining the management team and
23 the headquarters in Pittsburgh where they can effectively respond to the needs of the local

1 community. For these reasons, I firmly believe that his transaction is in the public interest
2 and should be approved.

Duquesne Light Company and
 DQE Communications Network Services LLC
 Docket No. A-110150F0035 and A-311233F0002

DII-I-3
 Sponsor: Chris Leslie
 Page 1 of 2

**RESPONSES TO DUQUESNE INDUSTRIAL INTERVENORS
 INTERROGATORIES – SET I**

3. Refer to the Duquesne Light Holdings, Inc. Schedule 14A – Proxy Statement pursuant to Section 14(a) of the Securities Exchange Act of 1934 for the proposed transaction.

Page 25 includes a reason for the merger “the fact that members of the Macquarie Consortium have a long history of acquiring utility assets and holding and operating such investments on a long term basis.” Please provide a detailed explanation of the factual basis for this statement including, but not limited to the length of time members of the Macquarie Consortium have held (if continuing) or held (if divested) any investments in utility assets of equal or greater size to this transaction.

RESPONSE:

The Macquarie Consortium consists of Macquarie managed funds and funds managed by non-Macquarie entities. A summary of the utility investments made by the non-Macquarie managed funds is included below. Macquarie Bank and Macquarie managed fund investments are included in the attachment. Macquarie managed funds have invested in over 100 assets of which, only ten have been subsequently divested.^{1,2}

Consortium member	Interest	Company	Business	Ownership period	Size
MTAA	None				
IFM	11%	Arqiva, UK	Telecommunications	2004 – present	NA
IFM	15%	Wales and West Utilities, UK	Gas distribution	2004 – present	KM of Pipeline: 34,000
IFM	34%	ZEC Lodz, Poland	Distributed heating	2005 – present	NA
IFM	26.4%	Epic Energy, Western Australia	Gas transmission	1998 – 2006	NA
IFM	49%	Gorodok natural gas pipeline, New South Wales	Gas transmission	2002 – 2006	NA
IFM	12%	Multinet, Victoria	Gas distribution	1999 – 2005	Customers: 643,431
State Super	11.1%	Epic Energy	Gas transmission	Dec 1996 - present	NA
State Super	4.1%	Northern Gas Network	Gas distribution	Dec 2004 -Present	Customers: 2.5MM

¹ Also sold minority investments in two Australian listed securities

² Merger application referred to assets sold as at June 30, 2006

Asset	Country	Sector	Financial Close Date	Primary Fund/MBL	Total Macquarie Managed Interest
Transoll	Australia	Roads	Mar-99	MIG	40.5%
M8 Toll	UK	Roads	Oct-99	MIG	100.0%
Tagua Crossings	Portugal	Roads	Oct-98	MIG	30.8%
Waznow Tunnel	Germany	Roads	Mar-00	MIG	70.0%
N3 Toll Concession	South Africa	Roads	May-00	SAIF	41.1%
Trans African Concessions (N4 Maputo Toll)	South Africa	Roads	May-00	SAIF	67.5%
Bakwena Platinum Corridor Concessionaire	South Africa	Roads	Aug-01	SAIF	25.0%
407ETR	Canada	Roads	Apr-02	MIG	30.0%
South Bay Expressway	US	Roads	Sep-02	MIG	100.0%
Gwangju 2nd Beltway, Section 1	Korea	Roads	Jan-03	MKIF	100.0%
Westlink M7	Australia	Roads	Feb-03	MIG	47.5%
New Daegu-Busan Expressway	Korea	Roads	Sep-03	MKIF	6.5%
Incheon International Airport Expressway	Korea	Roads	Dec-03	MKIF	24.1%
Woorunsan Tunnel	Korea	Roads	Dec-03	MKIF	38.0%
Hakone Tumpike	Japan	Roads	Mar-04	MBL	50.0%
Baekyang Tunnel	Korea	Roads	Mar-04	MKIF	98.2%
Machang Bridge	Korea	Roads	Jun-04	MKIF	100.0%
Cheonan-Nonsan Expressway	Korea	Roads	Sep-04	MKIF	60.0%
EastLink	Australia	Roads	Nov-04	ConnectEast	100.0%
Seoul-Chuncheon Expressway	Korea	Roads	Dec-04	MKIF	15.0%
Gwangju 2nd Beltway, Section 3-1	Korea	Roads	Dec-04	MKIF	75.0%
Skyway	US	Roads	Jan-05	MIG	45.0%
Soojongsan Tunnel	Korea	Roads	Jul-01	MKIF	100.0%
Sea to Sky	Canada	Roads	Jun-05	MEAP	100.0%
Dufes Greenway	US	Roads	Sep-05	MIG	100.0%
Yongin-Seoul Expressway	Korea	Roads	Dec-05	MKIF	35.0%
Edmonton Ring Road	Canada	Roads	Dec-05	MEAP	81.0%
APRR	France	Roads	Feb-06	MIG	40.7%
Incheon Grand Bridge	Korea	Roads	Mar-06	MKIF	41.0%
Daegu 4th Beltway East	Korea	Roads	Mar-06	MKIF	85.0%
Ibukiyama Driveway	Japan	Roads	Apr-08	MBL	50.8%
MSCR	US	Roads	May-08	MBL	100.0%
Indiana Toll Road	US	Roads	Jun-06	MIG	50.0%
Kilimanjaro Airport Development Company	Tanzania	Airports	May-00	SAIF	30.0%
Bristol Airport	UK	Airports	Sep-01	MAP	50.0%
Birmingham Airport	UK	Airports	Dec-01	MAP	24.1%
Rome Airport	Italy	Airports	May-02	MAP	44.7%
Sydney Airport	Australia	Airports	Jun-02	MAP	63.8%
Adelaide Airport	Australia	Airports	Jul-02	MSAM	5.3%
Copenhagen Airport	Denmark	Airports	Dec-04	MAP	53.4%
Bussaba Airport	Belgium	Airports	Dec-04	MAP	70.0%
Electranet	Australia	Electricity	Mar-01	MSAM	5.5%
Athalink	Canada	Electricity	May-03	MEAP	23.0%
United Energy Distribution	Australia	Electricity	Jul-03	DUET	68.0%
Cardinal Power	Canada	Electricity	Apr-04	MPT	100.0%
Duquesne Light	US	Electricity	Aug-06	DUET	7.7%
Prospect Water	Australia	Water	Jun-01	MSAM	49.0%
Aquion	US	Water	Pending	MBL	100.0%
Thames Water	UK	Water	Pending	MEIF II and others	100.0%
Broadcast Australia	Australia	Communications	Aug-02	MCG	100.0%
Arqiva	UK	Communications	Jan-05	MCG	100.0%
Multinet	Australia	Gas	Jul-03	DUET	79.9%
AllintaGas Networks	Australia	Gas	Jul-03	DUET	25.9%
Dampier to Bunbury Natural Gas Pipeline	Australia	Gas	Oct-04	DUET	71.8%
Wales & West Utilities	UK	Gas	Jun-05	MEIF	100.0%
SK EAS	Korea	Gas	Mar-06	MKOF	49.0%
The Gas Company	US	Gas	Jun-06	MIC	100.0%
NRE	The Netherlands	Gas	Pending	MEIF	49.0%
Obrogas Net	The Netherlands	Gas	Pending	MEIF	49.0%
Netbeheer Haarlemmermeer	The Netherlands	Gas	Pending	MEIF	40.0%
Artand Express	Sweden	Rail	Apr-04	MEIF	100.0%
Seoul Subway Line 9, Section 1	Korea	Rail	Dec-05	MKIF	24.5%
District Energy	US	District Energy	Dec-04	MIC	100.0%
Macquarie Parking	US	Car Parking	Sep-02	MIC	87.9%
Icon Parking	US	Car Parking	Jan-06	MBL	100.0%
Airports Services Business	US	FBO's	Jul-02	MIC	100.0%
Trajan	US	FBO's	Jul-08	MIC	100.0%
EPR UK	UK	Renewables	Mar-05	MEIF	100.0%
NIMRE (NM Renewable Energy)	UK	Renewables	May-05	MRF	50.0%
EPR Europe	France	Renewables	Jun-05	MEIF	100.0%
French Windfarms	France	Renewables	Pending	GIF II	100.0%
CJ CableNet	Korea	Media	Jun-05	MBL	8.0%
Red Bee Media	UK	Media	Jul-05	MCAG	100.0%
Macquarie Regional Radlworks	Australia	Media	Nov-05	MMG	100.0%

Asset	Country	Sector	Financial Close Date	Primary Fund/MBL	Total Macquarie Managed Interest
Taiwan E-Communications	Taiwan	Media	May-08	MMG	100.0%
European E-Com	The Netherlands	Other	Jul-06	MCAG	98.1%
RQNZ	New Zealand	Aged Care/Retirement	Jul-05	GIF II	100.0%
Retirement Care Australia	Australia	Aged Care/Retirement	Jul-05	MCAG	97.8%
Zip Inge	Australia	Aged Care/Retirement	Oct-05	MCAG	49.0%
Laburnworld	Canada	Aged Care/Retirement	Oct-05	MIIF	100.0%
Private Lifecare	New Zealand	Aged Care/Retirement	Dec-05	MBL	50.0%
Medicare	New Zealand	Aged Care/Retirement	Dec-05	MBL	41.0%
Retirement Services Australia	Australia	Aged Care/Retirement	Jun-08	MBL	39.2%
Smazta Carte	US	Airport Trolleys	Feb-06	MBL	100.0%
Wightlink Ferries	UK	Ferries	Jul-05	MEIF	100.0%
Steam Packet	UK	Ferries	Oct-05	MBL	100.0%
DCT Gdansk	Poland	Ports	Oct-05	GIF II	100.0%
Changshu Xinghua Port	China	Ports	Dec-05	MIIF	38.0%
Hanjin	Korea	Ports	Pending	MKOF	49.0%
TanQuid	Germany	Tank Storage	Nov-05	MIIF	100.0%
MTT	US	Tank Storage	May-06	MIC	50.0%
TanQuid add-on	Germany	Tank Storage	Jul-06	MIIF	100.0%
Abbotsford Hospital	Canada	Healthcare	Dec-05	MBL	81.0%
Academic Ambulatory Care Centre	Canada	Healthcare	Dec-05	MBL	81.0%
Mob	UK	Roadside Services	Jun-06	MBL	100.0%
ARR-Serv	US	Tyre Inflation	Jul-08	MCAG	96.5%
Itavelesca	Spain	Vehicle Inspection	Aug-06	GIF II	84.1%
JCADR	UAE	Other	Jun-06	ZIF	100.0%
Stagecoach	UK	Other	Aug-06	MBL	100.0%
Industrial City of Al Ain	UAE	Other	Sep-08	ZIF	100.0%
Boart Longyear	US	Other	Sep-08	MBL	58.1%

¹ Refers to interest purchased by DUET pursuant to interim financing agreement

DIVESTED ASSETS AS AT Sep 2008

Asset	Country	Sector	Initial Investment Date	Sale Date
Loy Yang A	Australia	Power Generation	May-87	Feb-08
Eastern Distributor (M1) ¹	Australia	Roads	Jun-87	Jul-08
Reef Networks	Australia	Communications	Jun-00	Mar-05
Detroit - Windsor Tunnel	US	Roads	Jan-01	Oct-08
Clstra	Spain	Roads	Jan-02	Oct-04
Michigan Electric Transmission Company ²	US	Electricity	Dec-03	Oct-06
South East Water ³	UK	Water	Apr-04	Oct-06
Yorkshire Link	UK	Roads	Oct-99	Feb-07 ⁴
M4	Australia	Roads	Dec-00	Jul-06
M5	Australia	Roads	Aug-96	Jul-06

¹ Macquarie still manages an investment through a non-discretionary mandate

² Macquarie held a minority stake in this asset and was forced to sell its interest by the majority shareholder

³ Sale required to consummate Thames acquisition

⁴ Expected close

PROPRIETARY INFORMATION

Docket Number A-110150 F-0035

Name of Document Exhibit CJL-4

Date Document Received 2-27-2007

DOCUMENT CONTAINS

PROPRIETARY INFORMATION

1. Duquesne Light will agree not to increase its distribution rates prior to January 1, 2009, absent substantial changes in regulation or federal tax policy. This provision shall not affect Duquesne's ability to adjust its rates on a timely basis to reflect changes to its FERC-approved transmission rates or changes in state taxes pursuant to the State Tax Adjustment Surcharge.

2. Duquesne Light commits to complete the Infrastructure Improvement Plan set forth in the attached Duquesne Light's response to OCA-III-8.

3. In future petitions to the Commission to set distribution rates, Duquesne Light

- Shall not request a capital structure for ratemaking purposes which is outside of a reasonable range of that used by comparable companies;
- Shall not claim, for 3 years following the Merger, any increase in its cost of capital due to any downgrading of Duquesne Light debt as a direct result of the Merger.

4. Duquesne Light agrees that the acquisition premium and transaction costs associated with the Merger, as set forth in Duquesne Light's response to the attached OCA-III-21, including all related tax effects, shall be excluded from future distribution rates. Duquesne Light also agrees that any increase in the Pennsylvania Capital Stock Tax as a result of the Merger shall not be recovered in distribution rates.

5. Subsequent to the effective date of the Commission's approval of the Merger, Duquesne Light shall not

- Guarantee the debt or credit instruments of DLH or any affiliate not regulated by the Commission, except as approved by the Commission,
- Grant a mortgage or other lien on any property used and useful by Duquesne Light in providing retail utility service to the public subject to the Commission's jurisdiction, except for the financing needs of Duquesne Light, or
- Make any loan or otherwise extend credit to DLH or any affiliate not regulated by the commission for a term of one year or more, except as approved by the Commission.

6. Duquesne Light agrees to maintain reasonable accounting controls and pricing protocols governing transactions between Duquesne and its affiliates. Upon written request, DLH and its subsidiaries will provide the Commission, the OTS, OCA and OSBA reasonable access to the books and records, officials and staff of DLH and its subsidiaries in Pittsburgh, Pennsylvania, subject to such companies' traditional rights to object to discovery.

7. Duquesne Light agrees to maintain debt held by investors not affiliated with Duquesne Light or its affiliates, unless the Commission authorizes to the contrary.

8. DLH and its subsidiaries, including Duquesne Light, will provide to OTS, OCA and OSBA access in connection with rate proceedings, upon request, of presentations given by DLH and its subsidiaries to common stock, bond, or rating analysts. Such material will be accorded confidential treatment.

9. Duquesne Light's long term debt ratio as a percent of total capitalization shall not exceed 60% during the 3 years following the closing.

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Docket No. A-110150F0035

Docket No. A-311233F0002

**Duquesne Light Company
DQE Communications Network Services, LLC**

Statement No. 3R

REBUTTAL TESTIMONY OF JOSEPH G. SAUVAGE

DIRECT TESTIMONY OF JOSEPH G. SAUVAGE

1 **Q. Please state your name and full business address.**

2 A. My name is Joseph G. Sauvage. My business address is 745 Seventh Avenue, 25th Floor
3 New York, NY 10019.

4 **Q. What is your position at Lehman Brothers Inc. ("Lehman")?**

5 A. I am a Managing Director and Co-Head of Lehman's Global Power Group which covers
6 regulated gas and electric utilities and electric generation companies. We provide a broad
7 range of strategic advisory and capital raising services to our clients. We have been the
8 primary investment banking advisor for Duquesne Light Holdings ("DLH"), and its
9 regulated utility subsidiary Duquesne Light Company ("DLC") since 1998.

10 **Q. How long have you worked at Lehman?**

11 A. I have worked at Lehman for the past 29 years. I started my investment banking career
12 here in 1977.

13 **Q. What are your qualifications, work experience and educational background?**

14 A. These are attached as Exhibit 1.

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

16 A. The purpose of my rebuttal testimony is to respond to the testimony of the Office of Trial
17 Staff witness Kevan Deardorff, Office of Consumer Advocate witness Matthew Kahal
18 and Office of Small Business Advocate witness Brian Kalcic. Each of these witnesses
19 contend that the acquisition of DLH by the Macquarie Consortium does not provide
20 affirmative benefits to DLC and its customers. I respond to these contentions by
21 explaining that this transaction is the best strategic alternative for DLH and DLC. In
22 support of my conclusions, I will:

- 1 • provide an overview of the current regulated utility mergers and acquisitions
2 (“M&A”) market environment;
- 3 • discuss my opinions of DLH’s strategic alternatives;
- 4 • discuss the benefits of private ownership of DLH and DLC upon becoming a wholly
5 owned subsidiary of the consortium of strategic infrastructure investment funds lead
6 by the Macquarie Group (the “Macquarie Consortium”); and
- 7 • discuss my views of the ratings actions taken by the major ratings agencies Standard
8 and Poor’s (“S&P”), Moody’s Investors Service (“Moody’s”) and FitchRatings
9 (“Fitch”) upon announcement of the acquisition.

10 **Q. Please described the proposed transaction?**

11 A. Under the terms of the Agreement and Plan of Merger (“Merger Agreement”), the
12 Macquarie Consortium will acquire all of the outstanding common shares of DLH for
13 \$20.00 per share in cash (the “Transaction”). This will result in Macquarie managed
14 funds holding 64.3% of the equity in DQE Holdings LLC, which will be a newly formed
15 special purpose entity to hold the equity of DLH. The Transaction has a total equity
16 market value of approximately \$1.59 billion, based upon the approximately 79.6 million
17 DLH common shares outstanding at the date of signing. The Macquarie Consortium also
18 will assume \$148 million of DLC’s preferred and preference shares on issue as well as
19 assuming approximately \$1.26 billion of DLH’s long-term debt (estimated at closing).
20 The offer represents a premium of 21.7% based upon DLH’s closing share price on July
21 3, 2006 and a premium of 24.0% over DLH’s average 30-day closing price ending July 3,
22 2006.

23 **Q. Please describe Lehman’s role in relation to the Transaction.**

1 A. Lehman has been engaged by the senior management of DLH to act as M&A advisor to
2 DLH and to provide a fairness opinion to DLH's Board of Directors as it relates to the
3 consideration to be received by DLH's shareholders.

4 **Q. Can you please provide a summary of your views on the current M&A market**
5 **environment as it relates to the regulated electric utility sector?**

6 A. Over the last two years there has been a relative increase in M&A activity throughout the
7 regulated electric utility sector. Since December 2004 there have been nine announced
8 transactions: four of which are currently pending (including this Transaction), three of
9 which have been completed and two which have been terminated. (Please see Exhibit 2)
10 The individual motivation for M&A transactions varies from transaction to transaction,
11 however, the nine transactions I mentioned can be bifurcated into two general categories:
12 Strategic Mergers / Acquisitions and Portfolio Acquisitions, please see Table 1.

Table 1	
Transaction Type	Representative Transactions (Acquirer / Target)
Strategic Mergers / Acquisitions	<ul style="list-style-type: none">• Peoples Energy Corp. / WPS Resources Corp.• National Grid / KeySpan Corp.• FPL Group / Constellation Energy• Duke Energy / Cinergy• Exelon / PSEG• PNM Resources / TNP Enterprises Inc.
Portfolio Acquisitions	<ul style="list-style-type: none">• Macquarie Group / Duquesne Light Holdings• Babcock and Brown / Northwestern Corp.• MidAmerican Energy Holdings Company / PacifiCorp

13 Many of the larger strategic mergers have been predicated on economies of scale,
14 increased scope and profitability of unregulated operations. In Strategic Mergers /
15 Acquisitions, a primary economic driver of the transaction is the potential to generate
16 synergistic savings with the expectation to create a sharing mechanism between

1 ratepayers and shareholders. Synergies are generally categorized into the following
2 areas, such as:

- 3 1. Staff reductions;
- 4 2. Unregulated operations cost savings or increased efficiency;
- 5 3. Corporate program benefits;
- 6 4. Supply chain improvements;
- 7 5. Non-labor information technology improvements;
- 8 6. Economies of scale;
- 9 7. Enhanced access to both debt and equity capital; and
- 10 8. Employment of best practices.

11 All of the transactions listed above in Table 1 as Strategic Mergers / Acquisitions,
12 are/were predicated on significant synergistic savings. Due to the strategic nature of the
13 transactions and the characteristics of the businesses, a significant portion of the expected
14 synergies are derived from staffing reductions and non-regulated operations.

15 As a result of the repeal of the Public Utilities Holding Company Act of 1935
16 ("PUHCA"), we have witnessed an increase in acquisition activity, particularly in
17 relation to strategic infrastructure funds such as the Macquarie Consortium. I believe that
18 this trend will continue as the focus on infrastructure investing has increased dramatically
19 in the last few years. These types of dedicated funds have significantly differentiated
20 themselves from other "private equity" investors in that they have a strategic long-term
21 buy and hold focus.

22 Unlike Strategic Mergers / Acquisitions, Portfolio Acquisitions have generally been
23 predicated on the benefits of replacing publicly traded equity with direct investments

1 primarily held by a sophisticated and professional investor base. Of the three Portfolio
2 Acquisitions listed in Table 1, none have been predicated on the generation of significant
3 synergistic savings. Instead, the justification for such mergers has derived primarily from
4 public to private benefits such as:

- 5 1. Enhanced access to equity capital and the removal of equity capital markets
6 access risk;
- 7 2. Improved access to debt capital markets as a result of financial size and reach
- 8 3. Long-term strategic focus and planning;
- 9 4. Maintenance of headquarters and reliance on existing management and
10 employees; and
- 11 5. Transfer of ownership to a sophisticated and targeted institutional investor base
12 with long-term return requirements.

13 I would expect this trend to continue as many smaller utilities and infrastructure funds
14 will likely seek strategic partnerships to cost effectively meet their capital requirements
15 as the U.S.'s aging utility infrastructure base continues to require higher and higher
16 expenditures to maintain appropriate reliability standards. I view this as a natural
17 evolution of capital markets as there is an efficiency in the appropriate direct alignment
18 of capital availability by funds such as the Macquarie Consortium with utilities such as
19 DLC who have a real time need for such capital and who may not continue to have access
20 to capital on as favorable terms if they remained as a standalone entity.

21 **Q. Can you please provide your opinion of the equity markets assessment of DLH's**
22 **future prospects?**

1 A. I believe the equity markets had a negative view of DLH's future prospects as it had one
2 of the highest proportion of shares sold short of regulated utility stocks. When investors
3 sell a company's shares short they are taking a bearish investment position, projecting
4 that the company's share price will decline in the future below the current price. The
5 numbers of shares held short is reported monthly and on June 30, 2006, the last reporting
6 date prior to the announcement of the Transaction, DLH had approximately 10 million
7 shares held short, or 12.7% of its fully diluted shares outstanding. As a comparison the
8 average (arithmetic) for the numbers of shares held short divided by the fully diluted
9 shares outstanding for the companies that comprise the Philadelphia Utility Index on June
10 30, 2006 was 2.7%. (Please See Exhibit 3) I believe that this trading characteristic of
11 DLH provided a clear insight into investor's views of DLH's future share price
12 performance. This also provides credence to Mr. O'Brien's direct testimony regarding
13 DLH's likely inability to maintain its current dividend, since if DLH was forced to cut its
14 dividend its share price would almost certainly decline to maintain an appropriate
15 dividend yield. As I will discuss later in my testimony, the acquisition of DLH by the
16 Macquarie Consortium will alleviate a number of these potential future equity capital
17 market issues.

18 **Q. Can you please provide your opinion in relation to DLH's strategic alternatives and**
19 **in the absence of this Transaction?**

20 A. I don't believe that DLH had many strategic alternatives. From a strategic perspective,
21 DLH's small market capitalization and declining earnings profile put pressure on DLH's
22 stock price. At its then current price and earnings profile, a strategic transaction with one
23 of DLH's larger surrounding utilities would likely have been unattractive from the

1 acquirer's perspective. The downward pressure on DLH's stock price, coupled with
2 expected operating synergies would likely eventually have led potential strategic
3 acquirer's to take an interest.

4 **Q. In the event that DLH was acquired by one of its larger surrounding utility holding**
5 **companies, do you believe that DLH's employees and headquarters would remain**
6 **intact?**

7 A. I would find it unlikely that DLH's senior management would remain intact and that its
8 headquarters would remain in Pittsburgh. In an attempt to create synergies, the relative
9 small size of DLH would likely result in the movement of corporate functions to the head
10 offices of the acquirer and the termination of the majority of senior management.

11 **Q. You refer to the emergence of infrastructure funds as becoming active participants**
12 **in regulated utility M&A; can you please provide your opinion of the investment**
13 **objectives of typical "private equity" investors versus "infrastructure funds" such as**
14 **the Macquarie Consortium?**

15 A. The rates of return ranges I will suggest should be viewed as guidelines and not
16 considered definitive parameters as there are many factors which will impact an
17 individual investor's required rate of return. A typical "private equity" investor will
18 likely seek to achieve an internal rate of return in excess of 20% within a five to eight
19 year time horizon. The likely method of realizing such return is generally achieved
20 through significantly increased upfront leverage, with an expectation to de-lever the
21 business over a period of time to prepare for the ultimate realization of the return through
22 a future sale of the business at expanded sales multiples over the original purchase
23 multiples.

1 A differentiating factor for today's infrastructure funds is the nature of their investor
2 constituency, which is comprised primarily of institutional pension and retirement equity
3 investors. The first primary difference between "private equity" investors and
4 infrastructure funds is their investment time horizon, with infrastructure funds having a
5 longer investment time horizon. Mr. Leslie expresses this view clearly in his rebuttal
6 testimony. Second is the expected internal rate of return. Infrastructure funds generally
7 have lower return expectations that stem from the fund owners' intent to appropriately
8 match the duration of their long-dated pension and retirement liabilities with similar long-
9 dated assets. As I mentioned earlier, as capital markets have become increasingly
10 competitive it is a natural evolution for professional institutional money managers to seek
11 direct investments in order to meet their required rates of return instead of through
12 purchasing publicly traded equities. This investment model has also been employed in
13 the insurance industry as well; the most compelling example that comes to mind is that of
14 Berkshire Hathaway.

15 When one notes that 100% of the ownership of DLH would be held amongst the
16 consortium of funds led by the Macquarie Group, one can conclude that the Transaction
17 is effectively an efficient transfer of ownership to the appropriate dedicated
18 professionally managed investor base. Based on this I would like to address statements
19 made in Mr. Kahal's testimony where he suggests that in the absence of being a public
20 entity, DLH may lack the proper internal financial and management discipline to
21 effectively operate the business. He states: "The absence of market discipline and
22 transparency under the proposed 'private equity' Board of Directors is a significant
23 change from the present governance structure." (Page 28 rows 16-24). This assertion is

1 inaccurate. The funds which will own DLH are subject to strict fiduciary standards,
2 particularly due to the pension and retirement nature of the capital they manage.
3 Accordingly I think that the direct involvement of the respective fund's principals on the
4 board of DLH will result in enhanced financial discipline. In contrast to public equity
5 ownership where equity owners have limited information on the internal workings of
6 their investment, the ownership and governance structure proposed by the Macquarie
7 Consortium will allow for direct oversight and accountability.

8 In addition, as Mr. O'Brien states in his direct testimony, so long as DLC or DLH has
9 registered publicly traded debt it will be required to continue to make quarterly public
10 SEC filings. As with any utility business it will be essential for the Macquarie
11 Consortium to maintain DLC's and DLH's access to the debt capital markets on
12 favorable terms. DLC's and DLH's fixed income instruments will continue to be rated
13 by the ratings agencies and covered by fixed income research analysts. Lastly I would
14 note that DLC will still be under the full regulation and oversight of the Pennsylvania
15 Public Utility Commission.

16 **Q. In Mr. Deardorff's testimony he states "In my professional experience analyzing**
17 **mergers, one factor supporting their approval by the involved utility commission is**
18 **that the entities involved can typically demonstrate a likely positive cost/benefit**
19 **analysis due to the business synergies of the merging entities, often due to favorable**
20 **economies of scale." (Page 4 rows 3-6). Based upon what you have discussed here so**
21 **far can you please provide you views regarding the benefits of this Transaction?**

1 A. In my earlier discussion regarding the rationale for Portfolio Acquisitions I outlined five
2 items which I believe provide benefits to the target company. I would like to provide my
3 opinion on how each of these may serve to benefit DLC and DLH.

4 *1. Enhanced access to equity capital and the removal of equity capital markets access*
5 *risk*

6 Private ownership allows DLH to avoid equity market timing and access risk when it
7 needs to source equity. DLH will have the ability to call on its existing owners, who are
8 actively seeking equity investment opportunities in infrastructure, and not subject DLH to
9 market timing risk and other macro economic factors which could significantly impact
10 DLH's access to equity capital. As an example the last time DLH issued equity on June
11 20, 2002 its file to price performance was (10.9%) down. More simply put this means
12 existing holders of equity generally experienced a (10.9%) decline in the value of their
13 equity holdings. As a point of comparison the average file to price performance for all
14 utility classified equity offerings since January 1, 2002 to today has been (4.5%) down on
15 average (arithmetic). Please See Exhibit 4

16 *2. Improved access to debt capital markets as a result of financial reach and size*

17 A significant benefit that the Macquarie Consortium will bring to DLC and DLH is in
18 relation to access to debt capital markets. Historically, both DLC and DLH have priced
19 new debt issuances at discounts greater than peers with similar ratings. If you refer to
20 Table 2 below you will see that both DLC's and DLH's new issue spreads have priced
21 significantly wider than the trading spreads of its peer companies with similar ratings.
22 This results in increased cost to ratepayers.

Table 2

Duquesne Light Holdings – Senior Unsecured Bonds – 10 Year

			Comparables			
<i>Issuer:</i>	DLH	<i>Issuer:</i>	CenterPoint Energy Inc.	Northeast Utilities	Pepco Holdings Inc.	DTE Energy Co.
<i>New Issue Spread:</i>	T+122	<i>Trading Spread ⁽¹⁾</i>	+115bps	+90bps	+90bps	+80bps
<i>Coupon:</i>	5.500%	<i>Coupon:</i>	7.875%	7.250%	6.450%	7.050%
<i>Maturity:</i>	2015	<i>Maturity:</i>	2013	2012	2012	2011
<i>Security:</i>	Senior Unsecured	<i>Security:</i>	Senior Unsecured	Senior Unsecured	Senior Unsecured	Senior Unsecured
<i>Senior Unsecured Rating:</i>	Baa3 / BBB-	<i>Senior Unsecured Rating:</i>	Baa3 / BBB	Baa2 / BBB-	Baa3 / BBB-	Baa2 / BBB-
<i>Issuance Date:</i>	8/11/2005					

Duquesne Light Holdings – Senior Unsecured Bonds – 30 Year

			Comparables		
<i>Issuer:</i>	DLH	<i>Issuer:</i>	DTE Energy Co.	Progress Energy Inc.	Pepco Holdings Inc.
<i>New Issue Spread:</i>	T+175	<i>Trading Spread ⁽¹⁾</i>	+137bps	+125bps	+150bps
<i>Coupon:</i>	6.250%	<i>Coupon:</i>	6.375%	7.000%	7.450%
<i>Maturity:</i>	2035	<i>Maturity:</i>	2033	2031	2032
<i>Security:</i>	Senior Unsecured	<i>Security:</i>	Senior Unsecured	Senior Unsecured	Senior Unsecured
<i>Senior Unsecured Rating:</i>	Baa3 / BBB-	<i>Senior Unsecured Rating:</i>	Baa2 / BBB-	Baa2 / BBB-	Baa3 / BBB-
<i>Issuance Date:</i>	8/11/2005				

Duquesne Light Company – Secured Bonds

			Comparables		
<i>Issuer:</i>	DLC	<i>Issuer:</i>	Houston Light & Power	Carolina Power & Light	ConEdison Company of New York
<i>New Issue Spread:</i>	T+94	<i>Trading Spread ⁽¹⁾</i>	+78bps	+70bps	+60bps
<i>Coupon:</i>	5.700%	<i>Coupon:</i>	5.700%	5.125%	4.875%
<i>Maturity:</i>	2014	<i>Maturity:</i>	2013	2013	2013
<i>Security:</i>	1st Mortgage Bond	<i>Security:</i>	General Ref Mortgage	First Mortgage	Debentures
<i>Rating:</i>	Baa1 / BBB+	<i>Rating:</i>	Baa2 / BBB	A3 / BBB	A1 / A
<i>Issuance Date:</i>	5/10/2004				

1. Trading spread is as of the date of the respective DLH and DCL issuance dates.

Source: Bloomberg and Lehman Brothers

- 1 I believe that ownership by the Macquarie Consortium will provide benefits to both DLC
- 2 and DLH as it relates to their cost of debt. Macquarie has worldwide access to financial

1 institutions as one of the largest borrowers of debt financing for infrastructure in the
2 world. In addition, Macquarie is capable of creating a competitive dynamic amongst
3 lenders competing for their capital markets financing business. This dynamic results in
4 lending institutions offering greater covenant flexibility and tighter spreads, meaning
5 lower financing costs, in order to win business for Macquarie's investment financings. I
6 would expect these benefits to accrue to both DLC and DLH.

7 ***3. Long-term strategic focus and planning***

8 An important characteristic of regulated utility operation is effective long-term planning.
9 A general irony of the United States equity markets, as it relates to effective utility
10 planning, relates to investors' expectations of managements' ability to be able to deliver
11 on quarterly and annual earnings estimates. In many cases these equity market
12 expectations force management to meet short-term market expectations as opposed to
13 making long-term budgeting and expenditure decisions. Private ownership offers
14 regulated utilities such as DLC the ability to engage in long-term planning which results
15 in more effective utility asset management and operation.

16 ***4. Maintenance of headquarters and reliance on existing management and employees***

17 The Macquarie Consortium, as owner, will require the existing management team and
18 employee base to properly manage the business. As I stated earlier, in most acquisitions
19 and mergers where synergistic savings are required to make a transaction work from an
20 economic perspective, head count reductions are generally a significant contributor to
21 achieving such synergies. The Macquarie Consortium's commitment to retaining
22 management and honoring current labor contracts serves to alleviate both DLH's and

1 DLC's management and employees' concerns of termination, which serves to maintain
2 management and employees' focus on their service to customers.

3 *5. Transfer of ownership to a sophisticated and targeted institutional investor base*
4 *with long-term return requirements in line with that of public markets*

5 As I stated earlier, I believe that the Macquarie Consortium represents focused
6 professional institutional ownership. The Macquarie Consortium has an economic
7 interest in maintaining the equity value of DLH in order to maintain and enhance the
8 value of their investment. Due to the low risk nature of funds such as the Macquarie
9 Consortium's, returns are predicated on stable returns over the long term and not windfall
10 "home runs" so to speak. This serves to align the owners interest with that of ratepayers
11 as the long term equity value of DLH will only be maintained through investing in the
12 business, providing excellent customer service, the application of the regulated utility rate
13 mechanism and the prudent management of operational risk and POLR liability.

14 **Q. Can you please discuss your views of S&P's, Moody's and Fitch's ratings actions in**
15 **relation to the announcement of the Transaction?**

16 **A.** The testimonies of Mr. Kahal and Mr. Deardorff incompletely describe the actions taken
17 by S&P and Moody's upon announcement of the Transaction as indicative of the
18 negative financial implications of the Macquarie Consortium's proposed acquisition
19 financing structure. There are many factors which impact the rating agencies actions as
20 they relate to the announcement of strategic transactions. The rating agencies will tend to
21 evaluate a number of factors relative to the target and transaction structure when
22 determining the appropriate action to take in the best interest of fixed income holders. I
23 would like to make a few observations regarding the specific reports published by S&P,

1 Moody's (which are referenced by Mr. Kahal and Mr. Deardorff) and FitchRatings,
2 which neither addressed.

3 Attached as Exhibit 5 to this testimony are the reports published by S&P, Moody's and
4 FitchRatings. Please note that FitchRatings affirmed its current ratings in relation to the
5 acquisition announcement, citing improved access to capital.

6 What is important to note is that the rating agencies cite many other factors which
7 influenced their actions.

8 S&P states:

9 "We will update the CreditWatch when appropriate as the acquisition
10 progresses and as important credit events are addressed, such as:

- 11 • Resolution of pending tax disputes,
- 12 • The outcome of a current Pennsylvania delivery rate case, and
- 13 • The company's proposal for its provider-of-last-resort obligations
14 beginning in 2008.

15 The final rating will incorporate our analysis of these issues and the final
16 financing and legal structure of the new entity."

17 Moody's states:

18 "The review will also consider that the company has significant capital needs
19 to support announced asset acquisitions and capital improvement spending for
20 utility operations. In addition, the company is currently in various stages of
21 filing requests with the Pennsylvania Public Utility Commission and FERC
22 for distribution and transmission rate base increases."

