Attachment E

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ORIGINAL

STATE OF INDIANA

INDIANA UTILITY REGULATORY COMMISSION

VERIFIED PETITION OF PSI ENERGY, INC. CONCERNING: (1) CERTAIN AFFILIATE TRANSACTIONS, INCLUDING SERVICE AGREEMENTS, (2) THE SHARING OF MERGER-RELATED BENEFITS WITH CUSTOMERS, (3) DEFERRED ACCOUNTING OF CERTAIN MERGER-RELATED COSTS, (4) AUTHORITY TO CONTINUE MAINTAINING CERTAIN BOOKS AND RECORDS OUTSIDE THE STATE OF INDIANA, AND (5) ANY AND ALL OTHER ISSUES RELATING TO THE MERGER OF CINERGY CORP., THE PARENT COMPANY OF PSI ENERGY, INC., AND DUKE ENERGY CORPORATION INTO A NEW PUBLIC UTILITY HOLDING COMPANY	)	CAUSE NO. 42873 APPROVED: MAR 1 5 2006

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BY THE COMMISSION:
David E. Ziegner, Commissioner
Scott R. Storms, Chief Administrative Law Judge

On June 15, 2005, PSI Energy, Inc. ("Petitioner" or "PSI") filed a Petition initiating this Cause with the Indiana Utility Regulatory Commission ("IURC" or "Commission"). In its Petition PSI sought the following relief relating to the impending merger ("Merger") of Cinergy Corp. ("Cinergy"), the parent company of PSI, and Duke Energy Corporation ("Duke"): 1) approval to share a portion of net Merger savings with its retail electric customers, and to defer certain Merger-related costs; 2) approval of new service agreements and other affiliate agreements; 3) opening a sub-docket to consider revisions to PSI's Affiliate Guidelines; 4) approval for PSI to continue to maintain certain books and records outside of the State of Indiana; and, 5) a finding that the Merger will not adversely impact PSI's customer service, reliability, rates, financial integrity, or other relevant performance.

On July 1, 2005 and on October 13, 2005, by docket entries, the Presiding Officers advised the parties that the Commission had designated certain members of its technical staff as Testimonial Staff ("IURC Testimonial Staff") for purposes of this proceeding pursuant to Ind. Code § 8-1-1-5(b). The following parties petitioned to intervene in this proceeding, which petitions were granted by the Presiding Officers: International Brotherhood of Electrical Workers, Local Union No. 1393 ("IBEW"); Wabash Valley Power Association, Inc. ("WVPA"); Steel Dynamics, Inc. ("SDI"); Nucor Corporation ("Nucor"); Hoosier Rural Electric Cooperative, Inc. ("Hoosier"); Citizens Acton Coalition of Indiana, Inc. ("CAC"); and PSI-Industrial Group ("PSI-IG").

On August 24, 2005, the Commission issued a Prehearing Conference Order in this matter in which it approved an agreed upon procedural schedule for the prefiling of evidence and

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the holding of an Evidentiary Hearing in this Cause. On December 8, 2005, prior to the Evidentiary Hearing, counsel for the IURC Testimonial Staff filed a *Notice of Settlement in Principle and Joint Motion to Suspend and Reset Procedural Schedule* ("Notice") in this proceeding. On December 8, 2005, the Presiding Officers issued a Docket Entry suspending the current procedural schedule and setting December 9, 2005 as an Attorneys' Conference to consider the proposed procedural schedule in the Notice.

On December 15, 2005, PSI filed a Settlement Agreement ("Settlement Agreement") between PSI, the IURC Testimonial Staff, the Office of Utility Consumer Counselor ("OUCC") and PSI-IG (collectively referred to as the "Settling Parties") with the Commission. The Settlement Agreement completely resolves all issues among the Settling Parties in this proceeding.[1]

A public Evidentiary Hearing in this proceeding was held beginning on January 20, 2006, at 10:30 a.m., EST, in Conference Center #32 in the Indiana Government Center South, Indianapolis, Indiana, and continued thereafter on January 24-26, 2006. PSI, OUCC, PSI-IG, CAC, Hoosier, Nucor, and IURC Testimonial Staff appeared and participated at the Evidentiary Hearing. No other persons or entities appeared or participated at the Evidentiary Hearing. Members of the general public were present during the Evidentiary Hearing.

