

**COMMONWEALTH OF KENTUCKY**  
**BEFORE THE PUBLIC SERVICE COMMISSION**

Joint Application of Duke Energy Corporation, )  
Duke Energy Holding Corp., Deer Acquisition )  
Corp., Cougar Acquisition Corp., Cinergy Corp., ) Case No. 2005-00228  
The Cincinnati Gas & Electric Company, and )  
The Union Light, Heat and Power Company for )  
Approval of a Transfer and Acquisition )  
of Control )

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**DIRECT TESTIMONY OF JOINT APPLICANTS**

**VOLUME I of II**

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED

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PUBLIC SERVICE  
COMMISSION

IN THE MATTER OF:

JOINT APPLICATION OF DUKE ENERGY ) CASE NO. 2005-00228  
CORPORATION, DUKE ENERGY HOLDING )  
CORP., DEER ACQUISITION CORP., )  
COUGAR ACQUISITION CORP., CINERGY )  
CORP., THE CINCINNATI GAS & ELECTRIC )  
COMPANY, AND THE UNION LIGHT, HEAT )  
AND POWER COMPANY FOR APPROVAL )  
OF A TRANSFER AND ACQUISITION OF )  
CONTROL )

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VOLUME 1 OF 2

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THE UNION LIGHT, HEAT AND POWER COMPANY

DIRECT TESTIMONY OF

- JAMES E. ROGERS
  - RICHARD J. OSBORNE
  - THOMAS J. FLAHERTY
  - GREGORY C. FICKE
  - JOHN C. PROCARIO
-

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**DIRECT TESTIMONY OF**

**JAMES E. ROGERS**

**ON BEHALF OF**

**JOINT APPLICANTS**

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## **I. INTRODUCTION**

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is James E. Rogers, and my business address is 139 East Fourth Street,  
3 Cincinnati, Ohio 45202.

4 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

5 A. I am Chairman, President and Chief Executive Officer of Cinergy Corp. ("Joint  
6 Applicant" or "Cinergy"). Cinergy is the parent holding company of The Union  
7 Light Heat & Power Company ("Joint Applicant" or "ULH&P" or "Company"),  
8 its parent company, The Cincinnati Gas & Electric Company ("CG&E"), and PSI  
9 Energy, Inc. ("PSI"). I am also Chairman and Chief Executive Officer of  
10 ULH&P.

11 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND PROFESSIONAL**  
12 **BACKGROUND.**

13 A. I received a bachelor's degree in Business Administration (1970) and a law  
14 degree (1974) from the University of Kentucky. I became Vice Chairman,  
15 President and Chief Operating Officer of Cinergy in October 1994, and I became  
16 Chief Executive Officer in 1995. Prior to joining Cinergy, I was Chairman and  
17 Chief Executive Officer of PSI and PSI Resources, Inc., the parent company of  
18 PSI ("PSIR"). Before coming to PSI in October of 1988 as Chief Executive  
19 Officer, I was Executive Vice President of the gas pipeline group of Enron Corp.,  
20 and President of Enron's interstate gas pipeline companies from 1985 to 1988.  
21 From 1979 to 1981 and from 1983 to 1985, I was in private law practice in  
22 Washington, D.C. with the law firm of Akin, Gump, Strauss, Hauer & Feld.

1 During that time, I represented natural gas pipelines, gas producers and electric  
2 utilities before the Federal Energy Regulatory Commission (“FERC”) and various  
3 federal courts. From 1981 to 1983, I was Deputy General Counsel for litigation  
4 and enforcement at the FERC. In that position, I directed FERC’s litigation  
5 efforts in cases involving electric rates, hydroelectric licensing, gas producer and  
6 gas pipeline rates. I began my career with the Kentucky Attorney General’s  
7 Office, representing consumer interests in utility cases.

8 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**  
9 **PROCEEDING?**

10 A. My testimony focuses on the strategic rationale behind the proposed merger of  
11 Cinergy and Duke Energy Corporation (“Duke Energy”), and the benefits of the  
12 merger for all stakeholders – customers, investors, communities, and employees.  
13 My testimony also provides some background information about Duke Energy,  
14 explains the proposed transaction, explains the shared management values that  
15 exist between Duke Energy and Cinergy, and discusses the success of the merger  
16 that created Cinergy (*i.e.*, the 1994 merger between CG&E and PSIR).

17 **Q. PLEASE BRIEFLY OUTLINE THE REMAINDER OF JOINT**  
18 **APPLICANTS’ CASE-IN-CHIEF FILING.**

19 A. Joint Applicants present the testimony of several witnesses designed to show that  
20 the merger will not adversely affect our Kentucky stakeholders. First, Joint  
21 Applicants present the testimony of Mr. Richard J. Osborne, Duke Energy’s  
22 Group Vice President, Public and Regulatory Policy. Mr. Osborne describes  
23 Duke Energy’s businesses, its corporate and business structure, its executive

1 team, and Duke Energy's technical, managerial and financial ability to own  
2 ULH&P's utility operations. He also details Duke Energy's philosophy regarding  
3 corporate governance, and its commitment to system reliability, customer service,  
4 economic development, charitable works, and environmental stewardship.

5 Next, Mr. Thomas J. Flaherty of Booz Allen Hamilton describes the work  
6 he did for Cinergy and Duke Energy related to identifying and quantifying the net  
7 savings expected to result from the merger. Mr. Flaherty describes the various  
8 areas where savings are expected, and the estimated costs to achieve those  
9 savings.

10 ULH&P President, Mr. Gregory C. Ficke's testimony focuses on the local  
11 effect of the merger on ULH&P's operations in Kentucky. He describes how the  
12 merger will not adversely impact the areas of local presence, reliability and safety,  
13 customer service, rates, financial integrity, economic development, charitable  
14 giving, and environmental commitment. Mr. Ficke also speaks to the  
15 reasonableness of various affiliate agreements that ULH&P expects to enter into  
16 as a result of the merger.

17 The testimony of Mr. John Procario, Cinergy's Senior Vice President and  
18 Chief Operating Officer of the Regulated Business Unit, focuses on ULH&P's  
19 provision of reliable natural gas and electric service presently and its continued  
20 commitment to providing reliable service to its customers after the merger.  
21 Additionally, Mr. Procario addresses ULH&P's continued commitment to the  
22 Midwest Independent Transmission System Operator, Inc. ("Midwest ISO").

1 Ms. Lynn J. Good, Vice President Finance and Controller for Cinergy,  
2 discusses accounting issues related to the merger, and sponsors a proposed revised  
3 Tax Sharing Agreement between ULH&P and its affiliates and *pro forma*  
4 financial statements related to the merger.

5 The testimony of Ms. Wendy L. Aumiller, Vice President and Treasurer,  
6 discusses how the merger is not expected to adversely affect the financial integrity  
7 of ULH&P, and sponsors the proposed Duke Energy Regulated Money Pool  
8 Agreement, which provides for loans between the utility company affiliates.

9 Mr. Steven M. Fetter, of REGULATION UnFETTERED, offers his  
10 opinion on financial issues related to the merger and on the reasonableness of  
11 ULH&P's merger savings sharing proposal.

12 The testimony of Mr. Barry F. Blackwell, Director Management Reporting  
13 and Analysis, discusses the service agreements, which will allocate costs among  
14 the various affiliates of the new company, and describes how the merger savings  
15 and costs to achieve merger savings calculated by Mr. Flaherty are then allocated  
16 among the various affiliated companies, including ULH&P.

17 Finally, the testimony of Mr. John P. Steffen, Vice President, Rates,  
18 describes in detail how the net merger savings will be shared with customers up-  
19 front, prior to processing any retail natural gas or electric base rate case, and  
20 beginning immediately after approval of the merger.

## **II. DUKE ENERGY CORPORATION**

21 **Q. PLEASE BRIEFLY DESCRIBE DUKE ENERGY AND DUKE POWER,**  
22 **ITS REGULATED UTILITY.**

1 A. Duke Energy is a diversified energy company with a portfolio of electric and  
2 natural gas businesses, both regulated and non-regulated, and an affiliated real  
3 estate company. Duke Energy is headquartered in Charlotte, North Carolina, and  
4 currently has approximately 21,500 employees. The subsidiaries of Duke Energy  
5 supply, deliver and process energy for customers in the Americas. As of  
6 December 31, 2004, Duke Energy had assets of \$55.5 billion, revenues of \$22.5  
7 billion, and net income of \$1.5 billion.

8 Duke Power is a regulated utility that has provided safe, reliable and  
9 economically priced electric utility service in North Carolina and South Carolina  
10 for over 100 years. Duke Power serves approximately 2.2 million customers in  
11 North and South Carolina and owns and operates over 18,000 megawatts of  
12 generation, consisting of coal-fired, nuclear, gas and oil-fired, and hydro units.  
13 Duke Power also owns and operates approximately 13,000 miles of transmission  
14 lines, and 94,000 miles of distribution lines. Duke Power's retail electric rates are  
15 highly competitive – currently 21% below the national average.

### **III. THE PROPOSED TRANSACTION**

16 **Q. PLEASE DESCRIBE THE PROPOSED MERGER TRANSACTION.**

17 A. The proposed merger will be accomplished via an all-stock transaction.  
18 Essentially, via a series of mergers, conversions, and reorganizations, Cinergy,  
19 Duke Power, Duke Capital LLC, and Duke Energy Shared Services, LLC will  
20 become wholly-owned subsidiaries of a new Duke Energy holding company (to  
21 be named “Duke Energy Corporation” and referred to herein as the “New Duke  
22 Energy”). Holders of Cinergy common stock will receive 1.56 shares of New

1 Duke Energy holding company common stock for each share of Cinergy common  
2 stock held – a 13.4% premium for Cinergy shareholders based upon the Duke  
3 Energy and Cinergy stock prices immediately prior to the date of the merger  
4 announcement. As a result, the current holders of Cinergy common stock will  
5 become holders of the New Duke Energy holding company common stock, and  
6 Cinergy will become a wholly-owned subsidiary of the New Duke Energy. After  
7 completion of the merger, Duke Energy shareholders will own approximately  
8 76% of the New Duke Energy holding company stock, and Cinergy shareholders  
9 will own approximately 24% of the New Duke Energy holding company stock.

10 **Q. HOW WILL THE BOARD OF DIRECTORS OF THE NEW DUKE**  
11 **ENERGY HOLDING COMPANY BE DETERMINED?**

12 A. Duke Energy will have the right to name ten directors to the New Duke Energy  
13 holding company board, and Cinergy will have the right to name five directors.  
14 Paul Anderson, Duke Energy’s Chairman and Chief Executive Officer, will be the  
15 Chairman of the New Duke Energy holding company board.

16 **Q. HOW WILL CINERGY’S AND ULH&P’S CORPORATE**  
17 **HEADQUARTERS BE AFFECTED BY THE MERGER?**

18 A. The New Duke Energy holding company’s corporate headquarters will be in  
19 Charlotte, North Carolina. ULH&P’s and Cinergy’s corporate headquarters will  
20 remain in Cincinnati, Ohio.

21 **Q. WHAT IMPACT WILL THE MERGER HAVE ON THE MANAGEMENT**  
22 **TEAM AND EMPLOYEES OF ULH&P AND CINERGY?**

1 A. Decisions on the composition of management teams have yet to be made, for the  
2 most part. Paul Anderson and I are completing a process of interviewing senior  
3 management from both companies and as our integration planning proceeds, we  
4 will select the absolute best team from both companies to present for approval to  
5 the board of the combined company. However, pursuant to the terms of the  
6 Merger Agreement, I will be the President and Chief Executive Officer of the  
7 New Duke Energy holding company. I do not foresee any significant  
8 management changes within ULH&P as a result of the merger.

9 With regard to employees, we are projecting that we will be able to reduce  
10 the total combined Duke Energy / Cinergy workforce by approximately 5%, due  
11 to elimination of duplicative and overlapping positions. Most of these reductions  
12 will occur in areas such as corporate and administrative functions, certain  
13 planning functions, purchasing, and information technology, as well as on the  
14 non-regulated sides of the businesses. The number of employees who are directly  
15 involved in the production, transmission, and distribution of electricity, the  
16 distribution of natural gas, and in customer service, is not expected to be affected  
17 by the merger. We will achieve the necessary workforce reductions primarily  
18 through means such as normal attrition and retirements, early retirements and  
19 other severance programs.

#### IV. STRATEGIC RATIONALE FOR THE MERGER

20 Q. WHAT IS CINERGY'S STRATEGIC RATIONALE FOR MERGING  
21 WITH DUKE ENERGY?

1 A. Cinergy's management and board of directors considered a number of factors  
2 pertaining to the strategic rationale for the merger, including:

3 • **Increased Scale and Scope, Diversification of Risk.** The combined  
4 company will have greater diversification of markets and regulatory  
5 operations and more balance in its electric and gas businesses and generation  
6 portfolio. For example, the generation portfolio will have a greater balance in  
7 terms of fuel source, as well as geography, dispatch, and load-servicing  
8 capabilities. The combined company will also create a stronger portfolio of  
9 utility businesses with approximately 3.7 million retail electric customers and  
10 1.7 million retail gas customers in Kentucky, Indiana, Ohio, North Carolina,  
11 South Carolina, and Ontario, Canada. The retail electric businesses will have  
12 more than 25,000 megawatts of generation and broad operational and  
13 regulatory experience. We believe that the regulated businesses will  
14 contribute to stable earnings for the combined company, and will create the  
15 financial strength and scale to participate in the continuing consolidation of  
16 the utility sector, all at lower risk due to the broader diversification described  
17 above.

18 • **Anticipated Financial Strength and Flexibility.** The combined company  
19 will have electric and gas businesses with stand-alone scale. Based on  
20 implied market capitalization, the electric business will be one of the top five  
21 in the United States; the gas business will be the largest in North America.  
22 This increased scale and diversification of the combined company's



1 operations are expected to provide improved earnings and cash flows, and  
2 improved financial stability and flexibility for the combined company.

- 3 • **Stronger Merchant Power Platform.** With more than 16,000 megawatts of  
4 unregulated generation, we believe that the combined merchant power  
5 operation will benefit from increased fuel and market diversity. We also  
6 believe that Duke Energy's gas-fired merchant generation in the Midwest  
7 complements Cinergy's coal-fired generation in this region.
- 8 • **Shared Vision.** Cinergy and Duke Energy share a common vision of the  
9 future of the energy industry, as well as a common and consistent  
10 commitment to providing low cost, reliable and high quality service to our  
11 customers.
- 12 • **Combined Expertise.** The merger will combine complementary areas of  
13 expertise, and the combined company is expected to be able to draw upon the  
14 intellectual capital, technical expertise, and experience of a deeper, more  
15 diverse workforce.
- 16 • **Common Regulatory Framework.** Each regulatory framework in the five  
17 states where the combined company will operate utilities has some unique  
18 attributes, but all provide constructive regulation for customers and investors.  
19 Moreover, the merger provides for the opportunity to benefit from both  
20 companies' experience and knowledge in dealing with the complexities of  
21 regulation.
- 22 • **Cost Savings and Synergies.** Although there are no guarantees that all these  
23 savings will be achieved, we have estimated that the combination will

1 ultimately produce a total of approximately \$1.3 billion of net savings by the  
2 end of five years, and over \$500 million in annual steady-state savings for the  
3 combined company going forward. These cost savings are expected to result  
4 from elimination of duplicate spending and overlapping functions, improved  
5 sourcing strategies, and the consolidation of the two companies' non-regulated  
6 business unit operations.

**V. STAKEHOLDER BENEFITS**

7 **Q. IN YOUR VIEW, WILL THE MERGER PROVIDE BENEFITS FOR**  
8 **CINERGY'S AND ULH&P'S STAKEHOLDERS – ITS CUSTOMERS,**  
9 **INVESTORS, COMMUNITIES AND EMPLOYEES?**

10 A. Yes, I strongly believe that the merger will benefit all of our stakeholders. All  
11 stakeholders will benefit from having a financially stronger and more diverse  
12 combined company.

13 Customers will benefit from the sharing of estimated synergies and cost  
14 savings, from the sharing of “best practices” with a high performing utility such  
15 as Duke Power, and from the combined company's continuing commitment to  
16 providing safe, reliable natural gas and electric utility service. The merger, and  
17 the synergies and savings that will be created as a result, will help ULH&P keep  
18 its rates competitive. The ability to partner with and learn from Duke Power – a  
19 top quality utility company – will only serve to improve the quality of service we  
20 provide to customers here in Kentucky.

1           Our shareholders will benefit from owning a stronger company, and from  
2 the impact of the estimated synergies and cost savings. In addition, they will  
3 benefit from the share exchange ratio negotiated in the merger agreement.

4           Our communities (and our customers) will benefit from the combined  
5 company's continued support of charitable, philanthropic, and service initiatives  
6 in the states we serve. We have a continuing commitment to maintain our local  
7 presence throughout our Kentucky service territory, and to continue our record of  
8 being a leader in economic development in the communities we serve. Duke  
9 Energy has an exemplary history with regard to community service, and our  
10 merger will be a unique opportunity to build on the combined experience and  
11 dedication of the employees of our two companies in this regard.

12           Our employees will benefit from having a financially stronger and more  
13 diversified employer. Opportunities for varied positions and career growth will  
14 be enhanced in the larger, multi-faceted organization. The increased scale and  
15 scope will position the New Duke Energy well for the future, making it an  
16 attractive company capable of maintaining the reputation Cinergy already enjoys  
17 as an employer of choice.

## VI. CINERGY'S MERGER TRACK RECORD

18 **Q. THIS IS NOT THE FIRST MERGER FOR ULH&P. NOW THAT IT HAS**  
19 **BEEN OVER TEN YEARS SINCE THE CREATION OF CINERGY, HOW**  
20 **DO YOU RATE THE SUCCESS OF THE CINERGY MERGER?**

21 A. I consider the Cinergy merger to be very successful. Cinergy's total shareholder  
22 return from October 1994 through 2004 was 227.8%, which is an annualized

1 average return of 12.7% to investors each year. Since 1994, Cinergy has  
2 increased its assets by 84%, operating income by 68%, and revenues by 62%.  
3 Cinergy has increased its retail customers by about 17%, all while decreasing its  
4 employee count (and thus labor costs) by about 12%. We are a larger, more  
5 efficient company providing greater value to all of our stakeholders.

6 Most importantly, with the Cinergy merger, we created approximately  
7 \$1.5 billion in cost savings over the first ten years. These savings helped keep our  
8 retail electric and gas rates in Indiana, Ohio and Kentucky lower than they  
9 otherwise would have been. In fact, Cinergy's operating utilities continue to have  
10 some of the lowest electric rates in the region. When adjusted for inflation,  
11 ULH&P's 2004 average retail electric rates are lower than they were in 1994.

12 In the volatile area of fuel costs, while on the rise due to higher natural gas  
13 and coal costs, Cinergy's overall fuel cost per MWH has remained relatively flat  
14 from 1994 to 2004. Cinergy's electric and natural gas customer service costs per  
15 customer have decreased since 1994, all while maintaining excellent customer  
16 service, as evidenced by our recent call center award from J.D. Power and  
17 Associates.

18 These cost containment achievements are remarkable considering that  
19 using the annual average CPI, inflation alone has increased costs by an average of  
20 27.4% since 1994.

21 At the same time, Cinergy has consistently outperformed the J.D. Power  
22 and Associates' regional and national average for customer satisfaction with  
23 Power Quality and Reliability. Additionally, since 1994 we have increased our

1 overall customer satisfaction as evidenced by customer and industry surveys. For  
2 the almost eleven years since the Cinergy merger, ULH&P has maintained a  
3 strong local presence in its service territories. As described in the testimony of  
4 Mr. Ficke, we have maintained a successful economic development program, and  
5 a continuing commitment to philanthropy in Kentucky.

6 ULH&P's and Cinergy's track record with its previous merger is  
7 excellent, and bodes well for the success of the proposed Duke Energy / Cinergy  
8 merger.

## VII. SHARED VALUES

9 **Q. FROM A REGULATED UTILITY PERSPECTIVE, WHY IS DUKE**  
10 **ENERGY A GOOD MERGER PARTNER FOR CINERGY AND ULH&P?**

11 A. As I previously mentioned, Duke Power, the regulated utility arm of Duke  
12 Energy, has a long and proud history and tradition of providing high quality  
13 electric service and of exhibiting good corporate citizenship. Our shared values in  
14 these areas are striking, and lead me to believe that the merger will be highly  
15 successful for all of our stakeholders.

16 At Cinergy, we believe our core purpose is to provide reliable,  
17 competitively priced energy and related services to millions of people, making  
18 their lives safer, healthier and more comfortable. We aspire to be the energy  
19 company preferred by each of our stakeholders: customers, employees, investors,  
20 suppliers, and the communities we serve. Cinergy's core values include:

- 21 • **Social Responsibility**
- 22 • **Economic Progress**

1           • **Environmental Improvement**

2           • **Ethical Business Practices**

3           As Cinergy strives to meet its purpose, we stay focused on the following guiding  
4           principles:

- 5           • Focus on the customer – Listen. Show respect. Take ownership. Take  
6           action. Honor commitments.
- 7           • Demonstrate environmental stewardship in all we do.
- 8           • Practice ethics, integrity and transparency in all that we do.
- 9           • Be bold, aim high, and expect high performance from yourself, your  
10          colleagues and your company.
- 11          • Strive for continuous improvement. Think beyond what has been done  
12          before and find new ways to work better, faster, and cheaper.
- 13          • Turn challenges and risks into opportunities by being proactive and  
14          creative.
- 15          • Be flexible by being open to change and willing to learn new skills.
- 16          • Demonstrate respect and value the opinions and differences of others.
- 17          • Emphasize “Safety Always!” – Watch out for the safety of each other and  
18          the public.
- 19          • Value teamwork – One company, one stock, one team.

20          Similarly, Duke Energy has adopted a Charter emphasizing that, in conducting  
21          its business, Duke Energy values:

- 22          • **Stewardship** – A commitment to health, safety, environmental  
23          responsibility and our communities.
- 24          • **Integrity** – Ethically and honestly doing what we say we will do.
- 25          • **Respect for the Individual** – Embracing diversity and inclusion,  
26          enhanced by openness, sharing, trust, teamwork and involvement.
- 27          • **High Performance** – The excitement and fulfillment of achieving  
28          superior business results and stretching our capabilities.
- 29          • **Win-Win Relationships** – Having relationships which focus on the  
30          creation of value for all parties.
- 31          • **Initiative** – Having the courage, creativity and discipline to lead change  
32          and shape the future.

1           These shared values should serve the combined-company well and make  
2 for a seamless and successful integration.

3           The testimony of Mr. Ficke details how CG&E's reliability, competitive  
4 rates, quality of customer service, support for economic development and  
5 charitable giving, and environmental commitment will not be adversely affected  
6 by the merger. Additionally, the testimony of Mr. Ficke and Mr. Osborne detail  
7 Duke Energy's commitment to these important values.

8 **Q. PLEASE DESCRIBE YOUR CONTINUING COMMITMENT TO**  
9 **BUSINESS ETHICS AND CORPORATE GOVERNANCE.**

10 A. At Cinergy, our code of conduct and business ethics and governing policies set  
11 the values and strategic guidance for how we want to perform as a company.  
12 Cinergy was one of the first companies in the U. S. to establish a board-level  
13 corporate governance committee in 1994. Cinergy has been frequently ranked in  
14 the top ten of U.S. companies under Institutional Shareholder Services' Corporate  
15 Governance Quotient rating. GovernanceMetrics International has given Cinergy  
16 a score of "8.0" out of "10" in both their Home and Global Markets. These  
17 ratings demonstrate that we have both a strong corporate governance structure and  
18 have executed on that structure.

19           Similarly, Duke Energy strives to serve its customers, employees,  
20 investors, business partners and suppliers ethically and honestly. In addition to its  
21 Charter outlining Duke Energy's purpose and values, Duke Energy has an  
22 extensive Code of Business Ethics including areas such as accuracy of books and  
23 records, confidential information, environment health and safety, political giving,

1 harassment, safeguarding company resources and risk management. Additionally,  
2 Duke Energy's Board has a Corporate Governance Committee.

3 I vow to continue my personal commitment to strong corporate  
4 governance and business ethics in the New Duke Energy.

5 **Q. ULH&P IS A FOUNDING MEMBER AND HAS BEEN A STRONG**  
6 **SUPPORTER OF THE MIDWEST ISO. WILL THE MERGER CHANGE**  
7 **THIS COMMITMENT?**

8 A. No. ULH&P is committed to the success of the Midwest ISO, and will remain so  
9 after the merger. We believe the Midwest ISO enhances reliability of the  
10 transmission system and can provide for an enhanced competitive wholesale  
11 energy market to the benefit of all of ULH&P's stakeholders. The merger will  
12 not affect ULH&P's participation in or commitment to the Midwest ISO.

#### **VIII. CONCLUSION**

13 **Q. PLEASE SUMMARIZE YOUR CONCLUSIONS CONCERNING THE**  
14 **IMPACT OF THE MERGER ON ULH&P AND ITS STAKEHOLDERS.**

15 A. Duke Energy and Cinergy are complementary companies, with shared values and  
16 a history of providing reliable and quality service to our customers. The  
17 combined company will be larger and more diverse, enabling it to adjust to  
18 changing market conditions. Cinergy, under my leadership, has solid history of a  
19 successful merger, including successfully executing on and producing large  
20 merger savings to the benefit of customers. I am committed to making the merger  
21 of Cinergy and Duke Energy a success by creating value for all of the  
22 stakeholders of the New Duke Energy.



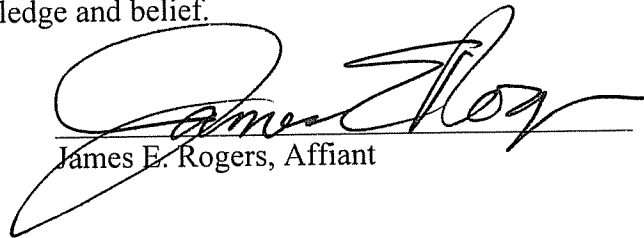
1 Q. DOES THAT CONCLUDE YOUR PREPARED DIRECT TESTIMONY?

2 A. Yes, it does.

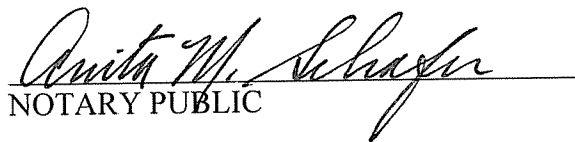
**VERIFICATION**

State of Ohio            )  
                                  )     SS:  
County of Hamilton    )

The undersigned, James E. Rogers, being duly sworn, deposes and says that he is the Chairman, President and Chief Executive Officer of Cinergy Corp. ("Cinergy"), that he has personal knowledge of the matters set forth in the foregoing testimony, and that the answers contained therein are true and correct to the best of his information, knowledge and belief.

  
James E. Rogers, Affiant

Subscribed and sworn to before me by JAMES E. ROGERS on  
this 8<sup>th</sup> day of July, 2005.

  
NOTARY PUBLIC

My Commission Expires: \_\_\_\_\_



**ANITA M. SCHAFER**  
Notary Public, State of Ohio  
My Commission Expires  
November 4, 2009



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## APPENDIX

ATTACHMENT RJO-1 – Duke Energy's North American Assets.

ATTACHMENT RJO-2 – Duke Energy’s Generation Assets.

**I. INTRODUCTION**

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. Richard J. Osborne, 526 South Church Street, Charlotte, North Carolina 28202.

3 **Q. PLEASE BRIEFLY DESCRIBE YOUR EDUCATION.**

4 A. I graduated from Tufts University with a Bachelor of Arts degree in economics  
5 and history, and I earned my MBA from the University of North Carolina at  
6 Chapel Hill.

7 **Q. WHO IS YOUR CURRENT EMPLOYER, AND WHAT IS YOUR  
8 CURRENT POSITION WITH THAT EMPLOYER?**

9 A. I am Group Vice President, Public and Regulatory Policy, for Duke Energy  
10 Corporation (“Duke Energy”). I have overall responsibility for the company’s  
11 public policy agenda and relationships with regulators, legislators, communities  
12 and other key stakeholders. I serve on the company’s Executive Committee,  
13 which drives corporate strategy, transactions, financial plans and enterprise  
14 policy.

15 **Q. PLEASE BRIEFLY SUMMARIZE YOUR WORK EXPERIENCE.**

16 A. I served in Duke Power’s financial/administration summer internship program in  
17 1974, and joined the company as a Financial Analyst in 1975. I was named  
18 Manager of Financial Relations in 1980, Manager of Treasury activities in May  
19 1981, and Treasurer in August 1981. I was elected Vice President of Finance in  
20 1988, Vice President and Chief Financial Officer in 1991, and Senior Vice  
21 President in 1994. Following the creation of Duke Energy in 1997, I was named  
22 Executive Vice President and Chief Financial Officer. I was named Executive

1 Vice President and Chief Risk Officer in 2000. I was named to my current  
2 position on January 1, 2004.

3 **Q. PLEASE DESCRIBE ANY PROFESSIONAL AFFILIATIONS AND**  
4 **OUTSIDE ACTIVITIES, IF ANY, YOU BELIEVE ARE RELEVANT TO**  
5 **YOUR TESTIMONY.**

6 A. I have been active in the Edison Electric Institute (“EEI”) and am past chairman  
7 of the EEI Executive Committee on Finance, Taxes and Regulation. I am also a  
8 member of the Financial Executives Institute.

9 I serve on the boards of directors of NEIL (Nuclear Electric Insurance  
10 Limited), Johnson C. Smith University, the Museum of the New South, the  
11 Charlotte Symphony and United Way of Central Carolinas.

12 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE ANY REGULATORY**  
13 **AGENCIES?**

14 A. Yes. I have testified before the North Carolina Utilities Commission and Public  
15 Service Commission of South Carolina.

16 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**  
17 **PROCEEDING?**

18 A. The purpose of my testimony is to introduce Duke Energy to the Commission, to  
19 discuss the strategic, policy and financial reasons that support our merger with  
20 Cinergy Corp. (“Cinergy”), and to establish that Duke Energy has the managerial,  
21 financial and technical capability to manage and operate The Union Light, Heat  
22 and Power Company. (“ULH&P”)

## **II. A GENERAL DESCRIPTION OF DUKE ENERGY**

### **A. THE DUKE ENERGY BUSINESS**

1 **Q. PLEASE PROVIDE A GENERAL FINANCIAL DESCRIPTION OF DUKE**  
2 **ENERGY.**

3 A. Duke Energy is a Fortune 500 company, ranking number 86 in the magazine's  
4 2005 rankings. As of December 31, 2004, Duke Energy has assets of \$55.5  
5 billion, revenues of \$22.5 billion and net income of \$1.5 billion.

6 **Q. PLEASE PROVIDE A FURTHER DESCRIPTION OF DUKE ENERGY**  
7 **AND ITS BUSINESSES.**

8 A. Duke Energy is a diversified energy company with a portfolio of both regulated  
9 and unregulated natural gas and electric businesses throughout the Americas, and  
10 an affiliated real estate company. Duke Energy is headquartered in Charlotte,  
11 North Carolina, and traces its roots to 1904 when its first hydroelectric power  
12 plant on the Catawba River opened to serve a single customer - a textile mill in  
13 South Carolina. Our current gas transmission businesses date to 1947, and began  
14 by building and expanding interstate pipeline systems to carry natural gas from  
15 the Gulf of Mexico to the Northeast United States. Over the past century, Duke  
16 Energy has grown to become one of the world's leading energy companies by  
17 continuing to focus on operational excellence, safety, environmental stewardship  
18 and customer and community service, wherever we do business.

19 Today, Duke Energy owns and operates power generation assets with the  
20 capability of 32,000 MW and operates an additional 3,000 MW of generation  
21 assets for others. Duke Energy owns 17,500 miles of natural gas transmission



1 pipeline, and jointly with ConocoPhillips, 59,000 miles of gas gathering pipeline.  
2 Attached as Attachment RJO-1 is a map illustrating the location of Duke Energy's  
3 North American assets.

4 Duke Energy's principal businesses include the following:

5 Duke Power, a division of Duke Energy, is headquartered in Charlotte,  
6 North Carolina, and is one of the largest investor-owned utilities in the United  
7 States with 2.2 million electric customers in its 22,000 square-mile service  
8 territory in central and western North Carolina and western South Carolina. Duke  
9 Power owns and operates a diverse mix of generating facilities, with eight coal-  
10 fired generating stations (7,754 MW), three nuclear stations (5,020 MW owned,  
11 6,996 MW operated), 31 hydroelectric stations, including two pumped storage  
12 facilities (2,819 MW), two combustion turbine stations and several additional  
13 combustion turbine units (2,446 MW). I attach as Attachment RJO-2, a more  
14 detailed description of Duke Power's generation assets. Duke Power's 13,000-  
15 mile electric transmission system has interconnection to the following eight  
16 neighboring utilities: AEP, Southern Company, Southeastern Power Association,  
17 Santee Cooper, South Carolina Electric & Gas, Progress Energy Carolinas,  
18 Yadkin, and TVA.

19 Duke Energy Gas Transmission ("DEGT") is headquartered in Houston,  
20 Texas, and transports natural gas through pipelines to markets in the northeastern  
21 and southeastern United States and in the Pacific Northwest and Canada. DEGT  
22 has more than 60 years of experience in designing, planning, constructing,  
23 operating and maintaining long-haul (interstate and interprovincial) natural gas

1 systems, with more than 17,500 miles of transmission pipeline. In addition to its  
2 transmission pipeline assets, DEGT has significant depleted reservoir and salt  
3 cavern natural gas storage capabilities of approximately 250 billion cubic feet in  
4 the United States and Canada, as well as two liquid natural gas storage and  
5 regasification facilities. DEGT's Texas Eastern Transmission, LP owns and  
6 operates 1,050 miles of pipeline in Ohio, 254 miles in Indiana and 691 miles in  
7 Kentucky. Texas Eastern Transmission, LP has compressor stations located in  
8 Athens, Berne, Five Points, Glen Karin, Lebanon, Somerset, Summerfield and  
9 Wheelersburg, Ohio; Batesville, French Lick, Gas City, Oakland City and  
10 Seymour, Indiana; and in Danville, Owingsville, and Tompkinsville Station,  
11 Kentucky. Through Union Gas, an integrated natural gas storage, transmission  
12 and distribution company, DEGT distributes natural gas to some 1.2 million retail  
13 customers in Ontario, Canada.

14 Duke Energy Americas includes Duke Energy North America ("DENA"),  
15 which owns and operates merchant power generation facilities and markets  
16 electricity, natural gas, energy management and related services to wholesale  
17 customers throughout North America, and Duke Energy International ("DEI"),  
18 which owns and operates power generation facilities and sells electric power and  
19 natural gas in Latin America.