23 Although the ultimate actions of the rating agencies remain to be seen, many of the issues
24 cited in their reports have been resolved, such as: DLC's rate case, the recent sale of
25 Montauk Energy Capital LLC, which serves to provide credit enhancement by reducing
26 DLH's financial exposure to unregulated operations and reducing DLH's debt, and the

1 closing of the acquisition of the minority ownership of the Keystone and Conemaugh
2 generation plants.

3 **Q. In Mr. Kahal's testimony he states "Applicants and the Commission can provide**
4 **benefits to customers from this Transaction by accepting a distribution service rate**
5 **cap extending to year-end 2010." (Page 6 rows 16-18). Can you please comment on**
6 **your views of the credit impact to DLC in regards to a distribution rate cap?**

7 **A.** I believe that a rate cap of this duration in the context of this contemplated acquisition
8 may have negative implications with the rating agencies and fixed income investors. I
9 would note that DLC and DLH's creditors already bear POLR risk. In the general
10 context of credit any restrictions which effectively limit a borrower's capability to
11 generate cash are viewed negatively. In addition I see a conundrum in the testimonies of
12 Mr. Kahal and Mr. Kalcic. On one hand, Mr. Kalcic suggests that DLC be required to
13 commit to its \$500 million capital expenditure program referenced in the direct testimony
14 of Mr. O'Brien, while on the other hand Mr. Kahal suggests that DLC be subject to a
15 distribution service rate cap. As it relates to credit quality this should be viewed
16 negatively. DLC would be put in a position whereby it would be forced to make capital
17 expenditures without timely recovery, thereby bearing increased leverage and increased
18 cost of capital. Limiting DLC's ability to seek a rate case for recovery of mandated
19 expenditures will not likely serve to enhance the creditworthiness of the utility.

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

21 **A.** Yes it does.

Exhibit JGS-1

Joseph G. Sauvage - Qualifications, Work Experience and Educational Background

Joe Sauvage is a Managing Director and Co-Head of Global Power. He joined Lehman Brothers in 1977 and has a wide variety of experience in the power and energy sectors working with both strategics and financial sponsors, including strategic advisory, financial restructuring, and equity and debt capital raising transactions.

Significant experience includes:

- The sale of Texas Genco to NRG, the initial public offering of ITC Holdings and the subsequent acquisition by ITC of Michigan Electric Transmission Company.
- The merger of Exelon Corporation with PSEG Enterprises.
- The restructuring of Edison Mission Energy, including the divestiture of its international generation business to International Power and Contact Energy.
- The divestiture of TXU's pipeline and gas distribution businesses to Atmos Energy.
- The sale of MidAmerican Energy Holdings to an investor group organized by Berkshire Hathaway.
- Gave advice to PG&E Corporation on the bankruptcy of the Pacific Gas and Electric Company and strategic alternatives regarding the National Energy Group.
- Additional experience includes acquisitions, divestitures and financings of electric utilities, merchant and contracted generation assets and gas pipelines for AES Corporation, Edison Mission Energy, and MEHC.

Mr. Sauvage is a Phi Beta Kappa and holds a B.A. degree, magna cum laude, in Economics from Washington University and an M.B.A. from the Wharton School at the University of Pennsylvania.

Regulated Utility M&A Transactions Since July 1, 2004

Acquirer	Target	Date of Announcement / Leak	Date of Completion	Form of Consideration	Premium to Price 1 Day Before Leak / Announcement	Premium to 30 Day Average Price Prior to Leak / Announcement
WPS Resources Corp	Peoples Energy Corp	7/6/2006	Pending	100% Stock	15%	12%
Macquarie Consortium	Duquesne Light Holdings	7/5/2006	Pending	100% Cash	22%	23%
Babcock and Brown	Northwestern Corp	4/25/2006	Pending	100% Cash	16%	17%
National Grid PLC	Keyspan Corp	2/25/2006	Pending	100% Cash	2%	18%
FPL Group Inc	Constellation Energy Grp Inc	12/14/2005	Terminated	100% Stock	9%	19%
MidAmerican	PacifiCorp	5/24/2005	3/21/2006	100% Cash	Private	Private
Duke Energy	Cinergy	5/9/2005	4/3/2006	100% Stock	13%	14%
Exelon	PSEG	12/17/2004	Terminated	100% Stock	12%	16%
PNM Resources	TNP Enterprises Inc	7/25/2004	6/6/2005	50% Cash / 50% Stock	Private	Private

Source: SDC and Lehman Brothers

Exhibit JGS-3

Numbers of Shares Sold Short as a Percentage of Fully Diluted Shares Outstanding as of June 30, 2006

As of June 30, 2006

Ticker Symbol	Company Name	Shares Sold Short ⁽¹⁾ (Millions)	Fully Diluted Shares Outstanding ⁽¹⁾ (Millions)	Shares Sold Short divided by Fully Diluted Shares Outstanding
DQE	Duquesne Light Holdings	10.0	78.5	12.7%
<i>Philadelphia Utility Index Companies (Ticker: "UTY")</i>				
AEE	Ameren Corp	5.8	200.8	2.9%
AEP	American Electric Power	4.2	391.0	1.1%
AES	AES Corp	7.2	664.6	1.1%
CNP	CenterPoint Energy Inc	11.8	346.0	3.4%
D	Dominion Resources Inc	5.2	344.4	1.5%
DTE	DTE Energy Co	5.1	176.1	2.9%
DUK	Duke Energy Corp	20.6	970.0	2.1%
EAS	Energy East Corp	7.9	147.5	5.3%
ED	Consolidated Edison Inc	9.3	244.7	3.8%
EIX	Edison International	3.9	332.0	1.2%
ETR	Entergy Corp	4.4	214.4	2.0%
EXC	Exelon Corp	19.5	676.0	2.9%
FE	First Energy Corp	3.7	330.0	1.1%
FPL	FPL Group Inc	29.4	385.7	7.6%
NU	Northeast Utilities	6.2	131.6	4.7%
PCG	PG&E Corp	7.4	397.0	1.9%
PEG	Public Service Enterprise Group Inc	3.1	244.4	1.2%
PGN	Progress Energy Inc	6.6	247.0	2.7%
POM	Pepco Holdings Inc	3.7	189.3	1.9%
SO	Southern Co	13.1	748.5	1.8%
TXU	TXU Corp	9.5	486.0	1.9%
XEL	Xcel Energy Corp	18.2	425.7	4.3%

UTY Average ⁽²⁾: 2.7%

1. Source: FactSet.

2. Arithmetic average.

Exhibit JGS-4

Regulated Utility Equity Offerings Since January 1, 2002

Pricing Date	Issuer	Total Amount Offered (\$ millions)	Market Capitalization Pre Offer (\$ millions)	% of Market Value	File to Offer % Change
12/7/06	Atmos Energy Corp	173.3	2,621.4	6.7%	(4.1%)
12/6/06	PNM Resources Inc	177.0	2,182.5	7.1%	(0.5%)
10/3/06	ITC Holdings	412.8	1,064.9	38.8%	3.2%
8/14/06	Cleco Corporation	163.9	1,227.6	13.7%	(3.2%)
8/10/06	Aqua America	79.3	2,989.6	2.7%	(2.8%)
6/15/06	Empire District Electric Company	76.8	543.2	14.5%	(7.2%)
5/23/06	Dynegy	185.2	1,685.9	11.2%	(6.5%)
5/17/06	Great Plains Energy	192.6	2,068.3	9.3%	(3.0%)
4/4/06	Ormat Technologies	142.9	1,142.6	12.8%	(14.4%)
1/25/06	NRG	1,169.2	3,974.6	29.7%	8.3%
12/6/05	Northeast Utilities	439.1	2,483.0	17.7%	3.2%
11/15/05	WPS Resources Corp	247.0	1,900.7	13.0%	(4.7%)
8/4/05	Plug Power Inc.	75.0	488.8	16.3%	(16.7%)
4/27/05	Pinnacle West Capital Corp	256.0	3,917.2	6.6%	(1.4%)
3/30/05	CMS Energy Corp	281.8	2,444.5	11.8%	(3.5%)
3/23/05	PNM Resources Inc	104.6	1,618.0	6.5%	(4.3%)
2/7/05	Southern Union Co	343.0	2,426.2	16.5%	0.0%
12/9/04	Idacorp Inc	105.0	1,145.8	9.2%	(4.9%)
12/7/04	Otter Tail Corp	73.8	663.1	11.1%	(5.3%)
11/18/04	AGL Resources Inc	297.7	2,026.2	14.7%	(3.8%)
11/9/04	Aqua America Inc	38.6	2,117.0	1.8%	(0.9%)
11/9/04	Cleco Corp	32.4	881.2	3.7%	0.0%
10/21/04	Atmos Energy Corp	346.5	1,547.3	22.4%	(1.7%)
10/7/04	CMS Energy Corp	259.4	1,214.3	21.4%	(2.7%)
9/9/04	MGE Energy Inc	35.0	600.9	5.8%	(1.5%)
9/9/04	Pepco Holdings Inc	250.3	3,323.8	7.5%	(5.4%)
8/18/04	Aquila Inc	117.3	499.0	20.4%	(17.2%)
7/26/04	Southern Union Co	206.3	1,255.7	16.4%	(2.9%)
7/13/04	Atmos Energy Corp	214.1	1,292.8	16.6%	(2.9%)
6/8/04	Great Plains Energy Inc	150.0	2,077.8	7.2%	0.3%
5/11/04	Consolidated Edison Co of New York	528.4	8,564.9	6.2%	(3.2%)
3/25/04	Westar Energy Inc	216.8	1,514.1	14.3%	3.8%
3/10/04	Hawaiian Electric Industries Inc	103.7	2,024.2	5.3%	(2.6%)
12/11/03	Empire District Electric Co	42.3	505.7	8.7%	0.7%
11/19/03	WPS Resources Corp	150.5	1,448.6	10.7%	(5.0%)
10/8/03	Sempra Energy	420.0	5,798.8	7.3%	(7.9%)
10/1/03	Public Service Enterprise Group Inc	344.4	9,491.5	3.6%	(0.6%)
9/11/03	FirstEnergy Corp	840.0	8,119.1	10.4%	(2.0%)
8/21/03	OGE Energy Corp	100.4	1,762.7	5.8%	1.9%
7/1/03	Alliant Energy Corp	288.8	1,811.0	16.1%	0.3%
6/18/03	Atmos Energy Corp	101.2	1,187.1	8.7%	0.0%
6/17/03	AES Corp	301.0	3,989.2	7.6%	(14.6%)
6/5/03	Southern Union Co	152.0	891.7	17.5%	8.2%
5/15/03	PPL Corp	248.6	6,591.0	3.9%	2.9%

Pricing Date	Issuer	Total Amount Offered (\$ millions)	Market Capitalization Pre Offer (\$ millions)	% of Market Value	File to Offer % Change
4/24/03	Black Hills Corp	108.0	645.4	17.5%	(3.6%)
2/27/03	American Electric Power Co Inc	1,047.5	7,118.8	14.8%	0.0%
2/11/03	AGL Resources Inc	123.2	1,269.8	9.9%	(3.7%)
1/14/03	Ameren Corp	222.8	6,279.6	3.6%	(1.6%)
12/17/02	Pinnacle West Capital Corp	179.6	2,699.7	6.7%	(0.9%)
11/25/02	TXU Corp	449.9	4,430.2	10.7%	(8.6%)
11/21/02	Great Plains Energy Inc	132.0	1,392.5	9.6%	1.5%
11/12/02	Public Service Enterprise Group Inc	398.3	5,135.3	7.8%	(2.9%)
11/6/02	NiSource Inc	658.8	3,820.9	17.3%	3.2%
10/15/02	Dominion Resources Inc	1,073.3	11,341.2	9.5%	2.9%
10/10/02	TECO Energy Inc	187.0	1,757.3	10.7%	(23.7%)
10/9/02	SCANA Corp	131.8	2,522.1	5.3%	(9.1%)
10/2/02	Northwestern Corp	87.5	248.5	36.5%	(15.5%)
9/25/02	Duke Energy Corp	1,000.1	15,261.3	6.6%	(4.6%)
9/12/02	PPL Corp	442.3	4,734.2	9.8%	(11.0%)
9/4/02	Ameren Corp	294.0	6,130.5	4.8%	(2.0%)
6/27/02	Aquila Inc.	281.3	1,072.5	26.4%	(32.6%)
6/20/02	El Paso Corp	897.8	9,749.6	9.2%	(7.4%)
6/20/02	Duquesne Light Holdings Inc	232.9	776.2	26.6%	(10.9%)
6/19/02	DTE Energy Co	237.9	6,777.3	3.5%	(10.7%)
6/6/02	FPL Group Inc	283.0	9,842.7	2.9%	(5.4%)
6/5/02	American Electric Power Co Inc	654.4	12,572.2	5.2%	(4.3%)
6/4/02	TECO Energy Inc	310.5	3,252.5	9.6%	(10.2%)
5/30/02	TXU Corp	562.7	13,316.5	4.3%	(5.8%)
5/16/02	Empire District Electric Co	51.9	430.8	12.7%	(3.5%)
4/24/02	Calpine Corp	759.0	3,550.8	21.4%	(13.7%)
3/14/02	NUI Corp	33.8	337.4	10.7%	(2.4%)
2/25/02	Xcel Energy Inc	450.0	7,817.8	5.8%	(3.2%)
2/26/02	Ameren Corp	197.5	5,492.3	3.6%	(6.0%)
1/24/02	Aquila Inc	253.0	3,006.1	8.5%	(9.2%)
	Mean				(4.5%)
	Median				(3.2%)

Source: Equidesk as of 1/2/2007. All U.S. Utilities marketed follow-on offerings greater than \$20 mm since 1/1/2002. Bolded deals denote companies in the UTY and in DQE's fairness opinion comps.

Published Rating Agency Reports

Standard and Poor's

"Research Update: Duquesne Light Holdings And Unit 'BBB' Rating Put On Watch Neg After Acquisition Announcement," July 5 2006.

Moody's Investor Service

"Moody's places ratings of Duquesne Light Holdings (Sr. Unsec. Baa3) and Duquesne Light Company (Sr. Sec. Baa1) Under Review for Possible Downgrade," July 5, 2006.

FitchRatings

"Fitch Comments on Duquesne Light Holdings following Acquisition Proposal," July 5, 2006.

STANDARD
POORS

RatingsDirect

RESEARCH

Research Update: Duquesne Light Holdings And Unit 'BBB' Rating Put On Watch Neg After Acquisition Announcement

Publication date: 05-Jul-2006
Primary Credit Analyst: Gerrit Jepsen, CFA, New York (1) 212-438-2529;
gerrit_jepsen@standardandpoors.com
Secondary Credit Analyst: Aneesh Prabhu, New York (1) 212-438-1285;
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Credit Rating: BBB/Watch Neg/NR

Rationale

On July 5, 2006, Standard & Poor's Ratings Services placed its 'BBB' corporate credit rating on electric transmission and distribution utility holding company Duquesne Light Holdings Inc. (DLH) and its utility subsidiary Duquesne Light Co. on CreditWatch with negative implications following the announcement that Macquarie Infrastructure Partners and Diversified Utility and Energy Trusts (DUETS), a unit of Macquarie Securities (USA) Inc., will acquire Duquesne for \$3.15 billion. The transaction is financed with a significant amount of debt and will increase consolidated debt by one-third.

Pittsburgh, Pa.-based Duquesne had \$1.05 billion of total debt and roughly \$150 million in preferred stock as of March 31, 2006.

The CreditWatch listing reflects our opinion that DLH's credit measures, which now support the 'BBB' rating, will likely weaken as a result of higher debt levels at closing. We will update the CreditWatch when appropriate as the acquisition progresses and as important credit events are addressed, such as:

- Resolution of pending tax disputes,
- The outcome of a current Pennsylvania delivery rate case, and
- The company's proposal for its provider-of-last-resort obligations beginning in 2008.

The final rating will incorporate our analysis of these issues and the final financing and legal structure of the new entity.

Also, the senior unsecured debt at DLH is rated one notch below the corporate credit rating to reflect its subordinated position to existing debt at subsidiary Duquesne Light. According to the company, DLH is contemplating refinancing of the operating company debt at the holding company level, which could result in senior unsecured debt being rated at the same level as the corporate credit rating.

Liquidity

Although DLH's internally generated cash should grow, the company will have negative free operating cash flow after capital expenditures and will require external funding for a portion of its higher than historical level of capital spending through 2008. The company's relatively high dividend payout, which has exceeded 60% in past years, further reduces internally generated cash flow available for capital spending. DLH, however, has adequate liquidity available, with \$22 million cash on hand as of March 31, 2006, and revolving

Exhibit JGS-5

credit facilities for Duquesne Light (\$150 million) and DLH (\$250 million) that both expire in July 2010.

As of March 31, 2006, these revolving facilities had \$225 million of available capacity after the inclusion of \$88 million in borrowings and \$87 million (including \$8 million at Duquesne Light) in LOCs related primarily to subsidiary DQE Financial Corp.'s affordable housing and landfill gas investments. As of April 30, 2006, available capacity was \$254.5 million after factoring in \$103 million in borrowings and \$42.5 million in LOCs. Liquidity will improve somewhat from a \$141 million equity contribution by the Macquarie consortium. DLH has sound liability management, with the next significant debt maturity due in 2008 (\$40 million) and none scheduled for several years afterward.

Ratings List

Ratings Placed On CreditWatch Negative

Duquesne Light Holdings Inc.

Corp credit rating	BBB/Watch Neg/--	BBB/Negative/--
Senior unsecured debt	BBB-/Watch Neg	BBB-

Duquesne Light Co.

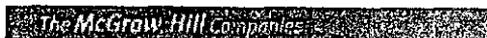
Corp credit rating	BBB/Watch Neg/--	BBB/Negative/--
Senior secured debt	BBB+/Watch Neg	BBB+

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Moody's Investors Service

Global Credit Research

Rating Action

5 JUL 2006

Rating Action: Duquesne Light Holdings, Inc.

MOODY'S PLACES RATINGS OF DUQUESNE LIGHT HOLDINGS (SR. UNSEC. Baa3) AND DUQUESNE LIGHT COMPANY (SR. SEC. Baa1) UNDER REVIEW FOR POSSIBLE DOWNGRADE**Approximately \$1.2 Billion Of Debt Affected**

New York, July 05, 2006 – Moody's Investors Service placed the ratings of Duquesne Light Holdings, Inc. (Holdings) and its primary operating subsidiary, Duquesne Light Company, under review for possible downgrade. This action follows today's announcement that a consortium led by Macquarie Infrastructure Partners, has signed an agreement to purchase 100% of the equity of Holdings for approximately \$1.6 billion. Ratings placed under review include the Baa3 senior unsecured debt of Holdings, and the Baa1 senior secured debt and Prime-2 commercial paper rating of Duquesne Light Company (the company has no commercial paper outstanding).

The announced transaction, which has been approved by Duquesne's Board of Directors, values the common equity of Holdings at \$1.6 billion; the Macquarie consortium will also assume Duquesne's existing debt, \$1.2 billion as of March 31, 2006 (including preferred and preference stock). The financing plan includes approximately \$770 million of incremental borrowings. The significant increase in additional leverage has the potential to result in a multi-notch downgrade for the holding company. Since the transaction is not expected to result in additional leverage at the operating company level, there is potential for a widening of the notching between Holdings and Duquesne Light Company. The acquisition remains subject to a number of regulatory approvals and is expected to close in the first quarter of 2007.

The review reflects the expectation that a significant amount of incremental debt will be incurred at the holding company level, resulting in a materially weaker financial profile, and considers that dividends from Duquesne Light are a primary source of cash for meeting the needs of the parent company.

The review will also consider that the company has significant capital needs to support announced asset acquisitions and capital improvement spending for utility operations. In addition, the company is currently in various stages of filing requests with the Pennsylvania Public Utility Commission and FERC for distribution and transmission rate base increases.

Headquartered in Pittsburgh, Pennsylvania, Duquesne Light Holdings is an electric utility holding company. Revenue for the year ended December 31, 2005 was \$922 million. Its primary operating subsidiary, Duquesne Light Company, is primarily engaged in providing transmission, distribution and supply of electricity to approximately 587 thousand customers in Southwestern Pennsylvania.

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Exhibit JGS-5



Fitch : Info Center : Press Releases

Fitch Comments on Duquesne Light Holdings following Acquisition Proposal Ratings

05 Jul 2006 3:11 PM (EDT)

Fitch Ratings-New York-05 July 2006: Fitch Ratings plans no immediate rating action for Duquesne Light Holdings, Inc. (Holdings), and its subsidiary Duquesne Light Company (DLC) following the announcement of a definitive agreement to be acquired by Macquarie Infrastructure Partners and Diversified Utility and Energy Trusts (Macquarie). As presently proposed, the acquisition will add considerable leverage, but also a well funded ownership with the ability to invest substantial new capital. Additional clarity regarding dividend policy and/or other management fees and future on-going capital management practices will be critical elements in determining the ultimate impact on ratings. Fitch will also consider whether traditional leverage measures are appropriate in this type of ownership structure or whether additional leverage can be supported.

Macquarie has agreed to pay \$1.59 billion for Holdings outstanding common stock (\$20 per share) and will assume approximately \$1.26 billion of consolidated debt and \$148 million of DLC preferred and preference shares. Macquarie intends to fund the acquisition with \$954 million of cash and a \$638 million term loan. Transaction costs and premiums associated with plans to refinance *certain existing debt* will add additional leverage. Macquarie will also contribute an additional \$141 million (\$16 per share) in new equity to assist the financing of Holdings previously announced acquisition of minority interests in the Keystone and Conemaugh generating stations. The incremental equity contribution replaces a previously planned equity offering for later this year. The financing plan will result in a consolidated capital structure of approximately 60% debt and 40% equity. The credit metrics of DLC are unaffected by the transaction.

The transaction is subject to regulatory approval by the Pennsylvania Public Utility Commission and Federal Energy Regulatory Commission, among others. For further information please refer to Fitch Rating's Duquesne Light Holdings, Inc. and Duquesne Light Company credit reports dated May 11, 2006.

Fitch's ratings for the Holdings and DLC are as follows:

Duquesne Light Holdings (formerly known as DQE Inc.):
 --Issuer Default Rating (IDR) 'BBB-';
 --Senior unsecured 'BBB-'.

Duquesne Light Company
 --IDR 'BBB-';
 --Senior secured 'BBB+';
 --Preferred stock 'BBB-';
 --Short-term 'F2'.

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**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Docket Nos. A-110150F0035 & A-311233F0002

DUQUESNE LIGHT COMPANY

STATEMENT 4R

**REBUTTAL TESTIMONY
OF FREDERICK J. EICHENMILLER
ON SERVICE QUALITY AND RELIABILITY**

1 Q. **Please state your full name and business address.**

2 A. My name is Frederick J. Eichenmiller. My business address is Duquesne Light
3 Company, 411 Seventh Avenue, Pittsburgh, PA 15219.

4 Q. **What is your position at Duquesne Light Company?**

5 A. I am currently employed as the Director of Rates and Regulatory Affairs.

6 Q. **How long have you worked at Duquesne Light?**

7 A. I have been employed by Duquesne Light Company ("Duquesne Light" or "the
8 Company") for over 33 years.

9 Q. **What are your qualifications and educational background?**

10 A. I have a Bachelor of Science Degree in Electrical Engineering from Grove City College,
11 and I am a graduate of the Management Program for Executives from the Katz Graduate
12 School of Business at the University of Pittsburgh. I am a licensed professional engineer
13 in the Commonwealth of Pennsylvania.

14 Q. **What has been your business experience?**

15 A. I began my career as an electrical engineer with Duquesne Light in 1973, and I have over
16 33 years of varied experience in line, staff and administrative positions. I have held line
17 positions related to almost all aspects of the distribution engineering, operations, and
18 operations support functions. In addition, from 1987 to 1989, I served as Executive
19 Assistant to the President, CEO and Chairman of Duquesne Light. Subsequently, I held
20 the position of Director of Operations Support, which provides supply chain (purchasing
21 and materials management), transportation and fleet management, and facilities
22 management services for the Company. Since then, I have had management and
23 leadership responsibilities for key processes that have direct impacts on system reliability
24 service restoration and customer satisfaction. Specifically, as Director of Work

1 Management and as Director of Operations and Underground, I have been responsible for
2 the company's work management processes, including operations and maintenance
3 management, construction, engineering, and vegetation management. In these positions,
4 I had oversight of the company's service centers located in communities throughout the
5 Duquesne Light service territory. In 2004, I assumed my current position as Director of
6 Rates and Regulatory Affairs.

7 **Q. Please describe your current responsibilities as the Director of Rates and**
8 **Regulatory Affairs.**

9 A. I am responsible for the oversight and direction of activities related to Duquesne Light's
10 rates and regulatory matters. My primary responsibilities are to assure continued
11 compliance with regulatory requirements, and to ensure that regulatory issues and
12 strategies are appropriately considered and deployed in Duquesne Light's business plans.
13 Additionally, the regulatory group is responsible for maintaining relationships with
14 regulators and legislators at the state and federal level. More recently, my position has
15 involved responsibilities relating to the development, oversight and direction of
16 Duquesne Light's recent distribution rate case filed at the Pennsylvania Public Utility
17 Commission ("Commission") and Duquesne Light's transmission rate case filing at
18 FERC. I am also responsible for Duquesne Light's filing to provide Provider of Last
19 Resort service commencing January 1, 2008, which filing will be made in the first quarter
20 of 2007.

21 **Q. What is the purpose of your rebuttal testimony?**

22 A. I will respond to proposals by the Office of Consumer Advocate regarding the
23 establishment of new and higher reliability and service performance standards for just
24 Duquesne Light. I will do so by:

- 1 ○ Documenting Duquesne Light's superior reliability and service quality
- 2 performance and explaining that this merger does not put that performance at risk;
- 3 ○ Explaining the service level standards, benchmarks, and reporting required by the
- 4 Commission to show that the scheme proposed by the OCA is unnecessary and
- 5 unfair; and
- 6 ○ Identifying quantitative service standards, should the Commission decide that
- 7 some additional standards are necessary in this proceeding.
- 8 ○ Addressing the proposed merger conditions relative to the implementation of a
- 9 two-prong solar energy initiative and why they are unwarranted.

10 **Q. Please summarize Ms. Alexander's testimony as you understand it.**

11 A. Ms. Alexander first appropriately acknowledges that Duquesne Light is currently
12 providing high quality service to its customers. She then opines that the proposed
13 acquisition of Duquesne Light Holdings ("DLH") by the Macquarie Consortium creates a
14 substantial risk that Duquesne Light's service quality will decline. She contends that
15 ratepayers should be protected against that risk by the imposition of a new set of
16 reliability and service quality standards applicable only to Duquesne Light and that
17 customers should be directly compensated for any violation of these standards through
18 rate refunds of up to \$2.8 million per year.

19 **Q. Do you agree with Ms. Alexander's concerns and her proposed solutions to those**
20 **concerns?**

21 A. No, I do not. There are several serious problems with Ms. Alexander's testimony.
22 Initially, there is simply no basis for Ms. Alexander's concerns regarding Duquesne
23 Light's service quality. Duquesne Light's service reliability and quality is excellent
24 today, and this result is expected to continue in the future. As explained in Mr. Leslie's

1 rebuttal testimony, the Macquarie Consortium is committed to a long-term investment in
2 Duquesne Light and fully understands the regulatory compact, including the obligation to
3 provide safe and reliable service to customers. Our commitment to provide high quality
4 service to customers will not change as a result of this transaction. As Mr. Leslie
5 explains, the transaction will improve Duquesne Light's access to capital which is
6 essential to continuing to provide reliable service. And, there will be an opportunity to
7 apply best practices to improve service and operating efficiency. All else equal, the
8 proposed transaction will only enhance our ability to provide quality service to our
9 customers.

10 In this regard, it should be emphasized that this is not the typical merger of two
11 utility operating companies, where there are likely to be substantial reductions in the
12 workforce and the relocation/centralization of utility operations. In that type of
13 transaction there may be legitimate concerns regarding future service quality that can be
14 appropriately addressed by the imposition of minimum service quality standards. Here,
15 however, we have a financial buyer, the Macquarie Consortium, which will not be
16 operating the utility. Existing utility management will continue in place in Pittsburgh,
17 and there should be no legitimate concerns regarding future service quality.

18 **Q. What has the PUC required with regard to reliability and service standards?**

19 **A.** Pennsylvania has adopted a system of standards with regard to reliability of service and
20 reporting requirements relative to customer service quality issues. The Commission has
21 established reliability benchmarks and standards for Duquesne Light in place today that
22 reflect sound industry performance measures. Reliability and customer service quality
23 performance is tabulated and reported by Duquesne Light consistent with Commission
24 set reporting requirements. This reporting is for a wide variety of customer service

1 metrics reflecting reliability, service restoration, customer call performance, complaints,
2 billing, meter reading and other matters.

3 The Commission's reliability benchmarks recognize that system reliability
4 measurement should reflect long-term trends. The Commission recognizes that there is a
5 certain amount of normal variability from year-to-year, which is to be expected,
6 particularly when looking at a relatively short time frame.

7 For that reason, the Commission set a 12-month Standard that is 20% above the
8 benchmark for all system reliability indices, and a three-year average Standard that is
9 10% above the annual benchmark. This standard for major EDCs is more stringent than
10 the standard for small EDCs.

11 The Commission states on its website that "Benchmarks are the Commission's
12 goals for each utility on the number and duration of outages. Reliability is considered
13 reasonable when the numbers fall between the benchmark and the percentage standards
14 described above." The Commission also states in its *Electric Service Reliability in*
15 *Pennsylvania: 2005* that: "If an electric distribution company's reliability performance
16 does not meet Commission standards, the Commission may require a report discussing
17 the reasons for not meeting the standard and the corrective measures the company is
18 taking to improve performance. In addition, Commission staff may initiate an
19 investigation to determine whether an electric distribution company is providing reliable
20 service."

21 **Q. What is Duquesne Light's performance with regard to its benchmarks and**
22 **standards?**

23 **A.** During the past several years, Duquesne Light has consistently performed better than the
24 reliability standards and benchmarks. Duquesne Light is second best in the state in

1 CAIDI and is the best in the state in SAIFI and SAIDI when compared to major EDCs.

2 OCA recognizes this overall level of performance in its testimony.

3 The chart presented by OCA on page 17 of its direct testimony is a good
4 representation of our performance and we believe it shows that Duquesne Light's
5 improvement initiatives have resulted in very strong service performance over the past
6 few years. No other utility in the state would be subject to such strict standards as
7 proposed by OCA.

8 In the Commission's Report, *Electric Service Reliability in Pennsylvania: 2005*,
9 it makes the following statements about Duquesne Light's levels of service reliability:

10 "Duquesne's overall performance continues to be better than the reliability
11 standard. In fact, Duquesne's 2005 CAIDI of 98 minutes was 10 minutes
12 better than the benchmark of 108 minutes."

13 "Duquesne's reliability performance falls well within the parameters of
14 acceptability for both CAIDI and SAIFI. CAIDI has remained
15 consistently below 100 minutes over the past several years. Interruption
16 frequency dropped to 0.98 in 2005, the lowest since 1997."

17 The Commission will begin enforcement of the three-year standard with the
18 submission of the annual reports due on or before April 30, 2007. Duquesne Light
19 supports this method of establishing standards.

20 **Q. Can you establish how Duquesne Light has achieved this high level of reliability**
21 **performance?**

22 **A.** There are many integrated practices and processes required to obtain and maintain these
23 high levels of reliability performance. There is no single silver bullet. I will briefly
24 identify several of these practices that significantly impact reliability performance.

25 (1) An Effective Vegetation Management (VM) Program.

26 Certainly the foundation and cornerstone of successful reliability effort in
27 Pennsylvania is contingent on a comprehensive vegetation control program. Duquesne

1 Light's Plan continues to maintain and have a positive impact on SAIDI and SAIFI trends
2 due to tree-related outages.

3 (2) Enhanced Protection and Fusing Program of the 23 KV Distribution System.

4 Duquesne Light has developed and deployed a program to modify the protection
5 scheme and to install strategically located line fuses on distribution system circuit
6 branches. This practice has proven to have a positive impact on SAIFI and enables
7 troubleshooters to locate and repair faulted portions of the distribution system more
8 quickly, positively impacting SAIDI.

9 (3) Formalized and Disciplined Service Restoration and Storm Preparedness
10 Processes.

11 Duquesne Light has a well defined storm plan which has proven to mitigate the
12 duration of storm damage and to provide effective communications with the public and
13 customers during these periods.

14 (4) An Automated 23 KV Distribution Control System with Centralized Control of
15 Line Sectionalizers.

16
17
18 Clearly Duquesne Light distinguishes itself from other utilities in the state and in
19 the country with the level of automation and sophistication of its automated distribution
20 control system. Duquesne Light extends its centralized control of automated devices well
21 beyond the typical distribution substation. With over 1,000 pole mounted sectionalizers
22 and reclosers, its operating professionals at its centralized distribution operations center
23 ("DOC") have immediate notification of disturbances on its 23 KV distribution system.
24 Additionally, within minutes and without dispatching line workers, DOC operators can
25 isolate the fault and through remote switching can redirect and restore service to large
26 blocks of customers. This system allows operators to access real time system conditions,

1 voltage and current, and to utilize remote switching to avert system overloads and other
2 abnormal system conditions.

3 **Q. Does the successful deployment of these reliability initiatives assure SAIDI, SAIFI**
4 **and CAIDI standards and benchmarks are achieved?**

5 A. No. While the successful completion and execution of these initiatives provides a high
6 level of assurance that Duquesne Light's customers receive the high levels of reliability
7 they expect, factors outside of Duquesne Light's control can have a significant impact on
8 actual results. Specifically, acts of nature and more severe weather patterns, contribute to
9 worsen reliability. For example, in July 2005, Duquesne Light's service territory
10 experienced a mid-size storm that contributed 10% of the total SAIFI for the year.

11 During the past three years Duquesne Light has experienced milder weather
12 patterns from normal and this has contributed to the high reliability statistics. Seasons of
13 worse than normal weather patterns, will cause reliability statistics to worsen from the
14 existing high levels. For these reasons it is not possible to commit to the level of
15 reliability that Ms. Alexander wishes to impose.

16 The Commission is well aware of the influence natural factors can have on
17 reliability and have introduced one-year and three-year standards for this exact reason.

18 **Q. Are the additional requirements proposed by Ms. Alexander necessary to insure**
19 **reliable service to customers?**

20 A. No, they are not. Ms. Alexander seems to ignore the fact that the Commission already
21 has very substantial powers to make sure that service quality does not deteriorate after the
22 proposed acquisition. For example, as noted previously we have a duty to provide
23 reliable service, and the PUC has detailed regulations and reporting requirements, ability
24 to open investigations and hear complaints, ability to order corrective actions and impose
25 civil penalties and to reflect any service inadequacy in rate decisions. Another current

1 example demonstrating the Commission's authority is the Notice of Proposed
2 Rulemaking (NOPR), revising Chapter 57 to implement Inspection and Maintenance
3 Standards at Docket L-00040167. This clearly demonstrates the PUC has the authority
4 and whereabouts to establish reliability standards and regulations and that the
5 introduction of new penalty oriented standards as Ms. Alexander would suggest, are
6 unnecessary and unproductive. In my view, the Commission clearly has more than ample
7 authority to address any service quality issues.

8 Ms. Alexander's proposals, reduced to their essence, would impose a completely
9 new and duplicative set of regulatory requirements which apply only to Duquesne Light
10 and nobody else. This is clearly not appropriate as part of a merger proceedings, and in
11 my view, would be extraordinarily poor public policy. The Commission has broad
12 powers regarding service quality and has exercised that authority to establish a
13 comprehensive set of regulatory requirements. There is no basis to establish a new set of
14 standards, where the utility is currently providing excellent service, and there is no
15 factual basis to conclude that this will not continue in the future.

16 **Q. Do you agree with the overall structure of the regulatory standards proposed by Ms.**
17 **Alexander?**

18 **A.** If OCA's proposal were to be adopted, this would send confusing signals to other utilities
19 and in my opinion, seriously harm future reliability in the Commonwealth. Utilities in
20 the state would try to just meet the existing Commission standards but never to do any
21 better. And, why would they ever try to perform better than the minimum standards if
22 they would end up with new, high standards difficult to maintain if they were to become
23 part of an acquisition or other transactions? There would be no reward for good
24 performance and a penalty imposed upon them later should there be an acquisition.

