

**BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION**

APPLICATION OF DUQUESNE	:	
LIGHT COMPANY FOR APPROVAL	:	
OF ITS RESTRUCTURING PLAN	:	Docket No. R-00974104
UNDER SECTION 2806 OF THE	:	
PUBLIC UTILITY CODE	:	

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

Draft - 11/8/98 3:30pm

The Environmentalists have reviewed the Generation Auction Plan dated August 29, 1998 and the Generation Exchange Agreement in Principle dated October 14, 1998 and offer these comments. Many of these comments consist of questions whose answers are not found in the auction plan. The Environmentalists assert that the Commission needs to find satisfactory answers to these questions before approving this auction.

Introductory Comments

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

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

Motion, we argued that, since more agreement terms will be added by Duquesne¹ and each term now included is subject to change, there is literally nothing we can comment on in final form. As such, our comments should be seen as preliminary, like the document we have been provided.

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

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

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

The plan Duquesne has advanced has two distinct parts that must be handled sequentially. First, under the CAPCO agreements, Duquesne was required to receive approval of the other joint owners of the CAPCO units before it could auction the units off as part of its capacity. Duquesne is presently in federal court in Ohio seeking a ruling that would allow it to auction its share of the CAPCO units without interference from other joint owners.² Duquesne sought a similar ruling from FERC, but was denied by a FERC Order, dated September 24. Having been stymied in getting the approval it sought in either forum, Duquesne now proposes to swap its shares in CAPCO units for some generating units with First Energy. Then it will proceed to step two and auction the units it gets from First Energy, together with the ones it retains. Evaluation of the auction, however, must await the completion of the swap.

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

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

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

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

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

Also, Duquesne's dispute about certain CAPCO capacity remains in Ohio federal court. When finalized, the swap is intended to resolve those issues. But nothing is certain. It depends on the specifics of the final agreement between Duquesne and First

Energy. As First Energy states in its Comments (p. 2), “These issues *may* be entirely obviated upon the consummation of the recently announced exchange of generating units between Duquesne and First Energy.” (emphasis added)

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

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

Undergirding the swap proposal is the offer by First Energy ensure that “the net proceeds from the DLC Auction will be sufficient, as a minimum, to maintain or reduce the level of stranded cost recovery approved by the PaPUC in its May 29, 1998 restructuring order.” [Agreement, ¶4, page 2]. First Energy will guarantee that the net proceeds of the auction will not fall below \$110 million, the figure assigned in the restructuring order as the market value of Duquesne’s generation assets.

Duquesne has repeatedly told the parties not to worry about the relative value of the generation assets being swapped because of this financial guarantee. There is no way, they say, that ratepayers will be worse off than they are under the order. But this argument transforms the auction from a true market-based approach to determine the market value of Duquesne’s generation units to an exercise whose success is measured by its ratification of the administratively-determined value.

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

The Environmentalists cannot help but think that the administratively-determined value of Duquesne’s generation assets of \$110 million was dreadfully low. How else to explain the willingness of First Energy to guarantee this level of net proceeds despite the risk and uncertainty (nuclear decommissioning, labor costs, Beaver Valley 2 lease costs, transaction costs, etc.) of the swap and auction? This observation should be kept in mind when evaluating the auction provisions.

The Generation Auction Plan

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

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

results of the auction because whatever they do not get for market price they will get from the competitive transition charge. The Commission therefore needs to protect the interests of the ratepayers and assure that the auction results in the maximum value for the generation assets.

Comment 6: The plan contains no guidance about asset bundling.

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

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

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

Duquesne later sells the plant? These are all questions which the Commission needs to have answered in its ruling on the auction.

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

Duquesne is now proposing that offering to auction off the Provider of Last Resort (“PLR”) service. The winning provider would supply wholesale power to Duquesne at the shopping credit rates contained in the compliance filing. [Supplement Filing, November 5, 1998, pages 3-4 and Appendix C].

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

The Auction Plan requires all transaction costs to be born by the ratepayers. [Auction Plan, Part VII, page 35]. The Environmentalists suggest that some sharing of the costs would be appropriate to reflect the value of these actions to the shareholders. Duquesne has stated that the proposed generation swap would relieve Duquesne of the cost of litigation and other actions to obtain legal authority to sell the assets it jointly owns with CAPCO. The Commission should allocate some of the transaction costs to the shareholders.

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

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

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

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

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

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

communities. The Commission needs much more information about these issues before it can approve the Auction Plan.

Comment 12: Will the bidder confidentiality agreement discourage bidder participation in the auction?

Appendix C of the Auction Plan is a draft confidentiality agreement which interested buyers must sign to participate in the auction. The appendix requires interested buyer to agree not to challenge the auction results, not to disclose any information about the auction for 3 years, to agree that Duquesne is entitled to equitable relief and attorneys fees in any action to enforce the agreement, etc. Are all of these provisions necessary? Are they likely to discourage bidder participation in the auction?

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

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

Comments 14: The accumulated SO₂ allowances should be retired.

The Auction Plan states that the Cheswick station has accumulated approximately 12,000 tons SO₂ of allowances which will be assigned to the new owner of the facility. [Auction Plan , p. 22]. The Environmentalists would like to see the Commission require Duquesne to retire these allowances, thus preventing the future release of 12,000 tons of SO₂ into Pennsylvania's environment. This would be a significant step in reducing pollution.

If the allowances are not retired, the Environmentalists suggest that they be auctioned separately and not as part of the Cheswick plant. There is a healthy market for SO₂ allowances and they will likely fetch a better price if they are auctioned to a broader market of companies needing SO₂ allowances but not necessarily in purchasing the Cheswick station.

The Generation Exchange

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

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

Several parties have asked, and Duquesne has attempted to provide data, about the book value of each set of plants, the expected market value of each set of plants,

the respective costs of environmental compliance and life extensions, etc. The Commission needs to address this data very carefully to determine that the generation assets which Duquesne obtains in the swap are no less valuable than the generation assets it is giving to First Energy.

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

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

The Commission must protect the ratepayers by assuring that the exposure of Duquesne's ratepayers is capped.

Comment 17: Does the exclusion of transmission access for the First Energy plants reduce their market value?

The First Energy plants in Ohio will have no capacity guaranteed to make certain the power can reliably and economically be transmitted to the Duquesne service territory. Will this reduce their market value, since the new operators will have to

acquire (and pay for) transmission access to get the power to customers in the Duquesne service territory?

Comment 18: Does the exclusion of transmission access for the First Energy plants limit their ability to serve customers in the Duquesne service territory?

As noted in the previous comment, the First Energy plants in Ohio will have no capacity guaranteed to make certain the power can reliably and economically be transmitted to the Duquesne service territory. What will be the effect of this on customers in the Duquesne service territory?

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

In the generation swap, First Energy insisted that the Duquesne plants it acquires under the agreement be accompanied by transmission lines so that its ability to transmit the power to Ohio is guaranteed. [Agreement, ¶ 10]. The Commission needs to understand what impact will this have on the remainder of the transmission system in the Duquesne service territory.

Respectfully submitted,

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Date: November 9, 1998