20 Duke Energy Field Services ("DEFS") is headquartered in Denver,  
21 Colorado and is the largest producer of natural gas liquids ("NGLs"), and one of  
22 the largest NGLs marketers, in North America. DEFS gathers, processes,

1 transports, markets and stores natural gas and produces, transports and markets  
2 NGLs. DEFS is a joint venture of Duke Energy and ConocoPhillips.

3 Crescent Resources is headquartered in Charlotte, North Carolina, and  
4 manages land holdings and develops high quality commercial, residential and  
5 multi-family real estate projects in nine states.

6 DukeNet Communications is headquartered in Charlotte, North Carolina  
7 and develops and manages fiber optic communications systems in North Carolina,  
8 South Carolina and Georgia for wireless, local and long-distance communications  
9 companies and selected large-business customers.

#### **B. CORPORATE STRUCTURE**

10 **Q. PLEASE DESCRIBE DUKE ENERGY'S CORPORATE AND**  
11 **MANAGEMENT STRUCTURE AND PROVIDE INFORMATION ABOUT**  
12 **DUKE ENERGY'S EXECUTIVE LEADERS.**

13 A. Currently, Duke Energy is a North Carolina corporation and is organized as  
14 follows: Duke Power is a division of Duke Energy and is not a separate legal  
15 entity. Duke Energy's wholly-owned subsidiary Duke Capital, is the parent of  
16 DEGT, DENA, DEI, Crescent Resources and DukeNet Communications, and  
17 holds Duke Energy's interests in DEFS.

18 Duke Energy is led by an Executive Committee that drives corporate  
19 strategy, transactions, financial plans and enterprise policy. The Executive  
20 Committee is comprised of Paul M. Anderson, Chairman of the Board and Chief  
21 Executive Officer; Fred J. Fowler, President and Chief Operating Officer; David  
22 L. Hauser, Group Vice President and Chief Financial Officer; Jim W. Mogg,

1 Group Vice President and Chief Development Officer; A.R. Mullinax, Group  
2 Vice President, Duke Energy Business Services and Chief Information Officer;  
3 Thomas C. O'Connor, Group Vice President, Corporate Strategy; B. Keith Trent,  
4 Group Vice President and General Counsel & Secretary, and me in my capacity of  
5 Group Vice President Public and Regulatory Policy.

6 Duke Energy's Expanded Executive Committee is charged with  
7 addressing succession planning, business unit strategies, goals and objectives,  
8 corporate policies that reach across business units, and other issues. The  
9 Expanded Executive Committee includes members of the Executive Committee  
10 and Ruth Shaw, President and CEO of Duke Power, Martha B. Wyrsh, President  
11 and CEO of DEGT, W.H. (Bill) Easter, Chairman, President and CEO of DEFS  
12 and Bobby Evans, President and CEO of Duke Energy Americas. These leaders  
13 of the major operating groups are integrated with strategy and policy to the extent  
14 appropriate under applicable Federal Energy Regulatory Commission's ("FERC")  
15 standards of conduct.

16 Now, let me provide the background of some of Duke Energy's leaders:

17 Mr. Anderson has been Chairman and CEO since November 1, 2003. Mr.  
18 Anderson previously served as managing director and CEO of global natural  
19 resources group BHP Billiton Ltd, an Australian-listed company, and BHP  
20 Billiton PLC, a U.K.-listed company from which he retired on July 1, 2002. Prior  
21 to joining BHP, Mr. Anderson had a career that spanned more than 20 years at  
22 Duke Energy and its predecessor companies, including a key leadership role in  
23 the merger of Duke Power and PanEnergy in June 1997. At the time of the

1 merger, Mr. Anderson was Chairman, President and CEO of PanEnergy and then  
2 served as President and COO of Duke Energy from 1997 until his departure for  
3 BHP Billiton in 1998.

4 Mr. Fowler has been President and COO of Duke Energy since November  
5 2002 and is responsible for the operational, commercial and financial results of  
6 Duke Energy's energy-related businesses. He joined the company in 1985 and  
7 became General Manager of subsidiary Panhandle Trading Company ("PTC"), an  
8 independent buyer and reseller of natural gas in the national spot market. In 1987,  
9 he was named Vice President and General Manager of PTC. Mr. Fowler became  
10 Vice President of Marketing, Transportation and Exchange for Panhandle Eastern  
11 Pipe Line Co. and Trunkline Gas Co. in 1988, and served in the same capacity for  
12 Panhandle Eastern, Trunkline and Texas Eastern Transmission Corp. in 1989. He  
13 was elected President of Trunkline in 1991 and Corporate Vice President of  
14 Marketing for PanEnergy in 1992. Mr. Fowler was elected President of Texas  
15 Eastern in 1994 and named Group Vice President for PanEnergy Corp. in 1996.  
16 He then became Group President of Energy Transmission for Duke Energy in  
17 1997.

18 Mr. Hauser joined Duke Power in 1973 and has been Group Vice  
19 President and CFO since February 2004. For the first 20 years of his career, he  
20 held various accounting positions, including controller. He later served as Vice  
21 President, Procurement Services and Materials; Vice President of Global Asset  
22 Development; and then Treasurer. He is a Certified Public Accountant and  
23 Certified Purchasing Manager.

1 Dr. Shaw has been President of Duke Power since 2003, and was named  
2 President and CEO in October, 2004. She leads one of the largest electric utilities  
3 in the United States. Dr. Shaw joined Duke Power in 1992 as vice president of  
4 Corporate Communications and was named Senior Vice President of Corporate  
5 Resources in 1994. Prior to her current role, she served as Duke Energy's  
6 Executive Vice President and Chief Administrative Officer, and as President of  
7 the Duke Energy Foundation. Prior to joining Duke Power, Dr. Shaw served as  
8 President of Piedmont Community College in Charlotte, and was previously  
9 President of El Centro College in Dallas, Texas.

10 Following the merger with Cinergy, the new Duke Energy Corporation  
11 ("New Duke Energy") will be a Delaware corporation. New Duke Energy will be  
12 headquartered in Charlotte, North Carolina. Mr. Anderson will be Chairman of  
13 the Board and Mr. James E. Rogers of Cinergy will become President and CEO.  
14 All of the business and corporate units, except for DEGT and DEFS will report to  
15 Mr. Rogers. Mr. Fowler will lead the gas businesses. Mr. Fowler will report to  
16 Mr. Anderson for strategy and to Mr. Rogers for operations. Local headquarters  
17 of the operating utilities will remain unchanged by the merger.

18 Although the full details of the post-merger corporate organization have  
19 not been finalized, we anticipate at this time that the New Duke Energy will be  
20 the parent of Duke Power Company, LLC, Cinergy, Duke Capital, LLC and a  
21 Services Company. Duke Capital will continue to be the parent company of  
22 DEGT, DENA, DEI, Crescent Resources, DukeNet Communications and hold  
23 Duke Energy's interests in DEFS. Duke Power will become a North Carolina

1 limited liability company. An integration team will work out the details of the  
2 combined company's structure and their work may result in additional  
3 reorganizations.

4 **Q. PLEASE DESCRIBE DUKE ENERGY'S PHILOSOPHY REGARDING**  
5 **ISSUES OF CORPORATE GOVERNANCE.**

6 A. Duke Energy has a tradition of social responsibility stretching back to its founding  
7 over a century ago. Duke Power's founder, James Buchanan Duke, explicitly  
8 envisioned it as a vehicle for providing service to a struggling region of the  
9 country, and reinvesting the resulting earnings into charitable causes through the  
10 then-affiliated Duke Endowment. This tradition continues today as we strive to  
11 serve our customers, employees, investors, business partners and suppliers  
12 ethically and honestly. Duke Energy's Charter incorporates our business purpose,  
13 objectives, values and success measures. Our Charter provides that in conducting  
14 our business, we value:

- 15 • Stewardship,
- 16 • Integrity,
- 17 • Respect for the Individual,
- 18 • High Performance,
- 19 • Win-Win Relationships and
- 20 • Initiative.

21 Duke Energy's Code of Business Ethics is another core document of our  
22 company, outlining the policies and procedures we must all know and follow.  
23 The Code applies to all employees of Duke Energy, its subsidiaries and affiliates.

1 Duke Energy requires all employees to complete annual training on the Code and  
2 provides the EthicsLine, a worldwide reporting system through which employees  
3 can anonymously report suspected unethical or improper conduct or ask questions  
4 to resolve ethical dilemmas within the organization without fear of retribution.  
5 The Corporate Compliance Committee implements and supervises the compliance  
6 program throughout the company. Corporate responsibility falls on the shoulders  
7 of every employee, but it begins with strong governance and ultimate  
8 accountability at the highest level of management.

### **III. THE MERGER**

9 **Q. PLEASE EXPLAIN THE STRATEGIC OBJECTIVES THAT LED DUKE**  
10 **ENERGY TO PURSUE A MERGER WITH CINERGY.**

11 A. We entered into the Plan of Merger to build a stronger combined company. The  
12 merger will create a stronger platform for our regulated and unregulated  
13 businesses by increasing the scale and scope of both. Our increased size will  
14 position us to take advantage of further consolidation opportunities in both the  
15 utility and merchant energy business. After the combination, New Duke Energy's  
16 electric and gas businesses each would be large enough to stand alone - - giving  
17 us the flexibility to separate them in the future if we determine that such a move  
18 would create more value. However, any such separation would not include the  
19 separation of The Cincinnati Gas & Electric Company's ("CG&E") and  
20 ULH&P's utility gas business from its electric business.

21 The transaction will add value to New Duke Energy with higher earnings  
22 after the first full year of operation. The benefits will increase further in future



1 years through cost efficiencies. These efficiencies and management commitment  
2 to capture them assure that the combined company will be able to offer attractive  
3 energy prices to its retail customers, competitive prices and services in wholesale  
4 businesses and sustainable returns to attract the capital needed to assure reliability  
5 and expand.

6 Cinergy offered the best strategic fit of assets and skills to meet our  
7 strategic objectives. In addition, Cinergy's management is experienced, highly  
8 capable and shares a vision of the future of the energy business that is very similar  
9 to Duke Energy's.

10 **Q. DESCRIBE, GENERALLY, THE EFFECTS OF A MERGER BETWEEN**  
11 **DUKE ENERGY AND CINERGY.**

12 A. The combination of Duke Energy and Cinergy creates a larger, more stable  
13 company. The merger will also add diversity of service areas, climates, economic  
14 and competitive conditions to reduce risk to the regulated operations as a whole  
15 from exposure to local conditions. Once combined, New Duke Energy will  
16 operate one of the five largest electric businesses in the United States on a stand-  
17 alone basis, and combined with the gas operations will be one of the largest  
18 diversified utility and gas operations in North America.

19 As of close of the stock market on May 6, 2005, the New Duke Energy  
20 would have had market capitalization of \$36 billion, and as of December 31,  
21 2004, total assets of \$70.5 billion, revenues of \$27.2 billion and net income of  
22 \$1.9 billion. The merger will increase financial flexibility. In particular, the  
23 significant synergies created by the merger will lower the overall cost structure of

1 the combined company. These cost savings should permit lower future rates than  
2 would otherwise have been necessary on a stand-alone basis for either of the two  
3 companies. In summary, the combination of Duke Energy and Cinergy, and the  
4 synergies that result, will create a new, diversified financially strong company  
5 with increased financial flexibility, efficiencies, productivity and revenue, and  
6 lower costs.

7 **Q. DOES THE NEW DUKE ENERGY HAVE THE FINANCIAL,**  
8 **TECHNICAL AND MANAGERIAL ABILITY TO OWN AND OPERATE**  
9 **CINERGY'S UTILITY OPERATIONS?**

10 A. Absolutely. Duke Energy is a recognized leader in the energy business. As I  
11 discussed before, the post-merger New Duke Energy will be a larger, diversified,  
12 and financially stronger company. The significant synergies created by the  
13 merger include reduced costs resulting from the elimination of duplicative  
14 spending and overlapping functions, increased purchasing power, the avoidance  
15 of planned expenditures, and the consolidation of certain operations. The  
16 combination of these synergies translates into increased productivity and lower  
17 costs, which creates a financially strong organization.

18 While we have embraced a century of change in customer needs, new  
19 technologies and market opportunities, our focus on operational excellence,  
20 safety, environmental stewardship and customer and community service,  
21 wherever we do business, has not wavered. This commitment, which we know  
22 Cinergy shares, will continue to guide our merged company. Duke Power  
23 consistently raises the industry bar for efficiency and safety. Duke Power has

1           earned the Edison Award, the electric industry's most prestigious honor three  
2           times - - more than any other utility. By combining Duke Power's operational  
3           and management strength with the Cinergy utilities' similar strong leadership, the  
4           New Duke Energy will have diverse talent and experience to effectively operate  
5           the Cinergy utility operations.

6   **Q.   HOW WILL THE MERGER AFFECT THE LOCATION OF THE**  
7   **HEADQUARTERS OF CINERGY'S OPERATING COMPANIES?**

8   A.   As I mentioned previously, the merger will not affect the headquarters for the  
9           local utility operating companies. Each will remain in its current location.  
10          Cinergy's, ULH&P's and CG&E's headquarters will remain in Cincinnati, Ohio,  
11          while the corporate headquarters for PSI Energy, Inc. will remain in Plainfield,  
12          Indiana. We anticipate that many of the same employees will remain in their  
13          current locations, particularly those who work directly with customers. Some of  
14          the overlapping corporate functions may relocate to Charlotte, but ULH&P  
15          customers should have the same access to their local utility as they enjoy today.

16   **Q.   TO WHAT DEGREE ARE MERGER SAVINGS A RESULT OF THE**  
17   **ELIMINATION OF JOBS?**

18   A.   While some workforce reductions are anticipated in the long term, the total  
19          reduction is expected to be about 1,500 positions, or 5% of the combined  
20          workforces of Duke Energy and Cinergy. Many of the workforce reductions will  
21          likely result from retirements, attrition and other efforts designed to minimize  
22          impacts upon the employees of both companies.

1 **Q. WHERE, SPECIFICALLY, WITHIN THE CORPORATIONS DO YOU**  
2 **FORESEE REDUCTIONS IN FORCE?**

3 A. No decisions have been made about any specific areas to be consolidated, but  
4 reductions will likely be spread over corporate, shared services, utility back office  
5 and non-regulated merchant operations. In addition to any short-term job losses,  
6 new career and long-term employment opportunities will also be created by the  
7 strengthened New Duke Energy after the merger.

#### **IV. OPERATIONS**

##### **A. SYSTEM RELIABILITY**

8 **Q. WHAT PROGRAMS DOES DUKE ENERGY'S REGULATED ELECTRIC**  
9 **UTILITY, DUKE POWER, HAVE IN PLACE TO ENSURE SYSTEM**  
10 **RELIABILITY?**

11 A. First, Duke Power's diverse generating fleet continues to excel in reliability and  
12 efficiency. Our maintenance, planning and operational systems consistently allow  
13 Duke Power to run one of the most efficient and reliable generation systems in the  
14 United States.

15 Duke Power monitors the adequacy and reliability of its transmission  
16 system and its interconnections through analysis of internal transmission models  
17 and participation in regional reliability groups. Corrective actions are planned  
18 and implemented in advance to ensure continued cost-effective high quality  
19 electric service is provided. Duke Power's screening methods for its internal  
20 models comply with Southeastern Electric Reliability Council policy and North  
21 American Electric Reliability Council Planning Standards. Duke Power also

1 participates in a number of regional reliability groups for coordination of analysis  
2 of regional, sub-regional and inter-control area transfer capability and  
3 interconnection reliability.

4 **Q. COULD YOU DEMONSTRATE THE RESULTS OF SUCH PROGRAMS**  
5 **ON DUKE POWER'S SYSTEM RELIABILITY?**

6 A. In 2004, our Catawba Nuclear Station set a new company reliability record,  
7 operating for 531 continuous days, and was recognized by the Nuclear Regulatory  
8 Commission for safe operations. Also in 2004, Electric Light & Power magazine  
9 named our Marshall Steam Station the most efficient coal-fired station in the  
10 United States.

11 In each of the five years 2000 through 2004, the TQS Key Accounts  
12 National Benchmark study, a nationally-recognized customer satisfaction study of  
13 large industrial and institutional customers, rated Duke Power among the top 10  
14 utilities in the country in customer satisfaction with Power Quality and Power  
15 Reliability. In each of these five years, at least 80% of Duke Power's Key  
16 Accounts indicated they were highly satisfied with the performance in these  
17 categories. In the 2005 SGS Transmission Reliability Benchmarking Study, for  
18 the five years 2000 through 2004, Duke Power's transmission system ranked in  
19 the first quartile nationally for average line outage frequency in the bulk power  
20 (230-500kV) and load serving (23-161kV) voltage classes.

21 These recognitions for reliable operation of our generation, transmission  
22 and distribution systems are important measures of Duke Power's reliability.

1 **Q. WHAT MORE IS DUKE POWER DOING TO MAINTAIN AND, WHEN**  
2 **POSSIBLE, IMPROVE UPON THAT RECORD?**

3 A. We operate one of the most diverse, efficient and reliable generating systems in  
4 the United States, but we are always working internally and externally through  
5 industry benchmarking groups and other organizations to improve upon our  
6 generation record. We also continually monitor and analyze our transmission and  
7 distribution systems to determine where new investments, technological  
8 advancements and operational efficiencies can be employed to improve our  
9 system reliability. Duke Power's internal analyses, participation in industry  
10 reliability councils, and process for managing transmission system projects  
11 contribute to continued system security and reliable operation.

12 **Q. PLEASE DISCUSS THE RELIABILITY HISTORY OF UNION GAS,**  
13 **DUKE ENERGY'S LOCAL DISTRIBUTION COMPANY IN ONTARIO,**  
14 **CANADA.**

15 A. Union Gas is Canada's second largest natural gas utility and distributes natural  
16 gas to some 1.2 million residential, commercial and industrial customers in  
17 Ontario. Union Gas has historically maintained a high level of reliability  
18 performance. Pertinent legislative requirements are targeted for 100%  
19 compliance and a set of performance measures is used to periodically measure  
20 and monitor performance levels in all related areas, including corrosion surveys,  
21 leakage surveys, leak repairs, fault repairs, conducting all related inspections in a  
22 timely fashion, and proactively performing maintenance activities. The company  
23 also participates in benchmarking studies to compare its reliability performance

1 results with the rest of the North American gas industry. For example, in 2004  
2 and 2005, system reliability benchmark studies conducted by the American Gas  
3 Association (“AGA”) confirmed the high reliability performance standing of  
4 Union Gas, with top quartile rankings in emergency response and employee  
5 safety.

6 **Q. WILL THE MERGER AFFECT CINERGY’S SYSTEM RELIABILITY,  
7 AND IF SO, IN WHAT WAYS?**

8 A. We expect Cinergy’s strong history of system reliability to continue. As a result  
9 of the merger, the Cinergy Operating Companies becoming part of the new Duke  
10 Energy will have greater resources and even greater depth of experience to  
11 continue the strong system reliability expected by customers of Duke Power,  
12 CG&E, PSI, ULH&P and Union Gas. This merger will allow the New Duke  
13 Energy utility operating companies to develop “best practices” drawing on the  
14 experience of the former Cinergy operating companies, Duke Power and Union  
15 Gas. Further, the broader employee base located in a larger geographic area will  
16 provide all retail customers access to greater resources in the event of severe  
17 weather or other uncontrollable outages or emergencies.

18 **Q. WHAT IMPACT WILL THE MERGER HAVE ON THE CINERGY  
19 OPERATING COMPANIES’ PARTICIPATION IN THE MIDWEST  
20 INDEPENDENT TRANSMISSION SYSTEM OPERATOR, INC.  
21 (“MIDWEST ISO”)?**

22 A. None. Duke Energy believes that regional solutions to transmission issues are  
23 preferable, and that the Cinergy operating companies’ decision to participate in

1 Midwest ISO is appropriate for the environments in their states of operation.  
2 Duke Power has also recently filed a plan with FERC to establish an Independent  
3 Entity and an Independent Monitor to provide additional transparency to the  
4 system's administration. Duke Power has retained Midwest ISO to perform the  
5 role of Independent Entity. While Duke Power is not joining Midwest ISO, we  
6 expect that Midwest ISO will assume responsibility for a number of core  
7 transmission functions.

**B. CUSTOMER SERVICE**

8 **Q. CAN YOU PROVIDE SPECIFIC EXAMPLES IN WHICH DUKE POWER**  
9 **HAS BEEN RECOGNIZED FOR EXEMPLARY CUSTOMER SERVICE?**

10 A. Yes. Duke Power is committed to providing superior value to our customers and  
11 has received numerous awards and honors for its customer service. Some of our  
12 most recent awards include the following: In J.D. Power and Associates' 2005  
13 Business Customer Satisfaction Index, Duke Power ranked No. 4 out of 53  
14 participating utilities across the country and second out of all southern region  
15 utilities. In J.D. Power and Associates' 2005 Residential Customer Satisfaction  
16 Index, Duke Power ranked 1<sup>st</sup> out of all southern region utilities, and 8<sup>th</sup> out of 78  
17 utilities nationally. In the 2005 Key Account National Benchmark Survey –  
18 Overall Satisfaction conducted by TQS Research, Inc., Duke Power ranked 3<sup>rd</sup>  
19 nationally. In 2005, J.D. Power and Associates certified Duke Power's customer  
20 call center for call service excellence, joining Cinergy as the only two energy  
21 company call centers to receive this designation. Duke Power also received the  
22 2004 Customer Service Project of the Year Award from Electric Light and Power



1 magazine and Chartwell, Inc. for enhancements we made to our automated phone  
2 systems, by using customer focus groups and adding an automated line for  
3 Spanish-speaking customers.

4 **Q. CAN YOU PROVIDE EXAMPLES OF UNION GAS' PROGRAMS AND**  
5 **RECOGNITION FOR CUSTOMER SERVICE?**

6 A. Yes. Union Gas defines its success by delivering a high level of customer service  
7 expressed in key service quality metrics. Union Gas uses the "balanced  
8 scorecard" approach to measure, improve and maintain a high level of customer  
9 service at optimum costs. Each year, a customer service quality matrix along with  
10 corresponding improvement performance targets is developed. The company also  
11 participates in benchmarking studies on an on-going basis, including the annual  
12 AGA benchmarking study to compare its customer service and productivity  
13 performance with rest of the North American gas industry. In the 2005 AGA  
14 benchmarking study of 85 gas and/or electric companies, Union Gas ranked as a  
15 top quartile performing company with regard to several service quality indicators  
16 including answer time, dispatch time, travel time, total response time and  
17 percentage of emergency responses within a specified length of time. In addition,  
18 Union Gas was recognized in 2004 as an Accredited Meter Verifier by  
19 Measurement Canada, the regulatory body for Canada that sets the rules of the  
20 marketplace with respect to trade measurement and ensures that the rules are  
21 uniformly implemented. This accreditation recognizes Union Gas' commitment  
22 to quality processes, accurate measurement and customer satisfaction.

1 **Q. HOW WILL THE MERGER IMPACT UPON CINERGY'S OPERATING**  
2 **UTILITIES' CUSTOMER SERVICE?**

3 A. We certainly expect that Cinergy's customers will continue to receive the level of  
4 customer service they have come to expect. The local headquarters for each  
5 utility will remain unchanged by the merger and customers will still have the local  
6 presence of, and access to, their electric and/or gas utility. And by the sharing of  
7 best practices among the separate companies, coming together, we expect to  
8 improve our provision of customer service both within the existing Duke Power  
9 franchised area as well as within the existing Cinergy operating companies'  
10 service territories.

**V. ECONOMIC DEVELOPMENT**

11 **Q. PLEASE COMMENT UPON DUKE POWER'S COMMITMENT TO**  
12 **ECONOMIC DEVELOPMENT WITHIN AREAS IN WHICH IT**  
13 **PROVIDES SERVICE.**

14 A. Duke Power is committed to economic development and has played a proud role  
15 in the development of North Carolina and South Carolina over the past century.  
16 The vision of Duke Power's founder, James Buchanan Duke, was one of  
17 economic development, spurred by an electric system that would power textile  
18 mills and transform the agrarian economy by driving the economic growth of the  
19 Piedmont region of the Carolinas.

20 Today, the presence of Duke Power's 10,000 employees in the  
21 communities we serve provides the foundation for our economic development  
22 strategy. We are responding to the changes in the automation of manufacturing

1 and the churn of the global economy. We are finding opportunities to recalibrate  
2 our economic development approach; to revamp funding and recruitment policies;  
3 to forge new alliances; and to advance technology and innovation. While the  
4 economic landscape has changed significantly over the past century, Duke  
5 Power's vision has not.

6 Since 1996, one of North Carolina's chief economic development  
7 incentive tools has been the industry tax credits established by the William S. Lee  
8 Act, named for Duke Power's former CEO and Chairman. This tribute  
9 acknowledges Bill Lee and Duke Power's prominent commitment to economic  
10 development.

11 Duke Power has many current economic development initiatives. Let me  
12 list a few. In 2004, Duke Power announced a profit-sharing approach that shares  
13 profits from its short-term, interruptible wholesale sales at market-based rates in  
14 the Carolinas. In North Carolina, these profits are contributed to public assistance  
15 heating and cooling programs, to provide worker retraining through Duke  
16 Power's Community and Technical College Fund and to reduce industrial  
17 customers' rates. In South Carolina, Duke Power established AdvanceSC, a  
18 limited liability company with an independent board of directors, to disburse these  
19 profits through grants for public assistance heating and cooling programs,  
20 education programs for economic development, economic development funding  
21 and manufacturing competitiveness funding.

22 Since 1994, Duke Power has offered innovative economic development  
23 rates to encourage businesses to locate or expand operations in North Carolina

1 and South Carolina. When our region's manufacturing base began to decline,  
2 particularly in the textile and furniture industries, Duke Power responded in 2002  
3 by offering economic redevelopment rates to promote use of unoccupied,  
4 industrial facilities.

5 Another recent example of Duke Power's commitment to economic  
6 development is our collaboration with the departments of commerce from both  
7 Carolinas to build a world-class GIS-based website that will give site selection  
8 consultants, industrial companies and economic developers convenient access to  
9 comprehensive information about industrial properties, local communities,  
10 workforce and infrastructure in the Carolinas.

11 Duke Power will continue to grow our partnerships with local, regional  
12 and statewide government economic development organizations, the private  
13 sector and academic circles to influence economic development policy and benefit  
14 the communities we serve. In addition, we believe that the combination of our  
15 competitive rates and record of superior reliability give us a strategic advantage  
16 and valuable economic development tool.

17 **Q. WILL THE MERGER AFFECT DUKE ENERGY'S COMMITMENT TO**  
18 **ECONOMIC DEVELOPMENT IN ANY WAY, AND IF SO, HOW?**

19 A. Duke Energy is a leader and key partner in the communities where we work and  
20 serve, as is Cinergy. The merger will not change this imperative.

21 **Q. WHAT DO YOU ANTICIPATE THE MERGER BETWEEN DUKE**  
22 **ENERGY AND CINERGY TO MEAN IN TERMS OF ECONOMIC**  
23 **DEVELOPMENT INITIATIVES WITHIN THE STATE OF KENTUCKY?**

1 A. We expect to maintain the commitment to economic development initiatives  
2 within Kentucky. As I discussed before, Duke Power has increased its  
3 commitment to economic development over the years and has seen great results  
4 with new industry locating in our service areas and existing customers expanding  
5 their operations. The economic development leadership and experience of Duke  
6 Power, CG&E, PSI, ULH&P and Union Gas combined with more competitive  
7 rates than otherwise would have been possible absent the cost savings from the  
8 merger should enable additional economic development opportunities in the areas  
9 served by New Duke Energy.

## VI. CORPORATE CITIZENSHIP / RESPONSIBILITY

### A. CHARITABLE WORKS

10 **Q. PLEASE BRIEFLY DESCRIBE DUKE'S CHARITABLE ACTIVITIES**  
11 **OVER THE PAST THREE YEARS.**

12 A. As I have discussed previously, Duke Energy is committed to the communities  
13 where we live and conduct business. Our financial contributions to selected  
14 charitable organizations are at the core of our commitment. The Duke Energy  
15 Foundation is a non-profit organization funded by shareholders and provides  
16 funding where our company sees the greatest need, within three focus areas:  
17 educational attainment, community vitality and competitive workforce. In 2004,  
18 the total Foundation giving was \$13.5 million. The Foundation funds two types  
19 of volunteer grants to employees and retiree chapters to encourage volunteerism.  
20 The Community Improvement Grant provides up to \$1,000 to purchase supplies  
21 and materials for the performance of a specific, one-time, hands-on project. A

1 Leadership Grant of \$1,000 is paid to a charitable organization on behalf of an  
2 eligible Duke Energy employee or retiree for outstanding volunteer efforts and  
3 dedication to service.

4 Duke Energy employees also give to and serve our communities. In 2004,  
5 Duke Energy employees, retirees and the Duke Energy Foundation pledged \$5.5  
6 million to 380 United Way organizations in the United States and Canada. Since  
7 1998, Duke Energy has sponsored our Global Service Event to encourage and  
8 highlight employee and retiree volunteerism. In 2004, the Global Service Event  
9 was lengthened from the traditional 30 days to 100 days to celebrate our 100<sup>th</sup>  
10 anniversary. The results were monumental: more than 9,000 employees gave  
11 over 27,000 volunteer hours to volunteer projects and charitable organizations.  
12 The Duke Energy Foundation also awarded \$145,000 in volunteer grants to  
13 charitable organizations selected by employees and retirees as part of the Global  
14 Service Event.

15 **Q. HOW WILL THE MERGER AFFECT DUKE AND CENERGY'S**  
16 **CHARITABLE ACTIVITIES?**

17 A. Duke Energy and Cinergy have similar corporate philosophies regarding  
18 involvement in our communities and charitable giving. The merger will not  
19 diminish the combined company's leadership role. We fully expect the tradition  
20 of charitable giving and civic leadership to continue in all communities where  
21 Duke Energy conducts business.

**B. ENVIRONMENTAL**

22 **Q. PLEASE DESCRIBE THE ENVIRONMENTAL ISSUES YOU BELIEVE**

1           **ARE OF MAJOR IMPORT TO DUKE ENERGY, AND ALSO EXPLAIN**  
2           **HOW DUKE ENERGY IS ADDRESSING THOSE ISSUES.**

3    A.    The scope, scale and diversity of its operations involve Duke Energy in most  
4           environmental issues.  However, global climate change is one of the pressing  
5           issues of our time.  Concern that greenhouse gases from human activities may be  
6           influencing changes in the earth’s climate system has resulted in a variety of local,  
7           state and regional responses, as well as increased policy debate at the national  
8           level.  Duke Energy shares this concern.

9                    We endorse a transition to a lower-carbon-intensive economy, promoting a  
10                   federal economy-wide approach – such as through a carbon tax – and are taking a  
11                   leadership role to engage stakeholders and craft a national policy consistent with  
12                   our principles.  This commitment is indicative of the integral part environment,  
13                   health and safety considerations play in all of our decisions.

14                   Duke Power was one of the first utilities in the nation to launch an  
15                   environmental and water quality department in 1923, and stewardship of the  
16                   environment remains one of Duke Energy’s guiding principles.  Duke Energy has  
17                   long been known for its efficient power plant operations and diverse fuel mix.

18                   Duke Energy strongly supported North Carolina’s 2002 clean air  
19                   legislation, which is becoming a model for other states pursuing stricter emissions  
20                   standards.  In compliance with that plan and the federal Clean Air Act, Duke  
21                   Power is investing approximately \$1.5 billion over the next several years to  
22                   reduce emissions at its coal-fired plants.  In addition, Duke Power has invested  
23                   \$653 million to comply with the Environmental Protection Agency’s NO<sub>x</sub> SIP

1 (State Implementation Plan) Call rule. Compared to 2000 levels, Duke Power  
2 will reduce its annual NO<sub>x</sub> emissions 66% by 2009, and annual SO<sub>2</sub> emissions  
3 65% by 2013.

4 New Duke Energy will be proactive in shaping climate change policy and  
5 continue to strive to contribute to the well-being of our communities and  
6 environment.

7 **Q. IN WHAT WAYS HAS DUKE ENERGY BEEN RECOGNIZED FOR ITS**  
8 **ENVIRONMENTAL STEWARDSHIP AND SAFETY FOCUS?**

9 A. We work closely with agencies and local groups to preserve cultural and natural  
10 resources, whether building new plants, pipelines or electric wires, managing real  
11 estate or siting telecommunications facilities. We support programs that promote  
12 environmental education and also foster a culture in which every employee at  
13 every level accepts responsibility and accountability for working safely. As a  
14 result, we have been recognized by these partners and other organizations over the  
15 years for our efforts. Some of the recent highlights include: 2005 Safety  
16 Achievement Award – American Gas Association (the fifth time that DEGT has  
17 earned AGA’s top safety award); 2005 Corporate Stewardship Award – South  
18 Carolina Department of Archives and History (for Crescent Resources’  
19 accomplishments in archaeology and historic preservation); 2005 Environmental  
20 Achievement Award – City of Calgary (for partnering with the Calgary Board of  
21 Education and the City of Calgary Parks to launch the Duke Energy Urban  
22 Ecology Program); 2004 Coastal America Partnership Award- Coastal America  
23 (for DEGT’s work to restore marshlands and construct trail system around the



1 historic San Jacinto battleground near Houston); 2004 Safety Awards for Pipeline  
2 Operations – Canadian Energy Pipeline Association (for DEGT’s lowest industry  
3 recordable injury rate in 2003); 2004 Eloy Chaves Medal – Association of  
4 Brazilian Concessionaires of Electrical Energy (DEI Brazil is the first company to  
5 receive this safety award for three consecutive years); and 2003 Outstanding  
6 Stewardship of America’s Rivers – National Hydropower Association (for Duke  
7 Energy’s work to protect trout streams and tributaries in North and South  
8 Carolina).

**VII. CONCLUSION**

9 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

10 A. The New Duke Energy will have the technological, managerial, and financial  
11 ability to own and operate ULH&P. Cinergy and Duke Energy share common  
12 values and commitments to corporate governance, reliability and safety, customer  
13 service, economic development, charitable activities, and environmental  
14 stewardship. This merger will result in a larger, stronger company with the same  
15 core values that have served Duke Energy and Cinergy well. We expect all of our  
16 stakeholders to benefit from the merger, and we are committed to making it a  
17 success.