1 Essentially, utilities would be incented to maintain mediocre service and reliability. In
2 addition, I have several fundamental problems with her proposal. First, and most
3 importantly, I disagree with the "no fault" structure of Ms. Alexander's proposals. Under
4 her new system of regulation, Duquesne Light would be subject to severe financial
5 penalties for any negative fluctuation in a series of service and reliability parameters.
6 This reflects a fundamental misunderstanding of utility operations. Service quality and
7 reliability can vary, within reasonable limits, over time, for a variety of reasons which are
8 completely beyond a utility's control. Such variability proves nothing regarding the
9 overall quality of service provided. Also, as noted earlier, events outside our control can
10 significantly effect whether the company meets a standard. Further, it merits noting that
11 small EDCs (like UGI) have a 135% degree of latitude because of their smaller service
12 territories and fewer customers while Pennsylvania major EDCs are held to a higher
13 standard(120% degree of latitude) without regard to the size of their service territory.
14 Because of our small and concentrated service territory, a storm can have a
15 disproportionate effect on Duquesne.

16 Under OCA's proposal, Duquesne Light would be subject to significant financial
17 penalties for events that were entirely beyond its control. Ms. Alexander's proposals, in
18 this context, are irrational and fundamentally unfair. To the extent any new or more
19 stringent service quality service standards were to be imposed in this case, and I believe
20 they are unnecessary, they should be based on longer-term averages for utilities in the
21 Commonwealth and/or have a substantial "flexibility" to reflect normal variations. There
22 should not be automatic penalties. At a minimum, the Company should have an
23 opportunity, in an on the record proceeding, to explain the reasons for any decline in

1 service quality, with remedial measures imposed only where there is a finding supported
2 by substantial evidence that the utility was affirmatively responsible for any sustained
3 decline in service quality.

4 **Q. Do you have other problems with Ms Alexander's service compensation proposal?**

5 A. Yes, I do. Initially, her selection of 1% of revenues as a measure of penalties is
6 inherently arbitrary. A \$100,000 penalty for each percentage point decline in any of her
7 service metrics is equally arbitrary and unsupported. Even more troubling is Ms.
8 Alexander's statement that Duquesne Light would incur the maximum penalty only if
9 there were a catastrophic decline in service quality. This is simply false. A 2.8% decline
10 in each of the 11 would produce maximum penalty. This could be due to normal
11 variation or in the instance when a minor storm had an effect in SAIFI. Obviously, it
12 would take very little for Duquesne Light to incur the maximum penalty and the events
13 causing this could well be completely beyond our control. This is a very slippery slope.
14 The Commission should summarily reject such an arbitrary and unproductive approach to
15 service quality.

16 In addition, Ms. Alexander's proposal is biased and asymmetric. If we are to be
17 penalized for downward movement in indices, this should be offset by upward
18 movements in rates or rewards to encourage the Company to further improve.

19 I am not aware of any instance where the Commission has adopted Ms.
20 Alexander's service compensation proposal. In fact, I note that OCA proposed the
21 service compensation in the FirstEnergy/GPU Merger proceeding and the Commission
22 specifically rejected it, stating as follows:

23 "that the penalty and restitution provisions of the SQI should be
24 considered only as guides for the Commission's consideration in any
25 complaint brought before it as a result of the annual SQI report."

1 [96 Pa. PUC 1 at 19]

2 As I will explain later in this testimony, the Pennsylvania operations involved in
3 such merger, MetEd, Penelec and Penn Power, have significantly worse reliability
4 performance as compared to Duquesne Light. Given the Commission decision in the
5 FirstEnergy case it certainly should not adopt the service compensation proposal in this
6 case, where in contrast Duquesne Light has been providing excellent service.

7 **Q. What is your proposal regarding service standards?**

8 A. For the reasons set forth above, we do not believe there is any valid reason to impose
9 additional standards in this case. However, if any stiffer standards were to be adopted,
10 they should be the ones I will explain below. Finally, and perhaps most importantly, any
11 exceedence of those standards should be followed by a report from the Company
12 explaining the reasons for the departure from the standard and the actions the Company is
13 taking to improve service. The automatic and arbitrary imposition of a customer refund
14 is clearly inappropriate.

15 **Q. If the Commission concludes that service quality standards must be adopted as a**
16 **condition to the merger, what would be the appropriate standards?**

17 A. As noted, the Company has provided consistently high levels of service. If standards are
18 to be adopted they should reflect the levels of service provided by the Company in the
19 past, they should provide flexibility for events that the Company cannot control and they
20 should also reflect the levels of service that are being provided by other major electric
21 utilities in the Commonwealth.

22 **Q. How would you develop proposed standards?**

23 A. I would develop standards for two basic areas. These are service reliability and ease of
24 customer access to the company. I will explain why I do not believe that there should not

1 be standards for interactions with customers relating to payment of bills and collection of
 2 unpaid bills.

3 **Q. How would you develop service reliability standards?**

4 A. I would start with a review of the Company's performance as compared to the other
 5 major electric utilities in the Commonwealth. Set forth in Table 1 below are the
 6 performance statistics reported to the Commission for CAIDI, SAIFI and SAIDI for 2005
 7 as compared to the Commission benchmarks and standards for each company.¹

TABLE 1

Customer Average Interruption Duration Index (CAIDI)

EDC	2005	Benchmark	Standard
Allegheny Power	195	170	204
Duquesne Light	98	108	130
Met-Ed (FE)	122	117	140
Penelec (FE)	151	117	141
Penn Power (FE)	151	101	121
PECO	99	112	134
PPL	125	145	174

System Average Interruption Frequency Index (SAIFI)

EDC	2005	Benchmark	Standard
Allegheny Power	1.15	1.05	1.26
Duquesne Light	0.98	1.17	1.40
Met-Ed (FE)	1.70	1.15	1.38
Penelec (FE)	1.87	1.26	1.52
Penn Power (FE)	1.56	1.12	1.34
PECO	1.02	1.23	1.48
PPL	0.97	0.98	1.18

System Average Interruption Duration Index (SAIDI)

EDC	2005	Benchmark	Standard
Allegheny Power	224	179	257
Duquesne Light	97	126	182
Met-Ed (FE)	209	135	194
Penelec (FE)	284	148	213
Penn Power (FE)	236	113	162
PECO	100	138	198
PPL	121	142	205

¹ Pennsylvania Public Utility Commission *Electric Reliability in Pennsylvania: 2005*.

1 As can be seen from the table, Duquesne Light has essentially the highest level of
2 performance on each of these metrics and also has the second highest benchmarks and
3 standards on average. Accordingly, Duquesne Light is already being held to a very high
4 standard by the Commission, relative to its peers.

5 In my opinion, our customers are adequately protected by these benchmarks and
6 standards for reliability. Nonetheless, if the Commission believes that closer monitoring
7 is justified given the merger, I would suggest that the Commission require a report if both
8 the SAIFI and SAIDI metrics exceed 1.29 and 153, respectively.

9 **Q. How have you selected these metrics and why have you focused on SAIFI and**
10 **SAIDI?**

11 A. I have focused on SAIFI and SAIDI because the Company has the ability to implement
12 practices that directly impact these measures and has more direct ability to affect
13 performance. The CAIDI statistic is calculated by the division SAIDI/SAIFI.

14 The metrics I have chosen for SAIFI (1.29) and SAIDI (153), represent the
15 standards the Commission uses for Duquesne Light's three-year average performance.
16 Also shown in Exhibit FJE-1, are the three-year and one-year standards for each of the
17 major electric companies. If the Commission wishes to monitor for decline in reliability,
18 it could require an annual report during the two-year stay-out provided to the
19 Commission and OCA, OTS and OSBA if SAIFI or SAIDI both fall below the stricter
20 three-year standards in a one-year period. The report would provide an explanation of the
21 reasons for exceeding those levels and would provide a basis for determining whether
22 there is an indication that further actions need to be taken. I note that such report could
23 also explain that the one-year decline is the result of relatively high incidences of non-
24 major storms, which would indicate that the circumstances in the one-year period were

1 unusual and that no corrective action was necessary. This clearly puts Duquesne Light in
2 a position of tighter bandwidth of control and still utilizes a Commission approved
3 process of maintaining "standards" and "benchmarks."

4 For these reasons, there should be no automatic investigation. The Commission
5 can determine, based upon such report, whether an investigation of reliability is
6 necessary.

7 **Q. Please address Ms. Alexander's proposed service quality standards.**

8 A. I will first address standards she proposes in the area of ease of customer access to the
9 Company. These are: (1) Percentage of calls answered within 30 seconds; (2) average
10 busy out rate; and (3) average call abandonment rate. Shown in Table 2 below are the
11 Company's 2005 and average 2003 - 2005 performance compared to average 2003 -
12 2005 performance for Pennsylvania electric companies and the standard proposed by Ms.
13 Alexander.

TABLE 2

	Duquesne 2005 Performance	Duquesne 2003-2005 Performance	2003 - 2005 PA Electric Average	OCA's Proposed Standard
Percent Calls Answered Within 30 Seconds	80.2%	79%	75%	80%
Average Busy/ Out Rate	0.02%	2%	2%	0.05%
Average Call Abandonment Rate	3.10%	3%	4%	3.0%

14 As shown in Table 2, Ms. Alexander again would hold Duquesne Light to its
15 2005 performance and require Duquesne Light to pay service compensation to customers
16 even though it clearly and substantially exceeds the average performance of other
17 Pennsylvania electric utilities. We believe this to be both unreasonable and unnecessary.

1 The Company reports this data on an annual basis. Clearly the Commission has
2 the power to initiate an informal investigation, and, if necessary, a formal investigation if
3 Duquesne Light's exemplary performance declines substantially. I note also that these
4 are all call center activities. Since there is no plan to move or consolidate call center
5 activities, as there likely would be in a merger of operating utilities, there is no basis to
6 conclude that there is likely to be a significant decline in these metrics.

7 **Q. If the Commission concludes that there should be specific metrics for ease of**
8 **customer access, how should they be set?**

9 A. They should not be set based only on Duquesne Light's very high performance in 2005,
10 but should reflect average performance of Pennsylvania electric utilities.

11 **Q. Please address Ms. Alexander's proposed standards on billing and collection**
12 **activities.**

13 A. Ms. Alexander proposed standards with regard to timely issuance of bills, issuance of
14 reports on customer disputes, justified residential termination rates, justified residential
15 payment arrangement request rate and justified residential complaint rate.

16 As to issuance of bills, Ms. Alexander proposes that Duquesne Light guarantee
17 issuance of every bill on time every month with no exception. This is a standard of
18 perfection, and is unreasonable. There is no basis to conclude that issuance of bills will
19 be affected by this merger. Accordingly, no standard is necessary.

20 As to issuance of reports with regard to customer complaints, we do not agree that
21 it is productive to shorten the time period in issuing such reports. We take the time that is
22 necessary to investigate customer complaints to the Company carefully. In this regard, I
23 note that our rate of infraction of Commission regulations on complaints filed with the
24 Commission is only 0.05% on average for the three years ending December 31, 2005, as

1 compared to 0.10% on average for electric utilities. Clearly, the extra time and care that
2 is taken to review and resolve complaints is in the interest of our customers.

3 **Q. Please address Ms. Alexander's recommendations on customer termination.**

4 A. Ms. Alexander also recommends that Duquesne Light be held to a standard of 3%
5 termination per 1,000 residential customers. She notes our 2005 termination rate of
6 4.22% but states that this is not the result of changes in the Public Utility Code now
7 included in Chapter 14.

8 Ms. Alexander is incorrect in her conclusion about terminations and her
9 recommended standard would improperly interfere with Duquesne Light's ability to
10 collect delinquent accounts.

11 Duquesne Light's termination of customers increased in 2005 because
12 terminations have become more feasible as a result of regulatory changes and because
13 customers that can afford to pay bills were not paying them. I note that customers
14 reconnected also increased from 58% of those terminated in 2004 to 68% in 2005. These
15 activities reduced the arrearage balances from 2004 to 2005 by approximately 10%.
16 Duquesne Light should not be prohibited from using terminations to collect bills from
17 customers who can afford to pay them. I note in this regard that the Commission in its
18 recent management audit encouraged Duquesne Light to attempt to reduce uncollectible
19 expenses. In this regard, I also note that Duquesne Light has an active and expanding
20 Customer Assistance Plan ("CAP") which provides discounts to low-income customers.
21 Duquesne Light has the highest percentage in the Commonwealth of identified low
22 income customers enrolled in its CAP program (65%) and the highest rate of retention of
23 CAP customers (94%). The program effectively assists low income customers.

1 Q. Please address Ms. Alexander's proposal to establish standards for justified
2 residential payment arrangements and justified residential consumer complaints.

3 A. I note, again, that Duquesne Light performs well in these standards relative to the average
4 for other electric utilities. Shown on Table 3 below is a comparison of Duquesne Light's
5 performance, the performance of other electric companies and Ms. Alexander's proposed
6 standard.

TABLE 3

	Duquesne 2003-2005	Average PA Electric Company 2003-2005	OCA's Proposed Standard
Justified Residential Payment Arrangement Request Rate	1.9	1.34	2.45
Justified Residential Consumer Complaint Rate	0.10	0.26	0.10

7 If standards are to be adopted with regard to residential complaint rates, we see no
8 reason for a standard in excess of that achieved on average by other companies. As to
9 residential payment arrangement request rate, we note that OCA's standard would be
10 acceptable if the Commission concludes that a standard is necessary, because it reflects
11 the fact that Duquesne Light has a higher percentage of payment troubled customers than
12 the average Pennsylvania electric company. However, we are concerned with developing
13 standards for these matters because the statistics require subjective determinations as to
14 whether arrangements to pay bills offered by the company and complaints by customers
15 about such arrangements are "justified." These matters are not black and white and do
16 not easily convert to a conclusion that the Company acted improperly. Furthermore, as
17 with termination of customers, these standards could unreasonably interfere with the
18 ability of the company to recover unpaid bills.

1 **Q. What is Duquesne Light's opinion with regard to proposed annual performance**
2 **standards for Lost Time Accident Rate proposed by OCA?**

3 A. Incidents concerning lost time generally are incurred by union employees located in the
4 field performing utility maintenance and construction work. Work environment and
5 safety are governed by the Occupational Safety & Health Act (OSHA). We report
6 regularly to OSHA, the agency, on incidents, our safety program, and compliance issues.
7 Also, OSHA regularly performs audits of our safety and incident reports. So this is an
8 area that is already fully regulated by government.

9 Moreover, this is an area that does not affect rates or customer service and quality,
10 areas which are governed by the PUC. The work environment is an area that affects
11 labor and union matters which the PUC avoids regulating. As such, we recommend that
12 the Commission not adopt the OCA's request to regulate this labor matter and conditions
13 negotiated by the union and the Company.

14 **Q. What are Duquesne Light's intentions with regard to customer service and**
15 **reliability?**

16 A. Duquesne Light's approach to reliability and service has been to develop and implement
17 best in class practices and to continue to advance processes that improve service to our
18 customers. We wish to be very clear that Duquesne Light and Macquarie Consortium
19 have no intention to have Duquesne Light's service deteriorate. We will commit that
20 reliability and service standards will not deteriorate as a result of the merger. We cannot
21 commit, however, that the high levels of performance will not deteriorate due to
22 circumstances out of our control or for other reasons. Duquesne Light continues to spend
23 large amounts of money on its infrastructure to try to maintain and improve reliability.
24 As performance improves, it becomes harder and harder to further improve reliability. If
25 standards are set at the higher levels of reliability, many reasons outside of the control of

1 Duquesne Light could cause Duquesne Light to fail to meet such higher standards.

2 Duquesne Light and our customers have enjoyed better than normal weather patterns for
3 the last 3 years. If we return to more normal weather patterns with more frequent storms,
4 the reliability service quality statistics could fluctuate negatively without any fault of
5 Duquesne Light. This is why we feel it is inappropriate to require Duquesne Light to
6 abide by new and very strict standards. Again, it is our intent to not only maintain
7 service but to try our very best to improve performance. But some of that is not within
8 our sole control.

9 **Q. Please summarize the key points of your rebuttal as it relates to Mr. Hughes'**
10 **testimony.**

11 A. Initially, I will state that Messrs. O'Brien and Leslie will respond to Mr. Hughes'
12 assertions that the merger, as proposed, does not provide the requisite substantial
13 affirmative benefits in their rebuttal testimony. I will focus solely on Mr. Hughes'
14 proposed solar energy merger conditions. Specifically, I will explain why this
15 proceeding is not the proper forum for these proposals, particularly in light of Duquesne
16 Light's recent financial and operational commitments to the development of renewable
17 energy in its service territory in our recently approved rate case settlement. In addition,
18 with our publically stated intent to file our POLR IV plan in the 1st quarter of 2007, the
19 issues raised by Mr. Hughes are best suited to be addressed in that proceeding and in
20 Pennsylvania's competitive electric and alternative energy markets.

21 **Q. Mr. Eichenmiller, would you please discuss those provisions of Duquesne Light's**
22 **recent base rate case settlement that are relevant to the solar energy initiatives**
23 **raised by Mr. Hughes?**

24 A. Absolutely. While it appears that Mr. Hughes acknowledges Duquesne Light's general
25 commitment to the environment, he fails to note our recent commitment to the

1 development of renewable energy technology in settling our recent base rate case.

2 Specifically, the Pennsylvania PUC recently approved the unanimous settlement reached

3 in Duquesne Light's base rate case, which provides that:

- 4 • Duquesne Light will evaluate other parties' proposals relating to energy
5 conservation and education, time of use metering and economic development in
6 developing its POLR IV plan; and
- 7 • Duquesne Light's agreement to provide \$1.5 million/year for four years in
8 shareholder contributions to the Pennsylvania Energy Development Authority
9 beginning in 2007 to fund renewable energy projects that meet the requirements
10 of Tier 1 technologies specified in the Alternative Energy Portfolio Standards Act
11 ("Act 213"), which includes solar.

12 It is clear from these settlement provisions that Duquesne Light's commitment to
13 renewable energy development and the environment is more than "aspirational." The
14 facts are that Duquesne Light has recently provided tangible and very substantial benefits
15 to the environment and to our customers in this regard.

16 **Q. In light of the Company's recent commitments to renewable energy development, do**
17 **you agree with Mr. Hughes that further commitments are warranted as part of the**
18 **merger?**

19 **A.** No, I do not. The additional expenditures associated with the "utility-driven" solar
20 energy program evaluation (unspecified cost) and customer solar grant program (\$4
21 million) are ill-advised and unwarranted at this time. As set forth in the Commission-
22 approved settlement of our rate case, the \$6.0 million in Duquesne Light contributions
23 will be administered by PEDA to fund renewable energy projects the meet the
24 requirements of Tier 1 technologies which includes solar energy as defined in

1 Pennsylvania's Alternative Energy Portfolio Standards Act. 73 P.S. §1648.2. Thus a
2 merger condition requiring Duquesne Light to expend additional funds and resources to
3 establish a company operated renewable energy program would be unnecessary as our
4 financial commitment to PEDDA will serve to largely address the concerns raised by Mr.
5 Hughes, the development of solar technology in our service territory.

6 **Q. Mr. Hughes appears to support the idea of Duquesne Light establishing and**
7 **operating utility sponsored solar energy programs, do you agree?**

8 A. I would recommend that the Commission reject the solar energy initiatives proposed by
9 Mr. Hughes in their entirety. As noted above, Duquesne has already agreed to provide \$6
10 million over the next four years to PEDDA for use in promoting the development of
11 renewable energy programs targeted to meet the Tier 1 requirements of Act 213. As
12 PEDDA's mission is to promote the development and use of Pennsylvania clean,
13 indigenous energy resources and to stimulate economic development and job
14 development in Pennsylvania's energy section, they are best equipped to establish or
15 invest in such initiatives. In my opinion, it would be best to allow the Pennsylvania's
16 competitive markets, PEDDA and renewable energy providers to undertake the
17 development of these sort of initiatives. Further, it would be a waste of resources to
18 require Duquesne Light to expend funds and staff resources on what appear to be largely
19 redundant activities. Also, it is important to note that Pennsylvania has established both
20 competitive retail electric and alternative energy markets. To require Duquesne Light to
21 provide additional funding beyond the commitments made in its recent rate case is clearly
22 unwarranted.

23 **Q. Are there other processes or mechanisms in place to ensure that renewable**
24 **applications are implemented in the provision of electric service?**

25 A. Without question. Under Pennsylvania's Alternative Energy Portfolio Standards Act,

1 Duquesne Light will continue to foster the development of renewable energy
2 technologies in Pennsylvania by its obligation to gradually increase the percentage of
3 electricity sold to our default service customers derived from alternative energy sources.
4 It is worth noting that Act 213 includes a "solar share" provision. That is, Act 213
5 provides a specific obligation for Duquesne Light relative to the use of solar photo-
6 voltaic resources to comply with its Act 213 obligations. Thus, solar energy will receive
7 heightened interest by Duquesne Light and the emerging alternative energy market as we
8 proceed into our POLR IV proceeding.

9 **Q. How does Duquesne Light intend to meet its Act 213 obligations?**

10 A. As noted above, Duquesne Light is currently working on its fourth transition plan for
11 providing default service (POLR) as the current plan expires December 31, 2007. As a
12 result the company will be filing its POLR IV plan for new default service provisions in
13 the very near term. In light of the passage of Act 213, Duquesne Light's POLR IV plan
14 will specifically address how we intend to meet our Act 213 obligations as our
15 compliance period under Act 213 begins on January 1, 2008. Therefore, it is my
16 opinion that the issue of solar energy initiatives in the merger case is misplaced as it is
17 more appropriate for these discussions to be considered in the impending POLR IV
18 proceeding which is expected to be filed in the first quarter of 2007.

19 **Q. How do you respond to Mr. Hughes position that if Duquesne does not implement**
20 **his solar energy conditions it will not fulfill its stated commitment to customers, the**
21 **environment and communities?**

22 A. The stated commitment to which Mr. Hughes refers is simply that "the Macquarie
23 Consortium and Duquesne Light share a strong commitment to customers, the
24 environment and to the communities in which they provide service." Duquesne Light's
25 strong commitment is already shown through its current efforts to benefit its customers,

1 the environment and the community and this commitment will continue. As a result, Mr
2 Hughes recommendations are not required for Duquesne Light to show its commitment.

3 **Q. Do you have any additional concerns relative to the proposed solar conditions**
4 **recommended by Mr. Hughes?**

5 A. Yes. Based upon a settlement term in the PECO/Unicom merger, Mr. Hughes
6 recommends that Duquesne be required to commit an additional \$4 million in
7 shareholder-funding to establish the "Duquesne Company Solar Initiative." As
8 demonstrated in the attached Citizen Power interrogatory responses, our attempts to
9 identify the specifics of Mr. Hughes' proposal and supporting evidence of the local
10 customer interest, the potential for success of such a program in southwestern
11 Pennsylvania and an appropriate funding mechanism for the solar energy initiative
12 proposed by Mr. Hughes yielded little information. (Exhibit FJE-2) Again, while it is my
13 opinion that this issue is best suited for our upcoming POLR IV proceeding, I conclude
14 that it would be ill advised for the Commission to earmark \$4 million in funding to a
15 program which is ill defined, focused solely on the generation of solar energy and that
16 lacks any specifics including a cost/benefit study.

17 **Q. Please summarize your testimony.**

18 A. As to reliability and service quality, Duquesne Light has provided the best overall service
19 of the major electric utilities in recent years. This does not happen without a commitment
20 from Senior Management to service. There is no basis to conclude that our Senior
21 Management team will reverse course because of the merger. The Commission has
22 standards of service and requires utilities to report as to their progress in meeting such
23 standards and Duquesne Light has put in place processes and facilities that will continue
24 to provide the best assurance that it will continue to provide a very high level of service

System Average Interruption Duration Index

Exhibit FJE -1

Company	2003	2004	2005	2003-2005		12-Month Standard	3-Yr Avg Standard
				3-year Average	Benchmark		
Duquesne Light	110	95	97	101	126	182	153
Allegheny Power	270	216	224	237	179	257	217
FE - Penn Power	192	172	236	200	113	162	136
FE - Penelec	239	248	284	257	148	213	179
FE - Met-Ed	140	197	209	182	135	194	163
PPL	107	173	121	134	142	205	172
PECO	103	106	100	103	138	198	167

System Average Interruption Frequency Index

Company	2003	2004	2005	2003-2005		12-Month Standard	3-Yr Avg Standard
				3-year Average	Benchmark		
Duquesne Light	1.30	1.03	0.98	1.10	1.17	1.40	1.29
Allegheny Power	1.25	1.13	1.15	1.18	1.05	1.26	1.16
FE - Penn Power	1.51	1.43	1.56	1.50	1.12	1.34	1.23
FE - Penelec	1.60	1.77	1.87	1.75	1.26	1.52	1.39
FE - Met-Ed	1.23	1.54	1.70	1.49	1.15	1.38	1.27
PPL	0.88	1.09	0.97	0.98	0.98	1.18	1.08
PECO	1.00	0.98	1.02	1.00	1.23	1.48	1.35

Customer Average Interruption Duration Index

Company	2003	2004	2005	2003-2005		12-Month Standard	3-Yr Avg Standard
				3-year Average	Benchmark		
Duquesne Light	85	92	98	92	108	130	119
Allegheny Power	216	190	195	200	170	204	187
FE - Penn Power	127	120	151	133	101	121	111
FE - Penelec	149	140	151	147	117	141	129
FE - Met-Ed	114	128	122	121	117	140	129
PPL	121	159	125	135	145	174	160
PECO	103	104	99	102	112	134	123

DUQUESNE LIGHT COMPANY, ET AL.
DOCKET NOS. A-110150F0035 AND A-311233F0002
RESPONSES OF CITIZEN POWER, INC.
TO INTERROGATORIES OF DUQUESNE LIGHT COMPANY SET I

satisfy the substantial affirmative benefits test without providing any environmental benefit.

INTERROGATORY NO. 2

2. On page 7 of Mr. Hughes' testimony, it is recommended that Duquesne be required to fund a solar program similar to the one in place in the PECO service territory.
- (a) Identify the proceeding in which such program was adopted, provide all testimony exhibits and data/interrogatory responses relating to environmental proposals in such proceeding and provide a copy of any settlement, recommended decision and final order in such proceeding.
- (b) Were there contentions by PECO or any other party in such proceeding that there would be synergy savings available to fund such program in the proceeding identified in answer to part (a)? If so, provide all testimony and exhibits referencing such synergy savings.
- (c) Were there alleged benefits to PECO or its affiliated companies resulting from combination of generation assets as a result of the transaction in which PECO agreed or was directed to adopt its "Solar Initiative?"

RESPONSE TO INTERROGATORY NO. 2

- 2(a) It is Mr. Hughes' understanding that the solar program in the PECO service territory described in his testimony was funded and implemented as the result of a settlement in PUC Docket No. A-00110550F0147, *Application of PECO Energy Company Pursuant to Chapters 11, 19, 21, 22 and 28 Of the Public Utility Code, For Approval Of (1) A Plan of Corporate Restructuring Including the Creation of a Holding Company and (2) The Merger of the Newly Formed Holding Company and Unicom Corporation*. Although Mr. Hughes recalls reading the Commission order approving the settlement when it was issued, Citizen Power was not a party to this PUC proceeding, and, to the best of Citizen Power's knowledge after reasonable search, Citizen Power does not have any of the documents requested in the question in its possession, custody or control. Citizen Power notes that PUC-issued documents in the case are generally available on the Commission's website. Citizen Power further notes that, in addition to the extensive information about the solar program included in Exhibit DH-2, certain information about the solar program in the PECO territory is available on the website of the Sustainable Development Fund for the PECO territory: <http://www.trfund.com/sdf/index.html>.

Sponsor: David Hughes
Executive Director
Citizen Power, Inc.

DUQUESNE LIGHT COMPANY, ET AL.
DOCKET NOS. A-110150F0035 AND A-311233F0002
RESPONSES OF CITIZEN POWER, INC.
TO INTERROGATORIES OF DUQUESNE LIGHT COMPANY SET I

- 2(b) Mr. Hughes does not know whether any such contentions were made. See also the response to subpart (a) above.
- 2(c) Mr. Hughes is not certain what the question means by "combination of generation assets." To the extent Duquesne is requesting information concerning allegations that the proposed PECO-Unicom merger would provide power supply benefits to PECO and its affiliates as a result of a merger with a company that may have controlled generation assets, Mr. Hughes does not have any knowledge of any such allegations. To the extent the question is asking whether there were allegations that PECO and/or its affiliates would benefit from diversifying its power supply portfolio by increasing its solar power resources, Mr. Hughes is unaware of specific allegations in the PUC proceeding that a solar program would benefit PECO. However, it is Mr. Hughes' understanding, as set forth more fully in his testimony and exhibits, that both "utility driven" and "customer driven" solar programs such as the ones described by Mr. Hughes generally are expected to provide benefits to utilities implementing such programs. See also the response to subpart (a) above.

INTERROGATORY NO. 3

3. Has Citizen Power made any comparison of the number of customers likely to be interested in a "Solar Initiative" in PECO's versus Duquesne's service territory? If so, please provide such analysis.

RESPONSE TO INTERROGATORY NO. 3

No.

INTERROGATORY NO. 4

4. Referencing to page 9 of Mr. Hughes' testimony, concerning the proposed expansion of LIURP to 4,000 customers per year:
- (a) Is it Mr. Hughes' position that all customers of LIURP at or below 150% of the poverty level will be willing to participate in the LIURP funding?
- (b) Provide all information available to Citizen Power concerning LIURP participation levels (percent of customers contacted that agree to participate) by utility in Pennsylvania.

Sponsor: David Hughes
Executive Director
Citizen Power, Inc.

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Docket No. A-110150F0035

Docket No. A-311233F0002

**Duquesne Light Company
DQE Communications Network Services, LLC**

Statement No. 5R

REBUTTAL TESTIMONY OF SUSAN S. BETTA

1 **Q. Please state your full name and business address.**

2 A. My name is Susan S. Betta. My business address is 411 Seventh Avenue, Pittsburgh,
3 PA 15219.

4
5 **Q. What is your position at Duquesne Light Company ("Duquesne Light" or**
6 **"Company")?**

7 A. I am the Controller at Duquesne Light.

8
9 **Q. What are your qualifications, work experience and educational background?**

10 A. I graduated from Franklin & Marshall College with a Bachelor of Arts degree in
11 Accounting in 1991. I was employed with KPMG Peat Marwick as an auditor for
12 seven years, and I was a Senior Manager when I left the firm. I have been employed
13 with Duquesne Light or an affiliate of Duquesne Light since 1999. I spent the first
14 year at an affiliate, DQE Financial, and have spent the past seven years at Duquesne
15 Light. I have been Controller at both Duquesne Light Holdings ("DLH") and
16 Duquesne Light since August 2003. My current responsibilities include overseeing
17 the accounting, reporting and budgeting functions for Duquesne Light and DLH.
18 Prior to August 2003, I served in various positions at the company, including
19 Assistant Controller of both DLH and Duquesne Light. I am a Certified Public
20 Accountant, and a member of both the Pennsylvania and American Institutes of
21 Certified Public Accountants.

22

1 Q. Have you ever testified before this Commission?

2 A. I provided written testimony before the PUC at Docket No. R-00061346 – Duquesne
3 Light’s most recent distribution base rate proceeding.
4

5 Q. Please briefly describe the subject matter for your testimony in this proceeding.

6 A. The purpose of my testimony is to respond to issues raised by Richard J. Hudson, Jr.
7 in his testimony submitted in this case on behalf of Strategic Energy, LLC
8 (“Strategic”) and the Retail Energy Supply Association (“RESA”). Specifically, I
9 will address issues Mr. Hudson raised regarding the potential anticompetitive effects
10 of alleged direct or indirect cross-subsidization of Duquesne Light Energy (“DLE”) by other
11 Duquesne Light companies, and the extent, if any, to which the proposed
12 merger may exacerbate these purported effects.
13

14 Q. Please summarize your conclusions.

15 A. DLH and Duquesne Light properly allocate costs among their subsidiaries and/or
16 affiliates and have protections in place to separate regulated and unregulated business
17 activities. This conclusion has been confirmed by two recent audits by independent
18 regulatory bodies. Further, while Duquesne Light has a full-requirements supply
19 agreement with Duquesne Power (“DP”) to supply default service for residential and
20 small commercial and industrial customers, that supply agreement does not
21 improperly subsidize the business activities of Duquesne Light’s retail affiliate, DLE.

22 Finally, Duquesne Light agreed as part of the Commission-approved settlement of
23 its recent distribution rate case to submit an analysis addressing whether any portion

1 of Duquesne Light's operations is subsidizing its affiliates, including its affiliate
2 electric generation supplier, DLE, as part of our upcoming Provider of Last Resort
3 ("POLR") IV filing. We have completed that analysis, and based on that analysis we
4 have made several minor revisions to our cost allocation process. I will also describe
5 these revisions in this testimony.

6
7 **I. Cost Allocation Procedures**

8
9 **Q. Describe how the Company identifies work performed by Duquesne Light
10 employees for its affiliates, including both DLE and DP?**

11 A. Duquesne Light uses a two-step process to ensure costs are assigned and allocated to
12 the proper corporate entity. First, where appropriate, costs are directly assigned to
13 affiliates to ensure that the relevant cost is accurately reflected at the proper company.
14 For example, affiliate employees, rent and office supplies, are directly accounted for
15 and incurred by the affiliates to ensure that these costs are separated from the
16 regulated utility or DLH. Second, Duquesne Light's and DLH's administrative costs
17 are reviewed to determine those functions that provide services to affiliates, so that an
18 appropriate allocation of these costs can be made.

19
20 **Q. Do Duquesne Light's affiliates have employees of their own, and do they have
21 their own directly incurred costs?**

22 A. Yes, there are employees at essentially all of Duquesne Light's affiliates, and there is
23 a separate payroll processed for each of these companies, such that the salaries and

1 related incentive compensation for these employees are captured directly at the
2 affiliates. In addition, the affiliates incur their own direct charges for items such as
3 consultants, computers, copiers, office supplies, and other items.
4

5 **Q. Are there certain Duquesne Light costs that are either directly assigned to**
6 **affiliates, and if so, please provide an example of the types of costs, and describe**
7 **how the assignment or allocation is determined?**

8 A. Duquesne Light assigns certain costs to the affiliates, such as rent, insurance,
9 healthcare benefits for employees of the affiliates, as well as other general expense
10 items, such as cell phones, for example. In order to determine the amount of rent
11 charged to each affiliate for the amount of space affiliate employees occupy in our
12 headquarters building, the budgeting department receives an annually updated
13 drawing of the building identifying the space occupied by each cost center or affiliate.
14 Based on the amount of square footage each affiliate occupies, along with an
15 allocation of the common space in the building, the amount of rent to be assigned to
16 the affiliate is determined. In fact, both DP and DLE, along with other affiliates, are
17 parties to sublease agreements with Duquesne Light that have been filed with and
18 approved by the Commission. These subleases pass on Duquesne Light's costs under
19 the master lease agreement.

20 The process followed for insurance is similar. If there is a specific insurance
21 policy that relates solely to the affiliate, it is directly assigned, with this determination
22 made annually by our insurance department. In addition, Duquesne Light has
23 contracts with healthcare providers to provide benefits to all of its and its affiliates'

1 employees. The affiliate employees are separately identified so that we can
2 accumulate the healthcare and dental benefits used by the affiliates' employees and
3 charge them for the costs incurred. For affiliate employees who have cell phones or
4 other electronic devices for which there is a separate monthly charge, our information
5 technology department has each device separately identified such that the affiliate is
6 charged directly for the actual amount incurred by its employees.
7

8 **Q. Are the affiliates directly charged costs associated with any letters of credit or**
9 **surety bonds issued on their behalf?**

10 A. Yes, letter of credit and surety bond fees are charged directly to the affiliate that
11 requires these items.
12

13 **Q. Please explain your administrative allocation process.**

14 A. The administrative allocation process begins when cost center managers submit their
15 budgets for the following fiscal year. The budgets are prepared on an annual basis,
16 including detail by month. The budget templates compiled by cost center managers
17 include a page for affiliate charges. On this page, cost center managers list each
18 employee who provides services to an affiliate. If a cost center manager's budget
19 includes specific expenses pertaining to an affiliate, that cost is also identified, so it
20 can be properly allocated to the affiliate.
21

22 **Q. How is the information from each of the cost center managers compiled?**

1 A. Once all of the cost center templates have been completed and returned to the
2 Budgeting Manager of Duquesne Light, the affiliate charges from each cost center are
3 assembled on one report called the "Monthly Administrative Costs Allocation." This
4 report identifies the costs allocated to affiliates on a monthly basis. In calculating the
5 monthly charge for employees who provide services to affiliates, the employee's
6 salary, incentive compensation and fringe benefits are included. This process ensures
7 that fully loaded employee costs are allocated to affiliates.
8

9 **Q. Is the information updated during the year, or are the initial allocations used for**
10 **the entire year, regardless of changes that may occur?**

11 A. Each cost center manager receives notification at the beginning of each quarter of the
12 current cost allocations, including the percentage of the time being allocated as well
13 as a detailed listing of other costs that are being allocated. The cost center managers
14 are asked to verify that both the percentage of time and total cost allocations for the
15 most recent quarter are appropriate, or to indicate how the amounts should be updated.
16 In addition, the cost center managers are asked to provide revised estimates of the
17 percentage of time and other cost allocations that should be utilized for the quarter
18 that has just begun. Once this information has been collected by the Budgeting
19 Manager, a true-up entry is made for any revisions required for the quarter that has
20 just ended, and the new allocation amounts are entered into the Monthly
21 Administrative Costs Allocation report. These amounts then become the allocation
22 for the quarter until the beginning of the following quarter, at which time the
23 verification and revision process is repeated. In mid-December, the fourth quarter's

1 allocations are verified with the cost center managers such that any final adjustments
2 required for the year can be made in the month of December in order to properly
3 reflect the costs for the year.
4

5 **Q. Do you believe that cost center managers are aware of the importance of these**
6 **cost allocations to affiliates?**

7 A. Yes, I do for two reasons. First, effectively managing budgets is a priority at
8 Duquesne Light. Cost center managers are held accountable to ensure that they are
9 properly managing costs and resources. Second, either the Budgeting Manager or I,
10 as part of our annual budgeting process, spoke directly with almost every single cost
11 center manager who allocates costs to affiliates. During these conversations, we
12 discussed the process that they and their employees use to determine the allocations
13 to affiliates.
14

15 **Q. Do you allocate costs to affiliates for either the revolving credit arrangement**
16 **maintained by DLH or any guarantees provided by DLH on behalf of affiliates?**

17 A. A portion of the fees associated with DLH's revolving credit arrangement is allocated
18 to the affiliates, who benefit from its availability. DLH also has provided some
19 parent guarantees on behalf of affiliates, but since there is no specifically incurred
20 cost related to the issuance of this guarantee, no allocation of costs is appropriate.
21

22 **Q. Has the Company recently conducted a more detailed review of its cost**
23 **allocation procedures?**

1 A. Yes, as I noted above, Duquesne Light agreed, as part of the settlement of its most
2 recent distribution rate case, to submit an analysis addressing whether any portion of
3 Duquesne Light's operations is subsidizing its affiliates, including its affiliate, DLE
4 as part of our upcoming POLR IV filing with the PUC.
5

6 **Q. Has the Company completed this analysis, and have you implemented any**
7 **changes to your cost allocations as a result of this analysis?**

8 A. We have completed this analysis, and have implemented some changes to our cost
9 allocations. For example, in preparing that analysis we discovered that we had not
10 historically charged affiliates a general corporate overhead allocation to cover items
11 such as a rent charge for the percentage of space occupied by employees who provide
12 services to an affiliate, and a supplies charge for supplies the employee may use in
13 providing services to affiliates. As a result, we reviewed our allocations, and as of
14 December 31, 2006, a general corporate overhead allocation was calculated in order
15 to charge affiliates for these costs in 2006. The amount of this general corporate
16 overhead allocation was not material. This allocation will be used in the future as
17 well to ensure that affiliates are charged appropriately for this overhead cost.
18

19 **Q. Were there other changes resulting from the analysis performed for the POLR**
20 **IV case?**

21 A. Yes, our analysis showed that the historical focus of the cost center managers has
22 been on allocating costs out of the regulated utility, Duquesne Light, to ensure that
23 ratepayers are not paying for costs properly allocated to unregulated affiliates.

1 However, in certain instances these costs were simply allocated out to DLH and were
2 not reallocated to an affiliate.

3
4 **Q. Can you provide an example?**

5 A. There are employees, such as myself, as an example, who do not perform a day-to-
6 day function that is directly related to one affiliate, but rather provide general
7 oversight to all affiliate companies. In instances such as this, there was an allocation
8 of the employee's time out of Duquesne Light, but this allocation may have been
9 made to the parent company, DLH, instead of to one or more affiliates, such as DP or
10 DLE.

11
12 **Q. Have you taken any action to augment this allocation process?**

13 A. Yes we have. We believe that our affiliates should be allocated their appropriate
14 share of costs based on the scope and nature of the work and services provided, and
15 thus as of December 31, 2006, we have allocated a portion of the costs that would
16 have otherwise resided at DLH to Duquesne Light's affiliates, including DP and
17 DLE. We will continue these allocations in the future as well to ensure that
18 Duquesne Light's affiliates are charged appropriately.

19
20 **Q. Are any costs incurred at DLH allocated to Duquesne Light and other affiliates?**

21 A. Yes, as an example, the cost associated with the Chief Executive Officer's (CEO)
22 office was incurred at DLH, and a portion of this cost was allocated to Duquesne
23 Light. As of December 31, 2006, we have also allocated a portion of the CEO office

1 costs to Duquesne Light's affiliates, including DP and DLE. We will continue these
2 allocations in the future as well to ensure that Duquesne Light's affiliates are charged
3 appropriately.
4

5 **Q. Has the Federal Energy Regulatory Commission ("FERC") recently conducted**
6 **an audit of DLH or its subsidiaries?**

7 A. Yes, the Division of Audits within the Office of Enforcement of FERC has recently
8 completed an audit of Duquesne Light to determine whether: (1) Duquesne Light is in
9 compliance with Standards of Conduct and OASIS (open access same time
10 information system) requirements; (2) Duquesne Light's transmission practices are in
11 compliance with applicable FERC rules and regulations as well as applicable open
12 access transmission tariffs; and (3) DLH's wholesale electricity marketing unit is in
13 compliance with its market-based rate authority.
14

15 **Q. What period did the FERC audit cover, and could you provide a few details?**

16 A. The audit covered the period from January 1, 2004 through February 28, 2006. The
17 audit was conducted by approximately six FERC employees with assistance on a
18 more limited basis from others. It has lasted for over a year and is nearing the
19 issuance of a final report.
20

21 **Q. Did the FERC audit review cost allocations?**

22 A. Yes, there was a thorough analysis of cost allocations, and it was determined by
23 FERC that our cost allocation procedure is proper and accurate. FERC, in its draft

1 report, recommended that we perform a further check of actual cost allocations by
2 confirming, after the fact, employees' actual allocation of time. We have already
3 implemented this recommendation through the procedures we described above,
4 whereby final adjustments are made in the month of December in order to properly
5 reflect the costs for the year.
6

7 **Q. Did the PUC recently conduct a management audit of Duquesne Light?**

8 A. Yes, in 2005 we had a thorough audit by the PUC staff. Cost allocation was reviewed
9 in detail by the PUC and found to be appropriate and accurate.
10

11 **Q. So two recent audits have reviewed this alleged subsidization issue raised by Mr.
12 Hudson and found your procedures to be fair and proper?**

13 A. Yes. Both the PUC and FERC have found no cross-subsidization. Also, in the FERC
14 order approving the proposed merger, issued on December 22, 2006, FERC
15 specifically examined whether the merger could cause cross-subsidization between
16 the utility and other energy affiliates. FERC found no concerns in the merger order
17 and found that there was no cross-subsidization.
18

19 **IV. Duquesne Light's Full-Requirements Supply Agreement with Duquesne Power**
20

21 **Q. Duquesne Light has a full-requirements supply agreement with DP. Does DP
22 have a full-requirements supply obligation with any other company?**

1 A. Yes, in addition to being the full-requirements supplier to Duquesne Light, DP also
2 has a separate full-requirements supply obligation to another affiliate, DLE.
3

4 **Q. What is DP required to provide under the full-requirements contract it has with**
5 **Duquesne Light?**

6 A. Duquesne Light's full-requirements supply agreement with DP covers the costs
7 (including energy, capacity, related ancillary services and other costs and risks)
8 associated with default service. The supply agreement was filed with the
9 Commission in Duquesne Light's POLR III proceeding and clearly delineates DP's
10 supply obligations related to default service supply and the total price for those
11 services. DP is responsible for planning, procuring, and scheduling electricity supply
12 to serve Duquesne Light's default service load. These costs are incurred at DP and
13 are recovered in the rates charged to Duquesne Light.

14 Since this arrangement deals with wholesale power costs, FERC regulates this
15 matter. FERC approved DP selling power to DLC at market-based rates in 2004.
16 After review, FERC explicitly granted a waiver from the affiliate standard.
17 Additionally, as noted above, FERC's recent audit found no subsidization as well, nor
18 anything improper or inappropriate with this wholesale power agreement.
19

20 **Q. How is DP compensated under this arrangement?**

21 A. The compensation paid to DP is based on the rates charged to POLR customers
22 supplied by Duquesne Light. Those rates were subject to hearings and Commission
23 review and ultimately approved by the Commission. The Commission determined

1 that Duquesne Light demonstrated that these rates represented prevailing market
2 prices over the POLR III period. Furthermore, PJM costs related to administration,
3 market expansion, and other management services are explicitly recovered in
4 Duquesne Light's generation rates charged to retail customers as specified in
5 Duquesne Light's Retail Tariff, Rider 1. These PJM costs are not included in the
6 distribution rates charged by Duquesne Light. Duquesne Light charges its POLR
7 customers a generation rate based on the number of kW and/or kWh consumed.
8 From this amount, Duquesne Light remits a payment to DP net of Pennsylvania gross
9 receipts tax. This is the total compensation that DP receives from Duquesne Light
10 under its full-requirements supply arrangement.
11

12 **Q. Is Duquesne Light paying DP for services such as scheduling, load balancing, or**
13 **ancillary services for both Duquesne Light and DLE?**

14 A. No, DP only receives compensation under the full-requirements contract with
15 Duquesne Light for the costs associated with providing default service. Duquesne
16 Light does not pay DP for such costs related to unregulated supply to DLE. The
17 supply agreement was developed and the POLR III rates were proposed in 2003.
18 DLE did not begin actively marketing to retail customers until late 2004.
19

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

21 A. Yes.
22

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

**Docket No. A-110150F0035
Docket No. A-311233F3002**

**Duquesne Light Company
DQE Communications Network Services, LLC**

Statement No. 6R

REBUTTAL TESTIMONY OF NEIL S. FISHER

1 I. **Introduction**

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

3 A. My name is Neil S. Fisher. My business address is 30 Monument Square, Suite 105,
4 Concord, MA 01742.
5

6 Q. **What is your current position?**

7 A. I am a Principal with The NorthBridge Group ("NorthBridge"), an economic and
8 strategic consulting firm for the electric and natural gas industries. NorthBridge has
9 advised Duquesne Light Company ("Duquesne" or "the Company") on restructuring
10 matters for many years. I have advised Duquesne on rate design and rate matters,
11 including issues relating to its provider-of-last-resort service ("POLR" or "default
12 service") since the start of retail access, including Duquesne's pilot, POLR I, POLR II,
13 and POLR III programs. Most recently, I have been assisting the Company develop its
14 default service filing for the period 2008 through 2010.
15

16 Q. **Please describe your educational and professional experience.**

17 A. I graduated from Swarthmore College with a Bachelor of Arts degree in Economics with
18 Honors. I graduated from Yale University with a Masters in Business Administration. I
19 joined NorthBridge in 1993. Before that, I worked as a consultant at Putnam, Hayes &
20 Bartlett, where I concentrated on electric and natural gas restructuring. As a consultant, I
21 have assisted regulated electric utility clients in several states design default service and
22 prepare for retail access. I have also developed strategies for unregulated retail electric
23 providers interested in participating in retail markets throughout the United States.

1 Q. Did you sponsor direct testimony in this proceeding?

2 A. No.

3

4 Q. Have you testified previously before the Pennsylvania Public Utility Commission
5 (“Commission”)?

6 A. Yes, I testified in Docket R-00061346, Duquesne’s most recent distribution rate case,
7 Docket P-00032071, Duquesne’s Petition for Approval of Plan for Post-Transition Period
8 POLR Service (“POLR III”), and in Docket P-00021969, Duquesne’s Petition Requesting
9 Modification to POLR II Plan to Permit Participation in PJM. I also participated in
10 Duquesne’s POLR II collaborative led by several Pennsylvania Commissioners.

11

12 Q. What is the purpose of your rebuttal testimony?

13 A. I address the concerns and recommendations voiced by Witness Richard J. Hudson, Jr.,
14 on behalf of Strategic Energy (“Strategic”) and certain unidentified members of the Retail
15 Energy Supply Association (“RESA”),¹ that the proposed acquisition of Duquesne Light
16 Holdings (“DLH”) by the Macquarie Consortium (“Macquarie”) “may have
17 anticompetitive effects that will frustrate the continued development of a competitive
18 retail market for electricity in Duquesne’s service territory.”² I do not respond to Mr.
19 Hudson’s statements and recommendations regarding the economic development
20 discounted rate program. This issue is addressed in Mr. O’Brien’s rebuttal testimony.

21

¹ As stated in footnote 1 of Mr. Hudson’s testimony, it is not clear which members of RESA support the views expressed in his testimony.

² SE/RESA Statement No. 1 at 3 (emphasis added).

1 Q. Please summarize your conclusions.

2 A. I conclude that Mr. Hudson's arguments are without merit and that his recommendations
3 should not be implemented. Specifically, I conclude that:

- 4 • Mr. Hudson's arguments are based on speculative assumptions that cannot be
5 supported.
- 6 • Specific claims made by Mr. Hudson to support his arguments are incorrect:
 - 7 a) Duquesne Light Energy's ("DLE") small number of employees does not
8 support Mr. Hudson's conclusion that DLE is being subsidized by other
9 Duquesne companies.
 - 10 b) Contrary to Mr. Hudson's claims, the economies of scale that Duquesne
11 Power ("DP"), Duquesne's unregulated wholesale supplier, may achieve by
12 supplying wholesale power to both DLE and Duquesne are available to other
13 wholesale suppliers in the market, so DLE receives no unfair advantage by
14 being supplied by DP.
 - 15 c) Duquesne's POLR rates do not subsidize DLE, and Mr. Hudson provides no
16 specific evidence that Duquesne's recently approved distribution rates
17 subsidize DLE.
 - 18 d) DLH's credit support to DLE does not represent an unfair advantage for DLE
19 over other competitive suppliers.
- 20 • Even if Mr. Hudson's arguments had merit, this does not suggest that the
21 Commission should reject the proposed acquisition.
- 22 • The Commission should not adopt Mr. Hudson's recommended measures to
23 mitigate his unsubstantiated anticompetitive claims, because the recommended

1 measures are not in the best interests of retail customers in Duquesne's service
2 territory, may potentially harm retail competition, and do not help to assure
3 compliance with the Competition Act.

4 Each of these conclusions is described in more detail below.

5
6 **II. Mr. Hudson's Arguments Are Based On Speculative Assumptions That Cannot Be**
7 **Supported**

8 **Q. Please summarize Mr. Hudson's main arguments.**

9 A. Mr. Hudson's main arguments are as follows. Macquarie is willing to pay above the
10 book value of DLH stock, so given the relative growth potential of the competitive retail
11 supply business, Macquarie must be planning for DLE to aggressively compete in this
12 business to recover its investment.³ Mr. Hudson believes that further competition from
13 DLE is likely to have anticompetitive effects, because, as Mr. Hudson states, "...we have
14 reason to believe that Duquesne is supporting the competitive operations of DLE through
15 cross-subsidies from other Duquesne companies, thus enabling DLE to consistently
16 undercut its competitors' prices."⁴ Mr. Hudson's suspicions regarding cross-subsidies to
17 DLE from other Duquesne companies are primarily based on the fact that DLE has a
18 relatively small number of employees.⁵ In addition, Mr. Hudson also believes that DLE
19 is provided an anticompetitive advantage by receiving a DLH parental guarantee to
20 support DLE's RTO membership activities and a DLH parental guarantee to DP which

³ SE/RESA Statement No. 1 at 5-6.

⁴ SE/RESA Statement No. 1 at 5.

⁵ SE/RESA Statement No. 1 at 8-9.

1 appears to negate the need for DLE to post collateral in its supply agreement with DP.⁶
2 As a result, he concludes that the acquisition, as currently proposed, should not be
3 approved by the Commission.⁷ As an additional reason not to approve the proposed
4 acquisition, Mr. Hudson contends that, "...the evidence supports the conclusion that
5 Duquesne and the Macquarie Consortium have a substantial interest in pursuing a POLR
6 IV plan that is not in the best interest of promoting a competitive market in the Duquesne
7 service territory."⁸

8
9 **Q. Do you believe that Mr. Hudson's arguments are well supported?**

10 A. No. Mr. Hudson's arguments are based almost entirely on speculation and he presents
11 very little concrete evidence.

12
13 **Q. Please provide some examples.**

14 A. As one example, Mr. Hudson argues that, in the area of power procurement, there is an
15 apparent but unquantifiable cross-subsidization of DLE by other Duquesne companies,
16 and this contention is primarily based on the fact that DLE has fewer employees than
17 some other competitive retail suppliers.⁹ As a second example, Mr. Hudson states that it
18 is likely that Macquarie would prefer that Duquesne propose a POLR IV plan that harms
19 retail competition.¹⁰ It is important to recognize that this argument involves speculation
20 that Duquesne might propose a certain type of plan to the Commission in the future. This

⁶ SE/RESA Statement No. 1 at 12-13.

⁷ SE/RESA Statement No. 1 at 3-4.

⁸ SE/RESA Statement No. 1 at 7.

⁹ SE/RESA Statement No. 1 at 8-12.

¹⁰ SE/RESA Statement No. 1 at 6-7.

1 argument does not provide evidence that DLH or any of its companies will practice
2 anticompetitive or discriminatory conduct. The Commission has the right to consider and
3 decide on Duquesne's POLR IV plan after it is filed based on its merits. As a third
4 example, Mr. Hudson submits that the proposed transaction is predicated on a business
5 strategy which involves growing DLE's generation supply business, and this assumption
6 is somehow supported by observing the price that Macquarie is proposing to pay for
7 DLH.¹¹ Putting aside the question of why Mr. Hudson believes that competition from
8 DLE is anticompetitive, it is clear that Mr. Hudson is somehow trying to speculate what
9 the merged company's corporate strategy will be, based on the price proposed by
10 Macquarie to acquire DLH. Mr. Leslie of Macquarie specifically addresses these
11 allegations in his rebuttal testimony.

12
13 **Q. What do you conclude in general about Mr. Hudson's arguments?**

14 **A.** Mr. Hudson's arguments have little merit, given the fact that they are based on a high
15 level of speculation and very little concrete supporting evidence.

16
17 **III. Specific Claims Made By Mr. Hudson to Support His Arguments Are Incorrect**

18 **Q. Please evaluate specific claims made by Mr. Hudson.**

19 **A.** Specific claims made by Mr. Hudson to support his arguments are incorrect. I will
20 respond to four allegations upon which he bases his arguments.

21 First, DLE's small number of employees does not support his conclusion that
22 DLE is being subsidized by its affiliates. DLE, like companies in many industries, has

¹¹ SE/RESA Statement No. 1 at 5.

1 the right to outsource certain business functions rather than retaining in-house employees
2 to perform these functions. For example, DLE is provided legal and administrative
3 services from other DLH companies, and DLE compensates these companies for the
4 services they provide. Duquesne witness Ms. Betta describes how such costs are
5 allocated. It is my understanding that DLE also outsources a significant portion of its
6 supply portfolio management activities (including planning, procuring, scheduling, and
7 hedging), and has contracted with DP for full requirements supply. DP (and/or the
8 entities that DP may contract with to help it manage its supply portfolio) must manage
9 these load obligations and the associated price and quantity risks. Without this full
10 requirements contract, DLE would be responsible for actively managing these obligations
11 and risks, and would require more in-house employees to do so. But because DLE has a
12 full requirements supply contract, and because it outsources other business functions, it is
13 possible that DLE can operate without a large number of employees. This allows DLE to
14 focus its efforts on retail marketing and not duplicate functions that can be provided more
15 efficiently by others. Furthermore, it is also highly possible that DLE chooses not to be
16 involved in certain business areas or offer services that some other competitive retail
17 suppliers do. This too could allow DLE to operate with fewer employees. For example,
18 DLE operates only in the Pittsburgh area, whereas some other retail suppliers expend
19 substantial resources to compete in many markets. It is also possible that DLE serves
20 larger size customers than other competitive suppliers. This also could affect the
21 relationship between the MWH served and the number of employees for a given
22 competitive supplier and any comparison across suppliers. Thus, I think it is

1 inappropriate to draw any conclusions about the existence of subsidies based on the
2 number of employees at DLE.

3 Second, contrary to Mr. Hudson's claims, any economies of scale like those
4 which DP may achieve by supplying power to both DLE and Duquesne are achieved by
5 other wholesale suppliers in the market, so DLE receives no unfair advantage by being
6 supplied by DP. Mr. Hudson's argument that DLE obtains an unfair advantage appears
7 to be conditioned on the assumption that, except for DP, no wholesale electric supplier
8 already has existing supply agreements from which it can build economies of scale. This
9 is entirely false. Competitors of DLE are free to contract with a variety of wholesale
10 electric suppliers, including DP. Many of these wholesale suppliers, like DP, already
11 have existing supply agreements with other parties from which they may be able to build
12 economies of scale. Therefore, DLE receives no unfair advantage simply because DP
13 provides POLR supply to Duquesne.

14 Third, contrary to Mr. Hudson's claims and suspicions, DLE receives no cross-
15 subsidies through Duquesne's regulated POLR supply rates. Mr. Hudson believes that
16 cross-subsidies are likely, as he questions how DP appropriately allocates the costs and
17 risks associated with meeting the load obligations of both Duquesne and DLE.¹² I
18 participated in developing the supply contract between DP and Duquesne, and throughout
19 the development of the contract, there was only consideration of Duquesne's default
20 service supply requirements. Furthermore, the contract was filed with the Commission as
21 a part of testimony in the POLR III proceeding, and the Commission ultimately approved
22 the POLR supply rates that were based on the pricing in the contract. It is also important

¹² SE/RESA Statement No. 1 at 11.

1 to note that at the time when the contract between DP and Duquesne was developed and
2 the POLR III supply rates were proposed in 2003, DLE did not even exist. DLE was
3 established about a year later in 2004. Therefore, I find it extremely hard to believe that
4 DP could have tried to recover DLE-related costs in the rates charged to Duquesne
5 several years before DLE ever existed. Finally, there is absolutely no support to any
6 claim that the costs incurred by DP or DLE associated with the contract between DP and
7 DLE are included in Duquesne's recently approved distribution rates.

8 Fourth, DLH's credit support to DP or to DLE does not provide an unfair
9 advantage to DLE over other competitive suppliers. Yet, Mr. Hudson incorrectly claims
10 that DLE is provided an unfair advantage in the form of a parental guarantee to support
11 DLE's RTO membership activities, and a parental guarantee to DP which appears to
12 negate the need for DLE to post collateral in its supply agreement with DP.¹³ Mr.
13 Hudson ignores the fact that other competitive retail suppliers are also provided similar
14 guarantees. In fact, Strategic's parent company, Great Plains Energy, Inc., has provided
15 \$122 million of guarantees to support Strategic's power purchases and regulatory
16 requirements.¹⁴ Similarly, Constellation Energy Group, CNE's parent company, reports
17 that its "contingent obligations increased \$4.4 billion during 2005, primarily due to the
18 issuance of additional letters of credit and guarantees by the parent company for
19 subsidiary obligations to third parties in support of the growth of our merchant energy
20 business."¹⁵ Meanwhile Direct Energy's parent, Centrica, has annual revenues of \$33

¹³ SE/RESA Statement No. 1 at 12-13.

¹⁴ Great Plains Energy, Inc., *Form 10-K*, Fiscal year ended December 31, 2005, at 47-48.

¹⁵ Constellation Energy Group, Inc., *Form 10-K*, Fiscal year ended December 31, 2005, at 61.

1 billion from businesses scattered throughout the world and claims that credit support
2 from Centrica “reduces costs and gives competitive advantage.”¹⁶

3
4 **Q. Do Mr. Hudson’s arguments and contentions have merit?**

5 **A. No. They are unsubstantiated and without merit.**

6
7 **IV. Even If Mr. Hudson’s Arguments Had Merit, This Does Not Suggest That the**
8 **Commission Should Reject The Proposed Acquisition**

9 **Q. Even if Mr. Hudson’s arguments had merit, does this suggest that the Commission**
10 **should reject the proposed acquisition?**

11 **A. No. His arguments do not relate to the acquisition.**

12
13 **Q. Please explain why Mr. Hudson’s arguments do not relate to the acquisition.**

14 **A. None of Mr. Hudson’s arguments show that the proposed acquisition is likely to result in**
15 **anticompetitive or discriminatory conduct. Instead, all of Mr. Hudson’s arguments relate**
16 **to Duquesne and its affiliates’ alleged current or future actions whether or not the**
17 **acquisition is approved.**

18 For example, Mr. Hudson identifies the competitive retail supply business as a
19 business with relatively high growth potential, and he predicates one of his arguments on
20 the assumption that a Macquarie-owned company will aggressively compete in the
21 competitive retail supply business through DLE.¹⁷ If there truly is the potential for
22 growth in this business, then DLE will aggressively compete regardless of whether the

¹⁶ “Centrica in North America,” December 6, 2005, at 18.

¹⁷ SE/RESA Statement No. 1 at 5-6.

1 acquisition is completed. Even Mr. Hudson realizes this, as he cites DLH's 2005 Form
2 10-K to support his contentions about DLE's strategy, and this 10-K was filed long
3 before the acquisition was proposed. So, there is no evidence that approval of the
4 proposed acquisition will affect DLH's or DLE's current or future strategy.

5 As another example, Mr. Hudson argues that DLE has an unfair advantage over
6 its competitors due to cross-subsidies from DLH and/or DLE's other affiliates. Once
7 again, Mr. Hudson's contentions have nothing to do with the proposed acquisition;
8 instead, they are simply complaints about DLE as it exists today, whether or not the
9 acquisition is approved.

10 As a third example, Mr. Hudson states that it is likely that a Macquarie-owned
11 company has a substantial interest in pursuing a certain type of POLR IV plan.¹⁸ Mr.
12 Hudson provides no valid reason why Duquesne's preference with respect to its POLR
13 IV filing would be any different if the acquisition were not approved, so once again, Mr.
14 Hudson's contention has nothing to do with the acquisition. The Commission has the
15 right to consider and decide upon the POLR IV filing after it is filed. The merits of that
16 filing should not be considered in this proceeding and are independent of the acquisition.
17 The outcome of the POLR IV filing will apply regardless of whether the Commission
18 approves the Macquarie acquisition.

19
20 **Q. Given that many of Mr. Hudson's arguments do not relate to the proposed**
21 **acquisition, would it be more appropriate for Mr. Hudson to instead voice his**
22 **complaints in other forums?**

¹⁸ SE/RESA Statement No. 1 at 7.

1 A. Yes. Mr. Hudson's arguments are based on complaints that DLE has an unfair
2 competitive advantage, and that Duquesne is likely to file a POLR IV plan that the
3 companies he represents do not like. With respect to Mr. Hudson's first complaint, DLE
4 is a Commission-licensed electric generation supplier ("EGS"). Mr. Hudson can voice
5 his complaints about DLE at the Commission if he believes that DLE is in any way
6 engaging in anticompetitive or discriminatory conduct. The Electricity Generation
7 Customer Choice and Competition Act created EGSs, who are specifically authorized to
8 serve the competitive retail electricity market. Affiliates of public utility companies are
9 permitted to be EGSs, assuming they meet the registration and licensing requirements for
10 fitness as established by the Commission. In fact, many of the EGSs in the state today
11 are affiliates of public utilities. Without them, the market would offer far fewer options
12 and choices to customers. Protections and safeguards have been established in the
13 Commission's regulations to assure that there is no unfair advantage to affiliated EGSs.

14 With respect to Mr. Hudson's second complaint, I am certain that if any of the
15 companies Mr. Hudson represents do not like any aspect of any future POLR filing made
16 by Duquesne, they will have ample opportunity to express their opinions about such
17 filing in the POLR proceeding that will be initiated after the filing is made.

18
19 **V. The Commission Should Not Adopt Mr. Hudson's Recommended Measures**

20 **Q. What does Mr. Hudson recommend to mitigate his alleged anticompetitive effects of**
21 **the proposed acquisition?**

22 **A. Mr. Hudson states that the "...merger approval must be conditioned on Duquesne**
23 **submitting a POLR IV plan which provides an open and transparent competitive**

1 procurement process that results in market responsive pricing. In addition, DP should be
2 precluded from participating in that process."^{19,20} Furthermore; Mr. Hudson recommends
3 that the Commission initiate an investigation to determine whether DLE's unregulated
4 operations are being supported by its affiliates, and should condition its approval of the
5 proposed acquisition on the outcome of this investigation.²¹

6
7 **Q. Do you agree that merger approval should be conditioned on Duquesne submitting**
8 **a POLR IV filing that relies on an open and transparent competitive procurement**
9 **process?**

10 **A.** No. It is not in the interest of retail customers to place restrictions on the type of POLR
11 plan that Duquesne may propose and the Commission may consider. I also believe that it
12 is not appropriate to address this issue in this proceeding. The method in which
13 Duquesne obtains electric supply for default service is an issue for the POLR proceeding.

14 Furthermore, the Competition Act does not require any specific method of
15 procuring default service supply. Section 2807 (e)(3) of the Competition Act requires
16 that at the end of the transition period when a utility completes its stranded generation
17 cost recovery, the electric distribution company or Commission-approved alternative
18 supplier "shall acquire electric energy at prevailing market prices and shall recover fully
19 all reasonable costs." While Duquesne acquires electric energy at prevailing market
20 prices, it should not be forced to procure its electric supply in a particular manner. A
21 given procurement method may not be appropriate in all market circumstances for all

¹⁹ SE/RESA Statement No. 1 at 16.

²⁰ In the alternative, Mr. Hudson requests that the Commission consolidate the instant proceeding with Duquesne's upcoming POLR IV case.

²¹ SE/RESA Statement No. 1 at 17.

1 customers. Other states allow default service suppliers discretion in how they obtain
2 electric supply.²² The Commission should not limit itself to a single approach to
3 procurement that may impose additional costs and/or risks on retail customers and may
4 potentially harm retail competition.

5 Prevaling market prices may be established using several methods. For example,
6 market prices could be established by relying on comparisons with other market prices in
7 the region, through a market price index formula, or by a solicitation. In fact, Duquesne
8 already has experience supplying and establishing "prevailing market price" default
9 service rates using each of these different methods,²³ and the Commission explicitly
10 recognized in Duquesne's POLR III proceeding that "a competitive procurement process
11 is not the exclusive method to arrive at a prevailing market price."²⁴

12 Finally, it is interesting to note that, contrary to its position in this case,
13 Strategic's own proposal in Duquesne's post-transition period POLR III proceeding did

²² For example, default service suppliers in Texas and in New York, which have relatively high levels of retail shopping, do not rely on a mandated type of procurement process and have allowed default service suppliers discretion in how they obtain supply to meet their default service obligations. In contrast, recent experience in neighboring states demonstrates that structured solicitations may not always foster a robust retail market for electricity. In many cases, electric generation suppliers have been unable to compete in markets where solicitations are used to determine default service rates (e.g., Maryland, New Jersey, and Massachusetts).

²³ The Company started serving default service customers from its owned generation. Duquesne subsequently divested its generating assets and served its default service customers by means of negotiated full-requirements supply contracts with a non-affiliate during the POLR I and POLR II periods. In POLR III, Duquesne treated large C&I customers differently from residential and small C&I customers. Large C&I customers were supplied with a PJM hourly market index formula rate. Alternatively, large C&I customers could elect a fixed rate established from a competitive solicitation. Meanwhile, POLR III residential and small C&I customers on default service were supplied at a three-year fixed price based on an agreement with Duquesne's affiliate, where the rate levels were established based on comparisons with recent solicitations. Each of these methods to supply and establish default service rates was approved by the Commission, and presumably, considered consistent with establishing rates at "prevailing market" prices per the Competition Act.

²⁴ Reconsideration Order at 26.

1 not require a competitive solicitation process nor did it impose any restrictions on how
2 default service was supplied. Instead, Strategic's witness in the POLR III proceeding
3 recommended a POLR service for small customers based on a 3-year forward price for
4 energy using the PJM West Hub Index, whereby retail rates were subject to a periodic
5 market price rate adjustment.²⁵

6
7 **Q. Do you agree that the Commission should commit to refrain from considering any**
8 **future POLR proposal which involves contracting with DP for some or all of the**
9 **default service supply?**

10 **A.** No. The Commission should not limit consideration of a particular form of POLR
11 proposal. If the Commission commits now to not consider certain types of POLR
12 proposals in the future, it may preclude implementation of a POLR plan that would have
13 been in the best interests of retail customers.²⁶ Mr. Hudson's proposal would prevent the
14 Commission from considering POLR proposals in which DP, a major wholesale supplier
15 of electricity in Duquesne's service territory, would be able to make an offer to supply
16 default service. It is puzzling why Mr. Hudson would make such a recommendation. If
17 DP were to bid well above other suppliers, it would not win the bid and such a
18 requirement would not be necessary. Presumably, Mr. Hudson must be concerned that
19 DP would win the solicitation at "below market" prices, and while a low price may

²⁵ Strategic Statement No. 2, Direct Testimony, Docket No. P-00032071, February 2004, at 5-6 and 14-15.

²⁶ For example, Duquesne found it very difficult to obtain fixed price bids at attractive price levels to serve large C&I customers using an open solicitation process. After an RFP in May of 2006 resulted in no supplier bids at any price, the Commission explicitly ordered several changes to the solicitation process including a requirement that Duquesne allow its affiliate, DP, to bid in the solicitation. Even after the Commission's changes were adopted, Duquesne only received one bid – from its affiliate DP.

1 benefit customers, it could frustrate retail competition. However, given the fact that a)
2 Duquesne has the highest retail shopping levels in Pennsylvania, b) Duquesne has high
3 retail shopping levels relative to most utilities in the United States, c) FERC has
4 previously granted DP with market-based rate authority and has granted DP a waiver of
5 the affiliate sales prohibitions,²⁷ and d) the failure of Strategic to present in this
6 proceeding any new substantial evidence that DP is somehow being subsidized by other
7 Duquesne affiliates, the Commission should reject Mr. Hudson's recommendation. In
8 any event, regardless of the merits of his arguments, I see no reason to tie Mr. Hudson's
9 recommendation with the proposed acquisition.
10

11 **Q. How do you respond to Mr. Hudson's recommendation that that the Commission**
12 **initiate an investigation to determine whether DLE's unregulated operations are**
13 **being supported by its affiliates, and that approval of the proposed merger should**
14 **be conditioned on the outcome of this investigation?**

15 A. Strategic, or any other party, has the right to exercise its rights and to request the
16 Commission to conduct an investigation into potential anticompetitive or discriminatory
17 conduct affecting the retail distribution of electricity. Even if Mr. Hudson exercises this
18 right and the Commission decides to conduct an investigation, I do not see how the
19 allegations that Mr. Hudson is expressing are relevant to this instant proceeding, so
20 approval of the proposed merger should not be conditioned on the outcome of any such
21 investigation.
22

²⁷ FERC Order Authorizing Disposition of Jurisdictional Facilities and Accepting Market-Based Rate Tariff, Docket No. EC04-36-000, August 6, 2004.

1 Q. Does this conclude your testimony?

2 A. Yes.

3

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

Docket No. A-110150F0035

Docket No. A-311233F0002

**Duquesne Light Company
DQE Communications Network Services, LLC**

Statement No. 7R

REBUTTAL TESTIMONY OF MICHELE SANDOE

1 A. No, I have not previously submitted testimony in this proceeding. I have
2 submitted testimony on behalf of Duquesne Light Company before the
3 Pennsylvania Public Utility Commission, Docket No. R-00061346.
4

5 **Q. What is the purpose of your rebuttal testimony?**

6 A. My rebuttal testimony responds to the assertions of witnesses on behalf of the
7 various interveners on the following topics:

- 8 1) The levels of funding and administrative support for universal services
9 programs (responding to Ms. Alexander);
- 10 2) The formation of a collaborative of local representatives of the low-income
11 community, CBOs and the OCA (responding to Ms. Alexander);
- 12 3) The levels of funding for the Stay Warm programs (responding to Ms.
13 Alexander);
- 14 4) The inclusion of CAAP and Pennsylvania weatherization network into the
15 administration and development of universal services programs (responding to
16 Mr. Wilson); and
- 17 5) The expansion of the existing LIURP program (Smart Comfort) and the
18 implementation of a pilot LIURP program for customers between 151% and
19 250% of the FPL (responding to Mr. Hughes).