18 **Q. WERE ATTACHMENTS RJO-1 AND RJO-2 PREPARED BY YOU OR**  
19 **UNDER YOUR SUPERVISION?**

20 A. Yes, they were.

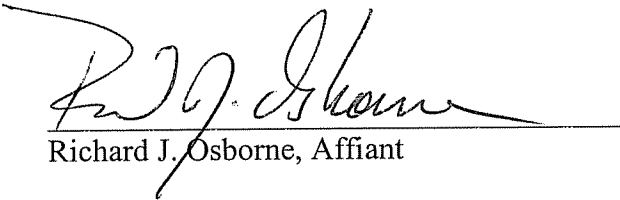
21 **Q. DOES THIS CONCLUDE YOUR PREPARED DIRECT TESTIMONY?**

22 A. Yes.

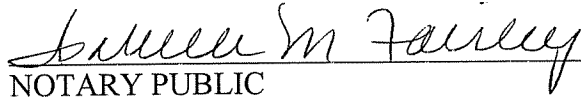
**VERIFICATION**

State of North Carolina    )  
  )  
County of Mecklenburg    )        **SS:**

The undersigned, Richard J. Osborne, being duly sworn, deposes and says that he is Group Vice President, Public and Regulatory Policy, for Duke Energy Corporation, and that the matters set forth in the foregoing testimony are true and correct to the best of his information, knowledge and belief.

  
Richard J. Osborne, Affiant

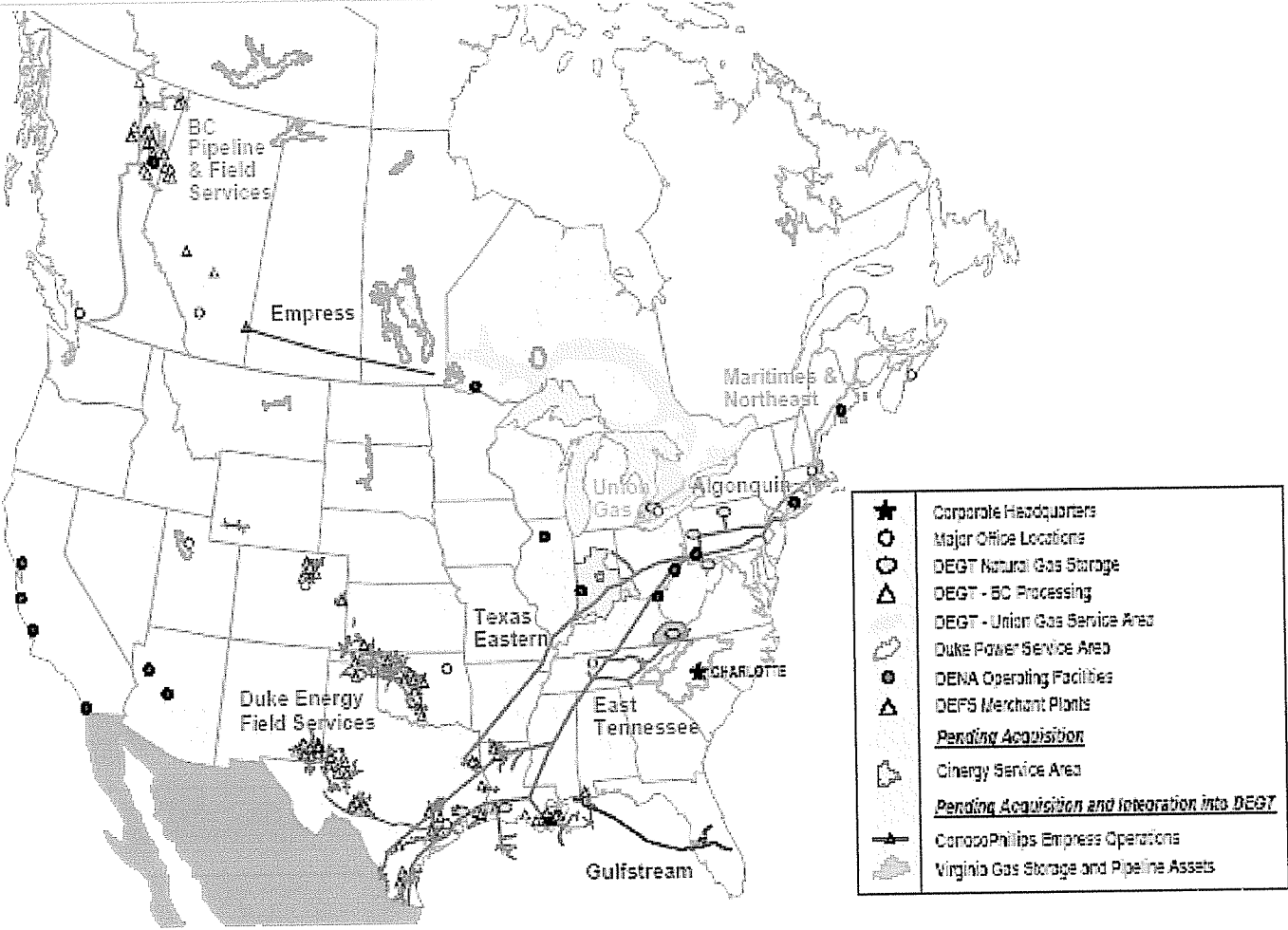
Subscribed and sworn to before me by Richard J. Osborne on this 15<sup>th</sup>  
day of July, 2005.

  
NOTARY PUBLIC

My Commission Expires: 4/13/08



# Duke Energy's North American Assets



## Duke Power Generating Stations

Plant	Location	MW	Fuel type	Yr. commercial
<b>FOSSIL</b>				
Allen Steam Station	Belmont, NC	1145 MW	Low sulfur coal	Units 1,2 – 1957 U3 – 1959 U4 – 1960 U5 - 1961
Belews Creek	Belews Creek, NC	2270 MW	Low sulfur coal	U1 – 1974 U2 - 1975
Buck	Spencer, NC	369 MW	Low sulfur coal	U3 – 1941 U4 - 1942 U5/6 - 1953
Cliffside	Cliffside, NC	760 MW	Low sulfur coal	U1,2 – 1940 U3,4 - 1948 U5 - 1972
Dan River	Eden, NC	276 MW	Low sulfur coal	U1 – 1949 U2 – 1950 U3 - 1955
Lee	Williamston, SC	370 MW	Low sulfur coal	U1,2 – 1951 U3 - 1958
Marshall	Terrell, NC	2110 MW	Low sulfur coal	U1 – 1965 U2 – 1966 U3 – 1969 U4 - 1970
Riverbend	Mt. Holly, NC	454 MW	Low sulfur coal	U1,2 – 1952 U3,4 - 1954
<b>COMBUSTION TURBINE</b>				
Lincoln	Lowesville, NC	1267.2 MW	Fuel oil/gas	1995
Mill Creek	Cherokee Co. , SC	595.4 MW	Fuel oil/gas	2003
<b>HYDRO</b>				
Bad Creek	Salem, SC	1360 MW (pumped storage)	Water	1991
Bear Creek	Tuckasegee, NC	9.45 MW	Water	1954
Bridgewater	Morganton, NC	23 MW	Water	1919
Bryson	Swain county, NC	.98 MW	Water	1925

Buzzard Roost (leased – expires in 2006)	Chapells, SC	7 MW	Water	1940
<b>Plant</b>	<b>Location</b>	<b>MW</b>	<b>Fuel type</b>	<b>Yr. commercial</b>
Cedar Cliff	Tuckasegee, NC	6.375 MW	Water	1952
Cedar Creek	Great Falls, NC	43 MW	Water	1926
Cowans Ford	Stanley, NC	325 MW	Water	1963
Dearborn	Great Falls, SC	42 MW	Water	1923
Dillsboro	Dillsboro, NC	.22 MW	Water	1958
Fishing Creek	Great Falls, SC	49 MW	Water	1916
Franklin	Franklin, NC	1.04 MW	Water	1925
Gaston Shoals	Blacksburg, SC	4.62 MW	Water	1908
Great Falls	Great Falls, SC	24 MW	Water	1907
Jocassee	Pickens Co. SC	680 MW (pumped storage)	Water	1973
Keowee	Pickens Co, SC	152 MW	Water	1971
Lookout Shoals	Iredell Co., NC	28 MW	Water	1915
Mission	Clay Co., NC	1.8 MW	Water	1924
Mountain Island	Mt. Holly, NC	58 MW	Water	1923
Nantahala	Macon Co., NC	50 MW	Water	1942
99 Islands	Cherokee Co., NC	9.55 MW	Water	1910
Oxford	Conover, NC	40 MW	Water	1928
Queens Creek	Swain Co., NC	1.44 MW	Water	1949
Rhodhiss	Rhodhiss, NC	30 MW	Water	1925
Rocky Creek	Fairfield Co., NC	27 MW	Water	1909
Tennessee Creek	Jackson Co., NC	9.8 MW	Water	1955
Thorpe	Jackson Co, NC	19.7 MW	Water	1941
Tuckasegee	Tuckasegee, NC	2.5 MW	Water	1950
Tuxedo	Saluda, NC	6.4 MW	Water	1920
Wateree	Ridgeway, SC	85 MW	Water	1919
Wylie	York Co., SC	72 MW	Water	1904 – rebuilt in 1925
<b>NUCLEAR</b>				
Catawba	York, SC	2258 MW	Uranium	U1 – 1985 U2 – 1986
McGuire	Huntersville, NC	2200 MW	Uranium	U1 – 1981 U2 – 1984
Oconee	Seneca, SC	2538 MW	Uranium	U1 – 1973 U2/U3 – 1974



**COMMONWEALTH OF KENTUCKY**  
**BEFORE THE PUBLIC SERVICE COMMISSION**

In the Matter of:

Joint Application of Duke Energy Corporation, )  
Duke Energy Holding Corp., Deer Acquisition )  
Corp., Cougar Acquisition Corp., Cinergy Corp., )  
The Cincinnati Gas & Electric Company, and )  
The Union Light, Heat and Power Company for )  
Approval of a Transfer and Acquisition )  
of Control )

Case No. 2005-00228

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**DIRECT TESTIMONY OF**

**THOMAS J. FLAHERTY**

**ON BEHALF OF**

**JOINT APPLICANTS**

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## **APPENDIX**

ATTACHMENT TJF-1 – Summary of Regulated Utility Experience

ATTACHMENT TJF-2 – Overall Cost Savings

ATTACHMENT TJF-3 – Costs to Achieve Elements



## **I. INTRODUCTION AND QUALIFICATIONS**

1 **Q. PLEASE STATE YOUR NAME AND BY WHOM YOU ARE EMPLOYED.**

2 A. My name is Thomas J. Flaherty, and I am a Senior Vice President in the Energy and  
3 Utilities practice of Booz Allen Hamilton. My business address is 901 Main St., Suite  
4 6500, Dallas, Texas 75202.

5 **Q. WOULD YOU BRIEFLY SUMMARIZE YOUR ACADEMIC AND**  
6 **PROFESSIONAL BACKGROUND?**

7 A. I graduated from the University of Oklahoma with a B.B.A. degree in Accounting and  
8 immediately joined Touche Ross & Co., where I began my career as a management  
9 consultant. Subsequently, I worked for Deloitte & Touche (formed by the merger of  
10 Touche Ross and Deloitte, Haskins & Sells in 1989) for more than 30 years until  
11 joining Booz Allen Hamilton ("Booz Allen") as a Senior Vice President. Over the  
12 course of my consulting career, I have specialized in the public utility industry and  
13 have performed a variety of assignments.

14 I have assisted managements from a number of electric and/or gas utilities in  
15 the identification, evaluation and integration of acquisitions, including: screening  
16 analysis; review of corporate restructuring alternatives; assessment of merger-related  
17 cost reduction opportunities; development of regulatory strategies; planning and  
18 execution of merger integration; and, assignment and allocation of costs and benefits  
19 related to mergers and acquisitions. In addition to my involvement in merger and  
20 acquisition consulting, I have participated in numerous other utility consulting

1 engagements in the areas of corporate growth, diversification, restructuring,  
2 organizational analysis, business process reengineering, benchmarking, strategic  
3 planning, strategic marketing, litigation assistance, economic feasibility studies,  
4 regulatory planning and analysis, and financial analysis.

5 I also have conducted or directed similar assignments for a variety of  
6 industries, including construction, retailing, publishing, health care, real estate and  
7 manufacturing, in addition to utilities. Attachment TJF-1 to this testimony details my  
8 previous experience with regulated utilities.

9 **Q. PLEASE SUMMARIZE YOUR EXPERIENCE IN UTILITY MERGERS AND**  
10 **ACQUISITIONS.**

11 A. I have evaluated more than 300 actual, proposed or potential transactions involving  
12 electric, electric and gas combination, gas, or water utilities. I have experience  
13 working for both buyers and sellers and have assisted client managements in their  
14 assessment of a broad range of transactional issues, including the following:

- 15 • Target analysis
- 16 • Asset quality analysis
- 17 • Customer analysis
- 18 • Competitor analysis
- 19 • Synergy assessment
- Financial analysis
- Transaction structuring
- Regulatory strategy
- Testimony
- Integration planning

20 The publicly announced transactions in which I have been significantly  
21 involved, other than the one that is the subject of this proceeding are: Kansas  
22 Power & Light and Kansas Gas and Electric, IPALCO Enterprises and PSI Resources,  
23 Entergy and Gulf States Utilities, Southern Union and Western Resources (Missouri

1 properties), Washington Water Power and Sierra Pacific Resources, Midwest  
2 Resources and Iowa-Illinois Gas & Electric, Northern States Power Company and  
3 Wisconsin Energy Corporation, PECO Energy Company and PPL Resources, Public  
4 Service Company of Colorado and Southwestern Public Service Company, Baltimore  
5 Gas & Electric and Potomac Electric Power Company, Delmarva Power and Atlantic  
6 Energy, WPL Holdings, IES Industries and Interstate Power, Puget Sound Power &  
7 Light and Washington Energy, TU Electric and ENSERCH, Western Resources and  
8 Kansas City Power & Light, Western Resources and ONEOK, Inc. (Kansas,  
9 Oklahoma gas properties), Houston Industries and NORAM Energy, Ohio Edison and  
10 Centerior, ENOVA and Pacific Enterprises, Brooklyn Union Gas and Long Island  
11 Lighting, Allegheny Energy and DQE, Inc., LG&E Energy and KU Energy, NIPSCO  
12 Industries and Bay State Gas, American Electric Power and CSW, BEC Energy and  
13 COM Energy, Northern States Power and New Century Energies, Dynegy and  
14 Illinova, DTE Energy and MCN Energy, ConEdison and Northeast Utilities, PECO  
15 Energy and Unicom, AGL Resources and Virginia Natural Gas, Energy East and  
16 RGE Energy, FPL Group and Entergy, PNM Resources and TNM Enterprises, and  
17 Exelon and PSEG Enterprises.

18 **Q. DO YOU HOLD ANY PROFESSIONAL CERTIFICATIONS?**

19 A. Yes. I am a Certified Management Consultant and a member of the Institute of  
20 Management Consultants.

## **II. PURPOSE OF TESTIMONY**

21 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

1 A. I have been asked to appear for Joint Applicants, Cinergy Corp. (“Cinergy”), The  
2 Cincinnati Gas & Electric Company, The Union Light Heat & Power Company,  
3 Cougar Acquisition Corp., Deer Acquisition Corp., Duke Energy Holding Corp., and  
4 Duke Energy Corporation (“Duke Energy”) to sponsor the costs and benefit analysis  
5 identifying the merger-related synergies from the announced combination of Duke  
6 Energy and Cinergy (“the Companies”). Booz Allen assisted the managements of  
7 both Companies in the identification and quantification of potential cost savings  
8 resulting from the proposed merger of the companies.

9 In this testimony I: (1) describe the categories of merger-related cost savings  
10 that are believed available from the merger of the Companies; (2) provide the basis  
11 for quantification of estimated merger-related cost savings; (3) explain the basis for  
12 and importance of costs-to-achieve on the identified savings; (4) describe the process  
13 by which such identified cost savings categories and estimated merger-related cost  
14 savings were derived by the Companies, and; (5) compare the level of merger-related  
15 cost savings identified in this merger with other transactions with which I am familiar.

16 **Q. HAVE YOU INCLUDED ANY ATTACHMENTS TO YOUR TESTIMONY?**

17 A. Yes. Attachment TJF-1 is a summary of my experience with regulated utilities, while  
18 Attachment TJF-2 provides a five-year summary of potential merger cost savings, and  
19 Attachment TJF-3 provides a detailed breakout of costs that may be incurred to  
20 achieve the identified merger.

### **III. SUMMARY OF TESTIMONY**

21 **Q. PLEASE SUMMARIZE YOUR TESTIMONY.**

1 A. The combination of the Companies enables the realization of substantial benefits in  
2 the form of economies, efficiencies and operating effectiveness across the corporate,  
3 shared services, regulated and, certain non-regulated operating areas. These synergies  
4 relate to a variety of operational functions and will result in benefits that will accrue  
5 to customers now, and in the future. These savings are directly attributable to the  
6 merger and would not occur in its absence.

7 The combination of the Companies is expected to provide the potential for  
8 approximately \$2.1 billion in total gross cost savings to be realized across the  
9 corporate, shared services, regulated and, non-regulated businesses over the first five  
10 years following the close of the merger. This total includes approximately \$780  
11 million in gross cost savings that are directly attributable to the non-regulated  
12 business segment, specifically the trading and marketing and competitive generation  
13 businesses.

14 In addition, approximately \$770 million in total corporate, shared services,  
15 regulated and, non-regulated costs-to-achieve and other offsets to the identified  
16 savings have been estimated associated with the closing of the transaction or the  
17 realization of the savings, of which approximately \$61 million relates to the non-  
18 regulated segment. These non-regulated cost savings and costs-to-achieve are  
19 excluded from further discussion in my testimony as they do not relate to any aspect  
20 of the regulated business. The total level of identified cost savings and costs-to-  
21 achieve are illustrated in Table 1.

22 Beyond these non-regulated business savings and related costs, approximately  
23 \$183 million in costs-to-achieve associated with corporate or regulated business

1 change-in-control costs have been removed from consideration for the purposes of  
2 this proceeding. These costs-to-achieve elements are not being considered in the  
3 determination of the net savings attributable to the regulated business and are not  
4 being requested for recognition and recovery against the identified cost savings. In  
5 effect, the Companies are increasing the level of cost savings available for the benefit  
6 of customers.

7 With respect to the regulated business segment, the managements of the  
8 Companies have identified approximately \$1.3 billion of corporate, shared services  
9 and utility-related gross cost savings over the first five years following the close of the  
10 transaction. In addition, approximately \$513 million of out-of-pocket costs-to-  
11 achieve these savings and \$10 million of cost cutting measures planned or initiated by  
12 Cinergy prior to the merger (pre-merger initiatives) have also been identified. These  
13 amounts are before any allocations between the regulated and non-regulated business  
14 segments and net to approximately \$807 million which is expected to benefit all  
15 stakeholders, including customers and shareholders, and result in a stronger, more  
16 competitive company. These savings will also be achieved without any adverse  
17 impacts to service quality, reliability or safety as the areas identified do not relate to  
18 direct operating areas. The net \$807 million in corporate and regulated cost savings is  
19 more definitively shown in Attachment TJF-2.

**TABLE 1: Total Savings**  
**(\$ in thousands)**

Five Year Total Potential Savings Summary

Potential Areas (\$ in 000s)

	Year 1	Year 2	Year 3	Year 4	Year 5	Five-year Total
<b>Regulated and Corporate:</b>						
Staffing Savings	\$59,415	\$96,154	\$110,311	\$116,904	\$123,788	\$506,572
Corporate & Administrative Programs Savings	\$60,594	\$73,506	\$77,979	\$81,269	\$84,730	\$378,077
Information Technology Savings	\$16,011	\$28,889	\$44,084	\$58,937	\$72,396	\$220,318
Supply Chain Savings	\$26,888	\$31,824	\$36,875	\$42,043	\$47,330	\$184,960
Fuel Savings	\$6,992	\$7,642	\$8,296	\$8,489	\$8,686	\$40,106
<b>Total Gross Corp/Regulated Savings</b>	<b>\$169,901</b>	<b>\$238,016</b>	<b>\$277,546</b>	<b>\$307,642</b>	<b>\$336,929</b>	<b>\$1,330,034</b>
Corp/Regulated Costs-to-Achieve	(\$260,660)	(\$124,229)	(\$58,328)	(\$34,723)	(\$34,744)	(\$512,684)
Corp/Regulated Pre-Merger Initiatives	(\$1,912)	(\$1,956)	(\$2,002)	(\$2,048)	(\$2,096)	(\$10,014)
<b>Net Corporate and Regulated Savings</b>	<b>(\$92,671)</b>	<b>\$111,830</b>	<b>\$217,216</b>	<b>\$270,871</b>	<b>\$300,089</b>	<b>\$807,335</b>
Corporate costs excluded from consideration	(\$183,308)					(\$183,308)
<b>Non-Regulated:</b>						
Non-Regulated Savings	\$127,942	\$154,014	\$159,879	\$165,976	\$172,313	\$780,123
Non-Regulated Costs-to-Achieve	(\$48,570)	(\$12,690)	\$0	\$0	\$0	(\$61,260)
<b>Net Non-Regulated Savings</b>	<b>\$79,372</b>	<b>\$141,324</b>	<b>\$159,879</b>	<b>\$165,976</b>	<b>\$172,313</b>	<b>\$718,863</b>
<b>SUMMARY</b>						
<b>Total Gross Savings</b>	<b>\$297,842</b>	<b>\$392,030</b>	<b>\$437,425</b>	<b>\$473,618</b>	<b>\$509,242</b>	<b>\$2,110,157</b>
<b>Total Costs-to-Achieve / Pre-Merger Initiative</b>	<b>(\$494,450)</b>	<b>(\$138,876)</b>	<b>(\$60,330)</b>	<b>(\$36,772)</b>	<b>(\$36,840)</b>	<b>(\$767,267)</b>
<b>Total Net Savings</b>	<b>(\$196,608)</b>	<b>\$253,154</b>	<b>\$377,095</b>	<b>\$436,847</b>	<b>\$472,403</b>	<b>\$1,342,890</b>

1                   From a customer perspective in particular, the cost savings identified above  
2                   from the merger of the Companies, once appropriately allocated to the regulated  
3                   business, are anticipated to permit lower rates than otherwise would have been  
4                   necessary on a stand-alone basis for either of the two Companies.

5                   The estimated cost savings referenced above reflect only merger-related  
6                   corporate and regulatory savings. They reflect the consensus of both Companies and  
7                   were jointly developed by management of the Companies, with the assistance of Booz

1 Allen. This joint development of merger-related cost savings provided a sound basis  
2 for identification and quantification and results in fully-documented and agreed-upon  
3 savings. As a result, the process utilized by the Companies was comprehensive and  
4 captures all significant sources of merger-related cost savings typically available.

5 The estimated cost savings reflect the potential creation of cost reduction or  
6 cost avoidance opportunities through the ability to consolidate separate, stand-alone  
7 operations into a single entity. This consolidation and integration thus may enable  
8 duplicative functions and positions to be eliminated; similar corporate activities to be  
9 combined, avoided or reduced in scope; external purchases of commodities and  
10 services to be standardized, rationalized and aggregated; and certain capital  
11 expenditures to be avoided.

12 Based on my experience in other mergers and on my direct involvement with  
13 the identification, evaluation, and quantification efforts related to estimated cost  
14 savings in this and other transactions, the process utilized for estimating potential  
15 merger-related cost savings was consistent with the process utilized by other  
16 companies in previous merger transactions. As a result, I believe the level of merger  
17 savings identified by the Companies is reasonably attainable provided that  
18 management executes its integration plans in a manner consistent with its intent and  
19 how other utilities have pursued similar opportunities.

20 The identified merger cost savings are also within the broad range of those  
21 developed by other companies in other similar situations recognizing the unique  
22 characteristics of both companies. The estimated levels are well within the range of



1 other transactions for staffing reductions and for non-fuel operations and maintenance  
2 expense.

3 Recent utility mergers and acquisitions in other states have produced  
4 substantial benefits to customers in the form of operational synergies and cost savings  
5 that reduce rates or slow the rate of growth in rates. Benefits to customers, however,  
6 will not materialize without costs being incurred and risks being assumed. In  
7 particular, out-of-pocket costs are incurred in the ordinary course of business to  
8 execute a transaction, comply with the various requirements of third-party agencies,  
9 successfully integrate the businesses and, close a transaction. In a number of cases,  
10 expenditures are incurred solely for the purposes of fulfilling fiduciary  
11 responsibilities, satisfying public agency filing requirements or demonstrating the  
12 benefits that are conveyed in the transaction. These costs require up-front expenditure  
13 of these out-of-pocket amounts without assurance that a transaction will, in fact, be  
14 closed. Other expenditures are incurred to assure that employees are treated equitably  
15 and that the business is ready for transparent operations on day-one after the close.

16 In any merger transaction, shareholders also assume the risk that the merged  
17 entity will achieve the strategic, financial, and operational benefits set forth as the  
18 rationale for the proposed combination. To the extent these objectives are not  
19 attained (*e.g.*, failing to realize cost savings), shareholders suffer from eroded equity  
20 value and / or lower returns. It is my opinion and an established regulatory principle  
21 that, to compensate for these risks and to reflect the shareholders' willingness to fund  
22 the costs necessary to realize potential cost savings, the utility should be provided the  
23 opportunity to recover the costs-to-achieve these savings and that the resulting net

1 cost savings should be equitably shared between customers and shareholders. This  
2 principle is borne out in a number of prior transactions where regulatory decisions  
3 have provided for equitable savings sharing after the consideration of related costs-to-  
4 achieve.

#### **IV. SYNERGIES IDENTIFICATION**

5 **Q. IN GENERAL, HOW ARE SAVINGS CREATED FROM THE**  
6 **COMBINATION OF TWO UTILITIES?**

7 A. The combination of two utilities enables the succeeding company to realize  
8 substantial benefits in the form of economies, efficiencies and operating effectiveness  
9 that would not otherwise be available to either company on a stand-alone basis.  
10 These synergies relate to a variety of operational functions and potentially will result  
11 in benefits that will directly accrue to customers. These potential savings areas are  
12 viewed as directly attributable to the merger and would not be attainable in the  
13 absence of the merger.

14 **Q. ARE THERE DIFFERENT TYPES OF COST SAVINGS THAT CAN RESULT**  
15 **FROM THE COMBINATION OF TWO UTILITIES?**

16 A. Yes. In identifying potential cost savings, only those opportunities that are directly  
17 related to the merger were quantified. The distinction between merger and non-  
18 merger related savings is highlighted below:

- 19 • Created savings - These are savings that are directly related to the completion of a  
20 merger and could not be obtained absent the merger. For example, the reduction  
21 of total cost through the avoidance of duplication or overlap and the ability to  
22 extend resources over a broader base of operating activities would naturally occur  
23 through the consolidation of similar functions. Without the combination, both

1 companies would continue to expend amounts on related activities, and as a  
2 result, would incur stand-alone cost levels higher than after consolidation.

- 3 • Enabled savings - These savings result from the acceleration or “unlocking” of  
4 certain events that could give rise to savings and therefore are considered merger  
5 savings. For example, technology differences that exist between companies may  
6 provide an opportunity to share technology and achieve productivity  
7 improvements more rapidly and more cheaply than would have occurred on a  
8 stand-alone basis. For example, one company that has adopted an enterprise  
9 resource planning information management approach will likely enjoy more  
10 seamless operation and management, lower costs and higher productivity than a  
11 company that has individual, customized packaged applications requiring unique  
12 support. While the company without the integrated technology environment can  
13 obtain such benefits from independent investment, the merger enables an existing  
14 technology environment to be more rapidly deployed and costly stand-alone  
15 investment and concept feasibility analysis to be avoided.
  
- 16 • Developed savings - Reductions in cost due to management decisions that could  
17 have been made on a stand-alone basis are unrelated to the merger. A decision to  
18 restructure or reorganize an organization will result in reduced costs but likely  
19 would have been achieved without the merger. None of the cost savings  
20 described in my testimony are in this category.

21 **Q. WHAT TYPES OF SAVINGS HAVE BEEN QUANTIFIED WITH RESPECT**  
22 **TO THE DUKE ENERGY AND CINERGY MERGER?**

23 A. The quantification effort focused on merger-related savings only, *i.e.*, those savings  
24 that would not be attainable but for the combination of the two companies. The  
25 savings described in my testimony almost exclusively fall under the "created savings"  
26 category described above. Potential areas of benefit, and subsequently the resulting  
27 cost savings, are determined to be merger-related if they are not attainable by any

1 action that management of either company could practically initiate on an  
2 independent basis. For example, management of either company could reduce labor  
3 costs by eliminating positions as part of undertaking a comprehensive performance  
4 improvement program. These reductions, however, would relate solely to that entity's  
5 independent operations and would not be related to any merger effects.

6 Quantified merger-related savings result only from action taken by  
7 management in association with the combination of the Companies. For example, the  
8 fact that both companies maintain separate investor relations activities provides an  
9 opportunity to consolidate these functions and avoid replication. This integration of  
10 similar functions and activities would not be possible without the merger of Duke  
11 Energy and Cinergy. Thus, the benefits identified are only those believed to be  
12 directly attributable to the merger.

13 Additionally, cost savings or cost avoidances that result from the new size and  
14 economic scope of the combined entity are merger-related. For example, routine  
15 activities that could not be economically outsourced by either company individually  
16 may now be candidates for outsourcing, given the new combined entity's greater  
17 volumes. Similarly, other activities that either of the companies now outsource might  
18 be performed more cost-effectively internally by the combined entity where volumes  
19 now justify specialized resources. The greater size of the combined entity should also  
20 enable it to be a more cost-effective purchaser of various products and services.  
21 Further, to the extent that the combination of two companies enables the companies to  
22 reduce costs by transferring technology or competencies to each other, these benefits  
23 are also merger-related if such actions could not have been effectively implemented

1 by the companies independently, or if such transfers enable operating costs to be  
2 reduced more rapidly or to a lower level than otherwise would have been the case.

3 Each of the examples described above, as well as other additional cost savings  
4 or cost avoidances that are directly attributable to the merger, are considered merger-  
5 related synergies. Conversely, cost savings or avoidances that would have occurred  
6 even in the absence of the merger are not merger-related and should not be included  
7 in a calculation of the savings attributable to the merger.

8 **Q. WHAT TYPES OF QUANTIFIED BENEFITS TYPICALLY RESULT FROM**  
9 **THE COMBINATION OF TWO UTILITIES?**

10 A. Savings estimates reflect those areas where the total level of costs can be affected by  
11 actions of management that are the direct result of the combination of Duke Energy  
12 and Cinergy. These savings areas are derived from the operational synergies that are  
13 created upon integration of two previously independent operations. These savings  
14 areas would typically impact operations in the following ways:

- 15 • Cost reduction - The total cost of service is reduced as a result of the merger by  
16 avoiding duplication of the cost input required to achieve the same level of output.  
17 For example, similar operating functions, such as corporate planning, could now  
18 be integrated and would require less input to achieve results on a combined basis.
- 19 • Cost avoidance - The total cost of service is reduced due to the ability to forego  
20 certain types of parallel expenditures. For example, redundant expenditures  
21 required by both entities (*e.g.*, information systems) could be avoided by selecting  
22 one set of development efforts to forgo duplication.
- 23 • Revenue enhancement - The creation of additional revenue streams by using  
24 existing regulated assets to supplement revenue sources could also be a means to

1           increase benefits for shareholders and customers. These revenue streams would  
2           be related directly to utilizing available resources, such as generation assets, in a  
3           more attractive manner, *i.e.*, to produce or increase off-system sales, than could be  
4           achieved independently.

5   **Q.   WHAT SPECIFIC CATEGORIES OF QUANTIFIABLE SAVINGS CAN BE**  
6   **EXPECTED TO RESULT FROM A UTILITY MERGER?**

7   A.   Quantifiable savings resulting from a merger typically can be categorized as follows:

- 8           • Corporate and Headquarters Staffing
- 9           • Utility Support Staffing
- 10          • Corporate and Administrative Programs
- 11          • Information Technology
- 12          • Supply Chain
- 13          • Fuel Supply

14          Each of these categories has been identified in this merger and will be described later  
15          in my testimony. These savings areas above relate to common functions and costs  
16          within the business and do not directly relate to service performance and areas that  
17          may affect service quality, reliability or safety.

18   **Q.   WERE COSTS-TO-ACHIEVE ALSO IDENTIFIED IN THE MERGER COST**  
19   **SAVINGS ANALYSIS?**

20   A.   Yes. Certain costs must be incurred to facilitate the realization of the identified cost  
21          savings. Costs-to-achieve are an inherent component of any merger transaction and  
22          are necessary to successfully complete a transaction and/or produce the level of  
23          intended benefits. These costs-to-achieve are expenses that are directly related to  
24          pursuing or executing the transaction and have the effect of offsetting the level of

1 distributable benefits. Were the total cost savings to be distributed without full  
2 recognition of these costs to achieve, the utilities would, in effect, be distributing a  
3 greater level of savings than in fact exist.

4 In addition, if these out-of-pocket costs were not recognized as a related  
5 element of producing cost savings, the Companies would effectively be required to  
6 support such expenditures without reimbursement. Thus, to be equitable to all parties,  
7 it is only the net level of savings that is available for sharing with customers. In the  
8 vast preponderance of utility merger transactions with which I am familiar, costs-to-  
9 achieve have been considered and recognized in determining the net level of benefits  
10 available to customers and shareholders. In other words, costs to achieve have been  
11 recognized and netted against gross merger synergies in determining distributable  
12 savings to customers and shareholders.

13 **Q. WHAT PROCESS WAS UTILIZED BY THE COMPANIES IN DEVELOPING**  
14 **THE ESTIMATED COST SAVINGS ASSOCIATED WITH THE PROPOSED**  
15 **MERGER?**

16 A. The process began by examining underlying data related to the organization of each of  
17 the Companies from both publicly available and internally provided sources. This  
18 information encompassed geographical, organizational and operational data and  
19 included: total numbers of positions, positions distributed by various departments,  
20 position location, and related salaries and benefits.

21 Next, information related to specific cost categories, including recent actual  
22 and expected future expenses for these categories, was identified and obtained.

1 Information obtained through this process included external spending, and various  
2 forecasts and budgets, as well as, internal operating plans.

3 General organizational and operational philosophies for each Company were  
4 also identified. As part of this process, potential organizational and operational  
5 approaches were discussed and areas for potential savings were identified. This  
6 process resulted in the development of a set of area-by-area operating assumptions.

7 Finally, from all of the information and analyses identified above, savings  
8 estimates were developed, reviewed, analyzed, and revised by the management  
9 working groups, with the assistance of Booz Allen, to produce the level of estimated  
10 savings reflected in the initial merger announcement. This level of savings was  
11 subsequently refined with minor adjustments made to reflect revised baseline data and  
12 timing assumptions.