20
21 1) **Levels of funding and administrative support for universal service programs**

22
23 **Q. How will the level of funding and administrative support for universal
24 service programs (CAP, CARES, LIURP, and Hardship funding) for the
25 next four year period, ending December 2010, be determined?**

26 A. The level of funding and administrative support for universal service programs
27 has previously been determined for 2007. The funding levels for 2008-2010 will
28 be determined by a needs based assessment completed by a third-party evaluator
29 and utilizing the PaPUC Bureau of Consumer Services methodology. The results
30 from the assessment will be incorporated into the Company's Universal Service

1 and Energy Conservation Plan 2008-2010. The Company will seek approval of
2 the plan from the PaPUC and will submit the plan in February 2007.

3
4 **Q. Do you agree that Duquesne should continue its current level of funding and**
5 **administrative support for universal service programs (CAP, LIURP,**
6 **CARES, and Hardship funding or Dollar Energy Fund) for the four year**
7 **period ending December 2010?**

8 A. The level of funding and administrative support for universal service programs
9 should be determined by the existing procedure of a needs based assessment and
10 *submittal of a universal service plan to the PaPUC.* However, I do agree that
11 Duquesne should continue at least its current level of funding and administrative
12 support for its universal services programs through 2010.

13
14 **Q. Do you agree that Duquesne should continue its current level of funding for**
15 **the four year period ending December 2010 without any further customer**
16 **contributions or change in the method of funding these programs?**

17 A. I agree that Duquesne should continue its current level of funding through
18 December 2010 without any further customer contributions or change in the
19 method of funding these programs. However, if CAP program expenditures
20 exceed the current level of funding, Duquesne will consider further customer
21 contributions or a change in the method of funding this program.

22
23 **2). Formation of a collaborative for universal services**

24
25 **Q. Do you agree with Ms. Alexander's proposal to form a collaborative for**
26 **universal services?**

27 A. Yes, I do. Duquesne will form a collaborative of local representatives of the low-
28 income community, community based organizations (CBOs), and the OCA and
29 will commit to bringing forward any proposed changes to its universal service
30 programs for discussion prior to implementation. The purpose of the

1 collaborative is to explore alternatives to improve the effectiveness and/or
2 efficiency of universal services within the budgets of the programs
3

4 **3) Stay Warm**
5

6 **Q. What are the funding levels for the five new Stay Warm programs identified
7 in the recent rate case filing?**

8 A. Ms. Alexander recommended that during a proposed stay out period of four years,
9 Duquesne should commit to the incremental funding for the five Stay Warm
10 programs. Duquesne has committed \$1.2 million for Stay Warm for the Winter
11 2006-2007 program year. Duquesne agrees to fund Stay Warm on an as needed
12 basis during a stay out period.
13

14 **4) Inclusion of CAAP and the Pennsylvania weatherization providers network**
15

16 **Q. In summary, what are the key recommendations offered by Mr. Wilson
17 regarding Duquesne Light's Smart Comfort program?**

18 A. Mr. Wilson proposes that Duquesne employs the community action agency
19 network and the Pennsylvania weatherization providers network in administering
20 its universal service programs. Mr. Wilson also proposes that CAAP and the
21 Pennsylvania weatherization providers network be involved in the development
22 and implementation of the Company's universal service programs.
23

24 **Q. Is Smart Comfort a weatherization program?**

25 A. No, it is not. Smart Comfort is primarily a baseload program. The baseload
26 program was initiated in 1992 from the more traditional approach of offering
27 usage reduction to heating customers to offering electric usage reduction
28 strategies to low-income residential electric service customers who met specific
29 baseload usage and other screening requirements. The program evolved from
30 strictly weatherization to an "end use" strategy. Baseload usage reduction

1 measures include cost effective appliance change-outs and lighting replacements
2 in addition to weatherization when warranted.
3

4 **Q. Why is Smart Comfort a baseload program?**

5 A. Duquesne Light provides service to roughly 524,500 residential customers in
6 Allegheny and Beaver Counties. As of November 2006, only 5.5% (28,798) of
7 the Company's residential customers are electric heating customers. The
8 predominant source of heating in Duquesne Light's service territory is natural gas
9 heating. Since the Company has a limited number of electric heating customers, a
10 baseload program provides a greater opportunity for usage reduction. By having
11 a baseload program, Smart Comfort can assist more low-income customers in
12 need than a traditional weatherization program.
13

14 **Q. Does Smart Comfort provide any weatherization measures?**

15 A. Yes, Smart Comfort does provide weatherization to qualified low-income
16 customers. However, it is only a small percentage of the Smart Comfort budget
17 based on the demographics of Duquesne Light's service territory. For example,
18 there were 3,003 usage reduction visits completed in 2005. Only 23 visits
19 provided weatherization measures such as insulation, furnace repair and/or
20 replacement, and water tank replacement. This was less than 1% of the
21 Company's total completed visits. Results for 2006 are similar.
22

23 **Q. Does CCI provide the weatherization measures?**

24 A. Conservation Consultants Inc or CCI administers Duquesne's Smart Comfort
25 Program. CCI does provide weatherization measures. CCI Energy Managers
26 identify weatherization measures required. CCI then coordinates with outside
27 local contractors for measure installation.
28

29 **Q. Do you agree with Mr. Wilson's recommendations to direct the Company to**
30 **employ the Pennsylvania weatherization providers network in the**
31 **administration and implementation of its Smart Comfort program?**

1 A. No, I do not. Smart Comfort should remain primarily a baseload program so it
2 can best meet the needs of Duquesne Light's low-income customers. Since Smart
3 Comfort is a baseload program, the Company should not be directed to employ a
4 weatherization providers network.

5
6 **Q. Why does Mr. Wilson recommend that Duquesne Light be directed to**
7 **consult and employ the local community action agency network and the**
8 **Pennsylvania weatherization providers network in the design and**
9 **administration of its universal service programs, particularly its Smart**
10 **Comfort program?**

11 A. Mr. Wilson indicated in his testimony that "because community action agencies
12 serve low income consumers on a broad range of issues facing those consumers,
13 they would be better able to provide resources that would address that consumer's
14 financial difficulties and not just energy related difficulties." Further, Mr. Wilson
15 stated, "the focus and experience of community based organizations make them
16 singularly suited to speak for the needs of the community."

17
18 **Q. Do you agree that CBOs serve low-income customers on a broad range of**
19 **issues?**

20 A. Yes, I do. The Universal Service programs work in conjunction to further serve
21 the needs of Duquesne Light's payment troubled low-income customers. The
22 Company uses multiple CBOs across the service territory such as Goodwill
23 Industries, Holy Family Institute, Catholic Charities and North Hills Community
24 Outreach to administer these programs. The CAP (Customer Assistance
25 Program) and CARES (Customer Assistance and Referral Evaluation Service)
26 programs assist payment-troubled customers and customers with special needs as
27 well as help low-income customers facing a broad range of issues. The CAP and
28 CARES representatives assist customers in completing various applications and
29 refer customers to local food banks, employment fairs and career services for
30 additional assistance. The CAP and CARES representatives from our CBOs also

1 make referrals to the Smart Comfort program to assist customers with energy
2 reduction.

3
4 **Q. What is the interrelationship between CAP and Smart Comfort?**

5 A. There is a strong interrelationship between CAP and Smart Comfort. The
6 completion of a Smart Comfort visit is mandatory for all CAP applicants who
7 meet the minimum baseload usage requirements of 500 kWh per month. As a
8 result, the vast majority of Smart Comfort customers interact with a CBO before
9 and after the scheduled Smart Comfort visit to enroll in CAP. In 2005, 97% of
10 Smart Comfort recipients were also enrolled in CAP. In 2006, 99% of Smart
11 Comfort recipients were also enrolled in CAP.

12
13 **Q. Do you agree with Mr. Wilson's recommendation that Duquesne Light be**
14 **directed to employ the local community action agency network in the design**
15 **and administration of its universal service programs, particularly its Smart**
16 **Comfort program?**

17 A. No, I do not. The current design and administration of the universal service
18 programs closely ties CAP, CARES, and the Hardship Fund together with Smart
19 Comfort. A low-income customer's situation is evaluated and programs are
20 applied based upon the specific needs of the customer. It is the responsibility of
21 the CBOs to determine the needs of the customer and work with him or her to
22 provide the appropriate assistance. For example, the CBO who is enrolling a
23 customer in CAP will evaluate the situation and, when needed, will complete the
24 Dollar Energy application, refer the customer to Smart Comfort, arrange a
25 CARES visit, and/or assist with the LIHEAP or CRISIS application.

26
27 As a result, the current design and administration of the universal service
28 programs has essentially created an integrated network. CAP and CARES are
29 administrated by CBOs such as Goodwill Industries and Holy Family Institute.
30 Dollar Energy Fund utilizes many other CBOs throughout the service territory.
31 These CBOs will service these customers on their individual needs and provide

1 resources to address the customer's financial difficulties. This includes the
2 mandatory completion of Smart Comfort to address energy related difficulties
3 before completion of enrollment in CAP.
4

5 Further, CCI has the necessary qualifications and experience in operating a usage
6 reduction program. For over 28 years, CCI has fulfilled its mission of responsible
7 energy use in homes and other buildings. CCI has worked with low-income
8 communities since the inception of LIURP in Pennsylvania (1988). Currently,
9 they implement several other utility usage reduction programs in Western
10 Pennsylvania for Dominion, Equitable Gas, T.W. Phillips and Columbia Gas.
11 CCI performs inter-utility audits by working in conjunction with Duquesne Light
12 and Equitable Gas to focus on combined conservation and usage reduction. An
13 electric baseload usage reduction program, working in parallel with a natural gas
14 weatherization program, is the best option for low-income payment-troubled
15 customers
16

17 **Q. Do you agree with Mr. Wilson's recommendation that CAAP and the**
18 **Pennsylvania weatherization providers network be involved with the**
19 **development of Duquesne's universal service programs?**

20 **A.** Duquesne has proposed the formation of a collaborative of local representatives
21 of the low-income community, community based organizations (CBOs), and the
22 OCA and will commit to bringing forward any proposed changes to its universal
23 service programs for discussion prior to implementation. Duquesne will invite a
24 representative from CAAP and the Pennsylvania weatherization providers
25 network to join the collaborative. This forum will provide both with an
26 opportunity to provide meaningful input to the ongoing development of
27 Duquesne's universal service programs.
28

29 **5) Smart Comfort (LIURP)**
30

1 Q. In summary, what are the key recommendations offered by Mr. Hughes
2 regarding Duquesne Light's Smart Comfort program?

3 A. Mr. Hughes proposes that Duquesne expand its existing Smart Comfort program
4 and implement a separate LIURP initiative that provides assistance to customers
5 not eligible for Duquesne's existing Smart Comfort program. Specifically, Mr.
6 Hughes proposes that Duquesne commit to increasing the number of LIURP
7 customers served to 4,000 per year with any required funding beyond the current
8 LIURP funding level in distribution rates (including carryover amounts) needed to
9 meet these targets would be funded by shareholders. Likewise, Mr. Hughes
10 recommends the creation of a new and separate LIURP program "HESP" which
11 would serve an additional 4,000 customers per year.
12

13 Q. How is the quantity of Smart Comfort visits completed per year determined?

14 A. In general, annual Smart Comfort levels are determined by a needs based
15 assessment. The results from the assessment are incorporated into the Universal
16 Services and Energy Conservation Plan, which is reviewed and approved by the
17 PaPUC. Based upon the Duquesne Light Company Needs Based Assessment
18 Low Income Usage Reduction Program (LIURP) completed in February 2004,
19 1,750 Smart Comfort visits per year were determined to be appropriate to the
20 needs of the Company's low-income payment troubled customers. Further, the
21 quantity of Smart Comfort visits per year was increased in the settlement of our
22 rate case by an additional 500 Smart Comfort visits for a total of 2,250 visits to
23 address the concerns that there may be more customers that need LIURP
24 assistance than the current plan provided.
25

26 Q: Do you agree that Duquesne should expand its existing Smart Comfort
27 program?

28 A. Duquesne has a strong commitment to the low-income and its universal service
29 programs. Duquesne has never refused a qualified low-income customer a Smart
30 Comfort visit. To further demonstrate this commitment, Duquesne will commit to
31 increasing the number of customers who receive Smart Comfort benefits to 3,000

1 visits per year. This represents an increase of 750 visits over the previous
2 commitment of 2,250 Smart Comfort visits per the combined needs based
3 assessment and rate case settlement.
4

5 **Q. Do you agree that Duquesne should create a new and separate LIURP**
6 **program?**

7 A. No, I do not. Mr. Hughes proposes that a new program be created to assist
8 customers who do not qualify for the existing Smart Comfort program. The new
9 program Home Energy Savings Program (HESP) would target customers who are
10 between 150% to 250% of the Federal Poverty Guidelines. In general, universal
11 service programs focus on assisting low-income customers who are at or below
12 150% of the Federal Poverty Guidelines. Expanding beyond this focus would
13 dilute the vision of helping those most in need. Alternatively, I would
14 recommend that Duquesne focuses on customers between 150% and 200% of the
15 Federal Poverty Guidelines for the additional 750 Smart Comfort visits proposed
16 in this testimony.
17

18 **Q. Should funding for Duquesne's existing Smart Comfort program be**
19 **increased to cover the expansion?**

20 A. No, I do not recommend increasing LIURP funding from current levels.
21

22 **Q. Does this conclude your rebuttal testimony?**

23 A. Yes, it does.
24

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Application of Duquesne Light Company)
for a Certificate of Public Convenience)
Under Section 1102(a)(3) of the Public)
Utility Code Approving the Acquisition)
of Duquesne Light Holding, Inc. by Merger)

Docket No. A-110150F0035

Application of DQE Communications)
Network Services LLC for a Certificate)
of Public Convenience under Section)
1102(a)(3) of the Public Utility Code)
Approving the Acquisition of Duquesne)
Light Holding, Inc. by Merger)

Docket No. A-311233F0002

DIRECT TESTIMONY

OF

MATTHEW I. KAHAL

ON BEHALF OF THE

PENNSYLVANIA OFFICE OF CONSUMER ADVOCATE

DECEMBER 21, 2006

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ASSOCIATES, INC.

5565 Sterrett Place

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1 I. QUALIFICATIONS

2 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

3 A. My name is Matthew I. Kahal. I am employed as an independent consultant retained in
4 this case by the Exeter Associates, Inc., an economic consulting firm. My business
5 address is 5565 Sterrett Place, Suite 310, Columbia, Maryland 21044.

6 Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND.

7 A. I hold B.A. and M.A. degrees in economics from the University of Maryland and have
8 completed course work and examination requirements for the Ph.D. degree in economics.
9 My areas of academic concentration included industrial organization, economic
10 development and econometrics.

11 Q. WHAT IS YOUR PROFESSIONAL BACKGROUND?

12 A. I have been employed in the area of energy, utility and telecommunications consulting for
13 the past 25 years working on a wide range of topics. Most of my work has focused on
14 electric utility integrated planning, plant licensing, environmental issues, mergers and
15 financial issues. I was a co-founder of Exeter Associates, and from 1981 to 2001 I was
16 employed at that firm as a Senior Economist and Principal. During that time, I took the
17 lead role at Exeter in performing cost of capital and financial studies. In recent years, the
18 focus of much of my professional work has shifted to electric utility restructuring, power
19 supply markets and competition.

20 Prior to entering consulting, I served on the Economics Department faculties at the
21 University of Maryland (College Park) and Montgomery College teaching courses on
22 economic principles, development economics and business.

23 A complete description of my professional background is provided in Appendix A.

1 Q. HAVE YOU PREVIOUSLY TESTIFIED AS AN EXPERT WITNESS BEFORE
2 UTILITY REGULATORY COMMISSIONS?

3 A. Yes. I have testified before approximately two-dozen state and federal utility
4 commissions in approximately 300 separate regulatory cases. My testimony has
5 addressed a variety of subjects including fair rate of return, resource planning, financial
6 assessments, load forecasting, competitive restructuring, rate design, purchased power
7 contracts, merger economics and other regulatory policy issues. These cases have
8 involved electric, gas, water and telephone utilities. In 1989, I testified before the U.S.
9 House of Representatives, Committee on Ways and Means, on proposed federal tax
10 legislation affecting utilities. A list of these cases may be found in Appendix A, with my
11 Statement of Qualifications.

12 Q. WHAT PROFESSIONAL ACTIVITIES HAVE YOU ENGAGED IN SINCE
13 LEAVING EXETER AS A PRINCIPAL IN 2001?

14 A. Since 2001, I have worked on a variety of consulting assignments pertaining to electric
15 restructuring, purchase power contracts, environmental controls, cost of capital and other
16 regulatory issues. Current and recent clients include the U.S. Department of Justice, U.S.
17 Air Force, U.S. Department of Energy, the Federal Energy Regulatory Commission,
18 Connecticut Attorney General, Pennsylvania Office of Consumer Advocate, New Jersey
19 Division of the Rate Counsel, Rhode Island Division of Public Utilities, Louisiana Public
20 Service Commission, Arkansas Public Service Commission, Maryland Department of
21 Natural Resources and Energy Administration, and MCI.

22 Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS COMMISSION?

23 A. Yes, I have testified on cost of capital and other matters before this Commission in gas,
24 water, telecom and electric cases during the past 25 years. A listing of those cases is
25 provided in my attached Statement of Qualifications, Appendix A.

1 Q. DO YOU HAVE ANY PAST EXPERIENCE WITH DUQUESNE LIGHT
2 COMPANY (DLC OR THE COMPANY)?

3 A. Yes. I testified on behalf of the Office of Consumer Advocate (OCA) on the
4 quantification of stranded costs in the DLC restructuring case (Docket No. R-00974104).
5 I also testified in the Duquesne/Allegheny Power proposed merger case in Docket No.
6 A-1101150F0015. That proposed merger was ultimately terminated by the parties and
7 was not completed.

8 As listed in Appendix A, I have testified in numerous other merger or corporate
9 restructuring cases in Pennsylvania as well as in other jurisdictions.

1 Applicants themselves cite to the Pennsylvania Supreme Court's City of York v.
2 Pa. P. U. C. decision as the legal standard, and in meeting that standard they claim
3 "substantial public benefits" will result from this merger.¹ These asserted benefits are
4 described in both the Application and in the supporting testimony of Morgan K. O'Brien
5 (Applicants' Statement No. 1), President of DLC, and Mr. Christopher J. Leslie
6 (Applicants' Statement No. 2), a senior executive with certain Macquarie subsidiaries. In
7 addition, Applicants argue that there is an absence of harm, e. g., no anticompetitive
8 impacts.

9 Q. HAVE THE APPLICANTS SHOWN THAT THE PROPOSED MERGER WILL
10 PROVIDE THE CLAIMED "SUBSTANTIAL PUBLIC BENEFITS"?

11 A. No, they have not. The Applicants, along with Mr. Leslie speaking for the Macquarie
12 Consortium, argue that the merger will not cause harm and is consistent with or
13 supportive of DLC's current business plans and practices. However, beyond retaining the
14 status quo, no specific customer benefits have been demonstrated.² The filing seems to
15 imply that retention of the status quo itself is a benefit. In addition, the Application
16 suggests unspecified benefits will flow from DLC having access to the Macquarie
17 Group's technical expertise.

18 Q. WHY DO YOU FIND AN ABSENCE OF "SUBSTANTIAL PUBLIC
19 BENEFITS" FROM THE TRANSACTION?

20 A. As will be explained in my testimony, Applicants' claims are either vague and
21 unsubstantiated or they are predicated upon the avoidance of a hypothetical adverse
22 development (e. g., the takeover of DLH, and therefore DLC, by an out-of-state utility).

¹ See Application, page 20. City of York v. Pa. P. U. C., 449 Pa. 136, 295 A. 2d 825 (1972).

² As discussed by Mr. O'Brien, DLC will conduct an economic development program in which it will offer up to 50 MW of power supply at an asserted \$3 per MWh market discount for three years for new non-residential loads. Since this program is not designed for residential customers, my testimony only briefly discusses this initiative. (Applicants' Statement No. 1, page 17-21)

1 Based upon my review, including information in discovery documents, none of these
2 claimed benefits can be verified. While it can be argued that there are no clear and
3 unambiguous merger harms,³ it appears that the merger at a minimum poses risks that are
4 difficult to evaluate. I therefore conclude that the merger, as filed and described, does not
5 meet the Commission's public interest standard for approval.

6 Q. COULD THE MERGER BE CONDITIONED TO MITIGATE RISKS AND
7 PROVIDE SUBSTANTIAL, AFFIRMATIVE BENEFITS?

8 A. While merger risks for Pennsylvania customers cannot be eliminated, I identify a set of
9 conditions that can provide important protections and go in the direction of providing a
10 public interest benefit. Such protections and benefits would include the following:

11 (1) Distribution Rate Cap

12 Electric utility mergers typically provide "synergy savings" that are flowed
13 through or shared with customers. Even the Applicants concede that this
14 transaction would not provide such savings. On the other hand, DLH
15 shareholders will enjoy a stock market price premium from this transaction of
16 nearly \$300 million.⁴ Applicants and the Consortium can provide benefits to
17 customers from this transaction by accepting a distribution service rate cap
18 extending to year-end 2010. (This cap would not apply to either transmission
19 service or POLR generation costs.)

³ The merger does not create asset concentration and does not seek to replace existing management or management structure at this time.

⁴ Applicants' estimate payments to DLH shareholders of \$283 million in excess of prevailing market value.
(Response to RESA II-3)

1 (2) Corporate Governance

2 Applicants plan for a DLH/DLC corporate governance arrangement that would
3 include a Board of Directors comprised of the representatives of the Consortium's
4 six investment funds plus the Chief Executive Officer (CEO) of DLC. For a
5 public utility company, with explicit public interest and local responsibilities, this
6 is an overly narrow governance structure. In addition to the Consortium
7 representatives, I believe there is a benefit to the inclusion on the Board of
8 "outside" directors (i.e., directors not in the employ of the Company or of the
9 funds themselves), with some Pittsburgh area representation.

10 (3) Transactions Costs and Other Acquisition-Related Costs

11 DLC must not include in customer rates any costs, directly or indirectly,
12 associated with the proposed merger transaction. "Transactions costs" should be
13 broadly interpreted to include the costs incurred by either DLC or the investors in
14 completing the transaction, any regulatory approval costs and fees, DLH/DLC-
15 related employee costs (if any) and other expenses that would not be incurred but
16 for the proposed transaction. This prohibition must apply both to Pa PUC retail
17 ratemaking as well as FERC transmission ratemaking. In addition, there should
18 be no "acquisition adjustment" or costs related to the acquisition premium paid by
19 Consortium investors charged directly or indirectly to DLC customers.

20 (4) Cost of Capital

21 The filing seems to imply -- but never explicitly states -- that DLC could enjoy a
22 cost of capital benefit from the proposed transaction. My concern is that the
23 transaction could lead to a higher cost of capital, or the future claim by DLC of a
24 higher cost of capital. An example is the apparent plan of the Macquarie
25 Consortium to sharply increase the DLC common equity ratio beyond current

1 levels and beyond what would be reasonable for a low-risk, delivery service
2 utility. Customers must not pay a higher rate of return as part of either Pa PUC
3 distribution rates or FERC-regulated transmission rates as a result of this
4 transaction.

5 (5) DLC Loan Guarantees

6 DLC should be prohibited from making loans to any affiliate, guaranteeing the
7 debt of an affiliate or pledging its assets to provide credit support for an affiliate.
8 The affiliate definition would include the various funds that are equity investors in
9 DLH/DLC and any entity in which any Macquarie Consortium member has an
10 ownership interest.

11 (6) Capital Stock Tax

12 DLC must not charge its retail customers or FERC transmission customers for any
13 increase in the Pennsylvania Capital Stock Tax due to the merger.

14 (7) Affiliate Services Agreement

15 The Macquarie Group apparently intends to provide certain services to DLC and
16 to charge the Company for the cost of these services pursuant to an amended
17 Services Agreement. Presumably, DLC would seek to recover such costs in retail
18 and wholesale rates. Up to now, the Applicants and the Macquarie Group have
19 been somewhat vague concerning the nature of these services. In any event, an
20 amended Services Agreement has not yet been submitted to the Commission or to
21 the parties in this case. The Applicants should be required to submit such
22 agreement for review by the parties and to the Pa PUC for its review and
23 approval. The merger should not be permitted to close until the affiliate Services
24 Agreement amendments have been approved.

1 (8) Progress Reporting on Compliance with Approval Conditions

2 DLC should submit annual reports for the next four years on a range of issues
3 pertaining to the transaction and the benefits associated with the transaction as
4 asserted by the Applicants and Mr. Leslie. In addition, DLC should submit a
5 report to be supported by testimony addressing the status of merger benefits and
6 issues as part of its next distribution rate case.

7 In addition to the approval recommendations outlined above, OCA witness
8 Alexander makes several recommendations concerning service quality, charitable
9 contributions and universal service programs that would apply during a rate cap period
10 over the next several years.

11 Q. THE APPLICANTS AND MR. LESLIE ON BEHALF OF THE MACQUARIE
12 GROUP CLAIM THE MERGER WILL PROVIDE SUBSTANTIAL,
13 AFFIRMATIVE BENEFITS IN ACCORDANCE WITH THE CITY OF YORK
14 STANDARD. DO YOU AGREE?

15 A. While I certainly hope they are correct, the evidence concerning these alleged benefits so
16 far presented has been both vague and unsubstantiated. In fact, as discussed in my
17 testimony, there is potential for harm. The proposed conditions outlined above and in
18 Ms. Alexander's testimony can help to avoid such harm from occurring and would
19 provide a greater likelihood that affirmative public interest benefits will be achieved.

20 Q. HOW IS THE REMAINDER OF YOUR TESTIMONY ORGANIZED?

21 A. Section III provides a summary of the proposed transaction and assesses the claimed
22 benefits from the transaction. In addition, in that Section I briefly discuss the reasons
23 why a utility merger should not be approved absent a reasonable showing of substantial,
24 affirmative public benefits and protective conditions. Section IV provides a discussion of
25 the recommended approval conditions. Finally, Section V summarizes my conclusions.

1 Q. IS YOUR TESTIMONY ACCOMPANIED BY SCHEDULES?

2 A. No, I have not prepared schedules. However, Appendix B accompanying my testimony
3 provides a summary of my recommended conditions that would accompany approval.

(1) Macquarie Infrastructure Partners (MIP)	22.1%
(2) Diversified Utility and Energy Trust (DUET)	28.9
(3) Macquarie Global Infrastructure Fund (GIF-2)	6.6
(4) Macquarie - FSS Infrastructure Fund (M-FIT)	<u>6.6</u>
Macquarie Group	64.3%
(5) Industry Funds Management (IFM)	22.8%
(6) Motor Trade Association (MTA)	6.6
(7) SAS Trustee Corporation (State Super)	<u>6.6</u>
Non-Macquarie Funds	35.7%
Total	100.0%

Source: Response to OTS I-1

2 Q. WHAT ARE THE TERMS OF THE ACQUISITION?

3 A. The Consortium will acquire the present Duquesne Holdings for \$20 a share (about \$1.6
4 billion based on nearly 80 million shares outstanding) and a total enterprise value of
5 \$3.15 billion. This sale price will provide current Duquesne Holdings shareholders with
6 an acquisition premium of about 22 percent, or an estimated \$283 million. (Response to
7 RESA II-3) Thus, shareholders will enjoy a substantial benefit from this transaction.

8 Q. DO THE CONSORTIUM MEMBERS HAVE EXPERIENCE WITH UTILITY
9 OWNERSHIP?

10 A. Consortium members have various investments in non-U. S. utilities including water,
11 electric transmission, electric distribution and gas. The funds have recently acquired two
12 retail U. S. utilities, Aquarion Water in New England and Hawaiian Gas Company. DLC
13 would be the first U. S. retail electric utility, and I believe that the Consortium members

1 may have an interest in further U. S. utility acquisitions. Given the Consortium's present
2 absence of other U. S. electric utility investments, I would conclude that the proposed
3 acquisition is not a horizontal merger.

4 Q. IS THERE ANY INDICATION THAT THE CONSORTIUM INTENDS TO
5 ALTER DLC'S BUSINESS PLANS OR OPERATIONS?

6 A. There is no indication of any significant operational or strategic changes as a result of the
7 acquisition, although those plans obviously could change over time. For example, the
8 present plan is to retain existing DLC management in its current role. However, the
9 Consortium has identified some important financial or capitalization changes that it plans
10 to make post closing. In particular, the Consortium intends to increase the Duquesne
11 Light Holdings debt balance (to help finance the transaction) and to substantially increase
12 the DLC common equity ratio by refunding debt.

13 Q. WILL THE CONSORTIUM MEMBERS PARTICIPATE IN THE
14 MANAGEMENT OF DLC?

15 A. Yes, it appears that they will to some degree. Mr. Leslie indicates that the Consortium
16 may provide "financial and technical expertise" (Applicants Statement No. 2, page 11) to
17 DLC, as needed and appropriate. However, neither the Application nor data responses
18 explain with much specificity the services that will be provided to DLC.

19 Mr. Leslie's testimony also describes the planned corporate governance. He
20 states that representatives of the six funds will serve as the Board of Directors, with Mr.
21 Leslie serving as Chairman. Mr. Morgan will serve as the DQE Holdings and DLC CEO
22 and therefore will be a member of the Board of Directors. (Id., page 10-11 and response
23 to OCA III-16)

1 Q. WHAT HAS BEEN THE REACTION OF THE CREDIT RATING AGENCIES
2 TO THE PROPOSED TRANSACTION?

3 A. The initial response has been somewhat negative. Following the public announcement of
4 the acquisition on July 5, 2006, both Standard & Poors (S&P) and Moody's Investors
5 Service (Moody's) placed DLC under review for possible downgrade.⁶ The credit rating
6 of DUET, which is the Macquarie Consortium member with the largest investment in
7 DQE Holdings has a credit rating of BBB-, with an outlook of "negative". Thus, the
8 acquiring entity has a weaker credit rating (i.e., DUET) and greater risk than DLC (a low
9 business risk distribution company).

10 **B. The Affirmative Benefit Standard**

11 Q. WHY IS IT APPROPRIATE THAT APPLICANTS BE REQUIRED TO
12 DEMONSTRATE THAT SUBSTANTIAL, AFFIRMATIVE BENEFITS WILL
13 ACCOMPANY A UTILITY MERGER?

14 A. Mergers, acquisitions and corporate restructuring reflect the normal operation of capital
15 markets and market forces. For example, in this case the Consortium's proposed
16 acquisition of Duquesne Holdings is reflective of a strong, emerging trend of private
17 equity transactions and is facilitated by the availability of abundant and low-cost capital
18 in global markets. Moreover, the private equity acquisitions of utilities also are the result
19 of the repeal of the Public Utility Holding Company Act (PUHCA) which became
20 effective earlier this year.

21 While these types of corporate transactions reflect market forces, at the same time
22 the track record of mergers and acquisitions presents a mixed picture at best. Some
23 mergers are successful in meeting objectives (in terms of shareholder returns and

⁶ S&P's report is entitled, "Duquesne Light Holdings and DLC Rating Put on Watch Neg after Acquisition Announcement." Moody's title states, "Moody's Places Rating of Duquesne Light Holding (Sr. Unsec. Baa3) and Duquesne Light Company (Sr. Sec Baa1) under Review for Possible Downgrade." (July 5, 2006) Provided in response to OCA III-1.

1 efficiencies) while others are not. The professional economics literature concerning
2 mergers documents this uneven track record of performance.

3 In this regard, there is a fundamental difference between utility mergers and those
4 not involving utilities. In the case of non-utility mergers, the failure to achieve planned
5 efficiencies or adequate returns on investment (including recovery of acquisition
6 premiums) will be borne entirely by investors. In the case of utility mergers, at least a
7 portion of the risk and cost of poor performance will be underwritten by captive utility
8 customers, unless (and except to the extent) such risk can be mitigated by protective
9 conditions required by the regulator. Moreover, as a practical matter merger-related risks
10 can never be eliminated, even by carefully-crafted conditions.

11 Q. WHY DOES THIS WARRANT AN "AFFIRMATIVE BENEFITS"
12 STANDARD FOR APPROVAL?

13 A. Each merger or corporate "change of control" proposal should be evaluated on its own
14 merits. While protective conditions can be helpful, it is probably inevitable that a merger
15 (or change in control) will expose utility customers to risks associated from a changed
16 ownership structure or failure of management to execute on the business strategy. For
17 this reason, it is important to carefully scrutinize the claimed benefits in order to have
18 some degree of confidence that the prospects for benefits reasonably compensate for the
19 risks that customers inevitably will bear. These risks potentially could take the form of
20 higher rates, diminished service quality and/or other public interest problems. A "no
21 harm" or status quo standard of approval does not adequately protect customers.

22 Q. CAN YOU CITE ANY RECENT EXAMPLES OF A MAJOR UTILITY
23 ACQUISITION THAT WAS NOT SUCCESSFUL?

24 A. Yes. In 2002, the German utility company, RWE Aktiengesellschaft (RWE), sought to
25 acquire the American Water Company system, including Pennsylvania American Water

1 Company, completing the transaction in 2003. In late 2005, RWE determined that
2 ownership of U. S. water utilities no longer fit its business plan, and it is in the process of
3 divesting American Water. This is a lengthy, costly and disruptive process.

4 Q. WHAT DO YOU CONCLUDE FROM THIS ANALYSIS?

5 A. Consistent with Pennsylvania policy, this transaction should not be approved if the
6 substantial, affirmative benefits standard cannot be met with a reasonable degree of
7 confidence. The Applicants' specific benefit claims must be carefully scrutinized to
8 determine whether they meet this standard. If not, and if the merger is to be approved,
9 conditions of approval must be crafted that properly protect customers and assure that the
10 standard can be met.

11 Q. HAS THIS STANDARD BEEN APPLIED IN PENNSYLVANIA FOR PAST
12 ELECTRIC UTILITY MERGERS?

13 A. Yes, my understanding is that it has been applied. Most recently, as part of the
14 Exelon/PSEG merger (involving the acquisition of Public Service Enterprise Group),
15 Docket No. A-110550F0160, a settlement was reached providing \$120 million in rate
16 reductions over four years and a delivery service rate cap through 2010. It also provided
17 a range of other benefits pertaining to renewable resources, universal service programs,
18 service quality and utility staffing. While this merger did not go forward, similar
19 conditions were applied to the earlier PECO/Unicom merger where a settlement provided
20 \$200 million of rate reductions, a delivery service rate cap of five years and a range of
21 other benefits pertaining to renewable resources, universal service programs, service
22 quality and utility staffing. (Docket No. A-110550F0147)

23 Similarly, for the First Energy acquisition of the GPU companies (including
24 Metropolitan Edison Company and Pennsylvania Electric Company), the Administrative
25 Law Judge (ALJ) recently recommended a sharing with customers of the synergy savings

1 from the merger upon consideration of this issue on remand. (Docket Nos. A-
2 110300F0095, et al.) This was in addition to previous conditions the Commission had
3 imposed regarding a Service Quality Index, universal service programs, economic
4 development programs, and other conditions. By comparison, the Macquarie acquisition
5 of DLC identifies no synergy savings for customers, nor do Applicants offer any tangible
6 or substantial rate benefits/protections for customers or other public interest benefits
7 beyond preserving the status quo.

8 **C. Assessing the Claimed Merger Benefits**

9 Q. WHAT CUSTOMER OR PUBLIC INTEREST BENEFITS DO THE
10 APPLICANTS AND MR. LESLIE, ON BEHALF OF THE MACQUARIE
11 CONSORTIUM, CLAIM FOR THIS MERGER?

12 A. The claimed benefits fall primarily into two categories. The first category of benefits
13 stems from Mr. O'Brien's suggestion that Duquesne inevitably is a "takeover" target, and
14 this proposed transaction would be superior to some other hypothetical merger. The
15 Macquarie Consortium acquisition is asserted to be superior because the Applicants
16 suggest that it would be less disruptive. Since the proposed transaction is described as
17 more of a long-term "infrastructure investment" than a traditional horizontal merger
18 (e.g., Exelon), the Consortium claims it will support DLC's current management and
19 business plan, and it states that it will maintain the corporate headquarters in Pittsburgh.
20 The Applicants appear to suggest that these benefits could be lost under some future
21 acquisition, and this merger will preserve the "status quo."

22 The second category of claimed benefits includes the positive improvements that
23 the Consortium allegedly can provide. Specifically, the Consortium states it can provide:

- 24 • Access to its technical expertise in managing large infrastructure and utility
25 investments.