13 **Q. WHAT WAS THE SCOPE OF THE ASSISTANCE PROVIDED BY BOOZ**  
14 **ALLEN RELATED TO THE POTENTIAL COST SAVINGS ASSOCIATED**  
15 **WITH THIS PROPOSED MERGER?**

16 A. Booz Allen was asked to assist the managements of the Companies in the  
17 identification and quantification of both potential savings and additional costs  
18 necessary to realize those savings associated with the merger. This assistance was  
19 provided based upon our previous experience and included assistance in the  
20 identification of necessary data elements and potential cost savings areas, discussion  
21 of potential organizational and operational philosophies, discussion of potential  
22 assumptions to be utilized by Companies, assistance in the identification and



1 quantification of estimated savings and costs-to-achieve and comparison of results to  
2 other previous transactions.

3 **Q. WERE PERSONNEL FROM THE COMPANIES INVOLVED IN THIS**  
4 **PROCESS?**

5 A. Yes, a number of senior management executives from both Companies were actively  
6 involved in the cost savings identification and quantification process described above.  
7 Initially, a small working group was involved in providing data to Booz Allen,  
8 confirming assumptions around the operating model and evaluating the identified  
9 savings opportunities, *i.e.*, the timing and amounts of savings. After announcement, a  
10 broader senior executive and middle management team was involved, representing the  
11 corporate, shared services and utility operating support areas of the Companies. These  
12 executives evaluated potential savings opportunities and provided guidance regarding  
13 the timing of savings realization, and in some cases, provided additional data to Booz  
14 Allen for purposes of developing savings estimates.

15 **Q. IS THIS PROCESS TYPICAL OF OTHER COST SAVING ESTIMATION**  
16 **PROCESSES IN WHICH YOU HAVE BEEN ENGAGED ?**

17 A. Yes. The overall process undertaken by the two Companies to identify merger cost  
18 savings was typical of other engagements in which I have been involved. Senior  
19 executives from each company were identified to lead a joint synergies team, of  
20 which Booz Allen was a part. These executives had good visibility across the  
21 organization and within their respective areas of responsibility and were able to  
22 provide insights into how the business operated and to how particular impacts may  
23 occur given anticipated changes to the operating model.

1           In addition, a broader working group was in place to support this identification  
2 and quantification process comprised of several members of middle management  
3 which further increased the knowledge base available for the synergies analysis. The  
4 involvement of these personnel in the pre-announcement analysis provided the  
5 requisite operating insights into operations of the Companies and enabled the  
6 management groups to understand and assess the identified savings prior to  
7 announcement.

8           In addition, a post-announcement refinement process was undertaken to  
9 further review the initially identified synergies and to obtain additional source data  
10 given the tight confidentiality limitations that existed prior to announcement of the  
11 merger. This process enabled all assumptions to be validated and extended the  
12 number of involved management personnel from the Companies. In addition, it  
13 allowed for deeper analysis and review of the synergies areas to increase the  
14 confidence in attainment of these expected amounts.

15           The combination of these involved management group members in the pre-  
16 announcement process and the expansion of the management group participation  
17 post-announcement, provided a sound basis for the identification and quantification of  
18 the estimated merger synergies.

19 **Q. HOW WERE THE COST SAVINGS QUANTIFIED IN THIS PROCESS?**

20 A. Estimates of cost savings were developed on a nominal cost basis over a ten-year  
21 period from the beginning of year one post-close (2006) through the end of year ten  
22 (2015), thus providing a longer-term view of attainable savings. Since the level of  
23 savings once integration is completed essentially simply grows with escalation, a five-

1 year period has been adopted for presentation of the cost savings information. This  
2 five-year period is representative of the level of ongoing savings and can be used as a  
3 reasonable determination of both annual and cumulative savings.

4 **Q. ARE THE IDENTIFIED COST SAVINGS ONLY ATTAINABLE DURING**  
5 **THIS DEFINED PERIOD?**

6 A. No. The majority of the identified savings components will generate benefits that will  
7 continue indefinitely into the future. For example, potential staffing reductions  
8 associated with the merger will generally continue into the future since they relate to  
9 redundant functions with no need to replace these displaced positions, although future  
10 business changes may require other resource additions to occur. Likewise, potential  
11 supply chain benefits will continue indefinitely as the cost of materials and supplies  
12 acquisition is reduced.

13 Although the cost savings estimated over the period generally will continue  
14 into perpetuity, only a five-year period has been used to present these savings as this  
15 period fully illustrates the ramp-up in savings realization. The estimates of cost  
16 savings are presented in nominal dollars over the relevant period of the merger to  
17 recognize that these savings increase annually from the ramp-up and that they will  
18 flow to customers and shareholders on that basis at some future point in time.

19 **Q. WHAT METHODS WERE USED TO QUANTIFY THE INDIVIDUAL COST**  
20 **SAVINGS COMPONENTS?**

21 A. Cost savings were developed using three principal methods of quantification:

- 1           • Direct analysis - Use of actual costs and changes to these costs based on planned  
2           consolidation activities (*e.g.*, position reductions were estimated based on detailed  
3           analyses of fully aligned individual functions and positions).
- 4           • Estimation - Determination, based upon more limited analysis of actual data, of  
5           potential merger-related cost reductions considering anticipated changes to  
6           markets and operations (*e.g.*, reduction in materials and supplies costs from  
7           enhanced strategic sourcing and additional volume buying).
- 8           • Comparison to other transactions - Utilization of expectations in other proposed  
9           utility mergers as a proxy for the Companies' impacts (*e.g.*, average insurance  
10          premium reductions based on expected or realized reductions achieved by other  
11          companies).

12                       Of the three methods, the vast majority of the savings were quantified by using  
13          direct analysis. These several methods of quantification are consistent with those  
14          utilized by other utility companies in prior mergers, particularly where subsequent  
15          negotiations will ensue. For example, it is well recognized that insurance premiums  
16          will be reduced from a merger; however, the actual amount of the reduction will not  
17          be known until negotiations with an insurance broker are finalized. Using other  
18          expected or realized reduction amounts is an appropriate method for quantification  
19          pending such negotiation.

20   **Q.    ARE THERE ALTERNATIVE ORGANIZATIONAL MODELS AVAILABLE**  
21   **TO THE COMPANIES TO ACHIEVE THE IDENTIFIED COST SAVINGS?**

22   A.    Yes. The Companies will have a great deal of flexibility in determining how to  
23          organize the business to provide for effective performance and to maximize the level  
24          of savings attained. Certain functions that are commonly performed for more than a

1 single entity will become part of a service company that is a legal entity; however, the  
2 existence of this entity does not impact how these functions can be aligned and  
3 organized in actually performing these functions.

4 The cost savings related to identical or similar functions within the Companies  
5 are, however, predicated upon achieving a level of integration that enables a common  
6 model for execution between the Companies. This integration could occur in several  
7 ways: within an expanded headquarters organization; within a corporate level shared  
8 services entity; within an operating level shared services entity; through a functional  
9 or process model across the companies; or by a combination of integration of  
10 corporate and headquarters function at the corporate level and integration of common  
11 technical support services into the operating units, such as the utilities. Any of these  
12 approaches would provide the Companies an opportunity to realize merger cost  
13 savings in those affected areas.

14 In quantifying cost savings, it was assumed that a fully aligned and integrated  
15 organizational model would be implemented, *i.e.*, related functions would be  
16 performed across the operating utilities on a common basis, regardless of where the  
17 responsible resource was actually located. This approach assumes that common  
18 corporate and headquarters functions would generally be performed in a shared  
19 services entity, with common technical support functions either similarly centralized,  
20 or located as required within the various operating units. I will further discuss the  
21 underlying organizational concept later in my testimony.

22 Cinergy already operates in a service company environment that provides a  
23 preliminary model for adoption and implementation. Given the breadth of

1 geographies served, the discrete business units in place within the Companies and the  
2 distribution of resources within these potential business units, certain of these  
3 business unit support functions, *e.g.*, human resources, budgeting, information  
4 management support, *etc.* are located within multiple operating areas throughout the  
5 system. Thus, the Companies have a broad degree of discretion on how to align (*i.e.*,  
6 centralize or decentralize) the processes, activities and resources within the  
7 headquarters, support and operating organizations.

8 **Q. CAN THE LEVEL OF SAVINGS ESTIMATED BY THE COMPANIES AND**  
9 **REFLECTED IN YOUR TESTIMONY BE ACHIEVED?**

10 A. Yes. The process utilized by the Companies for estimating potential merger cost  
11 savings was consistent with that utilized by other companies in previous merger  
12 transactions. As a result, the savings levels are reasonably attainable provided that  
13 management of the combined Company executes its integration plans in a manner  
14 consistent with its intent and how other utilities have pursued similar opportunities.

## **V. DETAILED COST SAVINGS DESCRIPTION**

### **A. Summary**

15  
16 **Q. YOU PREVIOUSLY TESTIFIED THAT APPROXIMATELY \$807 MILLION**  
17 **IN NET MERGER SAVINGS HAVE BEEN QUANTIFIED BY THE**  
18 **COMPANIES OVER THE FIRST FIVE YEARS POST-CLOSE. WOULD**  
19 **YOU IDENTIFY AND DEFINE THE PRINCIPAL CATEGORIES OF COST**  
20 **SAVINGS THAT COMPRISE THIS AMOUNT?**

21 A. Yes. As Attachment TJF-2 illustrates, there are six primary categories of cost savings  
22 that have been quantified. Each of these is described briefly below:

- 1           • Corporate and Headquarters Staffing - Position reductions related to redundancies  
2           in staffing levels associated with corporate and administrative functions, such as  
3           finance and accounting, human resources, information technology and supply  
4           chain, among others.
- 5           • Utility Support Staffing – Position reductions in operating support areas, such as  
6           asset management, operations planning, customer care and other business unit  
7           support related to redundancies in back-office staffing levels.
- 8           • Corporate and Administrative Programs - Reductions in non-labor programs and  
9           expenses, such as insurance and shareholder services, resulting from economies of  
10          scale and cost avoidance.
- 11          • Information Technology – Consolidation of operating environments including  
12          data centers, network servers, workstations and applications, among other areas,  
13          from selection of a single operating platform.
- 14          • Supply Chain – Improved strategic sourcing of materials and contract services  
15          from specification standardization, vendor consolidation, rationalization of  
16          requirements and, aggregation of spend for purchasing.
- 17          • Coal Supply - Consolidation of commodity supply requirements from alignment  
18          of sources, assessment of coal specification requirements and new supply strategy.

19                    These savings categories provide for approximately \$1.3 billion in gross cost  
20                    savings, before allocation between the regulated and non-regulated segments, over the  
21                    five-year period and continue thereafter.

22   **Q.    ARE THERE ANY ITEMS THAT OFFSET MERGER SAVINGS?**

23    A.    Yes. Cost savings initiatives which were already planned prior to the merger were  
24           subtracted from the gross savings estimates because there is likely to be some overlap  
25           between these initiatives and identified cost savings resulting from the merger. These

1 ongoing or future initiatives will contribute to lower total costs to customers and are  
2 estimated at \$10 million over the five-year period. The merger thus allows the  
3 Companies to achieve additional cost savings opportunities beyond those previously  
4 identified. These savings are subtracted from the gross merger savings because they  
5 are not merger-related initiatives.

6 Additionally, the costs to achieve the merger are offset against gross savings  
7 as discussed below.

8 **Q. WHAT ARE THE CATEGORIES OF AND APPROXIMATE COSTS**  
9 **NECESSARY TO ACHIEVE THE SAVINGS?**

10 A. There are several categories of costs that must be incurred to achieve the identified  
11 savings that are expected by the Companies. These costs reflect expenditures  
12 necessary to effectuate the cost savings identified from the merger through company  
13 integration. These categories of costs-to-achieve, as listed below, are further  
14 illustrated in Attachment TJF-3:

- 15 • Separation
- 16 • Retention
- 17 • Relocation
- 18 • Directors' and Officers Coverage
- 19 • Regulatory Process and Compliance
- 20 • Internal / External Communications
- 21 • Transition Costs
- 22 • Transaction Costs



1 Estimated costs-to-achieve total approximately \$513 million, which will principally  
2 be incurred in 2005 through 2008, but will extend over a multi-year period to reflect  
3 certain ongoing costs.

4 **Q. WHAT IS THE ANTICIPATED LEVEL OF TOTAL COST SAVINGS AFTER**  
5 **PRE-MERGER INITIATIVES SAVINGS AND COSTS TO ACHIEVE ARE**  
6 **REFLECTED?**

7 A. The total estimated cost savings identified from the merger over the first five years  
8 after the merger, after being adjusted for costs to achieve and pre-merger initiatives,  
9 are approximately \$807 million. The annual level of steady-state savings at the end of  
10 this five-year period will continue into perpetuity as related reduction decisions have  
11 been fully implemented.

12 **B. General Assumptions**

13 **1. Escalation Rates**

14 **Q. WHAT ASSUMPTIONS ABOUT THE ESCALATION OF COSTS WERE**  
15 **UTILIZED BY THE COMPANIES IN ESTIMATING COST SAVINGS?**

16 A. For the most part, cost savings were estimated based on 2005 budgeted expense  
17 levels. In certain cases, such as shareholder services, 2004 data was used because a  
18 greater level of accuracy could be achieved by using actual, as opposed to budgeted,  
19 data. To account for inflation appropriately, specific escalation rates were then  
20 applied, by category, to initial year savings levels to determine the level of savings in  
21 each of the subsequent years. Development of the estimated cost savings over the  
22 five-year period without application of an escalation factor would result in

1 understatement of the total cost savings available over this period due to the year-to-  
2 year change in baseline cost levels.

3 **Q. WAS THE SAME ESCALATION RATE USED FOR ALL SAVINGS**  
4 **CATEGORIES?**

5 A. No. A differential existed in the anticipated escalation rates for the cost categories  
6 included in the analysis (*e.g.*, differences between salaries and other cost categories).  
7 For this reason, a single escalation rate could not be used for all cost savings  
8 categories. Although approximately 2.3% was used for general inflation, a higher  
9 blended rate (approximately 4.4%) was used for salaries and benefits to reflect market  
10 requirements and existing contractual arrangements. This 4.4% level is consistent  
11 with the Companies' pre-merger, stand-alone assumptions for salary and benefit  
12 increases. This blended rate reflects an escalation rate of 9.1% for benefits due to the  
13 continuing high rate of inflation for medical costs that industry has experienced.  
14 These escalation rates are comparable to those used by other companies with which I  
15 am familiar and to other longer-term estimates for general inflation.

16 **2. Treatment of Capital Savings**

17 **Q. WERE THERE OTHER GENERAL ASSUMPTIONS OR METHODOLO-**  
18 **GIES EMPLOYED IN THE COST SAVINGS ANALYSIS?**

19 A. Yes. In treating capital deferrals and avoidance related to the merger, such as in  
20 information technology investment, it would be inappropriate to count the entire cash  
21 amount of the capital expenditure deferred or avoided as cost savings. For example,  
22 if it were anticipated that the Companies could avoid incurring a \$10 million system  
23 upgrade in 2007, this reduction in expenditures was not used for the actual savings.

1 Including the \$10 million as savings achieved in 2007 would not represent the  
2 avoided revenue requirements associated with that capital expenditure from either the  
3 company or customers' perspectives. Additionally, such a methodology would result  
4 in overstating the cost savings in the early years following the merger by taking credit  
5 for the entire avoided investment as cost savings in those years. Instead, it is more  
6 appropriate to reflect only the revenue requirements savings associated with capital  
7 deferral/avoidance as cost savings. The components of revenue requirements include  
8 financing, depreciation, insurance and property tax. A levelized revenue requirements  
9 approach, rather than a cash flow approach, provides a more appropriate  
10 determination of the savings estimated to be generated due to the merger.

11 **Q. WHAT METHODOLOGY WAS USED TO CAPTURE THESE CAPITAL**  
12 **DEFERRAL/AVOIDANCE SAVINGS?**

13 A. A levelized fixed charge rate for each year following completion of the merger was  
14 applied to each year's capital expenditure reductions. The fixed charge rate  
15 methodology, which reflects normal declining balance ratemaking treatment, was  
16 used to estimate annual savings levels. Fixed charge rates were determined by both  
17 Duke Power and the Cinergy operating companies and then were blended to  
18 determine both general rates for long term assets and specific rates for information  
19 technology-related expenditures. The levelized fixed charge rate for capital items  
20 other than information technology was 13.0% while for information technology items  
21 it was 27.3%, reflecting the more rapid (five year) depreciation period.

1 **C. Cost Savings Summary**

2 **1. Corporate and Headquarters Staffing**

3 **Q. PLEASE DISCUSS IN MORE DETAIL THE NATURE OF THE COST**  
4 **SAVINGS CREATED THROUGH THE INTEGRATION OF THE**  
5 **CORPORATE AND HEADQUARTERS STAFFING FUNCTIONS.**

6 A. The combined Companies expect to fully integrate existing corporate and  
7 headquarters areas, such as strategic planning, treasury and compensation, among  
8 others. Such integration would generate savings through the elimination of redundant  
9 positions within these functions as the scope of related activities are generally  
10 identical within each Company.

11 A merger between the Companies provides an opportunity to consolidate these  
12 functions and eliminate redundant activities. For example, the consolidation of two  
13 information technology functions would typically create significant savings. Potential  
14 redundancy within the two departments is identified through an alignment of sub-  
15 functions between the Companies to ensure comparability across different  
16 organizational structures. Each individual sub-function within the information  
17 technology area contains positions performing duplicate tasks. Overlapping positions  
18 for non-variable work activity can be consolidated and subsequently eliminated  
19 without an impact on remaining workload volumes.

20 **Q. HOW WAS THIS PRINCIPLE APPLIED TO DETERMINE THE**  
21 **POTENTIAL POSITION SAVINGS THAT WOULD RESULT FROM A**  
22 **MERGER OF THE COMPANIES?**

1 A. The first step in determining corporate and headquarters staffing savings was to  
2 develop a detailed functional alignment of each Company. Each Company provided  
3 functional and sub-functional breakdowns that identified each position within its  
4 respective organization. The stand-alone company functional areas then were aligned,  
5 by sub-function, so that position levels for similar activities performed by the  
6 respective companies could be compared. The analysis maintained consistency  
7 between the inter-company functional categories and aligned representative activities  
8 between the Companies.

9           Upon completion of the functional and sub-functional alignment, the positions  
10 necessary to perform the required activities on a merged company basis were  
11 identified. In determining the appropriate going-forward future position levels of the  
12 merged company, the following items were considered:

- 13 • The relevant operating model to be employed within the particular area
- 14 • The relative scale and resource concentration between the two companies
- 15 • The type of activity and potential for redundancy
- 16 • The fixed or variable nature of the activity

17           Consideration of these factors provided the means by which going-forward  
18 staffing levels could then be defined and resulting reductions determined.

19 **Q. WHAT OPERATIONAL MODEL WAS ASSUMED FOR DETERMINATION**  
20 **OF STAFFING REDUCTIONS IN THE CORPORATE AND**  
21 **HEADQUARTERS FUNCTIONS?**

22 A. Although no specific organizational structure was assumed to be in place post-closing  
23 of the transaction, there was a guiding presumption that the Companies would

1 establish an operating model that would allow them to capture available savings from  
2 alignment, standardization and integration of common functions. This meant that  
3 similar functions would be fully integrated, where practical, and that resources would  
4 be aligned in the most effective manner to execute corporate objectives. It was  
5 intended that full organizational design flexibility would be maintained by the  
6 Companies to develop an operating structure that reflected the prerogatives of  
7 management and the requirements of managing and executing the business.

8 At the corporate level, it was assumed that those functions that relate to  
9 managing the business on an enterprise basis, *e.g.*, strategic planning, finance and  
10 accounting, external relations, *etc.*, would be fully integrated to reflect the overlap and  
11 duplication in these areas. With respect to these functions, consolidation would occur  
12 in those areas that were not geographically dependent, such as investor relations, or  
13 were related to business policy, such as compensation and benefits.

14 The identified staffing reductions in the corporate and headquarters areas also  
15 assumed that a shared services entity, similar to what each company currently has in  
16 place, would also be in place after the close of the transaction. This type of entity  
17 typically aligns the common and transactional elements of the various functions, such  
18 as human resources, information technology, supply chain, *etc.*, that are performed to  
19 capture economies of scale. Without defining whether the scope of this shared  
20 services entity could increase to incorporate other transactional activities, it was  
21 assumed that this type of organization would remain in place and serve as a means to  
22 achieve standardization and lower unit costs for similar activities.

1 **Q. HOW WOULD COMPANIES' PROPOSAL FOR A SEPARATE SERVICE**  
2 **COMPANY AFFECT THIS ASSUMED OPERATING MODEL?**

3 A. The Companies propose the use of the service company to provide common functions  
4 on behalf of more than one entity within the holding company on a recurring basis.  
5 This organizational unit, however, does not impact the operating model or the  
6 organization structure in place. Its purpose is to capture relevant costs for purposes of  
7 regulatory compliance related to cost allocations. How a company elects to organize  
8 and operate is largely independent of the existence of the service company.  
9 Consequently, Duke Energy and Cinergy will be able to maintain substantial  
10 flexibility in organizing the company on a going-forward basis. This effectively  
11 means that there would be no impact on the level of identified staffing reductions in  
12 the corporate and headquarters functions as a result of maintaining a service company.

13 **Q. PLEASE DESCRIBE THE RESULTS OF THE CORPORATE AND**  
14 **HEADQUARTERS STAFFING ANALYSIS DISCUSSED ABOVE.**

15 A. As of June 2005, Duke Energy had a total of 2,904 positions in the corporate and  
16 shared services areas, while Cinergy had a total of 1,343 positions at this same date  
17 for these functions. Approximately 574 corporate and headquarters position  
18 reductions were identified by the Companies that could result from the consolidation,  
19 which constitutes 13.5 % of the combined corporate and headquarters position  
20 baseline. These reductions represent the anticipated level of functional duplication  
21 that would exist between the Companies and could be avoided through the creation of  
22 an integrated corporate and headquarters organization. The savings associated with  
23 this area are \$46.4 million in the first year and grow to \$79.0 million by the third year

1 when all information technology conversion is completed and steady-state operations  
2 are achieved.

## 3 **2. Utility Support Staffing**

4 **Q. WHAT OPERATING MODEL WAS ASSUMED FOR THE ANALYSIS OF**  
5 **THE UTILITY SUPPORT AREAS?**

6 A. Given that utility operating companies exist in multiple state jurisdictions and the  
7 different approaches to organization within these companies, a common model  
8 needed to be defined for consideration with respect to operations and organization. A  
9 model was adopted where similar and commonly performed functions were assumed  
10 to be aligned, harmonized and integrated, regardless of where they were located. This  
11 meant that work could be electronically shared across the utility operating companies,  
12 where practical, so that local resources could support company-wide operations  
13 efforts and reduce the total level of staffing required. Thus, the total plant or field  
14 support staff work requirements could be distributed across engineering staff located  
15 in any one of the states where the new company will operate and joint standards  
16 would be in place to guide the work performed. Similarly, common back-office  
17 support in areas such as operations planning, budgeting and project management  
18 could also be consolidated and executed from any location in support of overall utility  
19 operations.

20 With respect to the fossil supply business, it was assumed that the vast  
21 majority of the resources dedicated to this area would largely be unaffected by the  
22 merger as they are dedicated to plant operations and located at the physical facilities  
23 performing related work. However, for those functions that relate to areas such as



1 business unit management, engineering, outage planning, maintenance standards and  
2 other common functions in place to support each Company's fleet, it was assumed  
3 that these resources could be shared across the operating companies and would be  
4 aligned to allow for a fully integrated operating model to be employed. The adoption  
5 of this type of model does not require relocation of personnel between the Companies  
6 rather, it simply enables available resources to be jointly leveraged and scheduled to  
7 meet the total work requirements of the business. Under this operating model there is  
8 no reduction in the level of dedicated resources to either Company's plants, thus  
9 service reliability is not affected.

10 Similarly in the transmission and distribution business, the vast majority of  
11 resources are totally unaffected by the merger as the field work volumes are not  
12 reduced. Thus, there is no impact to service reliability, quality or safety from the  
13 merger as no reductions in staffing are expected in the field execution areas. Again,  
14 however, certain common back-office related functions, like those identified for the  
15 fossil supply business above in engineering, planning, *etc.*, would lend themselves to  
16 integration under such a "virtual" operating model concept. In these areas, resources  
17 would again be leveraged across the operating companies where common functions  
18 are performed for the benefit of the business as a whole.

19 With respect to the customer service area, the Companies intend to move to a  
20 single billing platform which will enable a variety of customer care functions like  
21 customer accounting, remittance processing and credit and collections to be fully  
22 integrated. The consolidation of these functions will enable back-office resources to  
23 also be reduced. In addition, customer inquiry will be integrated across the operating

1 companies similar to how Cinergy currently operates. The common billing platform  
2 will enable customer calls to be routed to any Company call center, regardless of  
3 location, and be handled in a standard, systematic manner. This will improve overall  
4 productivity and allow for the total customer representative staffing base to be sized  
5 to meet the combined needs of the Companies, rather than simply the sum of the two  
6 stand-alone companies.

7 In each of the operating models described above, the field operations of the  
8 Companies, *i.e.*, the plants and the crews, are unaffected with no impacts to service  
9 reliability, quality or safety, except to the extent they may be enhanced by ready  
10 access to additional emergency (typically storm) support personnel. In addition, there  
11 is no movement of assets or resources away from their jurisdictional control and,  
12 therefore, no impact to the ability of local regulators to continue to monitor operating  
13 company performance or to maintain access to responsible operating company  
14 management.

15 **Q. WHAT LEVEL OF SAVINGS WAS QUANTIFIED WITH RESPECT TO**  
16 **UTILITY SUPPORT STAFFING?**

17 A. The baseline level of utility staffing for Duke Power was 8,679 and for the Cinergy  
18 operating companies was 5,321. The identified staffing reductions in the utilities  
19 were 432 positions, which represent 3.1% of the overall staffing baseline in the utility  
20 support area. These amounts reflect reductions that arise directly from adoption of  
21 the “virtual” operating model where functions are consolidated and managed and  
22 executed across the operating Companies in the plant and field support back-office  
23 functions. The total level of labor savings in the utility support area was quantified at

1           \$13.0 million in the first year growing to \$31.3 million by the third year when steady-  
2           state operations are achieved.

3   **Q.   WHAT ARE THE ESTIMATED TOTAL POSITION REDUCTIONS FROM**  
4   **THE COMBINATION OF THE COMPANIES?**

5   A.   Total position reductions are estimated at 1,006 or approximately 5.5% of total  
6       current combined company corporate, shared services and regulated utility positions.  
7       These reductions reflect the operating models discussed above and result from the  
8       ability to reduce overlapping responsibilities, align related functions and activities and  
9       leverage a consolidated resource base.

10 **Q.   WHEN ARE THESE POSITION REDUCTIONS ASSUMED TO OCCUR?**

11 A.   The Companies intend to achieve a number of these reductions, 557, by the beginning  
12       of the first year following completion of the merger. Due to the need for extensive  
13       integration of information systems applications that will be required in association  
14       with consolidating operations of the Companies, approximately 449 reductions will  
15       not be fully realized until the second or third years following completion of the  
16       merger. These reductions have been synchronized with anticipated system  
17       completion dates to reflect the timing of system cut-overs, work practice  
18       standardization and process harmonization.

19 **Q.   ONCE THE POTENTIAL POSITION REDUCTIONS WERE IDENTIFIED,**  
20 **HOW WERE THE POSITION REDUCTION COST SAVINGS**  
21 **CALCULATED?**

22 A.   Average salary levels were calculated by function and then applied to the identified  
23       position reductions in those respective areas. The average blended salary for the

1 position reductions identified (excluding executives) is estimated to be approximately  
2 \$70,000 in 2006 dollars based on the expected salary levels for each company,  
3 weighted by the number of functional resources in each Company, and then escalated  
4 one year.

5 **Q. ARE THERE COST SAVINGS ASSOCIATED WITH POSITION**  
6 **REDUCTIONS OTHER THAN SALARY EXPENSE?**

7 A. Yes. Benefit costs are also considered when determining the cost savings associated  
8 with position reductions. Benefits include such items as health insurance, life  
9 insurance, employee investment plans, pension expense, accruals for retirement health  
10 benefits of active positions, incentives and bonuses, payroll taxes and others. A  
11 blended benefits loading rate of 30.9% was used to estimate average aggregate  
12 benefits cost. The resulting total compensation (excluding executives), including  
13 benefits, averaged approximately \$95,000 in 2006 dollars.

14 **Q. WAS ANY PORTION OF THESE CORPORATE, HEADQUARTERS AND**  
15 **UTILITY SUPPORT STAFFING SAVINGS CAPITALIZED?**

16 A. Yes. A certain portion of these expenses are capitalized rather than expensed  
17 annually, reflecting their relation to the capital or construction elements of the  
18 business. Capitalized amounts thus are recovered over the life of the asset to which  
19 these costs are assigned. A blended capitalization rate of approximately 4.2% was  
20 used based on the stand-alone expectations of each company weighted by relative  
21 size.

1 **Q. WHAT TOTAL SAVINGS LEVEL WAS ESTIMATED FROM CORPORATE,**  
2 **HEADQUARTERS AND UTILITY SUPPORT STAFFING**  
3 **CONSOLIDATION?**

4 A. Cost savings from corporate, headquarters and utility support staffing consolidation  
5 were estimated at \$59.4 million the first year, \$96.2 million in the second year, and  
6 \$110.3 million in year three, when steady-state operations is achieved. Total savings  
7 for the five-year period were estimated to be approximately \$507 million.

8 **Q. COULD THESE POSITION SAVINGS HAVE BEEN ACHIEVED WITHOUT**  
9 **THE MERGER?**

10 A. No. The position reductions described are solely attributed to the merger. The  
11 reduction opportunities arise from overlap and duplication in functional performance,  
12 rather than from stand-alone initiatives unrelated to the merger. The savings  
13 discussed above are triggered by the opportunity to combine functions and eliminate  
14 redundancy, not by assumed improvements in operating efficiencies. Although  
15 continuous improvement programs are regularly pursued, the savings identified above  
16 are not related to these stand-alone initiatives. Where cost reductions planned post-  
17 2005 were identified, these impacts were subsequently identified, quantified and  
18 offset against potential savings to avoid double-counting potential non-merger  
19 impacts. The subject of pre-merger initiatives is discussed further elsewhere in this  
20 testimony.

21 **3. Corporate And Administrative Programs**

22 **Q. WHAT COST SAVINGS CAN BE CREATED THROUGH CORPORATE**  
23 **PROGRAM AND EXPENDITURE CONSOLIDATION?**

1 A. The integration of corporate and administrative functions reduces certain non-labor  
2 costs, primarily through the consolidation of overlapping or duplicative programs and  
3 expenses.

4 Two examples, insurance and information systems expenses, will illustrate  
5 how these savings are created through a merger:

- 6 • Insurance - Cost savings typically would be realized in the areas of property  
7 insurance and excess general liability insurance, among others. On a stand-alone  
8 basis, each company carries insurance (or is self-insured) in these areas  
9 independently. A larger combined company will have a reduced risk profile  
10 because of its broader asset base. In addition, asset concentration will be less  
11 significant due to the broader geography and more diversified balance sheet,  
12 which should translate into lower rates for the combined company.
- 13 • Information systems - Organizations must facilitate systems development and  
14 support the information processing needs of each company. Companies typically  
15 have independent plans to develop a variety of systems in the future, including  
16 parallel systems development efforts. A combination would enable the  
17 Companies to avoid incurring these duplicate capital expenditures. Additional  
18 information systems savings could result from deferred capital projects, such as  
19 server upgrades or workstation purchases. Additionally, savings could be realized  
20 from the elimination of other duplicate costs, including disaster recovery, software  
21 support, miscellaneous software and hardware, license fees, and computer  
22 maintenance.

23 **Q. WHAT ARE THE AMOUNTS, BY SPECIFIC AREA, OF THE CORPORATE**  
24 **AND ADMINISTRATIVE PROGRAM SAVINGS?**

25 A. Savings were identified and quantified over the five-year period in the following  
26 areas:

	Five-Year Total <u>(\$Millions)</u>
1	
2	
3	
4	\$ 40.9
5	3.9
6	37.2
7	4.2
8	23.3
9	29.1
10	6.5
11	219.7
12	9.5
13	<u>3.9</u>
14	\$ 378.1

15 Each of the aforementioned categories is described below.

16 a. **Administrative and General Overhead**

17 **Q. WHAT TYPES OF EXPENSES ARE INCLUDED IN ADMINISTRATIVE**  
18 **AND GENERAL OVERHEAD EXPENSE AND HOW ARE THEY**  
19 **AFFECTED BY THE MERGER?**

20 A. Administrative and general overhead expense includes, but is not limited to,  
21 periodicals, postage (other than customer billing), employee travel and education, and  
22 office supply expenses related to employee support. These costs vary with the total  
23 number of positions and change as the level of employee staffing increases or  
24 decreases. As position reductions are realized, the related administrative and general  
25 support expenses will be reduced accordingly.

26 **Q. HOW WERE THE ESTIMATED COST SAVINGS QUANTIFIED FOR THIS**  
27 **AREA?**

1 A. Miscellaneous overhead expenses were identified and separated between fixed and  
2 variable components and divided by the total positions for which they were  
3 applicable. Between the two Companies, a total blended amount of approximately  
4 \$18,000 was derived for these miscellaneous overheads per employee. The variable  
5 portion of the total administrative and general costs for the Companies was  
6 approximately \$14,000 per employee and was then multiplied by total merger-related  
7 administrative and general corporate position reductions to arrive at a merger savings  
8 level for this area. The related merger savings were estimated at \$5.5 million in the  
9 first year, \$7.9 million in the second, and growing to \$9.0 million when steady-state  
10 operations are achieved by year three.

11 **Q. COULD THESE MISCELLANEOUS OVERHEAD EXPENSE SAVINGS BE**  
12 **ACHIEVED ABSENT A MERGER?**

13 A. No. These savings are directly related to the position reductions that would result  
14 from the merger.

15 **b. Association Dues**

16 **Q. PLEASE DESCRIBE HOW DUES AND MEMBERSHIPS COULD BE**  
17 **AFFECTED BY THE MERGER OF THE COMPANIES.**

18 A. Both companies are members of the Edison Electric Institute, the trade organization  
19 for the electric industry. The combination will allow opportunities to realize an  
20 overall lower level of expenditures under the EEI formula compared to the  
21 expenditures under the formula on a stand-alone basis. These savings arise due to the  
22 declining unit rate applied in each of the three factors after initial threshold levels are  
23 met.



1 **Q. HOW WERE SAVINGS IN DUES AND MEMBERSHIPS QUANTIFIED?**

2 A. A review of each company's industry and trade memberships was performed. A  
3 review for common organizations was conducted with overlapping memberships  
4 identified and the smaller expenditure was reduced or any formulaic calculations  
5 made to reflect the consolidation of memberships in these organizations. The  
6 resulting estimated savings identified were \$0.7 million in the first year and growing  
7 with escalation thereafter.

8 **Q. COULD THE SAVINGS IN DUES AND MEMBERSHIPS BE ACHIEVED**  
9 **ABSENT A MERGER?**

10 A. No, they can only be achieved by consolidating related memberships. Otherwise,  
11 there will continue to be two sets of memberships under separate formulas.

12 **c. Benefits**

13 **Q. HOW CAN COST SAVINGS RELATED TO BENEFITS ARISE FROM THIS**  
14 **MERGER?**

15 A. Benefits savings typically arise from two sources: the consolidation of benefits plan  
16 administration and related costs and the reduction in the cost of the dollar of benefits  
17 obtained. The benefits administration costs can be reduced through the alignment of  
18 plan trustees and the management of multiple plans through a single administrator.  
19 Through the consolidation of the benefits plan themselves, the cost of benefits can  
20 also be reduced from aggregation of the plan members and the reduction in the unit  
21 cost of the benefit dollar procured. This plan consolidation would be linked to  
22 existing contract expirations and the evaluation of national and regional providers  
23 from coverage, quality and cost perspectives.

1 **Q. WHAT IS THE LEVEL OF BENEFITS RELATED COST SAVINGS?**

2 A. The respective benefits administrative costs paid and benefits costs incurred by the  
3 Companies were reviewed to determine the opportunities for administrator and plan  
4 consolidation. The level of savings from the consolidation of the benefits program is  
5 estimated at \$8.1 million in the second year growing to \$8.9 million by the third year  
6 when steady-state operations is achieved.

7 **d. Directors' Fees**

8 **Q. HOW ARE SAVINGS IN DIRECTORS' FEES DERIVED FROM UTILITY**  
9 **COMBINATIONS?**

10 A. These savings result from the reduced number of total directors for the new company  
11 compared to that of Duke Energy and Cinergy today. The new Company will have a  
12 Board of Directors numbering fifteen directors, comprised of ten directors from Duke  
13 Energy and five from Cinergy. The elimination of seven board members will reduce  
14 overall director fees for meetings, committee participation and travel for these  
15 individuals. The source of the savings is the reduced meeting and committee fees  
16 paid to directors as a result of these directors leaving the board, as well as the  
17 reduction in travel related costs from the fewer directors on the new board.

18 **Q. HOW WERE COST SAVINGS ESTIMATES IN THIS CATEGORY**  
19 **DEVELOPED?**

20 A. The number of directors for each company was identified along with the associated  
21 costs. Based on the average fees and expenses for directors at each Company, the  
22 total savings would amount to \$0.8 million per year.

1 **Q. COULD THE SAVINGS ASSOCIATED WITH DIRECTORS' FEES BE**  
2 **ACHIEVED ABSENT A MERGER?**

3 A. No. These savings are directly merger-related in that they are derived from merger-  
4 related reductions in the number of board members required by the new Company  
5 when compared to the existing two companies. These savings could not be achieved  
6 without the merger since the total number of directors would not have been affected  
7 on a stand alone basis.

8 **e. Facilities**

9 **Q. WHAT SAVINGS CAN BE REALIZED THROUGH CONSOLIDATION OF**  
10 **TOTAL CORPORATE FACILITIES?**

11 A. Cost savings will arise in this category from the reduction of the total square footage  
12 needed to be maintained for the relevant employee base after adjustment for the  
13 reduced total employee level. This expense is variable with the number of employees  
14 and reflects the cost per square foot for space and related maintenance costs.

15 **Q. WHAT WAS THE MAGNITUDE OF SAVINGS ASSOCIATED WITH**  
16 **FACILITIES CONSOLIDATION?**

17 A. Because the location of the staff reductions will not be known until the integration  
18 process is further along, the average amount of square footage per employee for  
19 existing space and cost per square foot across all the corporate facilities was  
20 developed for application against expected staff reductions. This space would be  
21 sublet to another occupant at the prevailing market rate across the available locations.  
22 Based on this approach, facilities savings were estimated at \$3.1 million in the first  
23 year, ramping up to a level of \$5.1 million savings by the end of the third year

1 following the merger, when steady-state operations is achieved.

2 **Q. COULD THESE SAVINGS BE ACHIEVED ABSENT A MERGER?**

3 A. No. The facilities consolidation savings are possible only as the result of the  
4 consolidation of the Companies and the resulting position reductions described above.  
5 If the Companies were to remain as separate corporate entities, then these savings  
6 could not otherwise occur.

7 **f. Insurance**

8 **Q. PLEASE DESCRIBE THE RATIONALE OF HOW SAVINGS CAN BE**  
9 **ACHIEVED IN THE AREA OF INSURANCE.**

10 A. Utilities generally require insurance coverage in the areas of property, directors' and  
11 officers' liability and excess casualty. On a stand-alone basis, each company  
12 independently carries insurance in these areas which they have obtained on a  
13 negotiated basis from external brokers or through self-insurance. A combined  
14 company may have a reduced risk profile because of its broader and more diverse  
15 asset base, which translates into lower rates. Further savings can be attained through  
16 the ability to carry higher deductibles given the combined company's increased  
17 financial strength.

18 **Q. HOW WERE THE SAVINGS IN THE AREA OF INSURANCE QUANTIFIED**  
19 **IN THIS TRANSACTION?**

20 A. Savings on insurance premiums were calculated for property coverage, directors and  
21 officers coverage, fiduciary coverage and, liability coverage. These reductions were  
22 derived based on discussions with the risk managers in the respective companies and  
23 review of experience in other mergers regarding actual savings negotiated with

1 insurance brokers. The total estimated savings for insurance is \$5.5 million in the  
2 first year and growing with escalation thereafter.

3 **Q. COULD THE SAVINGS THAT HAVE BEEN IDENTIFIED IN THE**  
4 **INSURANCE AREA BE ACHIEVED ABSENT A MERGER?**

5 A. No. These savings are predicated directly on the assumption that there is a single  
6 company procuring insurance coverage on the basis of the combined risk profile of  
7 that entity.

8 **g. Professional Services**

9 **Q. WHAT GIVES RISE TO SAVINGS IN THE AREA OF PROFESSIONAL**  
10 **SERVICES?**

11 A. The combined company can reduce professional services activities through economies  
12 of scope, elimination of non-recurring duplicate services and increased utilization of a  
13 broader skill base. Audit costs and additional attest services (*e.g.*, bond insurance  
14 letter, pension plan audits, stock issuance) can be reduced as a result of duplication.  
15 Similarly, legal expenditures (regulatory and corporate) and consulting expenditures  
16 can be avoided due to redundancy and duplication and reduced from supplier  
17 rationalization and substitution of in-house resources for external services.

18 **Q. HOW WERE SAVINGS IN THE AREA OF PROFESSIONAL SERVICES**  
19 **QUANTIFIED, AND WHAT WAS THEIR MAGNITUDE?**

20 A. Expenditures, by category. *e.g.*, accounting, legal, consulting, *etc.*, were aligned  
21 between both companies to determine baseline professional fees. Each category was  
22 assessed based on the needs of the business, the nature of the services obtained, the  
23 level of third-party assistance obtained and the likely availability of internal resources

1 to be deployed against these specific needs. The total savings resulting from these  
2 reductions was estimated at \$40.2 million in the first year and growing thereafter.

3 **Q. COULD THESE SAVINGS BE ACHIEVED ABSENT A MERGER?**

4 A. No. They can only be achieved by consolidating the use of professional services  
5 within a single company. Otherwise, there will continue to be two different sets of  
6 independent auditors, two comprehensive sets of external legal counsel and two  
7 different sets of general consultants.

8 **h. Shareholder Services**

9 **Q. HOW WILL THE MERGER OF THE COMPANIES IMPACT THE**  
10 **EXPENSES INCURRED FOR SHAREHOLDER SERVICES?**

11 A. Cost savings will arise in this area with respect to both fixed and variable costs related  
12 to expenses for the annual report, annual meeting, proxy filings, securities registration  
13 and, other investor relations costs. These costs will be avoided in many cases as they  
14 are purely duplicative.

15 **Q. HOW WERE THE SAVINGS IN THE AREA OF SHAREHOLDER**  
16 **SERVICES QUANTIFIED?**

17 A. Costs were aligned, by category and compared to determine relative spend. These  
18 costs were also separated between fixed and variable levels and assessed across both  
19 companies. Duplicative costs, largely fixed, are reduced in following areas: annual  
20 report costs, stock transfer/registration fees and annual meeting costs; stock exchange  
21 fees and other outside services. Variable administration/postage costs, proxy services,  
22 stock transfer / registration fees and annual meeting costs were also reduced to reflect  
23 lower required costs and to reflect some overlap of investors. The total estimated

1 savings in the area of shareholder services is approximately \$1.8 million in the first  
2 year growing with escalation thereafter.

3 **Q. COULD THESE SAVINGS BE ACHIEVED ABSENT A MERGER?**

4 A. No. They can only be achieved by consolidating into a single company and thereby  
5 reducing the need for stand-alone costs to be incurred in the same areas.

6 **i. Transportation**

7 **Q. HOW WILL THE MERGER OF THE COMPANIES IMPACT THE**  
8 **EXPENSES INCURRED FOR TRANSPORTATION?**

9 A. Savings are achieved by minimizing the costs associated with available aircraft  
10 leasing and ownership options and optimizing the use of the planes presently  
11 employed by the two companies.

12 **Q. HOW WERE THE SAVINGS IN THE AREA OF TRANSPORTATION**  
13 **QUANTIFIED?**

14 A. Savings result from reducing overall aviation costs through reducing the need for total  
15 aircraft hours flown across multiple aircraft and maximizing the amount flown across  
16 fewer total planes. The use of each of the aircraft maintained by the Companies was  
17 reviewed along with the related operating costs. It was assumed that the existing mix  
18 of aircraft would be realigned to better optimize use and cost, thus reducing the total  
19 cost of ownership or lease. The total estimated savings in the area of transportation is  
20 estimated at approximately \$0.7 million in the first year and grows with annual  
21 escalation thereafter.

22 **Q. COULD THESE SAVINGS BE ACHIEVED ABSENT A MERGER?**

1 A. No. They can only be achieved by consolidating into a single company and thereby  
2 reducing the need for separate aircraft arrangements to be maintained.

3 **4. Information Technology**

4 **Q. HOW WILL INFORMATION TECHNOLOGY SAVINGS ARISE FROM THE**  
5 **PROPOSED MERGER OF THE COMPANIES?**

6 A. With the completion of the merger, the separate information technology operations of  
7 the Companies will be integrated which will allow the combined stand-alone  
8 operating and capital costs to be reduced. This cost reduction will occur from the  
9 standardization of the information technology architecture, rationalization of  
10 applications and planned projects and consolidation of the underlying infrastructure.

11 **Q. WHAT AREAS ARE EXPECTED TO PROVIDE COST SAVINGS IN THE**  
12 **INFORMATION TECHNOLOGY FUNCTION?**

13 A. Each company utilizes different systems and vendors for the principal applications  
14 areas of finance, human resources, supply chain, billing and work management.  
15 Rationalizing these individual backbone applications will provide for significant  
16 reduction in support and maintenance expenses. With Duke Energy using PeopleSoft  
17 and Cinergy using a modified internal system, it is expected that the combined  
18 company will adopt the current Duke Energy system, thus reducing applications  
19 support costs and the need for continuing upgrades to existing applications for  
20 Cinergy. Although no final decisions were made with respect to the complete  
21 inventory of applications between the companies, the merger will require that a single,  
22 common application in each area, such as work management and billing, be adopted  
23 across the business which will yield similar savings.



1            Additionally, the standardization and consolidation of the infrastructure will  
2            enable the number of data centers to be reduced, as well as, the number of servers  
3            used to support network computing. It is also expected that the number of  
4            workstations and related requirements for software will be reduced as the number of  
5            employees is reduced. Similarly, rationalization of the needs of the business will  
6            result in additional savings opportunities as the networks can be integrated between  
7            the companies, expenditures for communication devices reduced and plans for  
8            cellular, paging and other communications can be combined.

9    **Q.    WHAT ARE THE COMPONENTS OF THE SAVINGS IN THE**  
10    **INFORMATION TECHNOLOGY AREA?**

11    A.    Savings that will arise in the information technology area consist of both operation  
12           and maintenance expenses and carrying costs associated with either reduced  
13           capitalization of related expense or reduced capital expenditure levels. These savings  
14           thus reflect the reduced and avoided costs from standardization, rationalization and  
15           consolidation.    Capital savings reflect that approximately 60% of identified  
16           application savings will be capitalized and amount to \$3.5 million in the first year and  
17           grow to \$36.1 million by the last year of the five-year period. These savings reflect a  
18           five-year amortization of applicable costs related to development and upgrading  
19           expenditure avoidance. For the operation and maintenance related expenses, savings  
20           are \$12.5 million in the first year and grow to \$36.2 million by the end of the five-  
21           year period. The level of savings total related to information technology is estimated  
22           at \$16.0 million in the first year growing to \$72.4 million in the fifth year.

23    **Q.    COULD THESE SAVINGS BE REALIZED BY THE COMPANIES**

1           **WITHOUT THE MERGER?**

2     A.     No. There would be no opportunity to integrate the information technology  
3           infrastructure and consolidate applications in the absence of the merger. These  
4           savings, therefore, would not occur but for the merger.

5                               **5. Supply Chain**

6     **Q.     MR. FLAHERTY, PLEASE DISCUSS THE COST SAVINGS THAT CAN BE**  
7           **CREATED THROUGH THE SUPPLY CHAIN.**

8     A.     Combining companies can achieve savings through the centralization of purchasing  
9           and inventory functions related to the construction, operation and maintenance of  
10          generating plants, service centers, warehouses and headquarters. The greater  
11          purchasing power and the relative quantity of both goods and services that can be  
12          obtained as a result of the combination of companies provide additional cost savings.  
13          With respect to the purchase of goods (*i.e.*, materials and supplies), savings can be  
14          realized in the procurement of commodity items, consumable equipment (*e.g.*,  
15          conductors, wire, cable), and other equipment for electric utilities. Savings also may  
16          be realized from avoiding an initial reorder cycle from certain inventory item sharing.  
17          In addition, standardization of system components such as cable, meters,  
18          transformers, and conductors for electric utilities can be achieved through a common  
19          design process, providing additional savings opportunities.

20                 With respect to the procurement of services, particularly contract services such  
21                 as engineering, construction and maintenance related services, expenditures can be  
22                 consolidated through a combination and typically contracted from fewer sources.  
23                 Cost savings are created by achieving a lower per unit cost for the service provided

1 due to a broader contract or the repackaging of work into more attractive options to  
2 the contractor. This work package realignment and volume purchasing of service is  
3 the primary method through which service procurement savings are realized.

4 **a. Materials and Services**

5 **Q. WHAT ARE THE COST SAVINGS AVAILABLE FROM COMBINED**  
6 **PROCUREMENT OF MATERIALS AND SUPPLIES?**

7 A. Procurement savings should result from larger purchasing volumes and the  
8 availability of greater purchasing power. Expected annual purchases for 2005 for  
9 Duke Power and Duke Energy corporate are estimated at approximately \$300 million,  
10 while for similar units of Cinergy it will be approximately \$203 million. Savings  
11 were estimated for each of the principal materials operating segments, *e.g.*,  
12 transmission and distribution, and represent a reduction in total materials costs from  
13 extending strategic sourcing across the broad range of operating categories. This  
14 amount was determined based on the experience of other companies, review of certain  
15 component per unit costs, management's knowledge of vendors and potential  
16 approaches to material standardization and vendor concentration. This strategic  
17 sourcing improvement reflects permanent economies of scale through lower unit  
18 costs. Total savings in materials and supplies increase from \$10 million in year one  
19 to \$19.5 by the end of the five-year period.

20 **Q. SHOULD ANY OF THESE AMOUNTS BE CAPITALIZED BY THE**  
21 **COMPANIES?**

22 A. Yes. Approximately 70% of the materials and supplies savings have been allocated to  
23 capital accounts based on the combined Company's estimated capitalization rate for

1 all materials and supplies. Once again, the levelized fixed charge rate was applied to  
2 convert the capital cost reductions into revenue requirement savings.

3 **b. Contract Services**

4 **Q. WHAT IS THE NATURE OF SAVINGS FROM CONTRACT SERVICES AS**  
5 **A RESULT OF THE MERGER AND HOW WERE THEY QUANTIFIED?**

6 A. Similar to consolidating materials and supplies purchasing volumes, the combined  
7 Company will be able to gain economies of scale from the aggregation of related  
8 work activities and increased purchasing power with service providers. Examples of  
9 these services include certain engineering, construction and maintenance services.

10 The savings estimate also is dependent upon future negotiations with  
11 contractors and is similar to those estimated in prior transactions and represents  
12 purchasing power savings across the broad range of these services. The total Duke  
13 Power and Duke Energy corporate contract services for 2005 is expected to be \$758  
14 million, while for similar units of Cinergy they are estimated at \$415 million. The  
15 combined Company thus should be able to achieve additional economies of scale and  
16 scope from improved sourcing across all their vendors.

17 Some contract services savings should be considered capital savings. A  
18 capitalization rate of 54% was used to allocate contract services expenditures to  
19 capital accounts. These savings amounts were then converted to revenue  
20 requirements savings using the levelized fixed charge rate. The total estimated annual  
21 savings from contract services increase from \$16.9 million in the first year to \$27.8  
22 million by the end of the five-year period.

1 **c. Inventory**

2 **Q. PLEASE DESCRIBE THE INVENTORY SAVINGS THAT HAVE BEEN**  
3 **IDENTIFIED.**

4 A. It is anticipated that the Companies will be able to extend their transmission and  
5 distribution inventory reorder cycle on a one-time basis reflecting the ability to share  
6 certain portions of inventory and by leveraging the inventory management process  
7 across the business. Duke Power has estimated 2005 materials and supplies inventory  
8 (excluding nuclear) of \$287 million while the Cinergy operating companies maintain  
9 \$106 million in inventory. Partial reduction of these amounts is expected to result in  
10 \$1.1 million in annual savings which represents the carrying cost associated with the  
11 reduction in inventory levels.

12 **Q. COULD THESE SUPPLY CHAIN SAVINGS BE ACHIEVED ABSENT A**  
13 **MERGER?**

14 A. No. These savings are predicated directly on the assumption that there is a merged  
15 company that has greater purchasing power.

16 **6. Coal Supply**

17 **Q. HOW CAN COST SAVINGS BE ACHIEVED IN THE AREA OF COAL**  
18 **PROCUREMENT AND WHAT ARE THE ESTIMATED SAVINGS?**

19 A. Coal supply savings may be realized as a result of a revised strategy for the combined  
20 entity when pursuing new coal contracts. Duke Power and Cinergy both have a  
21 number of contracts expiring over the near-term. On a combined basis, the  
22 Companies will have the opportunity to develop a new supply strategy for coal supply  
23 that will consider specifications, sourcing, terms and volumes. Coal supply savings

1 were estimated based on the differences in current supply source and prices on a  
2 stand-alone basis compared to how the expiring contract volumes could be obtained  
3 in the future. Steady-state savings in year three are estimated at \$8.3 million, with  
4 five-year savings totaling \$40.1 million.

5 **Q. COULD THESE SAVINGS BE ACHIEVED ABSENT A MERGER?**

6 A. No. These savings are predicated directly on the integration of the coal supply  
7 requirements planning and sourcing of the Companies which would not be  
8 accomplished in the absence of the merger.

9 **Q. ARE THE CATEGORIES OF SAVINGS IN THIS MERGER CONSISTENT**  
10 **WITH THOSE TYPICALLY IDENTIFIED IN UTILITY COMBINATIONS?**

11 A. Yes, they are. There are, however, certain factors unique to this merger that affect the  
12 nature and level of synergies available.

13 **Q. PLEASE ELABORATE ON THESE FACTORS.**

14 A. Several factors typically affect the nature and level of merger synergies expected in  
15 utility combinations. These include: relative size (of the Companies), relative cost  
16 position, location, capacity position, organization and management philosophy.  
17 Certain of these factors affect the quantified merger synergies in this merger:

- 18 • First, there are multiple service territories within Duke Power and the operating  
19 companies of Cinergy. Overlapping service territories could have provided  
20 additional savings opportunities *e.g.*, reduction in facilities and sharing of relevant  
21 proximate resources;
- 22 • Second, membership of the Cinergy operating companies as part of the Midwest  
23 Independent Transmission System Operator, Inc. (“Midwest ISO”), which

1            dispatches local generation for its members, largely eliminates the potential  
2            benefits from joint dispatch of the generation fleets;

- 3            • Third, Cinergy does not own or operate any nuclear plants. Accordingly, there is  
4            no counterpart organization to the almost 4,100 employees dedicated to the  
5            operations of Duke Power's nuclear fleet;
- 6            • Fourth, Duke Power is an electric only utility and does not have any gas  
7            distribution operations similar to that of the operating companies of Cinergy, thus  
8            there is no counterpart organization and the almost 450 gas distribution personnel  
9            of Cinergy would be unaffected by the merger;
- 10           • Fifth, Duke Power owns and maintains a much larger hydro operating  
11           organization than Cinergy, which means that approximately 200 electric personnel  
12           at Duke Power are largely unaffected by the merger;
- 13           • Sixth, the respective organizations are somewhat disparate in size with Duke  
14           Power being approximately 20% larger than Cinergy in the relevant comparable  
15           functions at the corporate, shared services and utility support and operations areas,  
16           and;
- 17           • Finally, the Companies have utilized outsourcing in different ways in their  
18           businesses which further reduces the level of affectable staffing. For example,  
19           Cinergy has outsourced approximately 60% of its information technology support  
20           requirements while Duke Energy utilizes in-house personnel and Duke Power has  
21           totally outsourced its meter reading needs while Cinergy performs the majority of  
22           this function in-house.

23           All of these differences affect the alignment and comparability of the staffing  
24           levels and costs of operations. Accordingly, each of these differences needed to be  
25           considered in determining the potential level of savings opportunities available from

1 the merger.

2 **Q. HOW DO THE DUKE ENERGY AND CENERGY MERGER COST SAVINGS**  
3 **COMPARE TO THOSE IN OTHER TRANSACTIONS?**

4 A. The anticipated cost savings from the merger of Duke Energy and Cinergy are within  
5 the range identified by other companies in other recent utility mergers. In particular,  
6 anticipated position reductions and non-fuel operations and maintenance (“O&M”)  
7 expense reductions were reviewed -- two categories that provide a useful basis for  
8 comparative assessment of relative merger-related cost savings.

9 The approximate 5.5% position reduction amount for the merger of Duke  
10 Energy and Cinergy reflects the estimated total number of position reductions  
11 (~1,000) compared to the total number of positions at both companies prior to the  
12 initiation of the merger (~18,000 which reflects all the functions of the utilities in  
13 place even with no counterpart organization). The 5.5% reduction amount falls below  
14 the average reduction figure of 8.3% and is limited by the lack of overlapping  
15 operations and certain operating composition differences between the Companies. In  
16 particular, none of the field workforce is affected by the combination, *i.e.*, work  
17 volumes will not be reduced, thus those positions directly responsible for safety,  
18 reliability or service quality will not be reduced as a result of the merger. There is  
19 opportunity for consolidating certain back-office utility operations support functions;  
20 however, this does not offset the geographic distance which limits the level of  
21 potential field related reductions.

22 Similarly, the non-fuel O&M reductions that will result from the merger are  
23 also below the average of the same publicly announced transactions. The differences



1 in the relevant resource scale and related spend explained above are the principal  
2 reasons for the disparity between Duke Energy and Cinergy merger O&M cost  
3 savings and the average cost savings from other recently proposed utility mergers and  
4 would be anticipated based on the specific facts of this transaction. This result is  
5 largely driven downward by the significant amount of field related generation,  
6 transmission and distribution O&M expense in the denominator that is not affected  
7 from this merger. And, the number and scale of functions where no overlap exists,  
8 such as nuclear, hydro and gas distribution, further impact the comparison in a  
9 downward manner. Although not all of the saving elements found in other prior  
10 mergers are available in this transaction the cost savings and cost avoidances related  
11 to the merger of Duke Energy and Cinergy reflect those typically found within my  
12 previous industry experience.

**VI. COSTS-TO-ACHIEVE AND PRE-MERGER INITIATIVES**

13 **Q. PLEASE DESCRIBE THE APPROACH TO ESTIMATING THE COSTS**  
14 **THAT WILL BE INCURRED WITH THE INTEGRATION OF THE TWO**  
15 **COMPANIES.**

16 A. Costs are incurred in all merger transactions from the process of combining the two  
17 entities and attaining the identified cost savings. These costs reflect out-of-pocket  
18 cash payments and usually are one-time payouts incurred as a result of the merger.

19 **Q. PLEASE EXPLAIN THE PROCESS BY WHICH THE COSTS-TO-ACHIEVE**  
20 **WERE ESTIMATED BY THE COMPANIES.**

21 A. The cost category analysis approach described above that was used to determine  
22 potential merger savings opportunities areas was also extended to the potential out-of-

1 pocket costs associated with realizing the savings and closing the transaction.  
2 Specific identification of employee related separation cost was undertaken to identify  
3 the various elements that could be expected to be incurred. The out-of-pocket costs  
4 that will be incurred in merger integration such as, systems integration, regulatory  
5 processes, facilities restacking, communication expenses and other miscellaneous  
6 expenses also were identified. The methodology used by the Companies to develop  
7 the costs-to-achieve estimates was comprehensive, and similar to that used by other  
8 companies in estimating such costs.

9 **Q. WHAT EXPENSES ARE ESTIMATED TO BE INCURRED TO MERGE THE**  
10 **COMPANIES?**

11 A. Costs-to-achieve, before allocation between the regulated and non-regulated  
12 segments, are estimated at \$513 million over the five-year period utilized, with the  
13 largest portion of these costs (\$443) to be incurred over the first three years beginning  
14 in 2005. Certain costs-to-achieve will continue into succeeding years as annual  
15 payments will be required for items such as licenses. These cost estimates are  
16 consistent with estimates made by companies in other similar prior transactions and  
17 reflect differences in scale and scope and the unique circumstances of this merger.

18 **Q. WHAT ARE THE PRIMARY COMPONENTS OF THE COSTS-TO-**  
19 **ACHIEVE THE ESTIMATED MERGER SAVINGS?**

20 A. The primary components used to estimate costs-to-achieve were separation costs  
21 (estimated to cost \$108.3 million), relocation costs (\$10.1 million), retention costs  
22 (\$25.0 million), systems integration (\$225.2 million), facilities integration (\$10  
23 million), internal and external communication expenses (\$22.9 million), regulatory

1 process and compliance costs (\$36.6 million), transition costs (\$22.2 million),  
2 Directors' and Officers coverage (\$11.4 million), and transaction costs (\$41.1  
3 million).

4 **Q. PLEASE DESCRIBE THE MEANS THE COMPANIES ANTICIPATE USING**  
5 **TO ACHIEVE THE ESTIMATED POSITION REDUCTIONS.**

6 A. A major component of the merger cost savings is the reduction in work force which is  
7 primarily due to the elimination of duplicative functions and tasks. These reductions  
8 are expected by the Companies to be achieved through a variety of means including  
9 attrition, controlled hiring, work force redeployment, work realignment, and through  
10 voluntary separation or early retirement. For these targeted separations, out-of-pocket  
11 costs will be incurred to achieve the total position reductions.

12 **Q. HOW WAS THE LEVEL OF COSTS-TO-ACHIEVE FOR POSITION**  
13 **REDUCTIONS CALCULATED?**

14 A. The estimate used for the severance package calculation was three weeks of base pay  
15 per year of service (assuming an average of 14 years), plus eighteen months of health  
16 benefits from the date of separation. The separation package was applied to average  
17 salaries in affected groups and reflects approximately one year of salary for  
18 employees. For displaced executives, standard contract arrangements were utilized  
19 based on years of service and relative compensation levels.

20 The severance related programs that affect employees and executives are to be  
21 more fully defined during the transition process based on additional considerations of  
22 the management and human resources philosophy of the combined company and  
23 more specific analysis on the timing and location of reduced positions. Total

1 separation costs are estimated at \$108.3 million. An additional amount of \$25.0  
2 million for employee retention has also been identified to secure valuable employees,  
3 such as in the information technology area, during the transition period.

4 **Q. EXPLAIN HOW RELOCATION COSTS WERE CALCULATED.**

5 A. To provide for efficient consolidation, certain functional areas will be centralized and  
6 thus require employee relocation to a new site. Based on the functional analysis, it  
7 was determined that a number of positions possibly would need to be relocated  
8 between the headquarters locations at an estimated cost of \$10.1 million. The full  
9 cost of the actual relocation package to be offered to eligible positions has not yet  
10 been determined, as it ultimately will depend on the number of personnel that will  
11 move. The components of a relocation program could include moving expenses,  
12 house hunting costs, cost of living differentials, and closing costs. These cost  
13 estimates are consistent with estimates made by companies in prior similar  
14 transactions.

15 **Q. EXPLAIN HOW SYSTEMS CONSOLIDATION AND TELE-**  
16 **COMMUNICATIONS NETWORKING COSTS WERE CALCULATED.**

17 A. Significant effort will be expended by the Companies in integrating the information  
18 technology and services functions of the Companies. A principal element of these  
19 costs will relate to integrating the diverse applications of the Companies. In  
20 addition, the voice, data and video networks will also need to be integrated through  
21 expanded telecommunications capabilities, the data centers will be consolidated and  
22 elements of the network such as servers will be rescaled to meet the needs of the  
23 business.

1           Given the very different technology environments and back-bone applications  
2 within each company, substantial effort will be made to align platforms, rationalize  
3 vendors and reduce overlap. Particularly, the areas of converting to Duke Energy's  
4 PeopleSoft system and moving to a common billing system will require focused  
5 attention and dedicated expenditure.

6           Integration costs for these areas were estimated at \$225.2 million over the  
7 five-year period with some continuing costs thereafter. These cost estimates cover  
8 contract programming, hardware change out and conversion, increased T-1 capacity,  
9 and outside assistance and reflect scale, complexity, and platform differences. These  
10 expenses associated with systems and communications integration are expected to  
11 principally be incurred in 2006 and 2007, but will carry through the full period to  
12 reflect additional hardware lease costs and licenses.

13 **Q. CAN YOU DESCRIBE THE REGULATORY PROCESS AND COMPLIANCE**  
14 **COSTS-TO-ACHIEVE RELATED TO THE MERGER?**

15 A. To successfully complete the merger, certain costs will be incurred for preparation  
16 and pursuit of regulatory filings, such as those related to The Securities and Exchange  
17 Commission, the Federal Energy Regulatory Commission, the Nuclear Regulatory  
18 Commission and the Department of Justice filings and the merger cases before the  
19 various state regulatory jurisdictions. In addition, certain costs were incurred to satisfy  
20 expanded compliance and fiduciary requirements, such as in due diligence. These  
21 costs will include professional services for legal, tax, accounting and consulting  
22 assistance and certain other filing related costs and fees. Regulatory process costs are  
23 estimated at \$36.6 million.

1 **Q. PLEASE DESCRIBE THE ESTIMATED INTERNAL AND EXTERNAL**  
2 **COMMUNICATIONS COSTS-TO-ACHIEVE.**

3 A. Communication expenses will arise from the need to disseminate merger information  
4 to the various stakeholders of the individual organizations and combined company.  
5 Informational brochures will be sent to employees, shareholders, rating agencies, and  
6 state and federal commissions to explain the specifics of the merger. The various  
7 vendors, supplier and contractors will also receive communications that addresses the  
8 merger and the manner in which contacts and business arrangements will be  
9 conducted. Additional costs will be incurred with respect to changing related  
10 infrastructure elements such as signage. These expenditures are estimated to cost  
11 \$22.9 million.

12 **Q. WHAT IS THE NATURE OF THE TRANSITION COSTS TO ACHIEVE?**

13 A. These costs capture the out-of-pocket travel costs of internal employees groups in  
14 accomplishing the integration and relate to air, lodging and per diem expense.  
15 Additional support costs from third-parties for consulting assistance through this  
16 process are also reflected in this category. These costs are estimated at \$22.2 million.

17 **Q. PLEASE DESCRIBE THE DIRECTOR AND OFFICERS COVERAGE.**

18 A. With separation from the Companies, an ongoing level of insurance expense will be  
19 incurred on behalf of the departing directors and officers. This expense is necessary  
20 to provide adequate coverage to these individuals in the event of subsequent litigation  
21 to which they could become a party in view of their previous position with the  
22 Companies. These amounts have been estimated at \$11.4 million and reflect a one-  
23 time premium incurrence.

1 **Q. WHAT TYPE OF FACILITIES COSTS WILL BE INCURRED WITH**  
2 **RESPECT TO THE TRANSACTION?**

3 A. The reduction in total staffing will free-up a certain amount of square footage  
4 currently utilized by the Companies. These incurred costs relate to the restacking of  
5 floor space to accommodate a different amount of total employees, by location, and  
6 cover related moves, refurbishment, construction and other leasehold improvements.  
7 These costs have been estimated at \$10 million to realign the separate corporate  
8 facilities maintained by the Companies.

9 **Q. PLEASE EXPLAIN THE TRANSACTION COST COMPONENT INCLUDED**  
10 **WITHIN THE TOTAL COSTS-TO-ACHIEVE.**

11 A. Transaction costs include amounts paid to the investment banks for assistance with  
12 certain aspects of the merger. These costs specifically relate to fees paid for  
13 assistance in transaction structuring and negotiation and the provision of a fairness  
14 opinion to satisfy the needs of the Boards of Directors. Total transaction fees are  
15 estimated at \$41.1 million for the above categories.

16 **Q. PLEASE DESCRIBE THE APPROACH USED TO QUANTIFY THE PRE-**  
17 **MERGER INITIATIVES OVERLAP ADJUSTMENT INCLUDED AS PART**  
18 **OF THE NET MERGER SAVINGS QUANTIFICATION?**

19 A. Discussions with company management led to the identification of certain specific and  
20 existing cost reduction programs within Cinergy that needed to be recognized to avoid  
21 double-counting in the synergies estimation process. The Cinergy cost reduction  
22 program, CIN-10, estimated savings of \$44 million in 2005 and an additional \$25  
23 million in 2006. These implied cost reductions could be achieved in a variety of

1 means, such as through process improvement, reengineering, outsourcing, work  
2 elimination or contractor management; however, it was assumed that each individual  
3 business unit, such as corporate, shared services, delivery, fossil and nuclear would  
4 realize a pro-rata share of these reductions through a combination of the above  
5 methods. To avoid potential duplication with merger-related savings and CIN-10  
6 program savings, I reduced the total merger-related savings to reflect any potential  
7 overlap with potential CIN-10 initiatives. Although Duke Energy is continuously  
8 working to control costs, no adjustments for specific initiatives were identified to  
9 avoid potential double-counting of these programs with respect to the identified  
10 merger cost savings.