- 1 • Improved access to capital to finance improvements and expansion at DLC.
- 2 • The Consortium's commitment "to pursuing new and strategic initiatives with
- 3 Duquesne's current management to further improve ratepayer satisfaction and
- 4 continue to focus on product quality and operational efficiency."
- 5 (Application, pages 22-23)
- 6 • The Applicants and Consortium agree to continue existing employee
- 7 protections and the Company's community involvement.
- 8 • The Applicants will implement a 50 MW economic development program
- 9 involving the sale of generation to new business loads at a discounted price.

10 Q. WILL THE TRANSACTION PROVIDE "SYNERGY SAVINGS" OR
11 TRADITIONAL MERGER ECONOMIES OF SCALE SAVINGS?

12 A. The Applicants do not believe that it will, which helps to explain why so few affirmative
13 benefits have so far been offered to customers. As Mr. O'Brien states:

14 Because the transaction does not involve a combination of
15 operating utilities, it is not expected that synergy savings will be
16 realized as a result of the transaction. (Applicants' Statement
17 No. 1, page 21)

18 Since no synergy savings have been claimed or identified, there is no commitment at all,
19 post transaction, to achieving additional efficiencies or improvements.

20 Q. THE APPLICANTS INDICATE THAT A MERGER BENEFIT COULD
21 INCLUDE AN OPPORTUNITY FOR DLC TO IMPLEMENT "BEST
22 PRACTICES" TO BE IDENTIFIED BY CONSORTIUM MEMBERS BASED
23 ON THEIR GLOBAL UTILITY EXPERTISE. HAS THAT BEEN
24 SUBSTANTIATED?

25 A. No "best practices" or "strategic initiatives" have been either identified or described. The
26 response to OCA I-37 simply states that representatives of DLC and the Macquarie
27 Group will seek to identify such initiatives after merger completion. The response to

1 OCA I-41 identifies no timetable for addressing such initiatives other than after merger
2 approval. The response to OCA I-35 discusses some initiatives that have occurred (or
3 may occur) at other Macquarie Group utilities. However, with respect to DLC the
4 response states that the Consortium “does not believe that DLC needs to conduct a
5 comprehensive review of its processes. Instead, the Macquarie Consortium intends to
6 support the current management team in implementing its existing strategy.” (emphasis
7 added)

8 In light of these interrogatory responses, there is no clear indication that any effort
9 will be made to adopt “best practices” beyond what DLC management would introduce
10 on its own.

11 Q. APPLICANTS SUPPORT THE TRANSACTION BY ARGUING THAT
12 DUQUESNE IS A “TAKEOVER TARGET” IN A RAPIDLY
13 CONSOLIDATING INDUSTRY. DO APPLICANTS PROVIDE SUPPORT
14 FOR THE TAKEOVER ASSERTION?

15 A. Mr. O’Brien cites to investor analyst opinion on this issue. (Applicants Statement No. 1,
16 page 11) In response to OCA III-18, the Applicants provided a J. P. Morgan research
17 report dated February 14, 2006 which states:

18 DQE may be perceived as an acquisition candidate, although we
19 believe it is unlikely that the company would be acquired at current
20 price levels. We also believe the long-term regulatory uncertainty
21 would deter a potential buyer.

22 Thus, the alleged benefits from this transaction which stem from avoiding some other,
23 future acquisition seem speculative.

24 Q. SHOULD AVOIDANCE OF SOME OTHER FUTURE MERGER BE VIEWED
25 AS A PUBLIC INTEREST BENEFIT IN THIS CASE?

26 A. I do not believe it should be considered a public interest benefit for three reasons. First,
27 the attributes of a future, hypothetical acquisition of Duquesne are both unknown and

1 unknowable. Hence, the merits of some future merger simply cannot be compared to the
2 proposed Macquarie merger. For example, it is possible that a more traditional (i.e.,
3 horizontal) merger may provide significant synergy savings, which this proposed merger
4 does not provide and which this transaction therefore would preclude. Hence, there is no
5 basis for claiming that the avoidance of some other merger necessarily should be viewed
6 as a benefit.

7 The second reason is that any future merger or acquisition proposal will be
8 subject to this Commission's approval, including the application of the "substantial,
9 affirmative public benefits" standard. If such a future merger is found not to be in the
10 public interest under the approval standards, it can be rejected or properly conditioned.

11 Third, we have little information regarding the Consortium's future plans for
12 Duquesne or DLC. That is, the filing and Mr. O'Brien's testimony describe the current
13 plans to operate DLC as a "stand alone" utility, but future plans could change.

14 For all of these reasons, I do not believe the avoidance of a future, hypothetical
15 merger meets the Commission's "affirmative benefits" test.

16 Q. THE APPLICATION EMPHASIZES THE IMPORTANT ROLE THAT THE
17 CONSORTIUM CAN PLAY IN PROVIDING FINANCING FOR THE DLC
18 INFRASTRUCTURE IMPROVEMENT PLAN AND OTHER CAPITAL
19 PROJECTS. DO APPLICANTS OR THE CONSORTIUM PROVIDE ANY
20 SPECIFIC EVIDENCE OF A CAPITAL FUNDING OR COST OF CAPITAL
21 BENEFIT?

22 A. No. DLC has large capital outlays associated with its infrastructure improvement plan,
23 about \$530 million during 2005 to 2007. (Response to OCA III-8) The vast majority of
24 the capital expenditures will be made prior to the completion of the proposed merger (if
25 approved), and the majority of the capital has been subject to rate recovery in DLC's

1 most recent distribution rate case. (Pa PUC Docket No. R-00061346) DLC has also
2 submitted a request to FERC seeking extremely favorable rate treatment and revenue
3 support for its transmission capital spending going forward, presumably both as a
4 shareholder reward and to help facilitate financing of new transmission. Applicants
5 nowhere have stated that this “incentive” or special rate treatment to facilitate financing
6 will not be needed if the merger is approved.

7 In this regard, OCA III-6 asked Applicants to support their assertion of inadequate
8 access to capital for DLC. The response cites no instances or examples of inadequate
9 access to capital or any tangible evidence on this issue supporting Applicants’ assertions
10 that DLC presently faces unduly restricted access to capital. In that regard, DLC has a
11 stronger credit rating than the largest Consortium member (in terms of its proposed
12 Duquesne investment), i.e., DUET.

13 Q. WILL THE MERGER REDUCE DLC’S COST OF CAPITAL AND
14 THEREFORE ITS FAIR RATE OF RETURN?

15 A. Again, there is no evidence of a cost of capital reduction, and some risk of a cost of
16 capital increase (possibly due to the Consortium’s capital structure plans for DLC). OCA
17 III-3 asked the Applicants to identify any anticipated reduction in either the cost of debt
18 or cost of equity associated with the merger. The Applicants respond by stating, “The
19 acquisition will have no adverse effect on DLC’s ability to raise debt and equity capital
20 nor on the cost of that capital.” In other words, Applicants on this key issue are limited to
21 claiming only an absence of harm, not an affirmative benefit. As will be discussed in the
22 next section, I believe that even under the Consortium’s status quo plan, there is some
23 risk to customers of a higher cost of capital.

1 Q. DO APPLICANTS CLAIM A BENEFIT FROM MAINTAINING CORPORATE
2 HEADQUARTERS IN PITTSBURGH?

3 A. Yes, but this is a “status quo” benefit to be realized from not changing the current
4 arrangements. Moreover, there appears to be nothing to prevent the Consortium from
5 transferring activities or functions from the DLC Pittsburgh headquarters in the future, as
6 a result of this merger and its future U. S. utility acquisitions.

7 Q. HAS THE CONSORTIUM DOCUMENTED THE BENEFITS FROM ACCESS
8 TO ITS GLOBAL TECHNICAL EXPERTISE?

9 A. No. The OCA asked a series of questions seeking some specifics or support concerning
10 how the Consortium will bring value to customers, particularly by drawing on
11 Consortium technical expertise and managerial resources. The response to OCA I-37
12 merely states that at some future point in time, DLC management and Macquarie will
13 engage in a “strategic planning process” to identify possible “initiatives”. The response
14 to OCA I-40 states Macquarie’s commitment to enhancing service quality, and that this
15 activity will be tracked through normal Pa PUC reporting. The response to OCA I-41
16 does not identify a timetable for pursuing new initiatives other than stating this will occur
17 “once the merger is approved.”

18 Q. HAS THE CONSORTIUM IDENTIFIED ANY STRATEGIC INITIATIVES,
19 TRANSFER OF BEST PRACTICES OR SPECIALIZED EXPERTISE THAT IT
20 CAN PROVIDE DLC?

21 A. Generally speaking, it has not, perhaps other than using Macquarie’s expertise and
22 resources to help raise capital or for certain financial services. Thus, at this point, the
23 benefits to DLC customers from access to Macquarie’s expertise have not been
24 convincingly demonstrated. Once again, this does not seem supportive of the
25 Commission’s affirmative benefits standard of merger approval.

1 Q. DO YOU SEE ANY POTENTIAL DISADVANTAGES FROM THE SHARING
2 OF EXPERTISE?

3 A. Yes, I do. At the present time, Macquarie's utility footprint in the U. S. is quite small,
4 and the Duquesne acquisition would be a major expansion, both in size and into a new
5 business in the U.S. (i.e., electric utility delivery service). It seems apparent from the
6 Application and testimony that the Consortium members have a strong interest in further
7 utility expansion in the U. S. market, facilitated by the repeal of PUHCA. As expansion
8 is either pursued or even just contemplated, Macquarie may seek to draw upon the
9 managerial and technical talent at DLC to assist in utility acquisition activity. This will
10 remove or distract the key individuals from devoting their full time and energy to
11 providing DLC utility service. While this may provide a promotion or professional
12 benefit for these employees, it could be disadvantageous for customers.

13 In this context, the sharing of expertise and technical assistance between
14 Macquarie and DLC potentially is a double-edged sword, benefiting Macquarie at the
15 expense of DLC customers. Post merger, there would be nothing to prevent Macquarie
16 from engaging in managerial talent "cream skimming".

17 Q. IS THE PROPOSED 50 MW ECONOMIC DEVELOPMENT PROGRAM AN
18 AFFIRMATIVE BENEFIT?

19 A. It may provide a modest public benefit (depending on customer participation), but it is
20 not clear that a merger is required to implement this program. Also, its scope is rather
21 limited since the program is restricted to new business loads, i.e., no residential benefit.

1 Q. IS THE COMMITMENT TO RETAIN CURRENT EMPLOYEE
2 PROTECTIONS AND LOCAL COMMUNITY INVOLVEMENT A MERGER
3 BENEFIT?

4 A. This appears to be largely a continuation of present practice rather than a benefit
5 specifically to be provided by the merger.

6 Q. ARE THERE OTHER CLAIMED MERGER BENEFITS THAT HAVE BEEN
7 EXPLAINED OR DOCUMENTED?

8 A. At this time, Applicants and the Consortium have not demonstrated any other substantial,
9 affirmative public interest benefits that I am able to identify.

1 **IV. POTENTIAL CONDITIONS OF APPROVAL**

2 Q. WHAT IS THE PURPOSE OF THE CONDITIONS YOU HAVE
3 DEVELOPED?

4 A. If the Commission finds merit in the proposal to transfer control of DLC to the
5 Macquarie Consortium, I recommend that such approval be accompanied by conditions
6 that are protective of customers and conditions that have the potential to provide
7 affirmative public benefits. In addition to my conditions, OCA witness Alexander has
8 developed recommendations pertaining to service quality and universal service that
9 would further provide both protection and benefits.

10 Q. WILL YOUR CONDITIONS, IN CONJUNCTION WITH MS. ALEXANDER'S
11 RECOMMENDATIONS, ENSURE CUSTOMER BENEFITS FROM THE
12 MERGER?

13 A. Protective conditions are very helpful -- even essential -- but they cannot guarantee either
14 affirmative benefits or absence of harm from a merger. Important risks cannot be
15 completely eliminated. This is particularly true in this case because of a general lack of
16 experience in the U.S. with private equity acquisitions of utilities. However, I believe
17 that my recommended distribution rate cap would provide an affirmative benefit.

18 Q. HAVE THE APPLICANTS PROPOSED ANY PROTECTIVE CONDITIONS?

19 A. The Applicants and the Consortium have made certain, limited proposals, but these
20 proposals mainly take the form of a statement of intention to maintain the status quo.
21 This would include assertions to maintain or enhance service quality, retain existing
22 management, complete the ongoing infrastructure improvement plan, maintain the
23 Pittsburgh headquarters, honor existing union and employee arrangements and retain the
24 current role in the community. For the most part, these are stated as the Consortium's
25 intentions, but to a large extent they appear to be non-binding or not enforceable. In

1 addition, Applicants and the Consortium agree not to seek recovery of transaction costs.
2 (Response to OCA III-21)

3 Q. IN LIGHT OF THE ABSENCE OF PROTECTIONS AND AFFIRMATIVE,
4 SUBSTANTIAL BENEFITS IN THE APPLICATION AND TESTIMONY,
5 WHAT DO YOU RECOMMEND?

6 A. At this time, I recommend requiring conditions addressing the following principal areas,
7 as discussed in the subsections below.

8 A. **Distribution Rate Cap**

9 Q. ARE YOU RECOMMENDING ANY CONDITIONS THAT WOULD
10 INCREASE THE LIKELIHOOD THAT THE MERGER WOULD PROVIDE
11 CUSTOMERS WITH AFFIRMATIVE BENEFITS?

12 A. Yes. I recommend that the Commission require as a condition of approval a distribution
13 rate cap through year-end 2010. Since the earliest that Duquesne could obtain higher
14 distribution rates would be roughly January 1, 2008 (if it filed for higher rates in early
15 2007), this provides an "incremental" three-year rate cap.

16 Q. WHY IS THE RATE CAP CONDITION REASONABLE GIVEN THAT
17 APPLICANTS CLAIM NO SYNERGY SAVINGS?

18 A. In my judgment, this condition is needed to provide any benefits from the merger. In
19 recognition that Applicants identify no synergy savings, I am not recommending any rate
20 reduction, rate credits or synergy savings sharing that other electric utility mergers often
21 include. A rate cap will require cost control discipline by the new management of
22 Duquesne to meet profit targets.

23 *There are two key factors to consider in including the distribution rate cap as I*
24 *recommend. First, there seems to be an unreasonable imbalance of shareholders and*
25 *customer benefits. As mentioned earlier, shareholders will enjoy nearly \$300 million in*

1 market premium benefits from the transaction and zero for customers. This is inequitable
2 on its face. Second, we are not dealing with a situation where it has been many years
3 since the utility has obtained a rate increase. DLC just received a distribution service rate
4 increase through settlement of \$117 million, plus a pass-through mechanism for
5 transmission cost changes. I am not recommending any change to the transmission pass-
6 through mechanism.

7 **B. Corporate Governance for DLC/Affiliate Agreement**

8 Q. WHAT IS THE PLAN FOR CORPORATE GOVERNANCE POST MERGER?

9 A. The anticipated corporate governance is briefly described in the testimony of both Mr.
10 O'Brien and Mr. Leslie, with additional detail provided in response to OCA III-16.⁷ Mr.
11 O'Brien does not perceive the planned corporate governance as resulting in a significant
12 change: "I do not think there will be any significant change in the direction of our
13 business." (Applicants Statement No. 1, page 16) As he explains, the current Board will
14 be replaced by representatives of the various Consortium funds with Mr. Leslie serving as
15 Board Chairman. Mr. O'Brien in his CEO capacity will interact with and report directly
16 to the Board, just as he does today, as well as serving on the Board.

17 At pages 10-11, Mr. Leslie provides a similar description of corporate governance
18 stating that the sole function of the Board (to be populated by the DLC CEO and
19 Consortium representatives) is "to supervise the operations of DLH and Duquesne
20 Light." He goes on to say that there presently is no intention to merge DLH (and by
21 implication DLC) with any other Macquarie investment, but such an arrangement is
22 possible in the future, and at that time would be "based on an analysis of DQE."

23 Both Mr. Leslie on behalf of the Consortium and Mr. O'Brien on behalf of DLC
24 suggest that corporate governance will not change substantially. Just as the current DLH

⁷ In addition to the Board, which is the decision-making body, this response also describes a Management Committee, which advises the Board, and an "Asset Manager" who will be a Macquarie employee.

1 Board oversees the operations of DLC, the new Consortium-based Board will be playing
2 the same role, with Mr. Leslie serving as Chairman.

3 Q. DO YOU CONCUR WITH THESE WITNESSES THAT THE PLANNED
4 CORPORATE GOVERNANCE IS NOT A MAJOR CHANGE FROM THE
5 EXISTING GOVERNANCE?

6 A. No, not necessarily. The proposed structure introduces an important change in
7 perspective that raises a couple of concerns. The corporate decision makers (i.e., the
8 Board) would be Mr. Leslie and four other fund representatives and the DLC CEO, some
9 of whom may not even be located in the U.S. While DLC will have a responsibility to
10 provide cash flow and returns for its six owners, as a public utility, it also has obligations
11 to be responsive to its customers, the local community and this Commission. The Board
12 described by Mr. Leslie understandably will be focused on the management and strategic
13 direction of DLH/DLC that best meets the needs and investment objectives of the funds.
14 This is an important change in the Board perspective that could affect corporate policies,
15 financial polices and strategic plans.

16 A second concern pertains to the absence of market discipline. As a publicly-
17 traded corporation *Duquesne Holdings* (with DLC being the principal subsidiary) now
18 must operate in a transparent manner, with extensive public disclosure of its business
19 activities, risks and financial performance. Its performance is overseen not only by its
20 Board of Directors but also by the operations of public securities markets, principally the
21 stock market. In fact, capital markets serve to discipline and evaluate the performance of
22 the Board as well as that of the company itself. This absence of market discipline and
23 transparency under the proposed "private equity" Board of Directors is a significant
24 change from the present governance structure.

1 Q. WHAT DO YOU RECOMMEND TO ADDRESS THESE CONCERNS?

2 A. The corporate governance structure identified by Mr. Leslie clearly is the result of the
3 private equity ownership arrangement. Nonetheless, I believe that there is some room for
4 improvement that can be achieved by broadening the Board of Directors membership.⁸
5 The proposed private equity structure can be preserved, while addressing the concerns
6 discussed above, by including four outside directors on the Board along with the DLC
7 CEO and the five fund representatives. It also would be desirable if at least two of the
8 four outside directors are Duquesne service area residents. This more diverse Board
9 would bring a broader (including a "local") perspective to the oversight and strategic
10 direction of DLH/DLC while properly representing investor interests. Such a Board
11 potentially will be more responsive to the interests of both the Commission and local
12 community.

13 I believe that it is more important for a public utility than a non-regulated
14 company to have such a broad-based Board due to the fact that the utility has explicit
15 public interest responsibilities to its customers, its regulators and the local community
16 that comprises its franchise service territory. These responsibilities are part of the quid
17 pro quo for being granted monopoly status and an exclusive franchise to serve.

18 Q. WILL THE MACQUARIE GROUP PLAY A ROLE BEYOND THE
19 CORPORATE GOVERNANCE JUST DESCRIBED?

20 A. Yes. As further discussed by Mr. Leslie, Consortium members may provide management
21 and other professional services to DLC although these services apparently have not yet
22 been defined. It is clear that the provision of such services would be considered for

⁸ According to the Duquesne Light Holdings Annual Report to Shareholders, the present Board includes nine members (including Mr. O'Brien as an inside director). The Board appears to be diverse with most of the Board members active in the Pittsburgh or Western Pennsylvania area, both in terms of business and community activities (i.e., educational, charitable or cultural).

1 regulatory purposes to be affiliate transactions and therefore subject to the Commission's
2 oversight.

3 As stated in the Application and Mr. Leslie's testimony, affiliate transactions are
4 provided at cost pursuant to the Amended and Restated Administrative Services
5 Agreement among DLC, its parent and its affiliate. Applicants and the Consortium seek
6 authority to amend this existing agreement to include DQE Holdings and Macquarie
7 Bank Limited, its subsidiaries and affiliates. Mr. Leslie states that this amendment will
8 make possible DLC's access to the Consortium's expertise and resources, thereby
9 benefiting utility operations.

10 Q. DO YOU HAVE ANY OBJECTION TO THIS REQUEST?

11 A. Yes. This request cannot be approved at this time because the Applicants have not yet
12 provided the proposed amendments to the existing Services Agreement. Until this is
13 done and the amendments are determined to be appropriate, this request to authorize
14 transactions with the Consortium members (and/or their affiliates) should not be granted.
15 Moreover, this request appears to be integral to the merger itself. Hence, Applicants
16 must be required to submit the amended agreement to the parties for their review and to
17 the Commission for its review and approval. The merger transaction must not be
18 permitted to close until the affiliate transaction agreement issues are fully resolved.

19 C. **Cost of Capital Issues**

20 Q. WHAT ARE YOUR CONCERNS REGARDING COST OF CAPITAL?

21 A. In the context of Commission approval of this merger, there are several issues pertaining
22 to the cost of capital that warrant protective conditions. The issues that I have identified
23 would include the following:

- 24 • Customers should be protected against any increase in the DLC cost of capital
25 (and therefore fair rate of return) as a result of the merger, including cost of

1 capital increases associated with the Consortium's plans to change capital
2 structure in a manner that could adversely impact customers.

- 3 • Post transaction, DLC should not serve as a source of credit or credit support
4 for any affiliates, including the Consortium funds or entities owned by the
5 funds.
- 6 • DLC will incur substantial debt redemption costs as a result of the
7 capitalization changes proposed by the Consortium. Ratepayers should not be
8 charged for these costs absent a clear and convincing demonstration that the
9 incurrence of these costs is beneficial to customers.

10 Q. WILL THIS TRANSACTION IMPACT DLC'S COST OF CAPITAL?

11 A. Yes, it will. For reasons that are not entirely clear, the Consortium apparently intends to
12 substantially increase the common equity ratio of DLC, while at the same time adding
13 debt to the Duquesne Light Holding balance sheet. My concern is largely with the former
14 action.

15 Altering the DLC capital structure is not necessarily inappropriate if the purpose
16 is to minimize the Company's overall cost of capital or to maintain an investment grade
17 credit rating. However, in this case the DLC common equity ratio is being increased
18 from about 44 percent (which clearly is within the range of reasonableness for a low-risk
19 delivery service utility) to a completely unreasonable and overly expensive 69 percent.⁹
20 Moreover, in response to RESA III-2 (Confidential), Applicants provide the projected
21 DLC capital structures for 2008 and 2012, indicating continued use of an unacceptably
22 high equity ratio, that if used for ratemaking would improperly penalize customers.

23 Although capital structure is the most glaring adverse impact, there also is some
24 risk of increases in the cost of debt and equity associated with the merger. I earlier

⁹ See "Presentation to Interested Parties", October 18, 2006, page 13.

1 mentioned the negative credit rating reports following the merger announcement. At this
2 point in time, I am not predicting an increase in debt or equity cost rates attributable to
3 the merger, but it is certainly a possibility, particularly if the private equity-dominated
4 Board of Directors changes DLC's financial or business policies.

5 Q. GIVEN THESE CONCERNS, WHAT DO YOU RECOMMEND?

6 A. As an approval condition, DLC should not be permitted to include in its fair rate of return
7 for ratemaking a cost of capital premium attributable to the merger. This must be
8 applicable to both Pa PUC ratemaking as well as FERC ratemaking in order to protect
9 customers. In addition, there must be explicit recognition that the planned 69 percent
10 common equity ratio is improper for ratemaking (both at the Pa PUC and FERC). I note
11 that DLC's 2006 rate case settlement employed a 45.0 percent common equity ratio. In
12 future rate proceedings, DLC should be required to provide explicit and convincing
13 justification for the use (for ratemaking) of a common equity ratio higher than the current
14 45 percent.

15 A related issue pertains to the redemption costs associated with the plans to retire
16 substantial amounts of debt. The response to OCA III-15 estimates those costs at \$9
17 million and seems to indicate that DLC will seek rate recovery of those expenses in a
18 future rate proceeding. DLC should not be permitted to seek rate recovery unless it can
19 demonstrate that the incurrence of these redemption costs is cost effective and provides a
20 net benefit to customers. This explicit demonstration must be provided for both FERC
21 and Pa PUC rate cases in order for those expenses to be eligible for rate recovery.

1 Q. ARE THERE ANY OTHER COST OF CAPITAL CONDITIONS THAT
2 SHOULD BE REQUIRED?

3 A. Yes. To protect DLC's financial integrity and avoid cross subsidization, the Company
4 should not be permitted to make loans, extend credit, provide credit support, loan
5 guarantees or pledge assets for any affiliate, including Consortium members and entities
6 in which they have an investment interest without first obtaining Commission approval.¹⁰
7 In that regard, the response to OCA III-13 indicates that the Consortium intends to
8 replace DLC's existing Credit Agreement with a new (smaller) agreement to align it with
9 that of the parent company. It should be noted that the parent has a weaker credit rating
10 than DLC. Hence, a single, combined Credit Agreement for DLC and its parent has the
11 potential to increase DLC's borrowing costs. DLC should not combine its short-term
12 borrowing agreement with that of its parent (or another affiliate) if doing so will increase
13 its cost of borrowing.

14 **D. Other Ratemaking Issues**

15 Q. ARE THERE OTHER RATEMAKING ISSUES THAT REQUIRE
16 PROTECTIVE CONDITIONS?

17 A. Yes, there are two additional issues of concern. First, ratepayers must not be required to
18 pay a higher Capital Stock Tax as part of retail or wholesale (i.e., FERC transmission)
19 rates due to the merger. Second, customers should not be charged for any merger
20 transactions costs as part of either retail or wholesale rates.

21 Q. WHY IS THE PENNSYLVANIA CAPITAL STOCK TAX AT ISSUE?

22 A. Applicants' response to OCA II-2 states that "The Acquisition will increase the
23 Pennsylvania Capital Stock Tax for Duquesne Light Company due to the increase in the

¹⁰ This condition is not intended to affect the operation of the Cash Pool with DLC and DLH (and subsidiaries) recently approved by the Commission in Docket No. G-00051141. But this would not be extended to the Consortium funds.

1 net common equity after the merger.” OCA V-I sought a quantification for the increase,
2 but the response indicated that no estimate had been prepared. However, the response
3 also stated that the increase is not expected to be large. OCA V-2 inquired as to whether
4 the Company would absorb this small increase rather than flow it through in rates. The
5 response indicated that Applicants do not agree to absorb the increase, but at this time do
6 not take a position on cost recovery.

7 Given the acknowledged absence of any synergy savings or clear benefits from
8 this merger, I believe that an increase in the Pennsylvania Capital Stock Tax caused by
9 the merger should not be reflected in either PAPUC determined rates or rates set by
10 FERC for transmission.

11 Q. ARE THE APPLICANTS SEEKING RECOVERY OF TRANSACTION COSTS
12 FOR THE MERGER?

13 A. As stated in response to OCA III-21 (confidential), Applicants are not seeking the
14 recovery of transactions costs from customers. Nonetheless, some clarification is
15 required. This prohibition on rate recovery should apply to both FERC transmission rates
16 as well as PAPUC distribution rates. Moreover, it should cover all categories of
17 transactions costs and not just those listed in OCA III-21. For example, it should include
18 any employee-related transition costs, regulatory approval-related expenses, etc. In short,
19 it would exclude from rates any transition and transactions costs incurred by or allocated
20 to DLC that are merger transaction related.

21 E. **Reporting**

22 Q. WHY WOULD A PERIODIC REPORTING ON THE STATUS OF THE
23 MERGER BE DESIRABLE?

24 A. There are several reasons why I believe some system of progress reporting should
25 accompany this merger. This includes the general lack of experience in the U.S. with

1 private equity funds taking over large utilities (and the associated governance issues), an
2 absence of synergy savings, proposed changes in financial structure, uncertainty over the
3 role of affiliate transactions and the potential for harm. It would be appropriate for DLC
4 to submit annual status reports to the Commission, with supporting testimony in the next
5 rate case. The rate case would provide a forum for review of the post-merger experience,
6 and a determination could be made at that time whether further progress reports are
7 warranted.

8 Q. WHAT SHOULD THE ANNUAL PROGRESS REPORTS ADDRESS?

9 A. The reports should document the post merger experience, including any savings achieved
10 or higher costs incurred, a summary of affiliate transactions (including the role of
11 Consortium members in providing technical and management expertise), the
12 implementation of “best practices” as described in the Application and testimony,
13 financing and access to capital, a summary of transaction costs (or “transition costs”)
14 incurred by DLC and the status of DLC key personnel. This last item would include the
15 utilization or transfer of DLC technical and managerial personnel on behalf of
16 Consortium members.

17 F. **Other Corporate Operational Issues**

18 Q. ARE THERE OTHER CONDITIONS PERTAINING TO DLC’S FUTURE
19 OPERATIONS THAT SHOULD BE ADDRESSED?

20 A. Yes. Applicants and the Consortium have stated their intention to maintain a Pittsburgh
21 corporate headquarters. This should be an explicit condition of approval. However, that
22 condition will not be meaningful absent an explicit requirement that management retain
23 over time approximately the same overall level of corporate functions (and associated
24 staffing) at the Pittsburgh-sited headquarters. Adherence to this condition would require
25 periodic monitoring through a reporting requirement. In addition, DLC should maintain

1 full access to books, records and personnel of DLC, DLH and its subsidiaries at the
2 Pittsburgh headquarters.

3 A further and related concern is DLC's retention of key professional technical
4 staff and management. As mentioned, there is a significant risk that in an effort to pursue
5 additional acquisitions, Consortium members could devote the time of key DLC staff or
6 management to non-DLC activities or transfer them entirely to another venture. This
7 requires both a reporting plan as well as the development of a key personnel retention
8 plan to ensure DLC is not weakened.

1 V. CONCLUSION

2 Q. DO YOU BELIEVE THE PROPOSED TRANSACTION, AS FILED, IS IN THE
3 PUBLIC INTEREST?

4 A. No, I do not. The only tangible, substantial benefit is the nearly \$300 million market
5 premium that will be enjoyed by shareholders. None of the other benefits asserted in the
6 Application have been demonstrated. Moreover, the proposed transaction introduces a
7 number of significant risks, the potential for cost penalties and corporate governance
8 concerns. The as-filed merger request, does not meet this Commission's standard of
9 approval which requires affirmative, substantial benefits.

10 Q. CAN THIS PROPOSED MERGER BE IMPROVED THROUGH
11 CONDITIONS?

12 A. Yes, *such conditions, as outlined in my testimony and the recommendations of OCA*
13 *witness Alexander, are essential and will improve the attractiveness to customers of the*
14 *merger. The conditions that I am sponsoring are summarized in Appendix B.*

15 Q. DOES THIS COMPLETE YOUR DIRECT TESTIMONY?

16 A. This completes my Direct Testimony at this time.
17
18

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APPENDIX A

PROFESSIONAL QUALIFICATIONS OF

MATTHEW I. KAHAL

MATTHEW I. KAHAL

Mr. Kahal is currently an independent consulting economist, specializing in energy economics, public utility regulation and financial analysis. Over the past two decades, his work has encompassed electric utility integrated resource planning (IRP), power plant licensing and a wide range of utility financial issues. In the financial area he has conducted numerous cost of capital studies and addressed other financial issues for electric, gas, telephone and water utilities. Mr. Kahal's work in recent years has shifted to electric utility restructuring, mergers and competition.

Mr. Kahal has provided expert testimony on more than 250 occasions before state and federal regulatory commissions and the U.S. Congress. His testimony has covered need for power, integrated resource planning, cost of capital, purchased power practices and contracts, merger economics, industry restructuring and various other regulatory policy issues.

Education:

B.A. (Economics) - University of Maryland, 1971.

M.A. (Economics) - University of Maryland, 1974.

Ph.D. candidate - University of Maryland, completed all course work and qualifying examinations.

Previous Employment:

1981-2001 - Exeter Associates, Inc. (founding Principal).

1980-1981 - Member of the Economic Evaluation Directorate, The Aerospace Corporation, Washington, D.C. office.

1977-1980 - Economist, Washington, D.C. consulting firm.

1972-1977 - Research/Teaching Assistant and Instructor, Department of Economics, University of Maryland (College Park).

1975-1977 - Lecturer in Business/Economics, Montgomery College.

Professional Work Experience:

Mr. Kahal has more than twenty years experience managing and conducting consulting assignments relating to public utility economics and regulation. In 1981, he and five colleagues founded the firm of Exeter Associates, Inc. and for the next 20 years he served as a Principal and corporate officer in the firm. During that time, he supervised multi-million dollar support contracts with the State of Maryland and directed the technical work conducted both by Exeter

professional staff and numerous subcontractors. Additionally, Mr. Kahal took the lead role at Exeter in consulting to the firm's other governmental and private clients in the areas of financial analysis, utility mergers, electric restructuring and utility purchase power contracts.

At the Aerospace Corporation, Mr. Kahal served as an economic consultant to the Strategic Petroleum Reserve (SPR). In that capacity he participated in a detailed financial assessment of the SPR, and developed an econometric forecasting model of U.S. petroleum industry inventories. That study has been used to determine the extent to which private sector petroleum stocks can be expected to protect the U.S. from the impacts of oil import interruptions.

Before entering consulting, Mr. Kahal held faculty positions with the Department of Economics at the University of Maryland and with Montgomery College teaching courses on economic principles, business and economic development.

Publications and Consulting Reports:

Projected Electric Power Demands of the Baltimore Gas and Electric Company, Maryland Power Plant Siting Program, 1979.

Projected Electric Power Demands of the Allegheny Power System, Maryland Power Plant Siting Program, January 1980.

An Econometric Forecast of Electric Energy and Peak Demand on the Delmarva Peninsula, Maryland Power Plant Siting Program, March 1980 (with Ralph E. Miller).

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"Nuclear Power and Investor Perceptions of Risk," (with Ralph E. Miller), published in The Energy Industries in Transition: 1985-2000 (John P. Weyant and Dorothy Sheffield, eds.), 1984.

The Financial Impact of Potential Department of Energy Rate Recommendations on the Commonwealth Edison Company, prepared for the U.S. Department of Energy, October 1984.

"Discussion Comments," published in Impact of Deregulation and Market Forces on Public Utilities: The Future of Regulation (Harry Trebing, ed.), Institute of Public Utilities, Michigan State University, 1985.

An Econometric Forecast of the Electric Power Loads of Baltimore Gas and Electric Company, two volumes (with others), prepared for the Maryland Power Plant Siting Program, 1985.

A Survey and Evaluation of Demand Forecast Methods in the Gas Utility Industry, prepared for the Public Utilities Commission of Ohio, Forecasting Division, November 1985, (with Terence Manuel).

A Review and Evaluation of the Load Forecasts of Houston Lighting & Power Company and Central Power & Light Company -- Past and Present, prepared for the Texas Public Utility Commission, December 1985, (with Marvin H. Kahn).

Power Plant Cumulative Environmental Impact Report for Maryland, principal author of three of the eight chapters in the report (Paul E. Miller, ed.), PPSP-CEIR-5, March 1986.

"Potential Emissions Reduction from Conservation, Load Management, and Alternative Power," published in Acid Deposition in Maryland: A Report to the Governor and General Assembly, Maryland Power Plant Research Program, AD-87-1, January 1987.

Determination of Retrofit Costs at the Oyster Creek Nuclear Generating Station, March 1988, prepared for Versar, Inc., New Jersey Department of Environmental Protection.

Excess Deferred Taxes and the Telephone Utility Industry, April 1988, prepared on behalf of the National Association of State Utility Consumer Advocates.

Toward a Proposed Federal Policy for Independent Power Producers, comments prepared on behalf of the Indiana Consumer Counselor, FERC Docket EL87-67-000, November 1987.

Review and Discussion of Regulations Governing Bidding Programs, prepared for the Pennsylvania Office of Consumer Advocate, June 1988.

A Review of the Proposed Revisions to the FERC Administrative Rules on Avoided Costs and Related Issues, prepared for the Pennsylvania Office of Consumer Advocate, April 1988.

Review and Comments on the FERC NOPR Concerning Independent Power Producers, prepared for the Pennsylvania Office of Consumer Advocate, June 1988.

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An Economic and Need for Power Evaluation of Baltimore Gas & Electric Company's Perryman Plant, May 1991, prepared for the Maryland Department of Natural Resources (with M. Fullenbaum).

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A Need for Power Review of Delmarva Power & Light Company's Dorchester Unit 1 Power Plant, March 1993, prepared for the Maryland Department of National Resources (with M. Fullenbaum)

The AES Warrior Run Project: Impact on Western Maryland Economic Activity and Electric Rates, February 1993, prepared for the Maryland Power Plant Research Program (with Peter Hall).

An Economic Perspective on Competition and the Electric Utility Industry, November 1994. Prepared for the Electric Consumers' Alliance.

PEPCO's Clean Air Act Compliance Plan: Status Report, prepared for the Maryland Power Plant Research Plan, January 1995 (w/Diane Mountain, Environmental Resources Management, Inc.).