11 **Q. HOW WAS THIS DECLINE RELATED TO THE MERGER SAVINGS?**

12 A. Total estimated O&M savings in year five are \$248 million, or 7.3% of the forecasted  
13 year five O&M. This amount was assumed to apply across the various operating  
14 entities that contributed to the overall savings on a weighted basis reflecting their  
15 relative cost levels. Accordingly, the total cost savings were reduced to reflect the  
16 assumption that some of the planned cost reductions of Cinergy would affect the  
17 starting cost baseline for the synergies analysis. In effect, the planned cost reduction  
18 initiative of Cinergy is assumed to overlap at the same level as the identified merger  
19 savings affect the initial baseline. This reflects the fact that the planned cost  
20 reduction of Cinergy applied to a broader cost base than was affected by the merger,  
21 e.g., customer service offices. As a result of this calculation, I assumed that there  
22 would be overlap between the merger-related savings and CIN-10 initiatives in  
23 proportion to the merger savings impact on the total cost baseline, or \$1.9 million in



1 the first year and growing to roughly \$2.1 million by the last year of the quantification  
2 period.

3 **Q. WHAT IS THE RESULTING PRE-MERGER INITIATIVES OVERLAP**  
4 **ADJUSTMENT TO THE MERGER SAVINGS BASED ON THE**  
5 **METHODOLOGY JUST DESCRIBED?**

6 A. Based on this approach, we have adjusted the five year merger savings downward by  
7 \$10 million over five years to reflect the estimated overlap between the merger  
8 savings and Cinergy's stand alone planned cost reduction programs associated with  
9 CIN-10.

#### **VII. CONCLUSION**

10 **Q. BASED UPON YOUR EXPERIENCE ARE THE SAVINGS IDENTIFIED BY**  
11 **THE COMPANIES ATTAINABLE ?**

12 A. Yes. Based upon my experience with other mergers and upon my interaction with  
13 executives and middle management at both Companies the methodology used to  
14 estimate potential savings is consistent with that usually adopted by other companies  
15 in similar situations. The cost savings and costs-to-achieve that have been identified  
16 are reasonably attainable provided that the management of the companies integrate  
17 operations in a manner consistent with their plans and with similar processes used by  
18 other companies in similar transactions.

19 **Q. WERE ATTACHMENTS TJF-1 THROUGH TJF-3 PREPARED BY YOU OR**  
20 **UNDER YOUR SUPERVISION?**

21 A. Yes, they were.

22 **Q. DOES THIS CONCLUDE YOUR PREPARED DIRECT TESTIMONY?**

1 A. Yes, it does.

**VERIFICATION**

State of Texas                    )  
  )        SS:  
County of Dallas                )

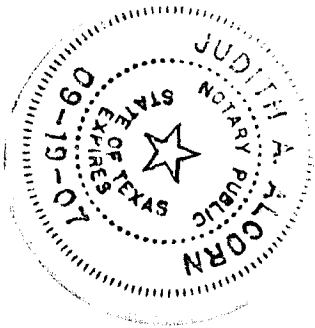
The undersigned, Thomas J. Flaherty, being duly sworn, deposes and says that he is the Senior Vice President, Booz Allen Hamilton, Inc., and that the matters set forth in the foregoing testimony are true and correct to the best of his information, knowledge and belief.

*Thomas J. Flaherty*  
\_\_\_\_\_  
Thomas J. Flaherty, Affiant

Subscribed and sworn to before me by Thomas J. Flaherty on this 27<sup>th</sup> day of June, 2005.

*Judith A. Alcorn*  
\_\_\_\_\_  
NOTARY PUBLIC

My Commission Expires: 9-19-07



**EXHIBIT TJF 1: SUMMARY OF REGULATED UTILITY EXPERIENCE**

Alaska Public Utilities Commission  
- Anchorage Sewer Utility

Arizona Corporation Commission  
- U S WEST Communications - Docket No. E-1051-88-146

Arkansas Public Service Commission  
- FPL Group, Entergy Corporation, WCB Holding corp. and Entergy Arkansas, Inc. – Docket No. 00-329U

Beaumont, Texas  
- Entex, Inc.  
- Gulf States Utilities Company

California Public Utilities Commission  
- The Washington Water Power Company and Sierra Pacific Power Company - Application No. 94-08-043  
- Pacific Enterprises and ENOVA Corporation - Application No. A-96-10-038

Clark County  
- Washington Public Power Supply

District of Columbia, Public Service Commissions  
- Baltimore Gas and Electric Company and Potomac Electric Power Company - Formal Case No. 951

Colorado Public Utilities Commission

- Public Service Company of Colorado and Southwestern Public Service Company - Docket No. 95A-513EG
- Delaware Public Service Commission
- Atlantic City Electric Company and Delmarva Power & Light Company - Docket No. 97-65

Federal Energy Regulatory Commission

- Baltimore Gas and Electric Company and Potomac Electric Power Company - Docket No. EC96-10-000
- IES Utilities Inc., Interstate Power Company, Wisconsin Power & Light Company, South Beloit Water, Gas & Electric Company, Heartland Energy Services and Industrial Energy Applications, Inc. - Docket No. EC96-13-000
- Trans-Alaska Pipeline System - Docket No. OR78-1
- Middle South Energy, Inc. - Docket No. ER-82-483-000
- Middle South Energy, Inc. - Docket No. ER-82-616-000
- Kansas Power and Light Company and Kansas Gas and Electric Company - Docket No. EC91-2-000
- Southwestern Public Service Company and Public Service Company of Colorado - Docket No. EC96-2-000
- The Washington Water Power Company and Sierra Pacific Power Company - Docket No. EC94-23-000
- Northern States Power Company and Wisconsin Energy Corporation - Docket Nos. EC95-16-000 and ER95-1357-000
- Midwest Power Systems Inc. and Iowa-Illinois Gas and Electric Company - EC95-4
- Ohio Edison Company, Pennsylvania Power Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company - ER97-412-000
- Atlantic City Electric Company and Delmarva Power & Light Company - EC97-7
- Union Electric and Central Illinois Public Service Company - EC-96-7-000

Federal Power Commission

- Organization and Operations Review

Florida Public Service Commission

- Florida Power & Light Company and Entergy Corporation - Docket No. 001148

- Garland, Texas
  - General Telephone Company of the Southwest
  - Lone Star Gas Company
- Georgia Public Service Commission
  - Georgia Power Company - Docket No. 3673-U
- Houston, Texas
  - Houston Lighting & Power Company
- Idaho Public Utilities Commission
  - The Washington Water Power Company and Sierra Pacific Power Company - Case Nos. WWP-E-94-7 and WWP-G-94-4
- Illinois Commerce Commission
  - Illinois Power - Docket No. 84-0055
  - Iowa-Illinois Gas and Electric Company and Mid-American Company Energy - Docket No. 94-0439
  - Central Illinois Public Service Company, CIPSCO Incorporated and Union Electric Company - Docket No. 95-0551
- Iowa Utilities Board
  - Midwest Resources Inc., Midwest Power Systems Inc. and Iowa-Illinois Gas and Electric Company - Docket No. SPU-94-14
  - IES Industries Inc., Interstate Power Company, WPL Holdings, Inc. - Docket No. SPU-96-6
- Iowa Electric Light and Power
  - Organization and Operations Review
- Kansas Corporation Commission
  - Southwestern Bell Telephone Company - Docket Nos. 117,220-U and 123,773-U
  - Kansas Gas & Electric - Docket No. 120,924-U
  - Kansas Power and Light Company and Kansas Gas and Electric Company - Docket No. 174,155-U
  - Western Resources and Kansas City Power and Light - Docket No. 190,362-U

- Western Resources, Inc. and Kansas City Power and Light - Docket No. 97-WSRE-676-MER
- Kentucky Public Service Commission
  - Louisville Gas & Electric Company - Case Nos. 5982, 6220, 7799, 8284, 8616 and 8924
  - South Central Bell Telephone Company - Case Nos. 6848, 7774 and 8150
  - Kentucky-American Water Company - Case No. 8571
- Louisiana Public Service Commission
  - American Electric Power Company, Inc., Southwestern Electric Power Company and Central and South West Corporation – Docket No. U-23327
  - Entergy Louisiana, Inc. and Entergy Gulf States, Inc. Merger with FPL Group, Inc. – Docket No. U-25354
- Maryland, Public Service Commission of
  - Baltimore Gas and Electric Company and Potomac Electric Power Company – Order No. 73405, Case No. 8725
- Massachusetts Department of Telecommunications and Energy
  - Boston Edison, Cambridge Electric Light Company, Commonwealth Electric Company and Commonwealth Gas Company – Docket D.T.E. 99-19
- Michigan Public Service Commission
  - Wisconsin Electric Power Company and Northern States Power Company - Case No. U-10913
- Minnesota Public Service Commission
  - Continental Telephone Company - Docket No. PR-121-1
  - Northern States Power Company - Docket No. E002/GR-89-865
  - Northern States Power Company and Wisconsin Energy Corporation - Docket No. E,G002/PA-95-500
- Mississippi Public Service Commission
  - Mississippi Power & Light Company - Docket No. U-4285
  - Entergy Mississippi, Inc., Entergy Corporation, FPL Group, Inc. and WCB Holding Corporation – Docket No. 2000-UA-925

- Missouri Public Service Commission
  - Union Electric Company - Case Nos. ER-84-168 and EO-85-17
  - Union Electric Company and Central Illinois Public Service Company - Case No. EM-96-149
  - Kansas City Power & Light Company - Case Nos. ER-85-128 and EO-85-185
  - Kansas Power and Light Company and Kansas Gas and Electric Company - Case No. EM-91-213
  - Southwestern Bell Telephone - Case No. TC-93-224
  - Western Resources and Kansas City Power and Light – EM 97-515
- Nevada Public Service Commission
  - Bell Telephone Company of Nevada - Docket No. 425
  - Central Telephone Company - Docket No. 91-7026
  - The Washington Water Power Company and Sierra Pacific Power Company - Docket No. 94-8024
- New Jersey Board of Public Utilities
  - Atlantic City Electric Company and Delmarva Power & Light Company - Docket No. EM-97-020103
- New Mexico Public Service Commission
  - Public Service Company of New Mexico
  - Southwestern Public Service Company and Public Service Company of Colorado - Case No. 2678
- New Mexico State Corporation Commission
  - Continental Telephone of the West - Docket No. 942
  - General Telephone Company of the Southwest - Docket Nos. 937 and 990
  - Mountain States Telephone and Telegraph Company - Docket Nos. 943, 1052 and 1142
  - U S WEST Communications - Docket No. 92-227-TC
- New Orleans, Louisiana
  - New Orleans Public Service Company
- New York, State of, Public Service Commission
  - Long Island Lighting Company and Brooklyn Union Gas Company - Case 95-G-0761



- Ohio Public Utilities Commission
  - Ohio Bell Telephone Company - Case No. 79-1184-TP-AIR
  - Cleveland Electric Illuminating Company
- Oklahoma Corporation Commission
  - Organization and Operations Review
  - Southwestern Bell Telephone Company - Cause No. 26755
  - Public Service Company of Oklahoma - Cause Nos. 27068 and 27639
  - Southwestern Bell Telephone Company - Cause No. 000662
  - American Electric Power Company, Inc., Public Service Company of Oklahoma and Central and South West Corporation - Cause No. PUD-980000444
- Oregon, Public Utility Commission of
  - Pacific Power and Light Company - Revenue Requirements Study
  - Portland General Electric Company - Revenue Requirements Study
  - The Washington Water Power Company and Sierra Pacific Power Company - Docket No. UM-696
- Riverside, City of
  - San Onofre Nuclear Generating Station
- Sherman, Texas
  - General Telephone Company of the Southwest
- Tennessee Public Service Commission
  - United Inter-Mountain Telephone Company - Docket Nos. U-6640, U-6988 and U-7117
- Texas Attorney General
  - Southwestern Bell Telephone Company

- Texas, Public Utility Commission of
  - Texas Power & Light Company - Docket Nos. 178 and 3006
  - Southwestern Bell Telephone Company - Docket Nos. 2672, 3340, 4545 and 8585
  - Houston Lighting & Power Company - Docket Nos. 2448, 5779 and 6668
  - Lower Colorado River Authority - Docket No. 2503
  - Gulf States Utilities Company - Docket No. 2677
  - General Telephone Company of the Southwest - Docket Nos. 3094, 3690 and 5610
  - Central Telephone Company - Docket No. 9981
  - Southwestern Public Service Company and Public Service Company of Colorado - Docket No. 14980
  - FPL Group, Inc. and Entergy Corporation – Docket No. 23335
  - Reliant Energy HL&P – Docket No. 22355
- Utah Public Service Commission
  - Utah Power and Light Company - Docket No. 76-035-06
- Vermont Public Service Board
  - New England Telephone and Telegraph Company - Docket Nos. 3806 and 4546
- Waco, Texas
  - Texas Power & Light Company
- Washington Utilities and Transportation Commission
  - The Washington Water Power Company and Sierra Pacific Power Company - Docket No. UE-94-1053 and UE-94-1054
  - Puget Sound Power and Light Company and Washington Natural Gas Company – UE-960195
- Washington Metropolitan Area Transit Authority
  - D.C. Transit
- Wisconsin Public Service Commission
  - Northern States Power Company and Wisconsin Energy Corporation – 6630-UM-100 and 4220-UM-101

- WPL Holdings, IES Industries Inc., Interstate Power Company, Inc. - Docket No. 6680-UM-100

Wyoming Public Service Commission

- Cheyenne Light, Fuel and Power Company (Southwestern Public Service Company and Public Service Company of Colorado) - Docket Nos. 20003-EA-95-40 and 30005-GA-95-39
- Mountain States Telephone and Telegraph Company - Docket No. 9343, Subs. 5 and 9
- Organization and Operations Review
- Pacific Power and Light Company - Docket No. 9454, Sub. 11

**Overall Cost Savings**

**5 Year Total Potential Savings Summary (O&M/Revenue Requirements)**  
 (Before Allocation)

Potential Areas (\$ in 000s)	Year 1 2006	Year 2 2007	Year 3 2008	Year 4 2009	Year 5 2010	Five-year Total
<b>Regulated and Corporate</b>						
Staffing						
Corporate	\$46,434	\$69,270	\$78,965	\$82,854	\$86,915	\$364,438
Utility	\$12,981	\$26,884	\$31,346	\$34,050	\$36,873	\$142,134
<b>Total</b>	<b>\$59,415</b>	<b>\$96,154</b>	<b>\$110,311</b>	<b>\$116,904</b>	<b>\$123,788</b>	<b>\$506,572</b>
<b>Corporate &amp; Administrative Programs</b>						
Administrative & General Overhead	\$5,466	\$7,916	\$8,975	\$9,183	\$9,396	\$40,937
Association Dues	\$746	\$763	\$781	\$799	\$817	\$3,906
Benefits	\$0	\$8,128	\$8,862	\$9,662	\$10,534	\$37,186
Directors' Fees	\$795	\$813	\$832	\$851	\$871	\$4,163
Facilities	\$3,113	\$4,508	\$5,112	\$5,230	\$5,351	\$23,315
Insurance	\$5,548	\$5,676	\$5,808	\$5,943	\$6,081	\$29,055
Inventory	\$2,145	\$1,090	\$1,090	\$1,090	\$1,090	\$6,505
Professional Services	\$40,238	\$42,009	\$43,857	\$45,787	\$47,801	\$219,692
Shareholder Services	\$1,805	\$1,847	\$1,890	\$1,934	\$1,979	\$9,456
Transportation	\$738	\$755	\$772	\$790	\$808	\$3,863
<b>Total</b>	<b>\$60,594</b>	<b>\$73,506</b>	<b>\$77,979</b>	<b>\$81,269</b>	<b>\$84,730</b>	<b>\$378,077</b>
<b>Information Technology</b>						
Information Technology (Capital)	\$3,464	\$9,223	\$17,317	\$26,092	\$36,149	\$92,246
Information Technology (O&M)	\$12,548	\$19,666	\$26,767	\$32,846	\$36,247	\$128,072
<b>Total</b>	<b>\$16,011</b>	<b>\$28,889</b>	<b>\$44,084</b>	<b>\$58,937</b>	<b>\$72,396</b>	<b>\$220,318</b>
<b>Supply Chain</b>						
Contract Services	\$16,917	\$19,545	\$22,234	\$24,986	\$27,801	\$111,483
M&S Purchases	\$9,972	\$12,279	\$14,641	\$17,057	\$19,529	\$73,477
<b>Total</b>	<b>\$26,888</b>	<b>\$31,824</b>	<b>\$36,875</b>	<b>\$42,043</b>	<b>\$47,330</b>	<b>\$184,960</b>
<b>Fuel</b>						
Coal	\$6,992	\$7,642	\$8,296	\$8,489	\$8,686	\$40,106
	\$6,992	\$7,642	\$8,296	\$8,489	\$8,686	\$40,106
<b>Gross Corporate and Regulated Savings</b>	<b>\$169,901</b>	<b>\$238,016</b>	<b>\$277,546</b>	<b>\$307,642</b>	<b>\$336,929</b>	<b>\$1,350,034</b>

Costs to Achieve Elements

Costs-to-Achieve	Year 1 2006	Year 2 2007	Year 3 2008	Year 4 2009	Year 5 2010	Five-year Total
Separation Costs	\$67,552	\$31,761	\$8,945	\$0	\$0	\$108,259
Retention Costs	\$12,500	\$12,500	\$0	\$0	\$0	\$25,000
Relocation Costs	\$5,063	\$5,063	\$0	\$0	\$0	\$10,125
System Integration Costs	\$39,755	\$66,577	\$49,383	\$34,723	\$34,744	\$225,182
Directors & Officers Liability Tail Coverage	\$11,400	\$0	\$0	\$0	\$0	\$11,400
Regulatory Process Costs	\$36,578	\$0	\$0	\$0	\$0	\$36,578
Facilities Integration	\$5,000	\$5,000	\$0	\$0	\$0	\$10,000
Internal / External Communications	\$22,850	\$0	\$0	\$0	\$0	\$22,850
Transition Costs	\$18,862	\$3,329	\$0	\$0	\$0	\$22,191
Transaction Cost	\$41,100	\$0	\$0	\$0	\$0	\$41,100
<b>Total</b>	<b>(\$260,660)</b>	<b>(\$124,229)</b>	<b>(\$58,328)</b>	<b>(\$34,723)</b>	<b>(\$34,744)</b>	<b>(\$512,684)</b>



**COMMONWEALTH OF KENTUCKY**

**BEFORE THE PUBLIC SERVICE COMMISSION**

In the Matter of:

Joint Application of Duke Energy Corporation, )  
Duke Energy Holding Corp., Deer Acquisition )  
Corp., Cougar Acquisition Corp., Cinergy Corp., )  
The Cincinnati Gas & Electric Company, and )  
The Union Light, Heat and Power Company for )  
Approval of a Transfer and Acquisition )  
of Control )

Case No. 2005-00228

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**DIRECT TESTIMONY OF**

**GREGORY C. FICKE**

**ON BEHALF OF**

**JOINT APPLICANTS**

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**APPENDIX**

ATTACHMENT GCF-1 -	Merger Commitments
ATTACHMENT GCF-2 -	Detailed Description of Transaction



## **I. INTRODUCTION AND PURPOSE**

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Gregory C. Ficke, and my business address is 139 East Fourth Street,  
3 Cincinnati, Ohio 45202.

4 **Q. WHAT IS YOUR CURRENT POSITION?**

5 A. I am Vice President of Cinergy Services, Inc. (“Cinergy Services”), President of  
6 The Union Light, Heat and Power Company (“ULH&P”), and President of The  
7 Cincinnati Gas & Electric Company (“CG&E”), both subsidiaries of Cinergy  
8 Corp. (“Cinergy”). I also serve on CG&E’s and ULH&P’s Board of Directors,  
9 and on the Board of Cinergy Foundation.

10 **Q. PLEASE SUMMARIZE YOUR EDUCATION AND PROFESSIONAL**  
11 **QUALIFICATIONS.**

12 A. I received a Bachelor of Science degree in physics from Miami University, a  
13 Master of Science degree in engineering from Ohio State University, a Master of  
14 Business Administration degree in finance from the University of Cincinnati, and  
15 a Juris Doctorate degree from Salmon P. Chase College of Law at Northern  
16 Kentucky University. I am a registered professional engineer and a member of  
17 the Ohio Bar. I have also completed various management development programs,  
18 including the Advanced Management Program at Harvard University Business  
19 School. I have held various management positions since joining CG&E in 1977,  
20 including General Manager – Environmental Services, Vice President – Gas  
21 Operations, and Vice President and Chief Information Officer for Cinergy Corp.’s  
22 Regulated Businesses Unit.

1 **Q. PLEASE SUMMARIZE YOUR RESPONSIBILITIES AS PRESIDENT OF**  
2 **ULH&P.**

3 A. I am a member of Cinergy's executive management team, with whom I share  
4 responsibility for the overall direction and strategy of ULH&P. As President of  
5 ULH&P, I am charged with ensuring that gas and electricity are reliably supplied  
6 to ULH&P's customers at reasonable costs. Additionally, I share responsibility  
7 for regulatory and financial planning for ULH&P, including achieving timely  
8 recovery of expenditures made to provide service to ULH&P's customers, and  
9 achieving reasonable returns on such expenditures. Finally, I also have primary  
10 responsibility for ULH&P's customer, community, economic development,  
11 regulatory, and governmental relations.

12 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**  
13 **PROCEEDING?**

14 A. My testimony focuses generally on how the impending merger of Duke Energy  
15 Corporation ("Duke Energy") and Cinergy will affect ULH&P and its customers.  
16 I focus on the key areas of: (1) reliability and safety; (2) customer service; (3)  
17 merger-related cost savings / rate impacts; (4) financial integrity; (5) economic  
18 development; (6) charitable giving; and (7) environmental stewardship. Several  
19 of these areas are discussed in more detail in the testimony of other witnesses as  
20 noted herein. My testimony also provides an overview of the affiliate transactions  
21 that ULH&P is filing with the Commission. Finally, I sponsor a list of  
22 commitments ULH&P is willing to make in connection with this merger, which I  
23 provide at Attachment GCF-1. These proposed merger commitments, as well as

1 other commitments proposed by various witnesses in this case (including a  
2 commitment to share net merger savings with consumers upfront) are virtually  
3 identical to proposals being made by ULH&P's utility affiliates in Ohio and  
4 Kentucky. In addition, I have attached as Attachment GCF-2 a detailed  
5 description of the Cinergy / Duke Energy merger transaction.

**II. OVERVIEW OF CINERGY'S AND ULH&P'S  
STRUCTURE AND OPERATIONS**

6 **Q. PLEASE DESCRIBE ULH&P'S RELATIONSHIP TO CINERGY.**

7 A. ULH&P is a wholly-owned subsidiary of CG&E, which is a wholly-owned  
8 subsidiary of Cinergy. Cinergy was formed in 1994 by the merger of CG&E and  
9 PSI Resources, Inc., the former parent company of PSI Energy, Inc. ("PSI").  
10 Cinergy, CG&E and ULH&P are headquartered in Cincinnati, Ohio. CG&E  
11 provides electric and gas utility service in the Cincinnati metropolitan area. PSI,  
12 ULH&P's affiliate, provides electric utility service throughout a large portion of  
13 Indiana and is headquartered in Plainfield, Indiana.

14 Cinergy is a registered public utility holding company under the Public  
15 Utility Holding Company Act of 1935 ("PUHCA"). Cinergy maintains a service  
16 company, Cinergy Services, Inc., which provides Cinergy's subsidiaries,  
17 including ULH&P, with a variety of centralized administrative, management, and  
18 support services, under a Service Agreement.

19 **Q. HOW WILL THIS STRUCTURE CHANGE WITH THE MERGER OF**  
20 **DUKE ENERGY AND CINERGY?**

21 A. ULH&P will continue to exist as a separate and distinct Kentucky corporation and  
22 public utility company subsidiary of CG&E. However, Cinergy and Duke Energy

1 will become part of a new holding company to be named Duke Energy  
2 Corporation (“New Duke Energy”). ULH&P’s new, larger ultimate parent  
3 company will have a broader knowledge base and an increased number of  
4 employees corporate-wide, which will have a positive impact on ULH&P and its  
5 customers, employees and the communities it serves.

6 **Q. PLEASE EXPLAIN THE RECENT LEGISLATIVE CHANGES RELATED**  
7 **TO PUHCA.**

8 A. I understand that both the U.S. Senate and the U.S. House of Representatives have  
9 passed a comprehensive Energy Bill which is expected to be signed into law by  
10 the President. Among other things, the Energy Bill provides for the repeal of  
11 PUHCA six months after enactment. As such, the Securities and Exchange  
12 Commission (“SEC”) will no longer have regulatory authority over public utility  
13 holding company systems like Cinergy and the New Duke Energy, and the  
14 companies do not intend to file for SEC approval of the merger under PUHCA.  
15 Despite PUHCA’s repeal, ULH&P still plans on entering into service agreements  
16 and other affiliate agreements that would have been subject to SEC approval but  
17 for the repeal of PUHCA, as described later in my testimony. Moreover, as  
18 described in the testimony of Ms. Wendy L. Aumiller, despite the repeal of  
19 PUHCA, ULH&P is proposing a number of commitments to assure the continued  
20 financial integrity of ULH&P.

21 **Q. WILL THE MERGER AFFECT THIS COMMISSION’S ABILITY TO**  
22 **REGULATE ULH&P?**

1 A. No. ULH&P will continue to be regulated by this Commission to the same extent  
2 it is today. ULH&P will also continue to be regulated by the Federal Energy  
3 Regulatory Commission (“FERC”).

4 **Q. PLEASE DESCRIBE ULH&P’S MISSION AND WHETHER IT WILL BE**  
5 **AFFECTED BY THE MERGER.**

6 A. Our mission is to provide our customers with safe, reliable and high quality gas  
7 and electric service at reasonable prices; to earn a fair return for our investors; to  
8 provide a challenging, rewarding, and safe workplace for our employees; to  
9 positively impact the many Northern Kentucky communities we serve; and to be  
10 environmentally responsible in how we go about our business.

11 We strive to be the energy supplier of choice, the investment of choice, the  
12 employer of choice, and a leader by choice. And we are committed to achieving  
13 these goals through careful and purposeful stewardship of our business, for the  
14 benefit of our stakeholders.

15 Importantly, ULH&P’s mission will not change as a result of the merger.  
16 Mr. James E. Rogers will be the CEO of the New Duke Energy, and we do not  
17 foresee any significant management changes within CG&E or ULH&P as a result  
18 of the merger. Further, Duke Energy has goals and a corporate culture that are  
19 very similar to Cinergy’s, including similar views on issues such as valuing all  
20 stakeholders, providing reliable, cost effective and efficient utility and customer  
21 service, and sustainability and environmental stewardship.

22 **Q. PLEASE DESCRIBE ULH&P’S GAS AND ELECTRIC UTILITY**  
23 **SYSTEM AND OPERATIONS.**

1 A. ULH&P purchases, sells, stores and transports natural gas in Boone, Campbell,  
2 Gallatin, Grant, Kenton and Pendleton Counties, Kentucky. ULH&P also  
3 purchases electricity, which it distributes and sells in Boone, Campbell, Grant,  
4 Kenton and Pendleton Counties, Kentucky. ULH&P serves approximately  
5 145,000 retail gas and electric customers and its service territory for electricity,  
6 gas, or both, covers approximately 2,171 square miles.

7 CG&E is in the process of transferring 1,105 megawatts of generating  
8 capacity to ULH&P, consisting of CG&E's 69% share of East Bend No. 2, a 648  
9 MW base load, coal-fired generating unit located in Rabbit Hash, Kentucky,  
10 Miami Fort No. 6, a 168 MW intermediate load, coal-fired generating unit located  
11 in North Bend, Ohio, and the 490 MW Woodsdale Generating Station, consisting  
12 of six peak load, gas or propane-fired generating units located in Trenton, Ohio.  
13 This Commission and the FERC have approved the transfer, and ULH&P is  
14 waiting for approval from the SEC. ULH&P plans for the closing to occur  
15 effective October 1, 2005. Additionally, ULH&P has an office and customer  
16 service center in Newport, Kentucky; operational facilities in Covington and  
17 Florence, Kentucky; a propane storage facility in Erlanger, Kentucky; and various  
18 facilities in Cincinnati, Ohio.

19 **Q. PLEASE EXPLAIN HOW THE MERGER OF CENERGY AND DUKE**  
20 **ENERGY WILL AFFECT ULH&P'S OPERATIONS AND**  
21 **MANAGEMENT.**

22 A. ULH&P's utility operations are not expected to be substantially impacted by the  
23 merger. However, some limited job reductions will be necessary to achieve more

1 efficient, lower cost operations. As explained in the testimony of Mr. Thomas J.  
2 Flaherty, about half of the benefits of the merger relate to consolidation of Duke  
3 Energy's and Cinergy's non-regulated operations and the allocable portion of  
4 their corporate and shared services organizations. Of the benefits that will flow to  
5 utility operations, cost savings are expected through the consolidation of  
6 corporate and headquarters functions, utility support functions, corporate and  
7 administrative programs, information technology, supply chain and some fuel  
8 savings.

9 Because Duke Energy's electric utility company, Duke Power, is not  
10 located adjacent to ULH&P's electric service territory (as PSI's service territory  
11 is adjacent to CG&E's), the merger will not create much duplication of field  
12 service employees responsible for the day-to-day operations of ULH&P's  
13 generation, transmission, distribution and customer service functions. As a result,  
14 ULH&P does not expect major utility operational changes due to the merger and  
15 the expected labor reductions will not negatively affect customer service or  
16 reliability functions.

17 The merger will have no impact on ULH&P's status as a Kentucky  
18 corporation, with its own board of directors, president and other corporate  
19 officers.

20 **Q. PLEASE EXPLAIN HOW THE MERGER OF CINERGY AND DUKE**  
21 **ENERGY WILL AFFECT ULH&P'S LOCAL PRESENCE.**

22 **A.** ULH&P will maintain a local presence throughout its Northern Kentucky service  
23 territory. ULH&P's corporate headquarters will remain in Cincinnati, Ohio, and

1 ULH&P will maintain a presence in Northern Kentucky through various field  
2 customer service and operational offices. The merger savings calculated by  
3 Mr. Thomas J. Flaherty did not assume any local field customer service or  
4 operational office closings. Below, I discuss ULH&P's continuing commitment  
5 to economic development and charitable giving. The merger will not have an  
6 adverse impact on ULH&P's local presence in Northern Kentucky.

### III. RELIABILITY AND SAFETY

7 **Q. PLEASE DESCRIBE HOW THE MERGER WILL IMPACT ULH&P'S**  
8 **RELIABILITY OF SERVICE AND SAFETY.**

9 A. ULH&P is and will remain committed to providing reliable gas and electric  
10 service. The testimony of Mr. John C. Procario describes how ULH&P has  
11 consistently proven its commitment to reliable gas and electric service in the past.  
12 For instance, ULH&P has consistently excelled in the region for emergency  
13 planning and service restoration after major storms and Cinergy won the Edison  
14 Electric Institute's Emergency Assistance award in 2004. Likewise, Duke  
15 Energy, through Duke Power, is committed to providing reliable electric utility  
16 service to its customers in the Carolinas. In 2004, the Catawba Nuclear Station set  
17 a new company reliability record, operating for 531 continuous days, and was  
18 recognized by the Nuclear Regulatory Commission for safe operations. Duke  
19 Power is a two-time winner of the Edison Electric Institute's Emergency  
20 Response award, winning in 2003 for outstanding efforts regarding a massive ice  
21 storm affecting almost all of Duke Power's service territory. It is clear that Duke



1 Energy, like ULH&P, knows that efforts like these are the first priorities for an  
2 energy provider, as described further in the testimony of Mr. Richard J. Osborne.

3 This shared commitment to providing reliable service leads me to  
4 conclude that reliability will continue to be a top priority for the merged company.  
5 As Mr. Procario explains, the changes expected from the merger will not  
6 adversely impact reliability.

7 Finally, Mr. Procario discusses how the ULH&P has committed to report  
8 its reliability scores to the Commission following the merger. Therefore, the  
9 Commission will be able to review these reports to assure itself of ULH&P's  
10 continued commitment to reliable service. ULH&P's commitment to continued  
11 reliability will remain a top priority for the New Duke Energy. Likewise, Cinergy  
12 and Duke Energy are both committed to providing safe electric and gas service to  
13 customers and employees. That focus will not change as a result of the merger.

#### IV. CUSTOMER SERVICE

14 **Q. WHAT ARE ULH&P'S GOALS WITH RESPECT TO UTILITY**  
15 **OPERATIONAL PERFORMANCE AND CUSTOMER SATISFACTION?**

16 **A.** Our goals are to deliver dependable and efficient electric utility service at  
17 reasonable prices, and to provide our customers with accessible and convenient  
18 customer service options while maintaining low costs. Our continuing challenge  
19 is to be one of the few gas and electric utility companies that achieves operational  
20 excellence in terms of service and reliability, with highly satisfied customers,  
21 while also managing to keep our costs and rates low.

1   **Q.   HOW HAS ULH&P PERFORMED IN TERMS OF PROVIDING HIGH**  
2   **QUALITY CUSTOMER SERVICE?**

3   A.   By all indications, ULH&P’s performance in customer service is strong. ULH&P  
4   has a history of providing excellent service across its various customer groups and  
5   has received acknowledgment from several independent entities concerning this  
6   performance. Examples of this recognition provided to Cinergy and ULH&P  
7   include:

- 8       •    The first energy company in the nation to be recognized as a J.D. Power  
9       and Associates Certified Call Center for providing “An Outstanding  
10      Customer Service Experience.”
- 11      •    According to the J. D. Power electric and gas utility residential customer  
12      satisfaction studies, Cinergy’s performance in overall satisfaction has  
13      outperformed the scores of the industry and the Midwest region averages  
14      every year for each study.
- 15      •    A rank of 12th out of 60 electric utilities in the annual Key Accounts  
16      National Benchmark Study by TQS Research of Alpharetta, Georgia.
- 17      •    A tie for 3rd out of 19 gas and electric companies in the American  
18      Customer Satisfaction Index produced by the Stephen M. Ross School of  
19      Business at the University of Michigan, in partnership with the American  
20      Society for Quality and the international consulting firm, CFI Group.

21           In addition, Cinergy regularly surveys its residential customers who have  
22   had a recent service contact with the Company. These surveys are conducted  
23   throughout the year by an independent research firm. Cinergy’s customer surveys  
24   point to strong customer service and attention to ULH&P’s customer needs. The  
25   Residential Customer Contact survey results from 1999 – 2005 confirms that  
26   Cinergy delivers high quality customer service for the major types of customer

1 contacts. Over 33,000 customer responses have been accumulated over this  
2 period and customers consistently rank customer satisfaction high with at least  
3 86% of these respondents being “very satisfied” or “satisfied” with the level of  
4 service delivered by Cinergy. Our most recent surveys indicated that for 2005  
5 (YTD through May), 87% of Cinergy’s customers who had contact with the  
6 Company said they were either “very satisfied” or “satisfied” with the service  
7 they received. ULH&P credits its long tradition of superior customer service to  
8 its employees and an overall commitment to high standards.

9 **Q. PLEASE DESCRIBE THE PRIMARY WAYS IN WHICH ULH&P**  
10 **PROVIDES CUSTOMER SERVICE.**

11 A. ULH&P works to be highly accessible to its customers and to enable its  
12 customers to do business with us through a number of convenient methods. For  
13 example, we have highly trained call center representatives available to take calls  
14 including a new business service center devoted to our commercial and industrial  
15 consumers’ needs. We also offer several self-service options through our Online  
16 Services as well as our automated telephone system. In addition, we offer a  
17 network of Pay Stations and Customer Service offices in various locations that  
18 enable customers to pay in person. These self-service channels combined with  
19 our call centers, Pay Stations and Customer Service offices offer customers the  
20 ability to do business with us through the method that best meets their needs.

21 ULH&P is also committed to providing a variety of customer programs  
22 and services that enable its customers to better manage their energy bills based on  
23 the varied needs of its customers. Some of the programs and services we offer are

1 Budget Billing, BillPayer 2000, Home Energy House Call, Home Weatherization,  
2 Adjusted Due Date, Speedpay, e-Bill, as well as financial assistance for our  
3 customers in need, through ULH&P's WinterCare program.

4 **Q. HOW WILL ULH&P CONTINUE TO PROVIDE THE SAME LEVEL OF**  
5 **CUSTOMER SERVICE IN THE FUTURE?**

6 A. The merger between Cinergy and Duke Energy will have no adverse impact upon  
7 customer service. Like reliability, customer service is an issue that is valued and  
8 given high priority by both Cinergy and Duke Energy. In 2005, Duke Power's  
9 call center was recognized for call center operational excellence and customer  
10 satisfaction by J.D. Power and Associates, and joins Cinergy as the only two  
11 energy company call centers so recognized. Mr. Osborne further describes Duke  
12 Power's commitment and accomplishments in the area of customer service. The  
13 merger will allow ULH&P to access Duke Power's wealth of customer service  
14 experience. This will enable the New Duke Energy utility operating companies to  
15 develop "best practices" drawing on the experience of the former Duke Power and  
16 Cinergy operating companies. This added expertise will enhance ULH&P's  
17 ability to provide superior customer service.

18 The merger will also present opportunities for savings in the customer  
19 service area, through efficiencies gained in the various call centers. The merger  
20 savings estimates do not reflect closing any specific call centers. The estimated  
21 reduction in customer care personnel reflect efficiencies that can be gained  
22 through initiatives like digitally connecting the various call centers to allow for

1 optimal management of incoming calls. This integration should provide a larger  
2 pool of call center personnel available to handle ULH&P customer calls.

3 Our goal and belief is that the transition will appear seamless to our  
4 customers as the merger will not adversely change the quality of services they  
5 currently receive. ULH&P will continue to offer a variety of service options that  
6 provide accessibility and convenience, as well as a consistent customer service  
7 experience, regardless of the service channel. We will continue to have qualified  
8 and skilled customer service representatives available twenty-four hours a day to  
9 respond to power outage calls. Customers will also have access to our online  
10 services and automated telephone service, twenty-four hours a day to perform  
11 routine interactions or to obtain general billing and customer information.

12 We will also continue to staff qualified and skilled customer service  
13 representatives during core business hours to handle all types of customer  
14 inquiries. Our commitment to a Quality Assurance (“QA”) process will remain  
15 intact to ensure that our call center is providing outstanding customer service.  
16 The QA process includes a review from trained mentors who listen to recorded  
17 telephone calls and then provide feedback and coaching, based on how the  
18 customer service representative handled the customer call.

19 Lastly, to ensure that the service we provide meets our customers’ needs,  
20 we will continue to survey our customers regarding their satisfaction and will  
21 integrate this information into our processes, programs, and services that impact  
22 our customers.

1           We are committed to quality customer service, and the merger will only  
2 strengthen that commitment. And, as we combine with Duke Energy and come to  
3 learn their systems, processes, and operations for achieving superior customer  
4 service, we will adopt the best practices of our combined companies to the benefit  
5 of our ULH&P customers.

**V.       COST SAVINGS/RATE IMPACTS**

**6   Q.   IS ULH&P A LOW COST GAS AND ELECTRICITY PROVIDER?**

7   A.   Yes. ULH&P continues to deliver gas and electricity at low cost, and our  
8 dedication to cost control is reflected in our rates. ULH&P's gas and electric  
9 rates are very competitive, both regionally and nationwide.

10           ULH&P has a pending application to increase its gas rates, because the  
11 Commission ordered ULH&P to file this case in 2005 in order to continue Rider  
12 AMRP. This rider is a cost recovery mechanism for ULH&P's accelerated cast  
13 iron and bare steel main replacement program. ULH&P's electric rates remain  
14 frozen through 2006, due to ULH&P's commitments in prior cases involving its  
15 wholesale power contract with CG&E and the transfer of the three generating  
16 plants from CG&E to ULH&P. ULH&P's rates continue to be attractive when  
17 compared to both regional and national average gas and electric rates.

1 Q. PLEASE DESCRIBE HOW THE COST SAVINGS AND COSTS TO  
2 ACHIEVE SUCH SAVINGS EXPECTED TO RESULT FROM THE  
3 MERGER WERE CALCULATED AND HOW MUCH OF THOSE  
4 ESTIMATED SAVINGS ARE ALLOCABLE TO ULH&P.

5 A. The testimony of Mr. Flaherty describes the expected level of merger savings.  
6 The savings are expected due to labor reductions in corporate, administrative, and  
7 operating areas, as well as cost savings in areas such as information technology  
8 and supply chain. Of course, there are costs associated with achieving these  
9 savings. As described in more detail in the testimony of Mr. Flaherty, the types of  
10 costs to achieve include: separation, relocation, retention, systems integration,  
11 facilities integration, internal and external communication, regulatory process and  
12 compliance, transition, directors' and officers insurance coverage, and transaction  
13 costs.

14 As Mr. Flaherty details, the overall gross cost savings in the corporate,  
15 shared services and regulated business support areas over the first five years  
16 following the close of the merger are expected to be approximately \$1.3 billion.  
17 For corporate, shared services and regulated business support areas,  
18 approximately \$696 million in out-of-pocket costs to achieve merger savings were  
19 identified related to the close of the merger and the realization of estimated cost  
20 savings.

21 As the testimony of Mr. Blackwell provides, these savings and costs are  
22 then allocated among the various companies. The regulated savings and costs are  
23 allocated among the utility operating companies, ULH&P, CG&E, PSI, and Duke

1 Power, while the corporate and shared services savings and costs are allocated  
 2 across a broader set of the New Duke Energy companies to arrive at company  
 3 specific gross savings. The bottom line for ULH&P, in terms of estimated retail  
 4 net merger savings over the first five years, is as follows, approximately:

	Year 1	Year 2	Year 3	Year 4	Year 5	Five Year Total
<b>Gas</b>	\$(0.7 M)	\$0.1 M	\$0.4 M	\$1.0 M	\$1.2 M	\$2.1 M
<b>Electric</b>	<u>\$(2.2 M)</u>	<u>\$1.8 M</u>	<u>\$4.4 M</u>	<u>\$5.6 M</u>	<u>\$6.2 M</u>	<u>\$16.0 M</u>
<b>Total</b>	\$(2.9 M)	\$1.9 M	\$4.8 M	\$6.6 M	\$7.4 M	\$18.1 M

5 The fifth year savings is assumed to be steady-state savings that continues  
 6 on an annual basis from year five going forward.

7 **Q. HOW WOULD ULH&P'S RETAIL GAS AND ELECTRIC CUSTOMERS**  
 8 **REALIZE SUCH MERGER SAVINGS AND COSTS?**

9 A. It depends on the type of savings and costs. For instance, any actual net fuel  
 10 savings achieved will be automatically flowed through to customers via  
 11 ULH&P's fuel adjustment clause after it becomes operational. Any deferred or  
 12 cancelled capital expenditures will be benefit customers, as well. However, under  
 13 the traditional regulatory framework, non-fuel savings would normally be retained  
 14 by the utility until the time of the utility's next retail base rate case. Likewise, the  
 15 costs incurred to achieve the merger savings would also be borne by the utility  
 16 until the time of the next retail base rate case. At the time of the next rate case,  
 17 the test period level, or a *pro forma* level, of merger related costs and savings  
 18 would be reflected in base rates.



1 **Q. DOES ULH&P HAVE A PROPOSAL TO SHARE THE NET MERGER**  
2 **SAVINGS WITH CUSTOMERS PRIOR TO ITS NEXT BASE RATE**  
3 **CASE?**

4 A. Yes. ULH&P recognizes that savings will be realized from this transaction. As  
5 mentioned above, there are also some related costs. Overall there will be net  
6 savings, and ULH&P is willing to provide customers a share of these estimated  
7 net savings, prior to the commencement of the next base rate case, in return for  
8 deferral and prompt recovery of the underlying costs to achieve. The testimony of  
9 Mr. John P. Steffen explains the required deferred accounting authority,  
10 ULH&P's proposed amortization of merger costs, and ULH&P's proposed  
11 explicit sharing of net non-fuel savings with customers. Essentially, ULH&P  
12 proposes to ramp up the level of net merger savings gas and electric customers  
13 receive, with approximately \$363,200 in year one after the merger and ramping  
14 up to approximately 50% of the net merger savings, or approximately \$1.8  
15 million, by the fifth year after the merger is consummated.

16 **Q. DO YOU BELIEVE THIS PROPOSAL IS FAIR TO CUSTOMERS AND**  
17 **THE COMPANY?**

18 A. Yes, I do. This proposal benefits customers in two significant ways. First, they  
19 will see the benefit of merger savings in their gas and electric bills much earlier  
20 than they would otherwise see them. ULH&P has a current gas rate case in  
21 progress. Although ULH&P will file a new retail electric base rate case in 2006,  
22 it will likely be some time before another base retail gas case will be processed.  
23 Second, under ULH&P's proposal, customers see some net benefit in Year 1,

1 even though costs are expected to exceed benefits in the first year. Third, because  
2 we are proposing to share these benefits based on our upfront estimates of savings  
3 to be achieved, customers are in effect guaranteed savings related to the merger,  
4 regardless of whether ULH&P actually achieves the savings. ULH&P will take  
5 the performance risk associated with actually producing the savings.

6 An additional benefit to customers is that at the time of the next base rate  
7 case, customers will realize 100% of the actual net merger savings achieved.

8 The proposal is also fair to the Company and its investors, because it  
9 provides that ULH&P can recover the costs to achieve merger savings in a timely  
10 manner, without the necessity of waiting until the next base rate case. Under this  
11 proposal ULH&P and its investors bear the risk that ULH&P must achieve the  
12 estimated merger savings, so it is reasonable that there be a sharing of net  
13 benefits, and that the sharing percentages ramp up over time.

## VI. FINANCIAL INTEGRITY

14 **Q. PLEASE GENERALLY DESCRIBE ULH&P'S FINANCIAL STATUS.**

15 **A.** We have worked to meet our investors' expectations to maintain investment grade  
16 credit ratings and to achieve fair returns for our equity investors. On the equity  
17 side, Cinergy has consistently outperformed its peers over the long term in total  
18 shareholder return. For 2004, Cinergy achieved a total shareholder return of  
19 12.6%. On the fixed income investment side, we have solid liquidity. In  
20 addition, our investment grade credit ratings were reaffirmed in 2005.<sup>1</sup> These

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<sup>1</sup> As Ms. Aumiller's and Mr. Steven M. Fetter's testimony indicate, following the announcement of the merger, Fitch and Moody's affirmed the credit ratings of Cinergy and its subsidiaries (including ULH&P)

1 positive financial achievements benefit our customers as well as our investors,  
2 through lower financing costs and ultimately through lower gas and electric rates.

3 **Q. PLEASE DESCRIBE THE IMPACT OF THE MERGER ON ULH&P'S**  
4 **FINANCIAL INTEGRITY.**

5 A. We do not believe the merger will adversely impact ULH&P's financial integrity.  
6 The increased scale and scope of operations resulting from the merger will  
7 strengthen the balance sheet of the New Duke Energy and increase financial  
8 flexibility. Additionally, ULH&P will retain the ability to obtain its own  
9 financing, subject to regulatory approvals, just as today. ULH&P will not  
10 guarantee the credit of any of its affiliates unless specifically approved by the  
11 Commission. As the testimony of Ms. Wendy L. Aumiller and Mr. Steven M.  
12 Fetter describe, we expect no adverse impact on ULH&P's financial integrity as a  
13 result of the merger.

#### **VII. ECONOMIC DEVELOPMENT**

14 **Q. PLEASE DESCRIBE ULH&P'S ECONOMIC DEVELOPMENT**  
15 **INITIATIVES.**

16 A. ULH&P remains active in the area of economic development. ULH&P's  
17 longstanding support for state and local economic development efforts, combined  
18 with ULH&P's competitive gas and electric rates, have resulted in a number of  
19 Northern Kentucky economic development successes in which ULH&P has  
20 played a part. With a small economic development staff (currently three persons),

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and assigned a "Stable" outlook to these ratings. Standard & Poor's placed the credit ratings of Cinergy and its subsidiaries on Credit Watch with "Negative" implications.

**GREGORY C. FICKE DIRECT**

1 we estimate that our cooperative efforts with state and local economic  
2 development officials have contributed to the creation of nearly 20,000 Kentucky  
3 jobs and more than \$1.5 billion of capital investment in Northern Kentucky since  
4 1995. For example, when A-Carb LLC (A-Carb) located to Northern Kentucky,  
5 ULH&P's economic development staff worked diligently with A-Carb officials to  
6 meet their needs, which ultimately led to the extension of a dedicated gas line. A-  
7 Carb has expanded twice since that time, in 2000 and 2001.

8 For the last six years, Cinergy has been named as one of the "Top 10 Best"  
9 utility economic development programs by *Site Selection* magazine, including the  
10 top honor for the past two years. Even more important to us, our surveys of local  
11 economic development officials indicate that they are highly satisfied (100%  
12 satisfaction rate) with ULH&P's economic development efforts and services.

13 Additionally, ULH&P recently filed for and received approval of three  
14 new economic development rates, to encourage expansion of new and existing  
15 businesses, reuse of existing abandoned buildings, and the development of  
16 Brownfield sites. These riders are intended to be used in conjunction with other  
17 state and local government economic development efforts.

18 Finally, with \$200,000 from the Cinergy Foundation, Cinergy will provide  
19 grants to local or regional economic development organizations for projects which  
20 result in the creation of new jobs and/or new capital investment in Cinergy's  
21 service territories, including ULH&P's.

22 **Q. PLEASE DESCRIBE HOW THE MERGER WILL IMPACT ULH&P'S**  
23 **ECONOMIC DEVELOPMENT EFFORTS.**

1 A. ULH&P's commitment to economic development will not be adversely impacted.  
2 To the contrary, Duke Energy is as committed to economic development, as  
3 Cinergy has been. In 2004, 5,552 new jobs were created by Duke Power  
4 customers along with new investment of \$999 million. In addition, Duke Power  
5 has initiatives such as the North Carolina Community College Grants to fund  
6 manufacturing worker training and provides grants through AdvanceSC, which  
7 supports training, economic development projects and public assistance programs  
8 in South Carolina. The testimony of Mr. Osborne further describes Duke Power's  
9 superior economic development record. Additionally, the merger savings  
10 calculated by Mr. Flaherty did not assume any reductions in economic  
11 development personnel. ULH&P's commitment to continued economic  
12 development in Northern Kentucky will remain a top priority for the New Duke  
13 Energy.

#### **VIII. CHARITABLE GIVING**

14 **Q. PLEASE DESCRIBE ULH&P'S CHARITABLE GIVING PHILOSOPHY.**

15 A. Cinergy and ULH&P make good corporate citizenship a priority by giving back to  
16 the communities we serve. Since 1994, our philanthropic affiliate, Cinergy  
17 Foundation, has contributed over \$1.9 million to Northern Kentucky charitable  
18 organizations in the communities we serve. And we strongly encourage a spirit of  
19 volunteerism among our employees, who contribute countless hours of volunteer  
20 time to support the many communities in which they live and work.

21 **Q. HOW WILL ULH&P'S CHARITABLE GIVING BE IMPACTED BY THE**  
22 **MERGER?**

1 A. ULH&P's commitment to charitable giving will not be adversely impacted by the  
2 merger. In fact, Duke Energy shares this commitment as detailed in the testimony  
3 of Mr. Osborne. For instance in 2004, the Duke Energy Foundation total giving  
4 to charitable organizations was \$13.5 million. Additionally, both Duke Power  
5 and ULH&P have heating assistance programs, and encourage volunteerism  
6 among their employees.

**IX. ENVIRONMENTAL STEWARDSHIP**

7 **Q. PLEASE DESCRIBE ULH&P'S COMMITMENT TO THE**  
8 **ENVIRONMENT.**

9 A. Through its Environmental Leadership Pledge, Cinergy accepts that we are  
10 responsible for reducing the impact of our operations on the air, water and land.  
11 Cinergy pledges to conduct our business with respect for the environment, while  
12 providing our customers with low cost, reliable and efficient energy services.

13 In support of that pledge, Cinergy has been a leader in environmental  
14 issues beginning with Cinergy's support for the Clean Air Act Amendments of  
15 1990, and continuing to today. Cinergy is a leader in supporting multi-pollutant  
16 reduction legislative efforts, voluntarily committing to greenhouse gas emission  
17 reductions, studying the effects of potential environmental policies through its  
18 2004 Air Issues Report to Stakeholders, and continuing its comprehensive cost-  
19 effective environmental compliance planning. Cinergy is one of the few utility  
20 companies named to the Dow Jones World Sustainability Index - two years  
21 straight.

1 **Q. HOW WILL ULH&P'S COMMITMENT TO THE ENVIRONMENT BE**  
2 **IMPACTED BY THE MERGER?**

3 A. Sustainability is an important part of Cinergy's mission and will remain an  
4 important part of the New Duke Energy's mission. Duke Energy and Cinergy  
5 have both supported reasonable carbon emissions policies, and reported carbon  
6 dioxide emissions to our stakeholders. Duke Energy was instrumental in  
7 supporting and promoting the North Carolina General Assembly's passage of the  
8 Clean Smokestacks Act in 2002, state legislation designed to reduce NO<sub>x</sub> and  
9 SO<sub>2</sub>. The U.S. EPA awarded the 2004 Clean Air Excellence award to Duke  
10 Energy for its collaborative work that resulted in the Act. The New Duke Energy  
11 will maintain a commitment to environmental stewardship.

**X. AFFILIATE TRANSACTIONS/AGREEMENTS**

12 **Q. WHAT AFFILIATE AGREEMENTS IS ULH&P FILING WITH THE**  
13 **COMMISSION?**

14 A. ULH&P is filing five new or revised affiliate agreements with the Commission in  
15 this proceeding: (1) Service Company Utility Service Agreement; (2) Operating  
16 Company / Nonutility Companies Service Agreement; (3) Operating Companies  
17 Service Agreement; (4) Money Pool Agreement; and a (5) Tax Sharing  
18 Agreement. I will briefly discuss each of these; however, supporting testimony  
19 from other ULH&P witnesses will provide more detail where indicated below.  
20 ULH&P requests a deviation under KRS 278.2207(2) for the pricing terms of  
21 these agreements, on the grounds that the requested pricing is reasonable and in  
22 the public interest, for the reasons discussed below.

1 **Q. PLEASE DESCRIBE THE PROPOSED SERVICE COMPANY UTILITY**  
2 **SERVICE AGREEMENT.**

3 A. This agreement will allow the new Duke Energy service company, Duke Energy  
4 Shared Services, LLC to provide services to multiple subsidiary companies,  
5 including ULH&P. The agreement provides for direct assignment or allocation of  
6 various costs among the companies. The testimony of Mr. Blackwell sponsors  
7 this agreement and describes the efforts to create a new utility service agreement  
8 for the New Duke Energy, using as the basis the current Cinergy Service  
9 Agreement and the Duke Energy Business Services arrangement.

10 Even though PUHCA is being repealed, ULH&P and its affiliates intend  
11 to enter into this service agreement, which formerly would have been approved by  
12 the SEC, as a reasonable means of allocating costs among the affiliates. We also  
13 propose to have services flow from Duke Energy Shared Services at fully  
14 embedded cost, at least for ratemaking purposes, as formerly required by the  
15 PUHCA. ULH&P believes this is an appropriate transfer pricing mechanism  
16 because pricing at fully embedded cost is fundamentally fair to both affiliated  
17 parties and is ULH&P's and the SEC's historical practice for pricing public utility  
18 holding company service company transactions. Moreover, fully embedded cost  
19 pricing prevents cross-subsidization, and is readily verifiable. Finally, all such  
20 transactions will remain subject to the Commission's ratemaking authority.

21 **Q. PLEASE DISCUSS ULH&P'S COMMITMENT IN THE CINERGY**  
22 **MERGER SETTLEMENT RELATING TO THE RATEMAKING**  
23 **TREATMENT OF TRANSACTIONS WITH AFFILIATES.**



1 A. In Commission Case No. 94-104, ULH&P agreed not to seek to overturn or  
2 change a decision by the Commission which pertains to recovery or ratemaking  
3 treatment of any expenses or allocation incurred by ULH&P as a result of a  
4 transaction with any affiliate of ULH&P on the basis that such expense or  
5 allocation has been filed with or approved by the SEC, or was incurred pursuant  
6 to an SEC-approved contract or allocation method.

7 **Q. HOW IS THIS COMMITMENT AFFECTED BY THE REPEAL OF**  
8 **PUHCA?**

9 A. Clearly, because the SEC will no longer have jurisdiction over ULH&P under  
10 PUHCA, this commitment is no longer required. As such, the Commission's  
11 authority over cost recovery and ratemaking treatment for ULH&P's transactions  
12 with affiliates remains.

13 **Q. PLEASE DESCRIBE THE PROPOSED OPERATING COMPANY/**  
14 **NONUTILITY COMPANIES SERVICE AGREEMENT, AND THE**  
15 **OPERATING COMPANIES SERVICE AGREEMENT.**

16 A. The Operating Company / Nonutility Companies Service Agreement is similar to  
17 another agreement governing certain service-related affiliate transactions that  
18 ULH&P has operated under for years, the Services Agreement. It is also an  
19 agreement that was formerly filed with and approved by the SEC. It will allow  
20 ULH&P to provide services to various non-regulated affiliated companies, and  
21 vice versa, using fully embedded cost pricing at least for ratemaking purposes.  
22 Mr. Blackwell also sponsors and describes this agreement. The primary  
23 difference between this agreement and the currently approved Service Agreement

1 is the inclusion of New Duke Energy non-regulated affiliates as entities that can  
2 receive or provide services to each other.

3 The proposed Operating Companies Service Agreement is an agreement  
4 between and among ULH&P, CG&E, PSI, Miami Power Corporation and Duke  
5 Power, LLC. It is similar in form and purpose to the Operating Company /  
6 Nonutility Companies Service Agreement. Under this agreement, the various  
7 utility companies could perform services for an affiliated utility company, using  
8 fully embedded cost pricing, at least for ratemaking purposes,.

9 Both agreements only provide for services. They do not provide for  
10 transfers of assets or goods, or power or fuel. These agreements will provide great  
11 value to ULH&P and both its non-regulated and regulated affiliates. The ability  
12 to draw upon the expertise and experience of its regulated and non-regulated  
13 affiliates, with pricing at cost, is a benefit to ULH&P, and ultimately ULH&P's  
14 customers. Just as with ULH&P's proposed pricing for service company  
15 activities, ULH&P believes fully embedded cost pricing is an appropriate transfer  
16 pricing mechanism in this context because it is fundamentally fair to both  
17 affiliated parties and is ULH&P's and the SEC's historical practice for pricing  
18 transactions under public utility holding company service agreements. Moreover,  
19 fully embedded cost pricing prevents cross-subsidization, and is readily verifiable.

1 **Q. PLEASE DESCRIBE THE REVISED MONEY POOL AGREEMENT.**

2 A. ULH&P is currently a party to a Utility Money Pool Agreement, which provides  
3 for loans between and among ULH&P, its utility affiliates and Cinergy. This, too,  
4 is an agreement that formerly required SEC approval under PUHCA. Ms.  
5 Aumiller's testimony supports and describes the revisions to this agreement in  
6 more detail. This agreement has provided significant benefit to ULH&P in the  
7 past and those benefits will only be expanded in the future.

8 **Q. PLEASE DESCRIBE THE REVISED TAX SHARING AGREEMENT.**

9 A. ULH&P is currently a party to a Cinergy Tax Sharing Agreement, which provides  
10 for the filing of consolidated tax returns. This is an agreement that formerly  
11 required SEC approval under PUHCA. In her testimony, Ms. Lynn J. Good  
12 describes the revisions to this agreement in more detail.

**XI. PLAN TO ACCOMPLISH MERGER**  
**IN ACCORDANCE WITH LAW**

13 **Q. PLEASE DESCRIBE THE PLAN TO ACCOMPLISH THE MERGER IN**  
14 **ACCORDANCE WITH LAW.**

15 A. The Joint Applicants have developed a plan to obtain the following state and  
16 federal approvals so that the merger will be accomplished in a lawful manner:

- 17 • Approval of this Commission in accordance with Kentucky statutory  
18 provisions governing utility mergers, based on ULH&P's utility  
19 operations in Kentucky;
- 20 • Approval of the Ohio Public Utilities Commission, based on CG&E's  
21 utility operations in Ohio;

- 1           •     Approval of Indiana Utilities Regulatory Commission for PSI's new  
2                     affiliate agreements related to the merger;
- 3           •     Approval of the North Carolina Utilities Commission, based on Duke  
4                     Power's utility operations in North Carolina;
- 5           •     Approval of the Public Service Commission of South Carolina, based on  
6                     Duke Power's utility operations in South Carolina;
- 7           •     Approval of the FERC;
- 8           •     Approval of the NRC;
- 9           •     Approval of the FCC;
- 10          •     A filing under the Hart-Scott Rodino Act, although Joint Applicants do not  
11                     believe that the proposed acquisition will implicate any provision under  
12                     federal antitrust laws.

13                     The Joint Applicants will provide the Commission with copies of these  
14                     applications and filings, and a copy of the orders by these other regulatory  
15                     agencies when they approve the merger. The merger thus will be accomplished in  
16                     accordance with law.

## **XII.     MERGER COMMITMENTS**

17   **Q.     PLEASE IDENTIFY ATTACHMENT GCF-1.**

18    A.     Attachment GCF-1 is a list of specific commitments that ULH&P is willing to  
19                     make related to the merger. The list is in addition to the other merger-related  
20                     commitments contained in my testimony and in the testimony of other witnesses.  
21                     I would note that ULH&P intends this list, together with the testimony in this

1 proceeding, to be comprehensive and to replace any preexisting Cinergy merger  
2 commitments coming out of Case No. 94-104.

### **XIII. CONCLUSION**

3 **Q. BASED ON YOUR FOREGOING TESTIMONY AND YOUR**  
4 **EXPERIENCE AS PRESIDENT OF ULH&P, DO YOU HAVE AN**  
5 **OPINION AS TO WHETHER DUKE ENERGY AND ITS AFFILIATES**  
6 **INVOLVED IN ACQUIRING CONTROL OF CINERGY HAVE THE**  
7 **FINANCIAL, TECHNICAL AND MANAGERIAL CAPABILITIES TO**  
8 **PROVIDE REASONABLE SERVICE FOR ULH&P'S CUSTOMERS?**

9 A. Yes. I believe that Duke Energy and the other Duke affiliates involved in the  
10 application have the financial, technical and managerial capabilities to provide  
11 reasonable service following the merger, and that the merger will enhance  
12 ULH&P's capabilities in these areas. The bases for my opinion are Cinergy's and  
13 ULH&P's commitment to high quality and reliable service, Duke Energy's  
14 commitments in these areas, and the fact that Jim Rogers and ULH&P have  
15 successfully merged before (when CG&E merged with PSI in 1994), with positive  
16 impacts for customers.

17 **Q. BASED ON YOUR FOREGOING TESTIMONY AND YOUR**  
18 **EXPERIENCE AS PRESIDENT OF ULH&P, DO YOU HAVE AN**  
19 **OPINION REGARDING WHETHER THE MERGER WILL BE IN**  
20 **ACCORDANCE WITH LAW, FOR A PROPER PURPOSE, AND**  
21 **CONSISTENT WITH THE PUBLIC INTEREST?**

1 A. Yes. I believe that the merger will be accomplished in accordance with all federal  
2 and state regulatory requirements, as I discussed earlier in my testimony. I also  
3 believe the benefits from the merger for all of ULH&P's stakeholders, discussed  
4 in my earlier testimony and the testimony of other witnesses, clearly establish that  
5 the merger is for a proper purpose and in the best interest of the general public.

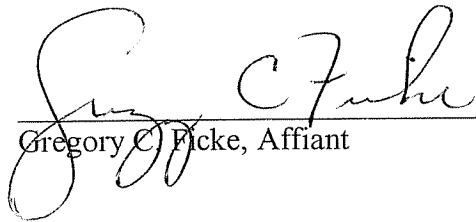
6 **Q. DOES THIS CONCLUDE YOUR PREPARED DIRECT TESTIMONY?**

7 A. Yes.

**VERIFICATION**

State of Ohio            )  
                                  )        SS:  
County of Hamilton )

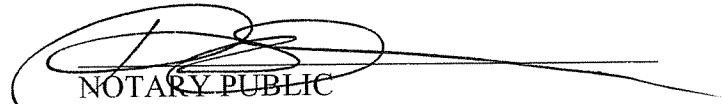
The undersigned, Gregory C. Ficke, being duly sworn, deposes and says that he is President of The Union Light, Heat and Power Company and The Cincinnati Gas & Electric Company, and that the matters set forth in the foregoing testimony are true and correct to the best of his information, knowledge and belief.

  
\_\_\_\_\_  
Gregory C. Ficke, Affiant

Subscribed and sworn to before me by GREGORY C. FICKE on this 30<sup>TH</sup>  
day of JUNE, 2005.



**ROCCO O. D'ASCENZO**  
ATTORNEY AT LAW  
Notary Public, State of Ohio  
My Commission Has No Expiration  
Section 147.03 R.C.

  
NOTARY PUBLIC

My Commission Expires: NO EXPIRATION

### MERGER COMMITMENTS

In addition to the commitments made in the testimony of the Joint Applicant witnesses, ULH&P makes the following commitments<sup>2</sup>:

1. ULH&P commits to provide the Kentucky Public Service Commission ("Commission") with access to the books and records of ULH&P and the books and records of any subsidiary of the new Duke Energy Corporation ("New Duke Energy") in which New Duke Energy holds a controlling interest, to the extent necessary to verify transactions with ULH&P.
2. ULH&P commits that it shall not incur any additional indebtedness, issue any additional securities, or pledge any assets to finance any part of Duke Energy Corporation's ("Duke Energy") acquisition of Cinergy Corp.'s ("Cinergy") stock.
3. The payment for Cinergy's stock shall be recorded on New Duke Energy's, Duke Energy's and Cinergy's books, and shall be excluded from the books of ULH&P for retail ratemaking purposes.
4. Any acquisition premium paid by Duke Energy for the Cinergy stock shall not be "pushed down" to ULH&P for retail ratemaking purposes.
5. No change in control payments will be allocated to the retail customers of ULH&P.
6. ULH&P commits to minimize, to the extent possible, any negative impacts on ULH&P's retail customer service and customer satisfaction levels resulting from workforce reductions due to the merger.
7. ULH&P commits to periodically filing the various reliability and service quality measurements as described in the testimony of Mr. John C. Procario, to enable the Commission to monitor ULH&P's commitment that reliability and service quality will not materially degrade as a result of the merger.
8. ULH&P commits that it will not achieve merger savings at the expense of material degradation in the adequacy and reliability of ULH&P's retail gas and electric service.

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<sup>2</sup> None of these commitments, of course, are intended to limit the Commission's existing statutory authority.



9. ULH&P commits that, for at least two years following the merger, ULH&P shall maintain a substantial level of involvement in community activities, through annual charitable and other contributions, comparable to ULH&P's participation levels prior to the date of the merger.
10. ULH&P commits to maintaining ULH&P's pro-active stance on developing economic opportunities in Kentucky and supporting economic development activities throughout ULH&P's service territory.
11. ULH&P commits that the accounting and reporting system used by ULH&P will be adequate to provide assurance that directly assignable utility and non-utility costs are accounted for properly and that reports on the utility and non-utility operations are accurately presented.
12. ULH&P commits to implement and maintain cost allocation procedures that will accomplish the objective of preventing cross-subsidization, and be prepared to fully disclose all allocated costs, the portion allocated to ULH&P, complete details of the allocation methods, and justification for the amount and the method.
13. ULH&P commits to protect against cross-subsidization in transactions with affiliates.
14. ULH&P acknowledges that, for rate-making purposes, the Commission has jurisdiction over ULH&P's capital structure, financing, and cost of capital, and that the Commission will continue to exercise this jurisdiction.
15. ULH&P commits to implement the rate mechanism and accounting deferrals to flow back a portion of net merger savings to customers, as described in the testimony of Mr. John P. Steffen.

## DETAILED DESCRIPTION OF TRANSACTION

An Agreement and Plan of Merger by and among Duke Energy, Cinergy, Duke Energy Holding Corp., a Delaware corporation (“Holdings”)<sup>1</sup>, Deer Acquisition Corp.<sup>2</sup>, a North Carolina Corporation (“Deer Acquisition”) and Cougar Acquisition Corp.<sup>3</sup>, a Delaware corporation (“Cougar Acquisition”), was entered into May 8, 2005 (“Plan of Merger”). The Plan of Merger sets forth a series of mergers and restructuring transactions as described below that will implement the business combination of Duke Energy and Cinergy.

Before the effective time of the Plan of Merger, Duke Energy will redeem all the outstanding shares of its preferred stock (the “Preferred Stock Redemption”). Under the Preferred Stock Redemption, each holder of Preferred Stock, par value \$100 per share, and Preferred Stock A, par value \$25 per share, will receive the redemption price to which it is entitled under the applicable preferred stock series, together with all dividends accrued and unpaid to the date of such redemption.

Following the Preferred Stock Redemption, Duke Energy will be merged with and into Deer Acquisition (the “Deer Acquisition Merger”) in accordance with the North Carolina Business Corporation Act (the “NCBCA”). As part of the transaction, the common stock shareholders of Duke Energy will receive shares of Holdings common

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<sup>1</sup> Holdings, a signatory to the Plan of Merger, has previously been created as a shell subsidiary of Duke Energy solely for purposes of achieving the Plan of Merger.