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A Status Report on Electric Utility Restructuring: Issues for Maryland, prepared for the Maryland Power Plant Research Program, November 1995 (with Daphne Psacharopoulos).

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Electric Restructuring and the Environment: Issue Identification for Maryland, March 1997, prepared for the Maryland Power Plant Research Program (with Environmental Resource Management, Inc.)

An Analysis of Electric Utility Embedded Power Supply Costs, prepared for Power-Gen International Conference, Dallas, Texas, December 1997.

Market Power Outlook for Generation Supply in Louisiana, December 2000, prepared for the Louisiana Public Service Commission (with others).

A Review of Issues Concerning Electric Power Capacity Markets, prepared for the Maryland Power Plant Research Program, December 2001 (with B. Hobbs and J. Inon).

The Economic Feasibility of Air Emissions Controls at the Brandon Shores and Morgantown Coal-fired Power Plants, February 2005, (prepared for the Chesapeake Bay Foundation).

The Economic Feasibility of Power Plant Retirements on the Entergy System, September 2005 with Phil Hayet (prepared for the Louisiana Public Service Commission).

Expert Report on Capital Structure, Equity and Debt Costs, prepared for the Edmonton Regional Water Customers Group, August 30, 2006.

Maryland's Options to Reduce and Stabilize Electric Power Prices Following Restructuring, with Steven L. Estomin, prepared for the Power Plant Research Program, Maryland Department of Natural Resources, September 2006.

Conference and Workshop Presentations:

Workshop on State Load Forecasting Programs, sponsored by the Nuclear Regulatory Commission and Oak Ridge National Laboratory, February 1982 (presentation on forecasting methodology).

Fourteenth Annual Conference of the Michigan State University Institute for Public Utilities, December 1982 (presentation on problems in forecasting).

Conference on Conservation and Load Management, sponsored by the Massachusetts Energy Facilities Siting Council, May 1983 (presentation on cost-benefit criteria).

Maryland Conference on Load Forecasting, sponsored by the Maryland Power Plant Siting Program and the Maryland Public Service Commission, June 1983 (presentation on overforecasting power demands).

The 5th Annual Meetings of the International Association of Energy Economists, June 1983 (presentation on evaluating weatherization programs).

The NARUC Advanced Regulatory Studies Program (presented lectures on capacity planning for electric utilities), February 1984.

The 16th Annual Conference of the Institute of Public Utilities, Michigan State University (discussant on phase-in and excess capacity), December 1984.

U.S. Department of Energy Utilities Conference, Las Vegas, Nevada (presentation of current and future regulatory issues), May 1985.

The 18th Annual Conference of the Institute of Public Utilities, Michigan State University, Williamsburg, Virginia, December 1986 (discussant on cogeneration).

The NRECA Conference on Load Forecasting, sponsored by the National Rural Electric Cooperative Association, New Orleans, Louisiana, December 1987 (presentation on load forecast accuracy).

The Second Rutgers/New Jersey Department of Commerce Annual Conference on Energy Policy in the Middle Atlantic States, Rutgers University, April 1988 (presentation on spot pricing of electricity).

The NASUCA 1988 Mid-Year Meeting, Annapolis, Maryland, June 1988, sponsored by the National Association of State Utility Consumer Advocates (presentation on the FERC electricity avoided cost NOPRs).

The Thirty Second Atlantic Economic Society Conference, Washington, D.C., October 1991 (presentation of a paper on cost of capital issues for the Bell Operating Companies).

The NASUCA 1993 Mid-Year Meeting, St. Louis, Missouri, sponsored by the National Association of State Utility Consumer Advocates, June 1993 (presentation on regulatory issues concerning electric utility mergers).

The NASUCA and NARUC annual meetings in New York City, November 1993 (presentations and panel discussions on the emerging FERC policies on transmission pricing).

The NASUCA annual meetings in Reno, Nevada, November 1994 (presentation concerning the FERC NOPR on stranded cost recovery).

U.S. Department of Energy Utilities/Energy Management Workshop, March 1995 (presentation concerning electric utility competition).

The 1995 NASUCA Mid-Year Meeting, Breckenridge, Colorado, June 1995, (presentation concerning the FERC rulemaking on electric transmission open access).

The 1996 NASUCA Mid-Year Meeting, Chicago, Illinois, June 1996 (presentation concerning electric utility merger issues).

Conference on "Restructuring the Electric Industry," sponsored by the National Consumers League and Electric Consumers Alliance, Washington, D.C., May 1997 (presentation on retail access pilot programs).

The 1997 Mid-Atlantic Conference of Regulatory Utilities Commissioners (MARUC), Hot Springs, Virginia, July 1997 (presentation concerning electric deregulation issues).

Power-Gen '97 International Conference, Dallas, Texas, December 1997 (presentation concerning utility embedded costs of generation supply).

Consumer Summit on Electric Competition, sponsored by the National Consumers League and Electric Consumers' Alliance, Washington, D.C., March 2001 (presentation concerning generation supply and reliability).

National Association of State Utility Consumer Advocates, Mid-Year Meetings, Austin, Texas, June 16-17, 2002 (presenter and panelist on RTO/Standard Market Design issues).

Louisiana State Bar Association, Public Utility Section, October 2, 2002. (Presentation on Performance-Based Ratemaking and panelist on RTO issues). Baton Rouge, Louisiana.

Virginia State Corporation Commission/Virginia State Bar, Twenty Second National Regulatory Conference, May 10, 2004. (Presentation on Electric Transmission System Planning.) Williamsburg, Virginia.

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
1.	27374 & 27375 October 1978	Long Island Lighting Company	New York Counties	Nassau & Suffolk	Economic impacts of proposed rate increase
2.	6807 January 1978	Generic	Maryland	MD Power Plant Siting Program	Load forecasting
3.	78-676-EL-AIR February 1978	Ohio Power Company	Ohio	Ohio Consumers' Counsel	Test year sales and revenues
4.	17667 May 1979	Alabama Power Company	Alabama	Attorney General	Test year sales, revenues, costs and load forecasts
5.	None April 1980	Tennessee Valley Authority	TVA Board	League of Women Voters	Time-of-use pricing
6.	R-80021082	West Penn Power Company	Pennsylvania	Office of Consumer Advocate	Load forecasting, marginal cost pricing
7.	7259 (Phase I) October 1980	Potomac Edison Company	Maryland	MD Power Plant Siting Program	Load forecasting
8.	7222 December 1980	Delmarva Power & Light Company	Maryland	MD Power Plant Siting Program	Need for plant, load forecasting
9.	7441 June 1981	Potomac Electric Power Company	Maryland	Commission Staff	PURPA standards
10.	7159 May 1980	Baltimore Gas & Electric	Maryland	Commission Staff	Time-of-use pricing
11.	81-044-E-42T	Monongahela Power	West Virginia	Commission Staff	Time-of-use rates
12.	7259 (Phase II) November 1981	Potomac Edison Company	Maryland	MD Power Plant Siting Program	Load forecasting, load management
13.	1606 September 1981	Blackstone Valley Electric and Narragansett	Rhode Island	Division of Public Utilities	PURPA standards
14.	RID 1819 April 1982	Pennsylvania Bell	Pennsylvania	Office of Consumer Advocate	Rate of return
15.	82-0152 July 1982	Illinois Power Company	Illinois	U.S. Department of Defense	Rate of return, CWIP

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16.	7559 September 1982	Potomac Edison Company	Maryland	Commission Staff	Cogeneration
17.	820150-EU September 1982	Gulf Power Company	Florida	Federal Executive Agencies	Rate of return, CWIP
18.	82-057-15 January 1983	Mountain Fuel Supply Company	Utah	Federal Executive Agencies	Rate of return, capital structure
19.	5200 August 1983	Texas Electric Service Company	Texas	Federal Executive Agencies	Cost of equity
20.	28069 August 1983	Oklahoma Natural Gas	Oklahoma	Federal Executive Agencies	Rate of return, deferred taxes, capital structure, attrition
21.	83-0537 February 1984	Commonwealth Edison Company	Illinois	U.S. Department of Energy	Rate of return, capital structure, financial capability
22.	84-035-01 June 1984	Utah Power & Light Company	Utah	Federal Executive Agencies	Rate of return
23.	U-1009-137 July 1984	Utah Power & Light Company	Idaho	U.S. Department of Energy	Rate of return, financial condition
24.	R-842590 August 1984	Philadelphia Electric Company	Pennsylvania	Office of Consumer Advocate	Rate of return
25.	840086-EI August 1984	Gulf Power Company	Florida	Federal Executive Agencies	Rate of return, CWIP
26.	84-122-E August 1984	Carolina Power & Light Company	South Carolina	South Carolina Consumer Advocate	Rate of return, CWIP, load forecasting
27.	CGC-83-G & CGC-84-G October 1984	Columbia Gas of Ohio	Ohio	Ohio Division of Energy	Load forecasting
28.	R-842621 October 1984	Western Pennsylvania Water Company	Pennsylvania	Office of Consumer Advocate	Test year sales
29.	R-842710 January 1985	ALLTEL Pennsylvania Inc.	Pennsylvania	Office of Consumer Advocate	Rate of return

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30.	ER-504 February 1985	Allegheny Generating Company	FERC	Office of Consumer Advocate	Rate of return
31.	R-842632 March 1985	West Penn Power Company	Pennsylvania	Office of Consumer Advocate	Rate of return, conservation, time-of-use rates
32.	83-0537 & 84-0555 April 1985	Commonwealth Edison Company	Illinois	U.S. Department of Energy	Rate of return, incentive rates, rate base
33.	Rulemaking Docket No. 11, May 1985	Generic	Delaware	Delaware Commission Staff	Interest rates on refunds
34.	29450 July 1985	Oklahoma Gas & Electric Company	Oklahoma	Oklahoma Attorney General	Rate of return, CWIP in rate base
35.	1811 August 1985	Bristol County Water Company	Rhode Island	Division of Public Utilities	Rate of return, capital structure
36.	R-850044 & R-850045 August 1985	Quaker State & Continental Telephone Companies	Pennsylvania	Office of Consumer Advocate	Rate of return
37.	R-850174 November 1985	Philadelphia Suburban Water Company	Pennsylvania	Office of Consumer Advocate	Rate of return, financial conditions
38.	U-1006-265 March 1986	Idaho Power Company	Idaho	U.S. Department of Energy	Power supply costs and models
39.	EL-86-37 & EL-86-38 September 1986	Allegheny Generating Company	FERC	PA Office of Consumer Advocate	Rate of return
40.	R-850287 June 1986	National Fuel Gas Distribution Corp.	Pennsylvania	Office of Consumer Advocate	Rate of return
41.	1849 August 1986	Blackstone Valley Electric	Rhode Island	Division of Public Utilities	Rate of return, financial condition
42.	86-297-GA-AIR November 1986	East Ohio Gas Company	Ohio	Ohio Consumers' Counsel	Rate of return
43.	U-16945 December 1986	Louisiana Power & Light Company	Louisiana	Public Service Commission	Rate of return, rate phase-in plan

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
44.	Case No. 7972 February 1987	Potomac Electric Power Company	Maryland	Commission Staff	Generation capacity planning, purchased power contract
45.	EL-86-58 & EL-86-59 March 1987	System Energy Resources and Middle South Services	FERC	Louisiana PSC	Rate of return
46.	ER-87-72-001 April 1987	Orange & Rockland	FERC	PA Office of Consumer Advocate	Rate of return
47.	U-16945 April 1987	Louisiana Power & Light Company	Louisiana	Commission Staff	Revenue requirement update phase-in plan
48.	P-870196 May 1987	Pennsylvania Electric Company	Pennsylvania	Office of Consumer Advocate	Cogeneration contract
49.	86-2025-EL-AIR June 1987	Cleveland Electric Illuminating Company	Ohio	Ohio Consumers' Counsel	Rate of return
50.	86-2026-EL-AIR June 1987	Toledo Edison Company	Ohio	Ohio Consumers' Counsel	Rate of return
51.	87-4 June 1987	Delmarva Power & Light Company	Delaware	Commission Staff	Cogeneration/small power
52.	1872 July 1987	Newport Electric Company	Rhode Island	Commission Staff	Rate of return
53.	WO 8606654 July 1987	Atlantic City Sewerage Company	New Jersey	Resorts International	Financial condition
54.	7510 August 1987	West Texas Utilities Company	Texas	Federal Executive Agencies	Rate of return, phase-in
55.	8063 Phase 1 October 1987	Potomac Electric Power Company	Maryland	Power Plant Research Program	Economics of power plant site selection
56.	00439 November 1987	Oklahoma Gas & Electric Company	Oklahoma	Smith Cogeneration	Cogeneration economics
57.	RP-87-103 February 1988	Panhandle Eastern Pipe Line Company	FERC	Indiana Utility Consumer Counselor	Rate of return

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58.	EC-88-2-000 February 1988	Utah Power & Light Co. PacifiCorp	FERC	Nucor Steel	Merger economics
59.	87-0427 February 1988	Commonwealth Edison Company	Illinois	Federal Executive Agencies	Financial projections
60.	870840 February 1988	Philadelphia Suburban Water Company	Pennsylvania	Office of Consumer Advocate	Rate of return
61.	870832 March 1988	Columbia Gas of Pennsylvania	Pennsylvania	Office of Consumer Advocate	Rate of return
62.	8063 Phase II July 1988	Potomac Electric Power Company	Maryland	Power Plant Research Program	Power supply study
63.	8102 July 1988	Southern Maryland Electric Cooperative	Maryland	Power Plant Research Program	Power supply study
64.	10105 August 1988	South Central Bell Telephone Co.	Kentucky	Attorney General	Rate of return, incentive regulation
65.	00345 August 1988	Oklahoma Gas & Electric Company	Oklahoma	Smith Cogeneration	Need for power
66.	U-17906 September 1988	Louisiana Power & Light Company	Louisiana	Commission Staff	Rate of return, nuclear power costs industrial contracts
67.	88-170-EL-AJR October 1988	Cleveland Electric Illuminating Co.	Ohio	Northeast-Ohio Areawide Coordinating Agency	Economic impact study
68.	1914 December 1988	Providence Gas Company	Rhode Island	Commission Staff	Rate of return
69.	U-12636 & U-17649 February 1989	Louisiana Power & Light Company	Louisiana	Commission Staff	<i>Disposition of litigation proceeds</i>
70.	00345 February 1989	Oklahoma Gas & Electric Company	Oklahoma	Smith Cogeneration	Load forecasting
71.	RP88-209 March 1989	Natural Gas Pipeline of America	FERC	Indiana Utility Consumer Counselor	Rate of return

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72. 8425 March 1989	Houston Lighting & Power Company	Texas	U.S. Department of Energy	Rate of return
73. EL89-30-000 April 1989	Central Illinois Public Service Company	FERC	Soyland Power Coop, Inc.	Rate of return
74. R-891208 May 1989	Pennsylvania American Water Company	Pennsylvania	Office of Consumer Advocate	Rate of return
75. 89-0033 May 1989	Illinois Bell Telephone Company	Illinois	Citizens Utility Board	Rate of return
76. 881167-EI May 1989	Gulf Power Company	Florida	Federal Executive Agencies	Rate of return
77. R-891218 July 1989	National Fuel Gas Distribution Company	Pennsylvania	Office of Consumer Advocate	Sales forecasting
78. 8063, Phase III Sept. 1989	Potomac Electric Power Company	Maryland	Depart. Natural Resources	Emissions Controls
79. 37414-S2 October 1989	Public Service Company of Indiana	Indiana	Utility Consumer Counselor	Rate of return, DSM, off- system sales, incentive regulation
80. October 1989	Generic	U.S. House of Reps. Comm. on Ways & Means	NA	Excess deferred income tax
81. 38728 November 1989	Indiana Michigan Power Company	Indiana	Utility Consumer Counselor	Rate of return
82. RP89-49-000 December 1989	National Fuel Gas Supply Corporation	FERC	PA Office of Consumer Advocate	Rate of return
83. R-891364 December 1989	Philadelphia Electric Company	Pennsylvania	PA Office of Consumer Advocate	Financial impacts (surrebuttal only)
84. RP89-160-000 January 1990	Trunkline Gas Company	FERC	Indiana Utility Consumer Counselor	Rate of return

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85.	EL90-16-000 November 1990	System Energy Resources, Inc.	FERC	Louisiana Public Service Commission	Rate of return
86.	89-624 March 1990	Bell Atlantic	FCC	PA Office of Consumer Advocate	Rate of return
87.	8245 March 1990	Potomac Edison Company	Maryland	Depart. Natural Resources	Avoided Cost
88.	000586 March 1990	Public Service Company of Oklahoma	Oklahoma	Smith Cogeneration Mgmt.	Need for Power
89.	38868 March 1990	Indianapolis Water Company	Indiana	Utility Consumer Counselor	Rate of return
90.	1946 March 1990	Blackstone Valley Electric Company	Rhode Island	Division of Public Utilities	Rate of return
91.	000776 April 1990	Oklahoma Gas & Electric Company	Oklahoma	Smith Cogeneration Mgmt.	Need for Power
92.	890366 May 1990, December 1990	Metropolitan Edison Company	Pennsylvania	Office of Consumer Advocate	Competitive Bidding Program Avoided Costs
93.	EC-90-10-000 May 1990	Northeast Utilities	FERC	Maine PUC, et. al.	Merger, Market Power, Transmission Access
94.	ER-891109125 July 1990	Jersey Central Power & Light	New Jersey	Rate Counsel	Rate of return
95.	R-901670 July 1990	National Fuel Gas Distribution Corp.	Pennsylvania	Office of Consumer Advocate	Rate of return Test year sales
96.	8201 October 1990	Delmarva Power & Light Company	Maryland	Depart. Natural Resources	Competitive Bidding, Resource Planning
97.	EL90-45-000 April 1991	Entergy Services, Inc.	FERC	Louisiana PSC	Rate of return
98.	GR90080786J January 1991	New Jersey Natural Gas	New Jersey	Rate Counsel	Rate of return

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
99.	90-256 January 1991	South Central Bell Telephone Co.	Kentucky	Attorney General	Rate of return
100.	U-17949A February 1991	South Central Bell Telephone Co.	Louisiana	Louisiana PSC	Rate of return
101.	ER90091090J April 1991	Atlantic City Electric Company	New Jersey	Rate Counsel	Rate of return
102.	8241, Phase I April 1991	Baltimore Gas & Electric Co.	Maryland	Dept. of Natural Resources	Environmental controls
103.	8241, Phase II May 1991	Baltimore Gas & Electric Company	Maryland	Dept. of Natural Resources	Need for Power, Resource Planning
104.	39128 May 1991	Indianapolis Water Company	Indiana	Utility Consumer Counselor	Rate of return, rate base, financial planning
105.	P-900485 May 1991	Duquesne Light Company	Pennsylvania	Office of Consumer Advocate	Purchased power contract and related ratemaking
106.	G900240 P910502 May 1991	Metropolitan Edison Co. Pennsylvania Electric Co.	Pennsylvania	Office of Consumer Advocate	Purchased power contract and related ratemaking
107.	GR901213915 May 1991	Elizabethtown Gas Co.	New Jersey	Rate Counsel	Rate of return
108.	91-5032 August 1991	Nevada Power Co.	Nevada	U.S. Dept. of Energy	Rate of return
109.	EL90-48-000 November 1991	Entergy Services	FERC	Louisiana PSC	Capacity transfer
110.	000662 September 1991	Southwestern Bell Telephone	Oklahoma	Attorney General	Rate of return
111.	U-19236 October 1991	Arkansas Louisiana Gas Company	Louisiana	Louisiana PSC Staff	Rate of return
112.	U-19237 December 1991	Louisiana Gas Service Company	Louisiana	Louisiana PSC Staff	Rate of return

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
113.	ER91030356J October 1991	Rockland Electric Company	New Jersey	Rate Counsel	Rate of return
114.	GR91071243J February 1992	South Jersey Gas Company	New Jersey	Rate Counsel	Rate of return
115.	GR91081393J March 1992	New Jersey Natural Gas Company	New Jersey	Rate Counsel	Rate of return
116.	P-870235 <u>et al.</u> March 1992	Pennsylvania Electric Company	Pennsylvania	Office of Consumer Advocate	Cogeneration contracts
117.	8413 March 1992	Potomac Electric Power Company	Maryland	Dept. of Natural Resources	IPP purchased power contracts
118.	39236 March 1992	Indianapolis Power & Light Company	Indiana	Utility Consumer Counselor	Least-cost planning Need for power
119.	R-912164 April 1992	Equitable Gas Company	Pennsylvania	Office of Consumer Advocate	Rate of return
120.	ER-91111698J May 1992	Public Service Electric & Gas Company	New Jersey	Rate Counsel	Rate of return
121.	U-19631 June 1992	Trans Louisiana Gas Company	Louisiana	PSC Staff	Rate of return
122.	ER-91121820J July 1992	Jersey Central Power & Light Company	New Jersey	Rate Counsel	Rate of return
123.	R-00922314 August 1992	Metropolitan Edison Company	Pennsylvania	Office of Consumer Advocate	Rate of return
124.	92-049-05 September 1992	US West Communications	Utah	Committee of Consumer Services	Rate of return
125.	92PUE0037 September 1992	Commonwealth Gas Company	Virginia	Attorney General	Rate of return
126.	EC92-21-000 September 1992	Entergy Services, Inc.	FERC	Louisiana PSC	Merger Impacts (Affidavit)

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127.	ER92-341-000 December 1992	System Energy Resources	FERC	Louisiana PSC	Rate of return
128.	U-19904 November 1992	Louisiana Power & Light Company	Louisiana	Staff	Merger analysis, competition competition issues
129.	8473 November 1992	Baltimore Gas & Electric Company	Maryland	Dept. of Natural Resources	QF contract evaluation
130.	IPC-E-92-25 January 1993	Idaho Power Company	Idaho	Federal Executive Agencies	Power supply clause
131.	E002/GR-92-1185 February 1993	Northern States Power Company	Minnesota	Attorney General	Rate of return
132.	92-102, Phase II March 1992	Central Maine Power Company	Maine	Staff	QF contracts prudence and procurements practices
133.	EC92-21-000 March 1993	Entergy Corporation	FERC	Louisiana PSC	Merger issues
134.	8489 March 1993	Delmarva Power & Light Company	Maryland	Dept. of Natural Resources	Power plant certification
135.	11735 April 1993	Texas Electric Utilities Company	Texas	Federal Executives Agencies	Rate of return
136.	2082 May 1993	Providence Gas Company	Rhode Island	Division of Public Utilities	Rate of return
137.	P-00930715 December 1993	Bell Telephone Co. of Pennsylvania	Pennsylvania	Office of Consumer Advocate	Rate of return, financial projections, Bell/TCL merger
138.	R-00932670 February 1994	Pennsylvania-American Water Company	Pennsylvania	Office of Consumer Advocate	Rate of return
139.	8583 February 1994	Conowingo Power Co.	Maryland	Dept. of Natural Resources	Competitive bidding for power supplies
140.	E-015/GR-94-001 April 1994	Minnesota Power & Light Co.	Minnesota	Attorney General	Rate of return

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141. CC Docket No. 94-1 May 1994	Generic Telephone	FCC	MCI Comm. Corp.	Rate of return
142. 92-345, Phase II June 1994	Central Maine Power Co.	Maine	Advocacy Staff	Price Cap Regulation Fuel Costs
143. 93-11065 April 1994	Nevada Power Co.	Nevada	Federal Executive Agencies	Rate of return
144. 94-0065 May 1994	Commonwealth Edison Co.	Illinois	Federal Executive Agencies	Rate of return
145. GR94010002J June 1994	South Jersey Gas Co.	New Jersey	Rate Counsel	Rate of return
146. WR94030059 July 1994	New Jersey-American Water Co.	New Jersey	Rate Counsel	Rate of return
147. RP91-203-000 June 1994	Tennessee Gas Pipeline Company	FERC	Customer Group	Environmental Externalities (oral testimony only)
148. ER94-998-000 July 1994	Ocean State Power	FERC	Boston Edison Co.	Rate of return
149. R-00942986 July 1994	West Penn Power Co.	Pennsylvania	Office of Consumer Advocate	Rate of return, emission allowances
150. 94-121 August 1994	South Central Bell Telephone Co.	Kentucky	Attorney General	Rate of return
151. 35854-S2 November 1994	PSI Energy, Inc.	Indiana	Utility Consumer Counsel	Merger savings and allocations
152. IPC-E-94-5 November 1994	Idaho Power Co.	Idaho	Federal Executive Agencies	Rate of return
153. November 1994	Edmonton Water	Alberta, Canada	Regional Customer Group	Rate of return (rebuttal only)
154. 90-256 December 1994	South Central Bell Telephone Co.	Kentucky	Attorney General	Incentive Plan True-Ups

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155.	U-20925 February 1995	Louisiana Power & Light Company	Louisiana	PSC Staff	Rate of return Industrial contracts Trust fund earnings
156.	R-00943231 February 1995	Pennsylvania-American Water Company	Pennsylvania	Consumer Advocate	Rate of return
157.	8678 March 1995	Generic	Maryland	Dept. Natural Resources	Electric Competition Incentive Regulation (oral only)
158.	R-000943271 April 1995	Pennsylvania Power & Light Company	Pennsylvania	Consumer Advocate	Rate of return Nuclear decommissioning Capacity Issues
159.	U-20925 May 1995	Louisiana Power & Light Company	Louisiana	Commission Staff	Class cost of service issues
160.	2290 June 1995	Narragansett Electric Company	Rhode Island	Division Staff	Rate of return
161.	U-17949E June 1995	South Central Bell Telephone Company	Louisiana	Commission Staff	Rate of return
162.	2304 July 1995	Providence Water Supply Board	Rhode Island	Division Staff	Cost recovery of capital spending program
163.	ER95-625-000 <u>et al.</u> August 1995	PSJ Energy, Inc.	FERC	Office of Utility Consumer Counselor	Rate of return
164.	P-00950915 <u>et al.</u> September 1995	Paxton Creek Cogeneration Assoc.	Pennsylvania	Office of Consumer Advocate	Cogeneration contract amendment
165.	8702 September 1995	Potomac Edison Company	Maryland	Dept. of Natural Resources	Allocation of DSM Costs (oral only)
166.	ER95-533-001 September 1995	Ocean State Power	FERC	Boston Edison Co.	Cost of equity
167.	40003 November 1995	PSI Energy, Inc.	Indiana	Utility Consumer Counselor	Rate of return Retail wheeling

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168. P-55, SUB 1013 January 1996	BellSouth	North Carolina	AT&T	Rate of return
169. P-7, SUB 825 January 1996	Carolina Tel.	North Carolina	AT&T	Rate of return
170. February 1996	Generic Telephone	FCC	MCI	Cost of capital
171. 95A-531EG April 1996	Public Service Company of Colorado	Colorado	Federal Executive Agencies	Merger issues
172. ER96-399-000 May 1996	Northern Indiana Public Service Company	FERC	Indiana Office of Utility Consumer Counselor	Cost of capital
173. 8716 June 1996	Delmarva Power & Light Company	Maryland	Dept. of Natural Resources	DSM programs
174. 8725 July 1996	BGE/PEPCO	Maryland	Md. Energy Admin.	Merger Issues
175. U-20925 August 1996	Entergy Louisiana, Inc.	Louisiana	PSC Staff	Rate of return Allocations Fuel Clause
176. EC96-10-000 September 1996	BGE/PEPCO	FERC	Md. Energy Admin.	Merger issues competition
177. EL95-53-000 November 1996	Entergy Services, Inc.	FERC	Louisiana PSC	Nuclear Decommissioning
178. WR96100768 March 1997	Consumers NJ Water Company	New Jersey	Ratepayer Advocate	Cost of Capital
179. WR96110818 April 1997	Middlesex Water Co.	New Jersey	Ratepayer Advocate	Cost of Capital
180. U-11366 April 1997	Ameritech Michigan	Michigan	MCI	Access charge reform/financial condition
181. 97-074 May 1997	BellSouth	Kentucky	MCI	Rate Rebalancing financial condition

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182.	2540 June 1997	New England Power	Rhode Island	PUC Staff	Divestiture Plan
183.	96-336-TP-CSS June 1997	Ameritech Ohio	Ohio	MCI	Access Charge reform Economic impacts
184.	WR97010052 July 1997	Maxim Sewerage Corp.	New Jersey	Ratepayer Advocate	Rate of Return
185.	97-300 August 1997	LG&E/KU	Kentucky	Attorney General	Merger Plan
186.	Case No. 8738 August 1997	Generic (oral testimony only)	Maryland	Dept. of Natural Resources	Electric Restructuring Policy
187.	Docket No. 2592 September 1997	Eastern Utilities	Rhode Island	PUC Staff	Generation Divestiture
188.	Case No.97-247 September 1997	Cincinnati Bell Telephone	Kentucky	MCI	Financial Condition
189.	Docket No. U-20925 November 1997	Entergy Louisiana	Louisiana	PSC Staff	Rate of Return
190.	Docket No. D97.7.90 November 1997	Montana Power Co.	Montana	Montana Consumers Counsel	Stranded Cost
191.	Docket No. EO97070459 November 1997	Jersey Central Power & Light Co.	New Jersey	Ratepayer Advocate	Stranded Cost
192.	Docket No. R-00974104 November 1997	Duquesne Light Co.	Pennsylvania	Office of Consumer Advocate	Stranded Cost
193.	Docket No. R-00973981 November 1997	West Penn Power Co.	Pennsylvania	Office of Consumer Advocate	Stranded Cost
194.	Docket No. A-1101150F0015 November 1997	Allegheny Power System DQE, Inc.	Pennsylvania	Office of Consumer Advocate	Merger Issues
195.	Docket No. WR97080615 January 1998	Consumers NJ Water Company	New Jersey	Ratepayer Advocate	Rate of Return

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
196.	Docket No. R-00974149 January 1998	Pennsylvania Power Company	Pennsylvania	Office of Consumer Advocate	Stranded Cost
197.	Case No. 8774 January 1998	Allegheny Power System DQE, Inc.	Maryland	Dept. of Natural Resources MD Energy Administration	Merger Issues
198.	Docket No. U-20925 (SC) March 1998	Entergy Louisiana, Inc.	Louisiana	Commission Staff	Restructuring, Stranded Costs, Market Prices
199.	Docket No. U-22092 (SC) March 1998	Entergy Gulf States, Inc.	Louisiana	Commission Staff	Restructuring, Stranded Costs, Market Prices
200.	Docket Nos. U-22092 (SC) and U-20925(SC) May 1998	Entergy Gulf States and Entergy Louisiana	Louisiana	Commission Staff	Standby Rates
201.	Docket No. WR98010015 May 1998	NJ American Water Co.	New Jersey	Ratepayer Advocate	Rate of Return
202.	Case No. 8794 December 1998	Baltimore Gas & Electric Co.	Maryland	MD Energy Admin./Dept. Of Natural Resources	Stranded Cost/ Transition Plan
203.	Case No. 8795 December 1998	Delmarva Power & Light Co.	Maryland	MD Energy Admin./Dept. Of Natural Resources	Stranded Cost/ Transition Plan
204.	Case No. 8797 January 1998	Potomac Edison Co.	Maryland	MD Energy Admin./Dept. Of Natural Resources	Stranded Cost/ Transition Plan
205.	Docket No. WR98090795 March 1999	Middlesex Water Co.	New Jersey	Ratepayer Advocate	Rate of Return
206.	Docket No. 99-02-05 April 1999	Connecticut Light & Power	Connecticut	Attorney General	Stranded Costs
207.	Docket No. 99-03-04 May 1999	United Illuminating Company	Connecticut	Attorney General	Stranded Costs
208.	Docket No. U-20925 (FRP) June 1999	Entergy Louisiana, Inc.	Louisiana	Staff	Capital Structure
209.	Docket No. EC-98-40-000 et. al. May 1999	American Electric Power/ Central & Southwest	FERC	Arkansas PSC	Market Power Mitigation

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
210.	Docket No. 99-03-35 July 1999	United Illuminating Company	Connecticut	Attorney General	Restructuring
211.	Docket No. 99-03-36 July 1999	Connecticut Light & Power Co.	Connecticut	Attorney General	Restructuring
212.	WR99040249 Oct. 1999	Environmental Disposal Corp.	New Jersey	Ratepayer Advocate	Rate of Return
213.	2930 Nov. 1999	NEES/EUA	Rhode Island	Division Staff	Merger/Cost of Capital
214.	DE99-099 Nov. 1999	Public Service New Hampshire	New Hampshire	Consumer Advocate	Cost of Capital Issues
215.	00-01-11 Feb. 2000	Con Ed/NU	Connecticut	Attorney General	Merger Issues
216.	Case No. 8821 May 2000	Reliant/ODEC	Maryland	Dept. of Natural Resources	Need for Power/Plant Operations
217.	Case No. 8738 July 2000	Generic	Maryland	Dept. of Natural Resources	DSM Funding
218.	Case No. U-23356 June 2000	Entergy Louisiana, Inc.	Louisiana	PSC Staff	Fuel Prudence Issues Purchased Power
219.	Case No. 21453 <u>et. al.</u> July 2000	SWEP CO	Louisiana	PSC Staff	Stranded Costs
220.	Case No. 20925 (B) July 2000	Entergy Louisiana	Louisiana	PSC Staff	Purchase Power Contracts
221.	Case No. 24889 August 2000	Entergy Louisiana	Louisiana	PSC Staff	Purchase Power Contracts
222.	Case No. 21453 <u>et. al.</u> February 2001	CLECO	Louisiana	PSC Staff	Stranded Costs
223.	P-00001860 and P-0000181 March 2001	GPU Companies	Pennsylvania	Office of Consumer Advocate	Rate of Return

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
224.	CVOL-0505662-S March 2001	ConEd/NU	Connecticut Superior Court	Attorney General	Merger (Affidavit)
225.	U-20925 (SC) March 2001	Entergy Louisiana	Louisiana	PSC Staff	Stranded Costs
226.	U-22092 (SC) March 2001	Entergy Gulf States	Louisiana	PSC Staff	Stranded Costs
227.	U-25533 May 2001	Entergy Louisiana/ Gulf States	Louisiana Interruptible Service	PSC Staff	Purchase Power
228.	P-00011872 May 2001	Pike County Pike	Pennsylvania	Office of Consumer Advocate	Rate of Return
229.	8893 July 2001	Baltimore Gas & Electric Co.	Maryland	MD Energy Administration	Corporate Restructuring
230.	8890 September 2001	Potomac Electric/Conectiv	Maryland	MD Energy Administration	Merger Issues
231.	U-25533 August 2001	Entergy Louisiana / Gulf States	Louisiana	Staff	Purchase Power Contracts
232.	U-25965 November 2001	Generic	Louisiana	Staff	RTO Issues
233.	3401 March 2002	New England Gas Co.	Rhode Island	Division of Public Utilities	Rate of Return
234.	99-833-MJR April 2002	Illinois Power Co.	U.S. District Court	U.S. Department of Justice	New Source Review
235.	U-25533 March 2002	Entergy Louisiana/ Gulf States	Louisiana	PSC Staff	Nuclear Uprates Purchase Power
236.	P-00011872 May 2002	Pike County Power & Light	Pennsylvania	Consumer Advocate	POLR Service Costs
237.	U-26361, Phase 1 May 2002	Entergy Louisiana/ Gulf States	Louisiana	PSC Staff	Purchase Power Cost Allocations

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
238.	R-00016849C001 et al. June 2002	Generic	Pennsylvania	Pennsylvania OCA	Rate of Return
239.	U-26361, Phase II July 2002	Entergy Louisiana/ Entergy Gulf States	Louisiana	PSC Staff	Purchase Power Contracts
240.	U-20925(B) August 2002	Entergy Louisiana	Louisiana	PSC Staff	Tax Issues
241.	U-26531 October 2002	SWEPCO	Louisiana	PSC Staff	Purchase Power Contract
242.	8936 October 2002	Delmarva Power & Lt.	Maryland	Energy Administration Dept. Natural Resources	Standard Offer Service
243.	U-25965 November 2002	SWEPCO/AEP	Louisiana	PSC Staff	RTO Cost/Benefit
244.	8908 Phase I November 2002	Generic	Maryland	Energy Administration Dept. Natural Resources	Standard Offer Service
245.	02S-315EG November 2002	Public Service Co. of Colorado	Colorado	Fed. Executive Agencies	Rate of Return
246.	EL02-111-000 December 2002	PJM/MISO	FERC	MD PSC	Transmission Ratemaking
247.	02-0479 February 2003	Commonwealth Edison	Illinois	Dept. of Energy	POLR Service
248.	PL03-1-000 March 2003	Generic	FERC	NASUCA	Transmission Pricing (Affidavit)
249.	U-27136 April 2003	Entergy Louisiana	Louisiana	Staff	Purchase Power Contracts
250.	8908 Phase II July 2003	Generic	Maryland	Energy Admin. Dept. of Natural Resources	Standard Offer Service
251.	U-27192 June 2003	Entergy Louisiana and Gulf States	Louisiana	LPSC Staff	Purchase Power Contract Cost Recovery