<sup>2</sup> Deer Acquisition, a signatory to the Plan of Merger, has previously been created as a shell subsidiary of Duke Energy solely for purposes of achieving the Plan of Merger.

<sup>3</sup> Cougar Acquisition, one of the signatories to the Plan of Merger, has previously been created as a shell corporation solely for purposes of achieving the Plan of Merger.

stock on a one-for-one basis. Duke Energy will be the surviving corporation and will continue its corporate existence under the laws of the State of North Carolina. It also will become a wholly-owned subsidiary of Holdings.

After the Deer Acquisition Merger becomes effective, Duke Energy will convert to a limited liability company to be called Duke Power Company LLC (the “Duke Energy Conversion”) pursuant to a plan of conversion adopted under Section 55-11A-11 of the NCBCA and Section 57C-9A-02 of the North Carolina Limited Liability Company Act. Conversion of Duke Energy to a limited liability company is a tax efficient means of addressing the potential tax impact of the distribution to Holdings of Duke Energy’s limited liability company interests in Duke Capital LLC (“Duke Capital”) described below. Following the Duke Energy Conversion, Duke Power Company LLC will remain a wholly-owned subsidiary of Holdings in that all of the limited liability company interests in Duke Power Company LLC will be held by Holdings. Additionally, Duke Power will remain a public utility subject to this Commission’s jurisdiction.

Immediately following the effectiveness of the Duke Energy Conversion, Duke Power Company LLC will distribute to Holdings all of the limited liability company interests in Duke Capital, causing Duke Capital to be a direct wholly-owned subsidiary of Holdings. Duke Capital will continue to own all of its direct and indirect subsidiaries, comprising all of the unregulated businesses of Duke Energy prior to completion of the merger.

After the Duke Capital distribution, Cougar Acquisition will be merged with and into Cinergy in accordance with the Delaware General Corporation Law (the “DGCL”) (the “Cougar Merger”). In connection with the mergers, each Cinergy shareholder will

receive 1.56 shares of Holdings common stock for each share of Cinergy common stock he or she owns. Cinergy will be the surviving corporation in the Cougar Merger and will continue its corporate existence under the laws of the State of Delaware. As a result of the Cougar Merger, Cinergy will become a wholly-owned subsidiary of Holdings.

Pursuant to the Plan of Merger and following consummation of the above transactions, Holdings will change its name to “Duke Energy Corporation” (hereinafter “New Duke Energy”). Based on the number of shares outstanding as of May 8, 2005, current Duke Energy shareholders will own approximately 76 percent of Holdings’ common stock and current Cinergy shareholders will own approximately 24 percent of Holdings’ common stock. New Duke Energy will maintain its headquarters in Charlotte, North Carolina.

As a result of the merger, New Duke Energy will establish a services company to be named Duke Energy Shared Services LLC (“DESS”), to provide goods and services to its utility and non-utility subsidiaries. DESS either will be formed from the existing service company, Cinergy Services, Inc., currently owned by Cinergy, or established as an entirely new company.

At the same time or shortly thereafter, ownership for a number of generation facilities located in the Midwest (collectively, the “DENA Midwest Assets”) which are owned and operated by DENA subsidiaries (collectively, the “DENA Subsidiaries”) are intended to be transferred to CG&E, subject to the receipt of necessary approvals and

consents.<sup>4</sup> These transfers will allow operational efficiencies and synergies that should significantly reduce operating costs for the combined generation fleet.

The DENA Midwest Assets and DENA Subsidiaries are:

- the Fayette Energy Facility, a natural gas-fired combined cycle generating facility located near Masontown, Pennsylvania with a nominal capacity of 620 MW, owned and operated by Duke Energy Fayette (“Duke Fayette”), a direct, wholly-owned subsidiary of DENA;
- the Hanging Rock Energy Facility, a natural gas-fired electric generation plant located in Lawrence County, Ohio with a nominal capacity of 1,240 MW, operated by Duke Energy Hanging Rock, LLC (“Duke Hanging Rock”), a direct, wholly-owned subsidiary of DENA;
- the Lee Energy Facility, a natural gas-fired, simple cycle electric generation plant located in Lee County, Illinois with a nominal capacity of 640 MW, owned and operated by Duke Energy Lee, LLC (“Duke Lee”), an indirect, wholly-owned subsidiary of DENA;<sup>5</sup>
- an undivided 75% interest in the Vermillion Energy Facility, a 648 MW gas-fired generation facility located in Vermillion County, Indiana, with such interest and corresponding entitlements owned and operated by Duke Energy Vermillion, LLC (“Duke Vermillion”), an indirect, wholly-owned subsidiary of DENA,<sup>6</sup> and
- the Washington Energy Facility, a natural gas-fired electric generation facility located in Washington County, Ohio with a nominal capacity of 620 MW, owned and operated by Duke Energy Washington, LLC (“Duke Washington”), a direct, wholly-owned subsidiary of DENA.

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<sup>4</sup> The transfer of the DENA Midwest Assets could take place on a piecemeal basis as necessary approvals and consents are received.

<sup>5</sup> Duke Lee is a direct, wholly-owned subsidiary of Duke Energy Lee Holding, Inc. which, in turn, is a direct, wholly-owned subsidiary of DENA.

<sup>6</sup> Duke Vermillion is a direct, wholly-owned subsidiary of Duke Energy Trenton, LLC (“Duke Trenton”). Duke Trenton is a direct, wholly-owned subsidiary of DE Power Generating, LLC which, in turn, is a direct, wholly-owned subsidiary of DE Power Generating Holdings, LLC (“DPGH”). DPGH is a direct, wholly-owned subsidiary of Catawba River Investments II, LLC which, in turn, is a direct, wholly-owned subsidiary of DENA.

The transfer of ownership of the DENA Midwest Assets will be accomplished either as a transfer of the assets to CG&E by the appropriate DENA Subsidiary, or as a transfer of the DENA Subsidiary itself. In the more likely event that transfer is accomplished as a transfer of the DENA Subsidiary itself, such transfer could be accomplished by having the owner of the DENA Subsidiary transfer its rights, title, and interest directly to CG&E or through a multiple-step process where, for business reasons, the DENA Subsidiary could be transferred momentarily to one or more Duke Energy entities before being transferred to CG&E. Once a DENA Subsidiary has been transferred to CG&E, the DENA Subsidiary may be merged with CG&E, with CG&E remaining as the surviving entity. Regardless of whether the transfer of the DENA Midwest Assets is accomplished through the transfer of a DENA Subsidiary's assets or the entire DENA Subsidiary, CG&E will be the entity that owns and controls the DENA Midwest Assets.

Duke Energy intends to effectuate the transfer of its DENA Midwest Assets as an equity infusion into CG&E at book value. In conjunction with the transfer of these assets, Duke Energy or another appropriate affiliate intends to enter into a financial arrangement with CG&E to eliminate any potential cash shortfalls that may result from owning and operating these assets.

**COMMONWEALTH OF KENTUCKY**  
**BEFORE THE PUBLIC SERVICE COMMISSION**

In the Matter of:

Joint Application of Duke Energy Corporation,	)	
Duke Energy Holding Corp., Deer Acquisition	)	
Corp., Cougar Acquisition Corp., Cinergy Corp.,	)	Case No. 2005-00228
The Cincinnati Gas & Electric Company, and	)	
The Union Light, Heat and Power Company for	)	
Approval of a Transfer and Acquisition	)	
of Control	)	

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**DIRECT TESTIMONY OF**

**JOHN C. PROCARIO**

**ON BEHALF OF**

**JOINT APPLICANTS**

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**APPENDIX**

ATTACHMENT JCP – 1 - Rolling 12 Month Average for Past Ten Years for ULH&P,  
SAIFI, CAIDI and SAIDI.



## **I. INTRODUCTION**

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is John C. Procario. My business address is 139 East Fourth Street,  
3 Cincinnati, Ohio 45202.

4 **Q. WHAT IS YOUR CURRENT POSITION?**

5 A. I am Senior Vice President and Chief Operating Officer of Cinergy Corp.'s  
6 ("Cinergy") Regulated Businesses Unit.

7 **Q. WILL YOU PLEASE SUMMARIZE YOUR EDUCATION AND**  
8 **PROFESSIONAL QUALIFICATIONS?**

9 A. I received a Bachelor of Science degree in electrical engineering from Ohio State  
10 University in 1973. I was awarded an Ohio Electric Utility Institute Fellowship  
11 and received a Master of Science degree concentrating in electric power from  
12 Ohio State University in 1974. I also completed approximately 30 credit hours in  
13 the MBA program at the University of Cincinnati.

14 I began my professional career with The Cincinnati Gas & Electric  
15 Company ("CG&E") in 1974 and have held various engineering and managerial  
16 positions, including Manager of Electric Planning and Manager of Electric System  
17 Operations. After the merger of the former parent company of PSI Energy, Inc.  
18 ("PSI") and CG&E to form Cinergy in 1994, I became General Manager of  
19 Electric System Operations for the Cinergy domestic utility subsidiaries, including  
20 The Union Light Heat and Power Company ("ULH&P" or "Company"). In 1998,  
21 I was promoted to Vice President of Electric Operations, and in 2000, I was  
22 promoted to Vice President and Chief Operating Officer for Cinergy's Regulated

1 Businesses business unit. I was made Senior Vice President and Chief Operating  
2 Officer in November of 2003.

3 I have also taught various electric power systems courses in the College of  
4 Engineering at the University of Cincinnati, starting as a Lecturer in 1975 and  
5 progressing to Adjunct Professor.

6 I am or have been a member of various industry committees and  
7 organizations, including the East Central Area Reliability (“ECAR”) Executive  
8 Board, the North American Electric Reliability Council (“NERC”) Engineering  
9 Committee, the EPRI Electrical Systems Division Committee, the Midwest ISO  
10 Advisory Committee, and the North American Energy Standards Board  
11 (“NAESB”) Board of Directors.

12 I am also a registered professional engineer in Ohio.

13 **Q. PLEASE SUMMARIZE YOUR DUTIES AS VICE PRESIDENT AND**  
14 **CHIEF OPERATING OFFICER OF CENERGY’S REGULATED**  
15 **BUSINESSES UNIT.**

16 A. As Senior Vice President and Chief Operating Officer of Cinergy’s Regulated  
17 Businesses Unit, I am responsible for the planning and operation of the Cinergy  
18 regulated utility companies’ gas and electric systems. This responsibility extends  
19 to overseeing electric transmission and distribution planning, design, construction,  
20 operation and maintenance activities and gas distribution planning, design,  
21 construction, operation and maintenance activities. As such, I am responsible for  
22 Cinergy policies related to the planning, design, construction, operation and  
23 maintenance of its electric and gas transmission and distribution systems.

1 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**  
2 **PROCEEDING?**

3 A. The purpose of my testimony is: (1) to describe ULH&P's gas and electric  
4 delivery system; (2) to explain ULH&P's overall policies relating to reliability and  
5 how ULH&P measures the reliability of its system; and (3) to explain that the  
6 proposed merger (the "Merger") of Cinergy and Duke Energy Corporation ("Duke  
7 Energy") will not adversely affect the reliability of ULH&P's system.

**II. ULH&P'S ELECTRIC AND GAS DELIVERY SYSTEM**

8 **Q. PLEASE GENERALLY DESCRIBE THE ULH&P ELECTRIC AND GAS**  
9 **DELIVERY SYSTEM.**

10 A. ULH&P owns and operates all of its electric distribution and local transmission  
11 facilities. Its parent, CG&E, owns and operates, subject to the Midwest  
12 Independent Transmission System Operator ("Midwest ISO") functional control,  
13 the bulk transmission facilities located in ULH&P's service territory. The  
14 ULH&P's electric and gas delivery system is used, among other things, to deliver  
15 retail electric and gas service to nearly 145,000 customers located in all or  
16 portions of six counties in northern Kentucky. ULH&P's electric delivery system  
17 includes approximately 106 circuit miles of transmission lines operating at 69 kV.  
18 It also includes 2,100 miles of primary distribution circuits operating at 34.5 kV or  
19 lower and approximately 800 miles of secondary distribution circuits operating at  
20 480 volts or below. The delivery system also includes approximately 31  
21 distribution substations, and 2 combined transmission and distribution substations  
22 with a combined capacity of approximately 1,400,000 kVA and various other

1 equipment and facilities. While the ULH&P electric system is not directly  
2 interconnected with any other control areas, it is served by transmission facilities  
3 within the Cinergy control area which, in turn, is directly interconnected with a  
4 total of 11 control areas.

5 ULH&P currently provides natural gas distribution service to customers in  
6 Boone, Campbell, Gallatin, Grant, Kenton and Pendleton counties in Northern  
7 Kentucky. ULH&P natural gas facilities include 3 city gate stations connected to  
8 2 interstate pipelines, 1,322 miles of transmission and distribution mains, 160  
9 pressure regulating stations, and one propane storage cavern with associated  
10 vaporization plant. System pressures range from 392 psig to 1/4 psig.

11 **Q. YOU MENTIONED THAT THE CINERGY CONTROL AREA IS**  
12 **DIRECTLY INTERCONNECTED WITH 11 OTHER CONTROL AREAS.**  
13 **IS THE CINERGY CONTROL AREA DIRECTLY INTERCONNECTED**  
14 **WITH THE DUKE POWER CONTROL AREA?**

15 A. No, it is not.

16 **Q. WHAT ARE THE COMPANY'S OBJECTIVES IN DESIGNING,**  
17 **CONSTRUCTING, OPERATING AND MAINTAINING ITS ELECTRIC**  
18 **DELIVERY SYSTEM?**

19 A. In designing, constructing, operating and maintaining its facilities, the Company  
20 strives to provide safe, cost-effective and reliable electric service.

21 **Q. PLEASE GENERALLY DESCRIBE HOW ULH&P'S TRANSMISSION**  
22 **AND DISTRIBUTION SYSTEM IS DESIGNED, CONSTRUCTED AND**  
23 **OPERATED.**

1 A. The electric transmission system is designed to deliver bulk electric power from  
2 local generating plants and other resources to regional substations, or to  
3 interconnect with other systems in order to enhance system reliability. Typical  
4 transmission voltages for ULH&P are 69 kV. The Cinergy Joint Transmission  
5 Agreement provides for the planning and operation of the combined transmission  
6 system of the Cinergy Electric Utilities as an integrated utility system. Cinergy  
7 Services is designated as the agent for PSI and CG&E, on behalf of ULH&P,  
8 under the Cinergy Joint Transmission Agreement. The Cinergy Joint  
9 Transmission Agreement also provides criteria for cost assignment and allocation  
10 of transmission facilities and revenues for the combined transmission system of  
11 the Cinergy Electric Utilities. This Agreement will remain in place after the  
12 merger.

13 The physical design of the electric system is generally governed by the  
14 National Electrical Safety Code (“NESC”). The system is operated in accordance  
15 with ECAR and NERC guidelines, and is under the functional control of the  
16 Midwest ISO.

17 The electric distribution system is designed to receive bulk power at  
18 transmission voltages, reduce the voltage to 12.5 kV or 4 kV for delivery to  
19 distribution transformers and ultimate delivery of power to customers’ premises.  
20 The physical design of the distribution system is also generally governed by the  
21 NESC.

22 The gas distribution system is designed in accordance with applicable  
23 safety codes promulgated by the United States Department of Transportation,

1 located at Code of Federal Regulations, Title 49 and by the American Society of  
2 Testing Materials. ULH&P follows the Department of Transportation safety  
3 regulations and the Commission's safety regulations in installing, operating and  
4 maintaining transmission and distribution facilities.

5 The Company monitors system performance with various systems such as  
6 Supervisory Control and Data Acquisition ("SCADA") and Trouble Call Outage  
7 Management System ("TCOMS"), fully implemented in 2002.

8 **Q. PLEASE GENERALLY DESCRIBE HOW ULH&P'S DELIVERY**  
9 **SYSTEM IS MAINTAINED.**

10 A. ULH&P maintains its delivery system in accordance with good utility practice by  
11 following several inspections, monitoring, testing, and periodic maintenance  
12 programs. Examples of these programs include: substation inspection program,  
13 line inspection program, vegetation management program, underground cable  
14 testing and replacement program, capacitor maintenance program, infrared  
15 scanning of equipment, leak surveys, pipeline patrol, valve inspections, and  
16 cathodic protection program and dissolved gas analysis. ULH&P uses various  
17 reliability indices to measure the effectiveness of its maintenance programs and  
18 system reliability.

19 **Q. PLEASE DESCRIBE SOME OF THE FACTORS THAT THE COMPANY**  
20 **MUST CONSIDER IN ATTEMPTING TO ACHIEVE ITS OBJECTIVES**  
21 **OF PROVIDING SAFE, COST-EFFECTIVE AND RELIABLE ELECTRIC**  
22 **AND GAS SERVICE.**

1 A. The Company must provide safe and reliable service while at the same time  
2 responsibly managing the costs of providing such service. The Company weighs  
3 various factors in selecting the gas and electric delivery system projects in which  
4 to invest, including the Company's planning criteria, requirements mandated  
5 either by regulatory authorities or reliability councils, and project cost versus  
6 customer benefits to name a few.

7 **Q. HOW DOES THE COMPANY BALANCE ALL OF THESE FACTORS?**

8 A. Annually, electric system studies are performed to determine where and when  
9 system modifications are needed to ensure load is adequately served. When these  
10 needs are identified, multiple solutions are developed, addressing not only the  
11 capacity need, but also providing opportunities to maintain or improve reliability  
12 and operating flexibility. Recommendations are made and discussed with the  
13 operations staff to ensure a balanced, workable plan has been developed.

14 In addition, for the gas business, system analysis is performed through  
15 modeling. These models are used to determine where and when system  
16 modifications are needed to ensure proper pressures are maintained to adequately  
17 serve the customer base. Standards and procedures must be followed and  
18 facilities maintained in accordance with these state and federal regulations.  
19 Quality assurance programs are followed such as the Integrity Management  
20 Program, the Cast Iron Maintenance Optimization System, Bare Steel  
21 Maintenance Optimization System, Accelerated Main Replacement Programs  
22 ("AMRP") and the Riser Optimization Program. These programs are used to  
23 monitor the condition of the system and to replace deteriorated equipment.

1 Further, the Company utilizes rigorous analytical techniques and  
2 aggressively negotiates with natural gas interstate pipelines and suppliers to  
3 purchase gas at a cost that is consistently one of the lowest in the state of  
4 Kentucky. When compared to the other three major LDCs in the state, the  
5 Company was the lowest cost provider of natural gas in three of the last five years.  
6 The policies and procedures currently in place for natural gas procurement are  
7 expected to continue after the merger.

8 **Q. YOU STATED THAT THE CINERGY TRANSMISSION SYSTEM IS**  
9 **UNDER THE FUNCTIONAL CONTROL OF THE MIDWEST ISO. WILL**  
10 **THIS CHANGE AS A RESULT OF THE PROPOSED CINERGY/DUKE**  
11 **MERGER?**

12 A. No. As this Commission is aware, Cinergy was instrumental in creation and  
13 development of the Midwest ISO. We are committed to support the regional  
14 transmission organization and its role in transmission grid reliability for  
15 ULH&P's customers.

**III. RELIABILITY OF ULH&P'S ELECTRIC**  
**AND GAS DELIVERY SYSTEM**

16 **Q. DO YOU HAVE AN OPINION AS TO THE RELIABILITY OF ULH&P'S**  
17 **SERVICE TO ITS CUSTOMERS?**

18 A. Yes. In my opinion ULH&P does an exceptional job of maintaining reliability of  
19 service. This opinion is based on my experience and observations as well as the  
20 various indices that we track and use to measure the reliability of our system.



1 **Q. YOU STATED THAT ULH&P USES VARIOUS INDICES TO MEASURE**  
2 **SYSTEM RELIABILITY. PLEASE EXPLAIN THESE RELIABILITY**  
3 **INDICES.**

4 A. These electric reliability indices are generally recognized standards for measuring  
5 the number, scope and duration of outages.

6 Customer Average Interruption Duration Index (“CAIDI”) is the average  
7 interruption duration or average time to restore service per interrupted customer,  
8 and is expressed by the sum of the customer interruption durations divided by the  
9 total number of customer interruptions.

10 System Average Interruption Duration Index (“SAIDI”) is the average time  
11 each customer is interrupted, and is expressed by the sum of customer interruption  
12 durations divided by the total number of customers served.

13 System Average Interruption Frequency Index (“SAIFI”) is the system  
14 average interruption frequency index, and represents the average number of  
15 interruptions per customer. SAIFI is expressed by the total number of customer  
16 interruptions divided by the total number of customers served.

17 A significant portion of the incentive compensation for employees  
18 responsible for system reliability is tied to system performance as measured by  
19 reliability indices, such as these. Incentive compensation is also tied to how our  
20 customers grade or judge our response after an outage occurs.

21 **Q. HOW HAS ULH&P’S SYSTEM PERFORMED AS MEASURED BY**  
22 **THESE RELIABILITY INDICES?**

1 A. For electric, ULH&P's system has performed well. ULH&P's Attachment JCP-1  
2 shows the ULH&P data for these three indices for the last 10 years, both with and  
3 without effects of major storms. In my opinion, this is an excellent reliability  
4 record. Virtually all utilities that have implemented outage management software  
5 systems such as TCOMS (discussed below) have experienced deterioration in  
6 their reliability indices' statistics. This does not mean that reliability has  
7 deteriorated, just that the utility is capturing more and better outage data. I believe  
8 that overall service improves with the use of such systems because it promotes  
9 better service restoration, as discussed below.

10 Gas Operations' major reliability measures are leaks repaired for its gas  
11 distribution system and the duration of customer outages. ULH&P's leak repairs  
12 have declined significantly, from 983 in 1999 to 537 in 2004, as a direct result of  
13 the AMRP. AMRP is a program to accelerate ULH&P's replacement rate for cast  
14 iron and bare steel mains, in order to improve the safety and reliability of its  
15 natural gas distribution system.

16 Customer outage duration is measured by CAIDI. Although CAIDI  
17 currently is not a gas industry accepted reliability measurement, Cinergy's Gas  
18 Operations has been a leader in tracking reliability by average duration of  
19 customer outages. We have advocated with the American Gas Association  
20 ("AGA") for acceptance of industry reliability standards, such as CAIDI. In 2003,  
21 only six companies responding to an AGA benchmarking study reported utilizing  
22 CAIDI as a reliability measurement. Cinergy's Gas Operations' 2004 CAIDI  
23 index was 5.4 hours.

1           Currently, the most accepted reliability standard utilized within the gas  
2 industry is Outages per 1,000 Customers. In a 2003 AGA Benchmarking Study  
3 on Outages per 1,000 Customers, Cinergy's Gas Operations placed 5<sup>th</sup> best out of  
4 46 U.S. companies participating in the study.

5 **Q.   WHAT FACTORS CONTRIBUTE TO THE RELIABILITY OF ULH&P'S**  
6 **DELIVERY SYSTEM?**

7 A.   In my opinion there are a number of factors, beginning with the design,  
8 construction, operation and maintenance of the system, as discussed above. This  
9 year ULH&P will invest approximately \$44 million on the Kentucky gas and  
10 electric delivery system. We will inspect and repair over 1250 miles of electric  
11 transmission and distribution lines and we will continue with our normal  
12 vegetation control. We are also installing a new "state-of-the-art" radio system  
13 used for daily operations and for emergency responses to system outages. The  
14 ongoing Integrity Management Program activities for 2005 include: identification  
15 of high consequence areas, evaluating pipeline threats and conducting risk  
16 assessments for each covered pipeline segment, identifying and implementing  
17 additional preventive and mitigation measures, conducting integrity assessments  
18 through pressure testing or direct assessment methods, and remediating conditions  
19 found during integrity assessments.

20           Even the best design, construction, operations and maintenance of  
21 transmission and distribution facilities will not prevent all outages. When storms  
22 and other events create outages, restoration of service becomes the priority for

1 providing reliable service. The Cinergy utilities consider service restoration to be  
2 an important part of reliability.

3 **Q. WHAT ARE SOME OF THE KEY FACTORS FOR SUPERIOR SERVICE**  
4 **RESTORATION?**

5 A. That depends on the type and magnitude of the outages the Company is dealing  
6 with. Routine minor outages such as ones caused by a vehicle knocking down a  
7 pole or a minor equipment failure are normally handled by our local service  
8 personnel located throughout ULH&P's service territory. Having experienced  
9 people and the necessary equipment available in the area is essential.

10 Major service restoration efforts, such as those required after a significant  
11 storm require far more effort and planning. Cinergy has emphasized emergency  
12 planning and preparation for dealing with these events. We have a comprehensive  
13 emergency plan in place that has been refined over time. This plan provides for  
14 the quick response and highly coordinated efforts of a large number of employees  
15 for different levels and types of emergency situations. For example, system  
16 operators continuously monitor weather conditions. When lightning, wind or ice  
17 storms approach or hit ULH&P's service territory, line crews are called or held  
18 over to respond. ULH&P will often call in several hundred employees to respond  
19 to severe storms, including Cinergy employees stationed in Ohio and Indiana. We  
20 also mobilize other employees such as transportation, information technology, and  
21 engineering personnel as necessary or required. If necessary, ULH&P will contact  
22 other utilities for additional line crews through a mutual assistance program. We  
23 routinely set up an emergency response center adjacent to the System Operations

1 Center to coordinate storm operations and use several sophisticated tools such as  
2 the trouble call outage management system (“TCOMS”), crew tracking and outage  
3 reporting to provide decision support. In some cases, we locate emergency  
4 response centers in affected areas to better coordinate our response.

5 **Q. PLEASE DESCRIBE HOW THE TCOMS SYSTEM HELPS THE**  
6 **RELIABILITY OF THE ULH&P SYSTEM.**

7 A. TCOMS is a tool to help with the restoration of service after an outage has  
8 occurred. It is used both for routine outages and for major events. Customers  
9 typically report outages by telephone through ULH&P’s call center. The call  
10 center creates an outage call through a telephone software application that  
11 interfaces with TCOMS, a state-of-the-art outage management software  
12 application that ULH&P adopted in 2001 to improve its ability to monitor and  
13 respond to outages. TCOMS analyzes the calls and identifies to ULH&P’s  
14 dispatchers the piece of equipment (circuit breaker, recloser, fuse, transformer,  
15 *etc.*) that has isolated the probable location of the outage. The dispatcher contacts  
16 the field trouble response person through the radio system to direct him/her to the  
17 location to make repairs and restore electric service to the customers. Generally,  
18 the field trouble response person inspects the circuit or segment of line in question  
19 to identify and report the cause of the outage. Cinergy has recently committed to a  
20 new, upgraded version of TCOMS, and expects to have this newer version  
21 available by the end of the year.

#### IV. RELIABILITY AFTER THE MERGER

22 **Q. WILL THE PROPOSED MERGER OF THE CINERGY COMPANIES,**

1           **INCLUDING ULH&P WITH DUKE ENERGY, HAVE ANY IMPACT ON**  
2           **THE RELIABILITY OF ULH&P'S SERVICE?**

3    A.    In my opinion there will not be any adverse impacts on ULH&P's reliability as a  
4           result of the Merger. Cinergy has been committed to providing reliable service  
5           and this commitment will continue after the Merger. There are no plans to  
6           eliminate service centers as a part of the Merger; there are no plans to eliminate  
7           control centers as a part of the Merger; there are no plans to reduce equipment,  
8           such as crew trucks as a part of the Merger; there are no plans to reduce the  
9           numbers of critical field personnel such as electric linemen, gas mechanic  
10          operators or the plant personnel; and, as discussed by Richard Osborne, Duke  
11          Energy is also committed to reliability. In my opinion, the only impacts on  
12          reliability arising from this Merger will be positive.

13   **Q.    WHY DO YOU BELIEVE THAT THERE WILL POSITIVE IMPACTS ON**  
14          **RELIABILITY ARISING OUT OF THE PROPOSED MERGER?**

15   A.    My belief is based on our experience implementing the Cinergy merger. We  
16          found that PSI and CG&E had different approaches to some issues. We were able  
17          to select best practices from both companies. The operating companies have also  
18          been able to share personnel, call center capacity, equipment and spare parts. In  
19          my opinion, this has led to better service for our customers throughout the Cinergy  
20          system. I would expect to see some of the same results from this Merger.

21   **Q.    ARE THERE OBJECTIVE INDICES THAT THIS COMMISSION COULD**  
22          **USE TO MEASURE ULH&P'S RELIABILITY?**

1 A. Yes. As I mentioned, ULH&P tracks its reliability in accordance with, CAIDI,  
2 SAIDI, and SAIFI, which are generally recognized standards for measuring  
3 electric reliability. As a way for this Commission to monitor ULH&P's reliability  
4 after the merger, ULH&P will commit to make an annual filing with this  
5 Commission that sets forth ULH&P's CAIDI, SAIDI, and SAIFI data for the  
6 previous year.

7 **Q. WAS ATTACHMENT JCP-1 PREPARED BY YOU OR UNDER YOUR**  
8 **SUPERVISION?**

9 A. Yes, it was.

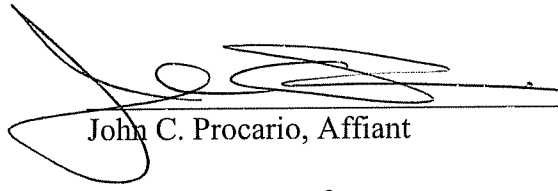
10 **Q. DOES THIS CONCLUDE YOUR DIRECT TESTIMONY?**

11 A. Yes.


**VERIFICATION**

State of Ohio            )  
                                  )  
County of Hamilton )       SS:

The undersigned, John C. Procario, being duly sworn, deposes and says that he is Senior Vice President for The Union Light, Heat and Power Company and The Cincinnati Gas & Electric Company, and Chief Operating Officer, Regulated Businesses for Cinergy Corp., and that the matters set forth in the foregoing testimony are true and correct to the best of his information, knowledge and belief.

  
\_\_\_\_\_  
John C. Procario, Affiant

Subscribed and sworn to before me by John C. Procario on this 1<sup>st</sup>  
day of July, 2005.

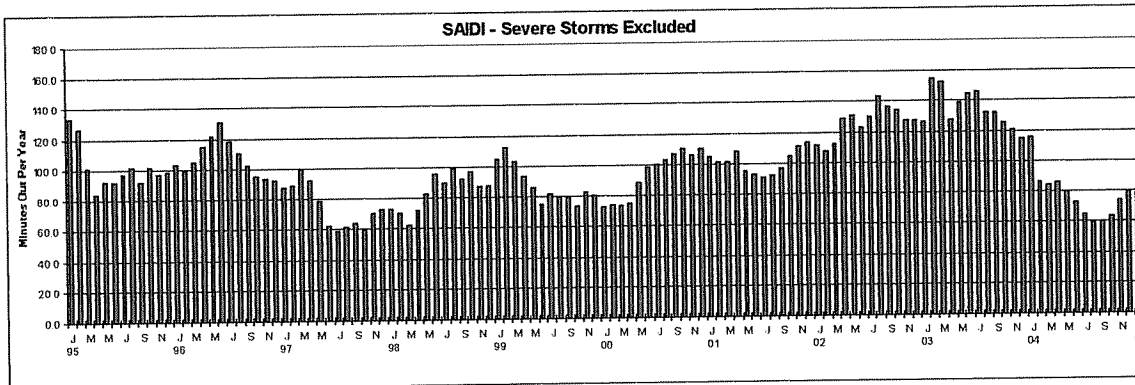
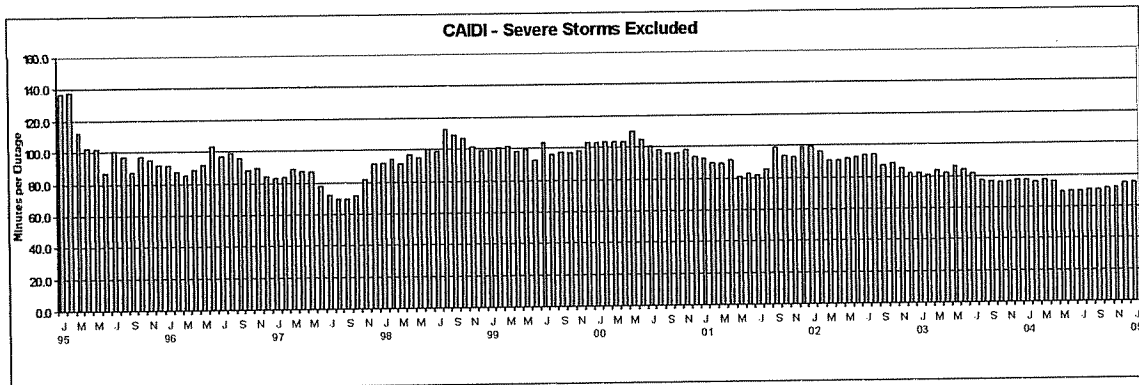
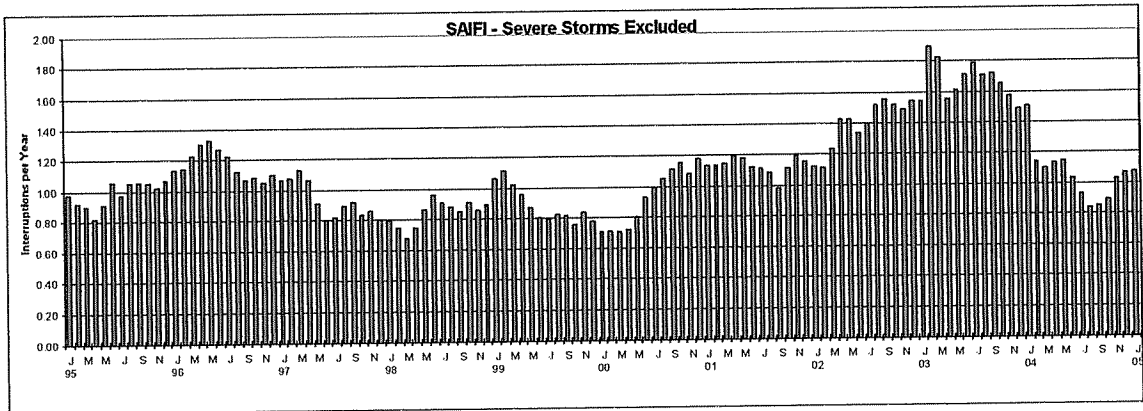
  
\_\_\_\_\_  
NOTARY PUBLIC

My Commission Expires: 9-15-09

PATTY A. SELM  
NOTARY PUBLIC, STATE OF OHIO  
My Commission Expires 09-15-2009



The following three charts show the rolling 12 month average for the past ten years for ULH&P SAIFI, CAIDI, and SAIDI with major storms removed.



The following three charts show the rolling 12 month average for the past ten years for ULH&P SAIFI, CAIDI, and SAIDI with no major storm exclusions.