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
252.	C2-99-1181 October 2003	Ohio Edison Co.	U.S. District Court	U.S. Department of Justice <u>et. al.</u>	Clean Air Act Compliance Economic Impact (Report)
253.	RP03-398-000 December 2003	Northern Natural Gas Co.	FERC	Municipal Distributors Group/Gas Task Force	Rate of Return
254.	8738 December 2003	Generic	Maryland	Energy Admin Department of Natural Resources	Environmental Disclosure (oral only)
255.	U-27136 December 2003	Entergy Louisiana, Inc.	Louisiana	PSC Staff	Purchase Power Contracts
256.	U-27192, Phase II October/December 2003	Entergy Louisiana & Entergy Gulf States	Louisiana	PSC Staff	Purchase Power Contracts
257.	WC Docket 03-173 December 2003	Generic	FCC	MCI	Cost of Capital (TELRIC)
258.	ER 030 20110 January 2004	Atlantic City Electric	New Jersey	Ratepayer Advocate	Rate of Return
259.	E-01345A-03-0437 January 2004	Arizona Public Service Co.	Arizona	Federal Executive Agencies	Rate of Return
260.	03-10001 January 2004	Nevada Power Co.	Nevada	U.S. Dept. of Energy	Rate of Return
261.	R-00049255 June 2004	PPL Elec. Utility	Pennsylvania	Office of Consumer Advocate	Rate of Return
262.	U-20925 July 2004	Entergy Louisiana, Inc.	Louisiana	PSC Staff	Rate of Return Capacity Resources
263.	U-27866 September 2004	Southwest Electric Power Co.	Louisiana	PSC Staff	Purchase Power Contract
264.	U-27980 September 2004	Cleco Power	Louisiana	PSC Staff	Purchase Power Contract
265.	U-27865 October 2004	Entergy Louisiana, Inc. Entergy Gulf States	Louisiana	PSC Staff	Purchase Power Contract
266.	RP04-155	Northern Natural	FERC	Municipal Distributors	Rate of Return

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
	December 2004	Gas Co.		Group/Gas Task Force	
267.	U-27836 January 2005	Entergy Louisiana/ Gulf States	Louisiana	PSC Staff	Power plant purchase and cost recovery
268.	U-199040 et al. February 2005	Entergy Gulf States/ Louisiana	Louisiana	PSC Staff	Global Settlement, Multiple rate proceedings
269.	EF03070532 March 2005	Public Service Electric and Gas	New Jersey	Ratepayers Advocate	Securitization of Deferred Costs
270.	05-0159 June 2005	Commonwealth Edison	Illinois	Department of Energy	POLR Service
271.	U-28804 June 2005	Entergy Louisiana	Louisiana	LPSC Staff	QF Contract
272.	U-28805 June 2005	Entergy Gulf States	Louisiana	LPSC Staff	QF Contract
273.	05-0045-EI June 2005	Florida Power & Lt.	Florida	Federal Executive Agencies	Rate of Return
274.	9037 July 2005	Generic	Maryland	MD. Energy Administration	POLR Service
275.	U-28155 August 2005	Entergy Louisiana Entergy Gulf States	Louisiana	LPSC Staff	Independent Coordinator of Transmission Plan
276.	U-27866-A September 2005	Southwestern Electric Power Co.	Louisiana	LPSC Staff	Purchase Power Contract
277.	U-28765 October 2005	Cleco Power LLC	Louisiana	LPSC Staff	Purchase Power Contract
278.	U-27469 October 2005	Entergy Louisiana Entergy Gulf States	Louisiana	LPSC Staff	Avoided Cost Methodology
279.	A-313200F007 October 2005	Sprint (United of PA)	Pennsylvania	Office of Consumer Advocate	Corporate Restructuring
280.	EM05020106 November 2005	Public Service Electric & Gas Co.	New Jersey	Ratepayer Advocate	Merger Issues

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
281.	U-28765 December 2005	Cleco Power LLC	Louisiana	LPSC Staff	Power plant certification, financing, rate plan
282.	U-29157 February 2006	Cleco Power LLC	Louisiana	LPSC Staff	Storm Damage Financing
283.	U-29204 March 2006	Entergy Louisiana Entergy Gulf States	Louisiana	LPSC Staff	Purchase power contracts
284.	A-310325F006 March 2006	Alltel	Pennsylvania	Office of Consumer Advocate	Merger, Corporate Restructuring
285.	9056 March 2006	Generic	Maryland	Maryland Energy Administration	Standard Offer Service Structure
286.	C2-99-1182 April 2006	American Electric Power Utilities	U. S. District Court Southern District, Ohio	U. S. Department of Justice	New Source Review Enforcement (expert report)
287.	EM05121058 April 2006	Atlantic City Electric	New Jersey	Ratepayer Advocate	Power plant sale
288.	ER05121018 June 2006	Jersey Central Power & Light Co.	New Jersey	Ratepayer Advocate	NUG contracts cost recovery
289.	U-21496, Subdocket C June 2006	Cleco Power LLC	Louisiana	Commission Staff	Rate stabilization plan
290.	GR0510085 June 2006	Public Service Electric & Gas Company	New Jersey	Ratepayer Advocate	Rate of return (gas services)
291.	R-000061366 July 2006	Metropolitan Ed. Co. Penn. Electric Co.	Pennsylvania	Office of Consumer Advocate	Rate of return
292.	9064 September 2006	Generic	Maryland	Energy Administration	Standard Offer Service
293.	U-29599 September 2006	Cleco Power LLC	Louisiana	Commission Staff	Purchase Power Contracts
294.	WR06030257 September 2006	New Jersey American Water Co.	New Jersey	Rate Counsel	Rate of return

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	<u>Docket Number</u>	<u>Utility</u>	<u>Jurisdiction</u>	<u>Client</u>	<u>Subject</u>
295.	U-27866/U-29702 October 2006	Southwestern Electric Power Co.	Louisiana	Commission Staff	Purchase Power/Power Plant Certification
296.	9063 October 2006	Generic	Maryland	Energy Administration Department of Natural Resources	Generation Supply Policies
297.	EM06090638 November 2006	Atlantic City Electric	New Jersey	Rate Counsel	Power plant sale
298.	C-2000065942 November 2006	Pike County Light & Power	Pennsylvania	Consumer Advocate	Generation Supply Service
299.	ER06060483 November 2006	Rockland Electric Company	New Jersey	Rate Counsel	Rate of Return

APPENDIX B.

SUMMARY OF RECOMMENDED CONDITIONS

**RECOMMENDED CONDITIONS TO ACCOMPANY
CHANGE OF CONTROL**

In the event that the Commission approves the change of control proposed in this case for Duquesne Light Company, I recommend that the approval be accompanied by the conditions listed below. These conditions are in addition to the recommendations concerning service quality, charitable contributions and universal service set forth in the testimony of OCA witness Alexander.

(1) Rate Cap Benefit

DLC shall not seek to increase its distribution base rates to be effective prior to year-end 2010. This would include a prohibition during this period of any new rate surcharges but would not affect the operation of STAS, POLR service rates or the currently-approved transmission rate recovery mechanism.

(2) Transaction and Transition Costs

DLC may not seek rate recovery in Pennsylvania retail rates or FERC transmission rates of any transaction or transition costs associated with the merger. In addition to the costs and cost categories identified in OCA III-21, this would include but not be limited to any and all costs associated with obtaining regulatory approvals, any personnel-related costs (such as retention bonuses or relocation costs), and costs associated with corporate governance changes, and securities issuance costs associated with completion or financing the merger. This is a non-exclusive list and would include any transaction or transition cost that is incurred that would not have been incurred but for the merger. In addition, DLC shall not reflect in customer rates, directly or indirectly, any acquisition premium.

(3) Cost of Capital Hold Harmless

DLC shall not seek to include in its authorized fair rate of return a cost of capital premium or cost increase caused by or attributable to the merger. This premium prohibition would apply to the cost of debt, cost of preferred stock, cost of equity and capital structure. The Company may not claim a rate of return cost increase that is caused by the merger.

(4) Capital Structure Change

DLC shall not reflect in any rate case rate of return request a common equity ratio above 45 percent (i.e., the settlement value in Docket No. R-00061346) without first demonstrating that a higher common equity ratio is reasonable and in the best interest of its customers.

(5) Debt Refinancing or Reacquisition Costs

In order to seek recovery of any debt refinancing costs related to the merger in a future (i.e., post rate cap) rate proceeding, DLC must demonstrate that the costs were prudently incurred and cost-beneficial for customers.

(6) Corporate Governance

In addition to the Consortium fund representatives and the DLC CEO, the Board of Directors should be expanded to include four additional outside directors, including two of whom reside in the service area. In addition, there shall be no substitution among the existing fund members without first obtaining PaPUC approval.

(7) Debt/Credit Guarantees

DLC shall not extend credit, make loans, pledge assets, provide loan guarantees or credit support to any affiliate, including any Consortium member or any entity in which a Consortium member has a financial interest. This restriction would not apply to the recently-approved Cash Pool involving DLC and DLH and its subsidiaries.

(8) Affiliate Agreements

Applicants shall submit the amendments to the affiliate Services Agreement in order to permit affiliated transactions with Consortium members for review by the parties and review and approval by the Commission. The merger transaction may not close until the amendments to the Services Agreement are approved by the Commission.

(9) Pennsylvania Capital Stock Tax

DLC may not include in rates charged to its customers any increase in its Pennsylvania Capital Stock Tax caused by the merger.

(10) Retention of Key DLC Personnel

Applicants and the Consortium shall be committed to the retention at DLC of key technical and managerial staff and to ensure that the merger does not cause either an undue loss of such staff or an inappropriate or excessive allocation of key DLC staff time to non-DLC duties (such as assistance to the Consortium with other acquisitions). In that regard, (a) Applicants and the Consortium shall develop and submit a key staff retention plan; and (b) DLC shall report periodically on the status of key personnel including key personnel retention and allocation of DLC staff time to non-DLC activities.

(11) Corporate Headquarters Retention in Pittsburgh

DLC shall retain its corporate headquarters in Pittsburgh, with the overall scope of corporate functions and associated staffing levels at its Pittsburgh headquarter at least comparable to current levels. In addition, DLC, DLH and its subsidiaries shall provide access to books, records and personnel at the Pittsburgh headquarters.

(12) Periodic Reporting on Merger Status

DLC shall submit to the Commission and the parties annual progress reports following the closing of the transaction. The report shall include at a minimum the post-merger experience including (a) any savings or cost increases associated with the merger; (b) a summarization of affiliate transactions (including the role of Consortium members in providing technical or managerial expertise); (c) the implementation of “best practices” or new “strategic initiatives” as described in the Application and testimony; (d) financing changes, access to capital and any credit rating changes; (e) a summary of transactions and transition costs incurred; (f) the status (e.g., loss or reassignment) of key DLC personnel; and (g) the status of (or changes in) Pittsburgh headquarters functions/staffing. At the time of the first post-merger rate case (no sooner than 2010), the annual report shall be sponsored by testimony as part of the rate case for review and investigation at that time. At that time, a determination can be made concerning whether continued progress reporting is warranted.

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Application of Duquesne Light Company)
for a Certificate of Public Convenience)
Under Section 1102 (a)(3) of the Public) Docket No. A-110510F0035
Utility Code Approving the Acquisition)
of Duquesne Light Holding, Inc. by Merger)

Application of DQE Communications)
Network Services LLC for a Certificate)
of Public Convenience under Section) Docket No. A-311233F0002
Approving the Acquisition of Duquesne)
Light Holding, Inc. by Merger)

SURREBUTTAL TESTIMONY

OF

MATTHEW I. KAHAL

ON BEHALF OF THE

PENNSYLVANIA OFFICE OF CONSUMER ADVOCATE

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SECRETARY'S BUREAU

JANUARY 23, 2007

1 I. INTRODUCTION

2 Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

3 A. My name is Matthew I. Kahal. I am employed as an independent consultant retained in
4 this case by the Exeter Associates, Inc., an economic consulting firm. My business
5 address is 5565 Sterrett Place, Suite 310, Columbia, Maryland 21044.

6 Q. HAVE YOU PREVIOUSLY TESTIFIED IN THIS CASE?

7 A. Yes, on December 22, 2006, I submitted Direct Testimony on behalf of the Office of
8 Consumer Advocate (OCA). That testimony evaluated the claimed benefits associated
9 with the acquisition of Duquesne Light Company (DLC or the Company) by the
10 Macquarie Consortium. I also recommended a series of approval conditions needed to
11 protect customers, and I addressed Pennsylvania's "substantial, affirmative benefits"
12 merger approval standard in the event this Commission is inclined to approve this
13 transaction.

14 Q. WHAT IS THE PURPOSE AT THIS TIME OF YOUR SURREBUTTAL
15 TESTIMONY?

16 A. The Applicants and the Consortium submitted rebuttal testimony on January 10, 2007
17 responding to me and the witnesses for other parties. This rebuttal testimony argues that
18 the proposed merger, as filed, meets the substantial, affirmative benefits standard for
19 merger approval, although the Applicants' witnesses are willing to accept certain limited
20 conditions for Commission approval. However, Applicants and the Consortium reject (or
21 substantially weaken) most of the approval conditions proposed by the parties, including
22 the OCA.

23 My Surrebuttal Testimony responds to the rebuttal testimony of witnesses
24 Sauvage, Leslie and O'Brien, i.e., the portions of their testimonies relevant to the
25 conditions that I recommend.

1 Q. HAS THE COMPANY'S REBUTTAL TESTIMONY CAUSED YOU TO
2 MODIFY ANY OF YOUR CONCLUSIONS OR RECOMMENDED
3 CONDITIONS?

4 A. No. The Applicants' rebuttal witnesses do not provide any convincing evidence that the
5 merger, as proposed, will provide "substantial, affirmative benefits" and therefore meet
6 the Pennsylvania standard for approval. Moreover, the package of approval conditions
7 accepted by Applicants and the Consortium in the rebuttal testimony are not adequate or
8 particularly effective in protecting customers or providing the required substantial
9 benefits. I continue to support the conditions set forth in my Direct Testimony. OCA
10 witness Alexander recommends additional conditions pertaining to service quality and
11 universal service programs.

12 Q. HOW IS THE REMAINDER OF YOUR SURREBUTTAL TESTIMONY
13 ORGANIZED?

14 A. Section II discusses the evidence presented by witnesses Sauvage, Leslie and O'Brien in
15 their rebuttal testimonies claiming that the "as filed" merger meets the substantial,
16 affirmative benefits standard. Section III reviews the adequacy of the conditions that
17 Applicants and the Consortium have agreed to accept.

1 **II. MEETING THE SUBSTANTIAL, AFFIRMATIVE BENEFITS STANDARD**
2

3 Q. BASED ON YOUR READING OF APPLICANTS' REBUTTAL TESTIMONY,
4 DO APPLICANTS RECOGNIZE THE NEED TO MEET THE
5 "SUBSTANTIAL, AFFIRMATIVE BENEFIT STANDARD" FOR MERGER
6 APPROVAL?

7 A. Mr. O'Brien's testimony seems to recognize that this standard must be met, and he argues
8 that this transaction does so, primarily by preserving DLC's current status and operations.
9 At page 3, he states that preserving the status quo is an affirmative benefit because doing
10 so retains for the Pittsburgh area "a major employer and contributor to the business and
11 civic life of our community." Absent the takeover by the Consortium, he assumes these
12 "status quo," positive contributions would be lost, as Duquesne's role in Pittsburgh is
13 diminished.

14 Mr. O'Brien and other witnesses for the Applicants claim other major merger
15 benefits, including:

- 16 • It will provide or maintain DLC's access to capital as needed for
17 infrastructure improvement;
- 18 • The merger will enable DLC to procure capital on more reasonable (less
19 expensive) terms, as compared to a stand-alone company; and
- 20 • *The merger will create opportunities to employ "best practices" based on*
21 the Consortium's expertise with other utilities that it controls.

22 In addition to these points, Mr. O'Brien seems to question the Company's long-term
23 financial viability, if it remains a stand-alone company, noting that its "Back to Basics"
24 strategy narrows its earnings base, and its financial circumstances threaten the
25 sustainability of its dividend. He suggests that this financial weakness could lead to a
26 stock price decline, making an acquisition by another utility all but inevitable.

1 Q. MR. O'BRIEN'S PREDICATE FOR THIS MERGER IS THAT DLC AND
2 DUQUESNE LIGHT HOLDINGS, INC. (DLH) ARE TOO SMALL TO BE
3 FINANCIALLY VIABLE ON A STAND-ALONE BASIS. DO YOU AGREE?

4 A. No. I do not. While DLH is certainly not the size of FirstEnergy or Exelon, companies
5 that are major players in the unregulated generation business, DLC is hardly a "small
6 utility." It is classified by the Value Line Investment Survey (December 1, 2006) as "mid
7 cap," and there are a number of mid caps and small cap independent electric utility
8 companies that have operated successfully for many decades. DLH's market equity
9 capitalization is \$1.8 billion, with a total enterprise value of about \$3 billion. DLC
10 accounts for the vast majority of the enterprise value and is expanding its asset base.

11 DLC has solid middle to high triple B investment grade credit ratings. While
12 DLH has a relatively leveraged capital structure (about 36 percent common equity),
13 DLC's common equity ratio is a relatively strong 46 percent, which is very much in line
14 with industry norms and credit rating requirements. Above all, DLC is a electric delivery
15 service utility providing monopoly service to its Pittsburgh area service territory. As
16 such, its business risk is quite low and cash flows stable. There is no reason why it
17 cannot continue to operate very successfully in that stand-alone role, absent an
18 acquisition by the Consortium or anyone else, as evidenced by the successful outcome for
19 the Company of the recent rate case settlement. On the transmission side, DLC presently
20 has an application pending before the Federal Energy Regulatory Commission (FERC)
21 for a formula rate plan.

1 Q. IF DLC CAN OPERATE VERY SUCCESSFULLY AS A STAND-ALONE
2 DELIVERY SERVICE UTILITY, WHAT IS THE PREDICATE FOR THIS
3 MERGER?

4 A. The “driver” of this merger is the 20 to 25 percent premium that DLH shareholders will
5 receive (in cash) as a result of this transaction, in effect a nearly \$300 million bonus
6 payment. *I sincerely doubt that this merger would proceed absent this substantial*
7 *shareholder bonus payment.*

8 Q. MR. O’BRIEN QUESTIONS THE SUSTAINABILITY OF THE DLH
9 DIVIDEND PAYMENT ABSENT THE MERGER. IS THIS AN IMPORTANT
10 CONSIDERATION FOR THE COMMISSION?

11 A. No. The dividend is set by the DLH Board of Directors based on their business
12 judgment. Neither DLC customers nor the Commission has made those decisions. Mr.
13 O’Brien is certainly correct that the \$1 per share annual dividend is high relative to
14 current and recent DLH earnings. It should be noted that Value Line projects that by the
15 end of this decade, DLH earnings will increase to \$1.50 per share, with dividends
16 remaining flat at \$1 per share, resulting in a 66 percent dividend payout, which
17 approximates a normal payout for a utility.

18 Whether or not the dividend should be retained at \$1 per share is a decision of the
19 DLH Board. However, protecting the dividend cannot serve as the basis for this
20 Commission’s approval of a merger, particularly one that fails to provide “substantial,
21 affirmative benefits” for its customers and the public.

1 Q. MR. O'BRIEN IS CONCERNED WITH THE DLH STOCK PRICE AND THE
2 POSSIBILITY IT COULD DECLINE. SHOULD THIS CONCERN SERVE AS
3 A BASIS FOR MERGER APPROVAL?

4 A. No. The pre-announcement stock price was in the \$16 to \$17 range and in prior months
5 had been languishing. To some degree the pattern of the stock price may reflect DLH
6 non-regulated operations (including its debt leverage). While Mr. O'Brien may have
7 concerns about this stock price, this still reflects a very substantial premium over the
8 DLH net book value, estimated to be \$8.70 at year-end 2006. The DLH pre-
9 announcement stock price also reflects a very strong price/earnings ratio.

10 Absent the merger, the DLH stock price will depend on management's success in
11 operating DLC as a delivery service utility and executing its "Back to Basics" plan.
12 Doing so will result in a reasonable market valuation of DLH stock and access to equity
13 capital on reasonable returns. There is nothing to suggest that management cannot
14 achieve this success on a stand-alone basis, absent this merger.

15 Q. APPLICANTS' WITNESSES ARGUE THAT ABSENT APPROVAL OF THIS
16 TRANSACTION, ANOTHER ACQUISITION OF DLH/DLC IS INEVITABLE,
17 AND THIS OTHER, HYPOTHESIZED ACQUISITION WOULD BE LESS
18 FAVORABLE TO DLC CUSTOMERS AND THE PITTSBURGH
19 COMMUNITY. IS THIS A VALID ARGUMENT FOR APPROVING THIS
20 MERGER?

21 A. No, it is not. In fact, if this argument were to be accepted, it effectively would destroy
22 Pennsylvania's substantial, affirmative benefits standard for merger approval by
23 rendering it meaningless. First, let us assume for discussion purposes that Mr. O'Brien is
24 correct that DLH is a highly coveted acquisition target (an assertion that has not been
25 well supported). If the Consortium merger is rejected, in the future it is possible that

1 another acquisition of DLH/DLC could take place and that merger could involve some of
2 the business changes that Mr. O'Brien seeks to avoid (such as moving corporate
3 headquarters). However, Mr. O'Brien overlooks the fact that this future, hypothetical
4 merger can only proceed with this Commission's approval, and the Commission will
5 grant that approval if and only if the evidence demonstrates that this hypothetical merger
6 passes the "substantial, affirmative benefits" test. That test could encompass all of the
7 issues that Mr. O'Brien mentions and could either be rejected or properly conditioned.

8 In effect, Mr. O'Brien is advocating approval of the Consortium acquisition
9 because he speculates that (a) another acquisition attempt will occur; and (b) the
10 Consortium acquisition will provide greater customer and community benefits than this
11 hypothetical alternative acquisition. The standard for merger approval he is advocating is
12 that the merger application must be compared with the terms of some unknown,
13 hypothetical merger that is inherently inferior. This is an unworkable and unreasonable
14 standard for this Commission to apply.

15 Q. APPLICANTS' REBUTTAL TESTIMONY ARGUES THAT ONE OF THE
16 SUBSTANTIAL, AFFIRMATIVE BENEFITS IS THE CONSORTIUM'S
17 APPLICATION OF ITS UTILITY MANAGEMENT EXPERTISE TO
18 IMPLEMENT "BEST PRACTICES" FOR DLC. WHAT BEST PRACTICES
19 ARE IDENTIFIED IN THE REBUTTAL FILING?

20 A. There are none, merely an assertion that this is a benefit. While it is possible that the
21 Consortium could make available "Best Practices" for DLC that it otherwise might not
22 employ, there is no tangible evidence in Applicants' rebuttal testimony, the initial
23 application or data responses that this will occur or is even likely to occur. The assertion
24 is at best speculative.

1 Q. APPLICANTS' REBUTTAL WITNESSES ARGUE THAT A STAND-ALONE
2 DLC WILL NOT HAVE ADEQUATE ACCESS TO CAPITAL. DID THE
3 REBUTTAL TESTIMONY INTRODUCE ANY NEW EVIDENCE ON THIS
4 ISSUE?

5 A. No. Applicants' rebuttal witnesses argue that the proposed merger passes the
6 "substantial, affirmative benefits" test by curing an access to financial capital problem
7 that DLC now faces (or will face) and by lowering the DLC cost of capital, which is a
8 form of synergy savings. I discussed the evidence (or lack of evidence) for these
9 assertions in my Direct Testimony (pages 17-21), and no substantive, new evidence has
10 been presented in rebuttal on these issues. The data responses provided to the OCA fail
11 to document (or even acknowledge) any capital access problem or cost of capital savings
12 from the merger. In fact, Mr. O'Brien specifically denies that this merger provides
13 "synergy savings." (O'Brien, Surrebuttal, pages 9 and 20).

14 I am not suggesting that there can be no validity to the assertions in rebuttal
15 testimony on capital access or costs, but no objective, convincing evidence on these
16 claims has so far been provided by Applicants. In fact, for the reasons discussed in my
17 Direct Testimony, I am concerned that the merger has the potential to cause an increase
18 in the DLC cost of capital, as explained in my Direct Testimony.

19 Q. DO APPLICANTS EMPHASIZE THE IMPORTANCE OF INVESTING IN
20 DLC'S INFRASTRUCTURE?

21 A. Yes, Applicants' witnesses commit to the \$500 million plus Infrastructure Improvement
22 Plan to be conducted during 2005 to 2007. However, that plan appears to have little to do
23 with the proposed merger since the capital spending will be largely completed prior to the
24 expected closing on this merger, i.e., mid 2007. DLC intends additional capital spending
25 after 2007, including transmission upgrades, and has submitted a request to the FERC for

1 very favorable ratemaking treatment for its new transmission investments in order to
2 minimize risk, enhance cash flow and facilitate financing. The FERC request for
3 favorable treatment is not dependent on or linked to this merger.

4 Q. DOES MR. O'BRIEN DOCUMENT A CAPITAL ACCESS PROBLEM FOR
5 DLC?

6 A. No, to the contrary, he acknowledges that no such problem exists. As he states at
7 page 11,

8
9 Absent approval of the transaction, it is not clear that DLH and
10 Duquesne Light can continue to raise equity on reasonable terms
11 given the business risks facing the Company which I discuss
12 above.

13 *He is suggesting that access to equity may be an issue in the future if the Company (or its*
14 *parent) is considered to be very risky. But there is no question that DLC itself is a very*
15 *low risk, monopoly delivery service utility and therefore there is no basis for claiming a*
16 *capital access problem. He further admits at page 11:*

17
18 Duquesne Light has historically been able to access capital markets
19 to finance capital projects, but this access is no longer assured.

20 In other words, Applicants' assertion of "substantial, affirmative benefits" for this
21 merger is based upon the merger addressing an issue that has not existed historically,
22 does not exist now but might exist in the future, although there is no tangible evidence of
23 that occurring. This is suggesting that Pennsylvania's merger standard can be met based
24 on hypothesized, speculative benefits that cannot be documented. I urge that the
25 Commission reject Applicants' attempt to "lower the bar" on Pennsylvania's merger
26 approval standards.

1 Q. DO THESE CONDITIONS PROVIDE ADEQUATE PROTECTION FOR
2 CUSTOMERS?

3 A. In general, they do not. Applicants reject certain proposed conditions that the OCA
4 believes are essential to protecting customers and providing for some benefit, and the
5 conditions that they have proposed are inadequate. OCA witness Alexander addresses in
6 her surrebuttal testimony issues and conditions associated with Universal Service and
7 Service Quality, and these topics will not be covered in my testimony.

8 Q. OTHER THAN SERVICE QUALITY AND UNIVERSAL SERVICE, WHAT
9 CONDITIONS RECOMMENDED BY THE OCA ARE REJECTED BY THE
10 APPLICANTS?

11 A. Applicants reject outright the OCA's recommendation concerning corporate governance
12 (i.e., Board of Directors membership), retention of key personnel and the submission of
13 affiliate service agreements. The other OCA recommended conditions are addressed in a
14 fashion, but in most instances Applicants' modifications severely weaken the consumer
15 protections.

16 Q. WHY DID THE OCA RECOMMEND A CHANGE TO THE PROPOSED
17 BOARD OF DIRECTORS?

18 A. The original proposal, outlined in Mr. Leslie's Direct Testimony, would have a Board
19 consisting entirely of the fund managers that own DLH/DLC. While this normally may
20 be an appropriate corporate governance arrangement for a (non-public) business, this is
21 not appropriate for a regulated utility, with an exclusive franchise providing a vital
22 service to the public. I therefore recommended the inclusion on the Board (albeit on a
23 minority basis) of outside and local directors. As indicated in Mr. O'Brien's Exhibit
24 MKO-3 and in my Direct Testimony, the Consortium is now willing to include the DLC
25 Chief Executive Officer (CEO) on the Board. Mr. O'Brien states that the CEO, a

1 Management Committee and others at DLC can provide the Board with the needed local
2 input.

3 Q. IS THIS CHANGE SATISFACTORY?

4 A. No, it is not. Although the inclusion on the Board of the DLC CEO was both a welcome
5 and meaningful change from the original proposal, it does not adequately address my
6 concern. The CEO will be essentially an employee of the Consortium, working at its
7 pleasure, and is not by any standard “independent.” Under the Applicants’ plan there will
8 be no independent directors. While the CEO, Management Committee and others can
9 provide some “local input,” the bottom line is that the Board is the only decision-making
10 entity and is free to ignore the local input if it has other priorities. This is a clear step
11 backwards from the current DLH/DLC Board of Directors which emphasizes both
12 outside directors and a local perspective.

13 Applicants’ proposal will result in corporate governance that is exclusively
14 oriented toward the investment objectives of the Consortium funds and would be less
15 responsive to the local community and the Commission than the current Board. It is
16 unclear how the “local input” will be reflected in Board decisions.

17 Q. APPLICANTS REJECT THE OCA’S RECOMMENDATION FOR REVIEW
18 AND APPROVAL OF THE AMENDED AFFILIATE AGREEMENT. WHY?

19 A. Mr. Leslie states that this recommendation is unreasonable, will unduly delay merger
20 completion and is not needed “since no major initiative or service is currently planned.”
21 (Rebuttal Testimony, page 6)

1 Q. WHAT IS YOUR RESPONSE?

2 A. Mr. Leslie's response is not consistent with my reading of the Application originally filed
3 in this case. At page 20, the Application states:

4
5 In conjunction with the transaction, this agreement will be
6 amended to include DLH's new parent, DQE Holdings LLC and
7 Macquarie Bank Limited, its subsidiaries and affiliates where
8 relevant.

9 The "agreement" referenced in the above citation is the Amended and Restated
10 Administrative Service Agreement (July 19, 2004). I interpreted this statement to mean
11 that the Applicants intend to submit the amendment to the Agreement as part of this
12 proceeding, not at some unspecified time in the future long after the merger has closed. It
13 is not reasonable for Applicants to state their intention to amend an affiliate services
14 agreement as part of the merger Application in this proceeding but not be willing to share
15 their proposed amendments with the parties for their review and the Commission for its
16 approval. This creates uncertainty concerning the scope and terms of future affiliate
17 transactions.

18 I disagree with Mr. Leslie's position and urge that Applicants be required to
19 submit the amendments for review and approval in this proceeding prior to merger
20 closing.

21 Q. IS MR. LESLIE'S OFFER OF A DISTRIBUTION RATE CAP THROUGH
22 JANUARY 1, 2009 ADEQUATE (EXHIBIT CJL-5)?

23 A. This is a potential benefit but a modest one in these circumstances, and does not
24 adequately compensate for merger risks that customers would face. Duquesne recently
25 received a very large distribution rate increase, and even if it were to file a new base rate
26 case early this year (and there are no indications of any plans to do so), the increase
27 would not take effect prior to year-end 2007 or early 2008. Hence, when this lag is

1 recognized, it is clear that Applicants at most are offering distribution rate increase
2 protection for no longer than about one year. This does not meet the “substantial,
3 affirmative benefit” requirement in these circumstances.

4 Related to this issue is Mr. O’Brien’s acceptance of my recommendation to
5 provide annual monitoring reports on the various merger issues listed in my testimony.
6 However, Applicants would commit to provide these reports only “during the distribution
7 rate stay-out period” (Exhibit MKO-2), which would end December 31, 2008. Assuming
8 the merger closes by mid 2007, the first such annual report would be submitted mid 2008.
9 However, this first report would also be the last such report since the obligation to
10 provide monitoring reports on merger issues would end in December of 2008 under Mr.
11 O’Brien’s proposal. Mr. O’Brien, in reality, is willing to submit only one such “annual”
12 report.

13 Q. YOUR DIRECT TESTIMONY DISCUSSES THE NEED FOR A COST OF
14 CAPITAL “HOLD HARMLESS.” ARE APPLICANTS AGREEABLE TO
15 THAT PROTECTION?

16 A. As explained by Mr. Leslie, Applicants are willing to offer some limited protection
17 against a cost of capital increase caused by the merger. This includes a willingness for a
18 period of three years to exclude from rates a cost of capital increase due to a credit
19 downgrading that is caused by the merger and to maintain a long-term debt ratio during
20 this period that does not exceed 60 percent. In addition, DLC will not seek an approved
21 capital structure for ratemaking that is outside the range of those used by “comparable
22 companies.”

23 These protections are extremely limited, having a duration of merely three years,
24 and they could be counter productive. As explained in my Direct Testimony, I have a
25 concern that the Consortium intends to retire substantial amounts of DLC’s existing debt

1 which will lead to a very high common equity ratio. This much higher common equity
2 ratio would not be appropriate for a low-risk distribution utility, and therefore would be
3 inappropriate for ratemaking. I recommend a condition to protect customers against this
4 adverse increase in the cost of capital caused by the merger. My recommended condition
5 requires DLC to justify for ratemaking purposes any increase in its common equity ratio
6 compared with the value (i.e., 45 percent) accepted in DLC's most recent rate case.

7 Q. WHY DOES MR. LESLIE'S CAPITAL STRUCTURE PROPOSAL FAIL TO
8 PROTECT AGAINST AN INCREASED COST OF CAPITAL?

9 A. The Consortium clearly intends to dramatically increase the DLC equity ratio which
10 would adversely impact ratepayers if reflected in rates. Mr. Leslie's condition would
11 only constrain the ratemaking capital structure to the "range" of comparable company
12 capital structures, not the average value. For example, assume DLC in a rate proceeding
13 selects a group of comparable companies with an average of common equity ratio of 45
14 percent (equal to that currently in effect for DLC), but with a range of 35 to 60 percent.
15 Following Mr. Leslie's proposal, DLC would have carte blanche to utilize for ratemaking
16 a capital structure with an equity ratio as high as 60 percent. And this is true even if that
17 comparable company is not permitted by its state regulator to use that 60 percent equity
18 ratio for ratemaking purposes.

19 Clearly, DLC ratepayers are not protected by Mr. Leslie's proposed condition
20 and, in fact, are likely to be harmed.

21 Q. WHAT IS YOUR CONCERN REGARDING THE PROPOSED TREATMENT
22 OF THE CAPITAL STOCK TAX AND MERGER TRANSACTION COSTS?

23 A. The proposed condition is inadequate, fails to provide needed protections and inevitably
24 will result in harm to DLC customers. Keep in mind that these capital stock tax increases
25 and transaction costs are costs that would not exist "but for" the merger. Applicants and

1 the Consortium identify no synergy savings that would offset these added costs, and
2 hence, if ratepayers are to avoid being harmed, DLC must agree not to include these costs
3 in customer rates. The Applicants' response to OCA III-21 commits to not seek rate
4 recovery, at least for the transaction costs listed in the data response.

5 The commitment set forth in rebuttal testimony, however, offers only partial
6 protection. As noted in Mr. O'Brien's testimony, DLC only agrees to exclude transaction
7 costs and capital stock tax increases from distribution rates. They specifically reserve the
8 right to flow these costs through FERC-regulated transmission rates. (O'Brien, Rebuttal
9 Testimony, page 21) DLC customers either directly or indirectly pay FERC-regulated
10 transmission rates since DLC charges its retail customers for these transmission costs as a
11 flow through item, even during a distribution rate cap period. The clear end result is that
12 DLC has every intention of charging its ratepayers for merger-related transaction costs
13 and capital stock tax increases caused by the merger, even though it identifies no
14 synergy savings offset. The result inevitably is a net harm to customers.

15 Q. IS IT APPROPRIATE TO EXTEND THIS RATE PROTECTION TO FERC
16 TRANSMISSION RATES IF THE PAPUC DOES NOT SET THOSE RATES?

17 A. Yes. The issue is not one of jurisdiction over rates but ensuring ratepayers are not
18 harmed by the merger. This objective cannot be accomplished if Applicants are
19 permitted the loop hole of flowing transactions costs through transmission ratemaking
20 while agreeing not to do so when setting distribution rates.

21 An additional problem is that Mr. Leslie would limit even the distribution rate
22 protection to those transaction costs listed on Applicants' response to OCA III-21. There
23 may be additional transaction costs that are not listed on that response that DLC is free to
24 include in its distribution rates. Customers should be protected from paying all merger
25 transaction costs.

1 Q. DOES THIS CONCLUDE YOUR SURREBUTTAL TESTIMONY?

2 A. Yes, it does.

3 *00092367.DOC*