At the Evidentiary Hearing, PSI offered the initial testimony and exhibits of James E. Rogers, Richard J. Osborne, Thomas J. Flaherty, Kay Pashos, John C. Procario, Lynn J. Good, Wendy L. Aumiller, Steven M. Fetter, Barry F. Blackwell and John P. Steffen. Hoosier offered the initial testimony of Thomas L. Bernardi. CAC offered the initial testimony and exhibits of Robert M. Fagan. PSI also offered the rebuttal testimony and exhibits of Thomas J. Flaherty, Kay Pashos, John C. Procario, Steven M. Fetter, Barry F. Blackwell and John P. Steffen. PSI offered the settlement supporting testimony and exhibits of Kay Pashos, John C. Procario, and John P. Steffen. OUCC offered the testimony of Robert M. Endris supporting the Settlement Agreement. CAC offered the settlement opposing testimony and exhibits of Robert M. Fagan. Finally, PSI offered the settlement supporting rebuttal testimony of Kay Pashos, Wendy L. Aumiller and Barry F. Blackwell. The IURC Testimonial Staff supported the settlement supporting testimony and exhibits offered by PSI and the OUCC. No other party offered or sponsored any other witnesses at the Evidentiary Hearing in this proceeding. At the close of the record, the parties were authorized to file proposed orders and briefs in support, as well as exceptions to proposed orders and reply briefs, in accordance with a procedural schedule established by the Presiding Officers.

The Presiding Commissioner and Chief Administrative Law Judge attended all of the Evidentiary Hearings in this proceeding and have thus observed the demeanor and credibility of the witnesses. This Commission has considered the evidence presented herein, including the Settlement Agreement, in making the findings and conclusions in this Order. Based on the applicable law and evidence presented herein, and being duly advised, this Commission now finds as follows:

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[1] While IBEW, WVPA, Hoosier, CAC, Nucor and SDI are not parties to the Settlement Agreement, the only party to testify in opposition to the Settlement Agreement was the CAC.

1. **Notices and Jurisdiction.** Due, legal and timely notice of the filing of the Petition herein was given and published by PSI as required by law. Due, legal and timely notices of the Prehearing Conference and the Evidentiary Hearing in this proceeding were given and published by the Commission as required by law. PSI is a public utility within the meaning of Ind. Code § 8-1-2-1 and is subject to the jurisdiction of this Commission, in the manner and to the extent provided by the Indiana Public Service Commission Act, Ind. Code 8-1-2. This Commission has jurisdiction over PSI and the subject matter of this proceeding.

2. **PSI's Characteristics.** PSI is a public utility organized and existing under the laws of the State of Indiana, and has its principal office at 1000 East Main Street, Plainfield, Hendricks County, Indiana. PSI is engaged in rendering electric utility service in the State of Indiana, and owns, operates, manages and controls, among other things, plant and equipment within the State of Indiana used for the production, transmission, delivery and furnishing of such electric service to the public. PSI is a wholly-owned subsidiary of Cinergy.

3. **Duke's Characteristics.** Mr. Richard J. Osborne, Duke's Group Vice President for Public and Regulatory Policy, testified as to Duke's corporate structure and background. Mr. Osborne stated that Duke is a diversified energy company which operates a variety of regulated and unregulated natural gas and electric businesses throughout the Americas, and also operates a real estate company known as Crescent Resources. (Pet. Ex. B, pp. 3 and 6.) Mr. Osborne explained that Duke owns assets valued at $55.5 billion, and has annual revenues of $22.5 billion and net income of $1.5 billion. Mr. Osborne indicated that Duke owns and operates generating stations of 32,000 megawatts ("MW"), and operates an additional 3,000 MW of generating assets for others. Mr. Osborne also stated that Duke owns 17,500 miles of natural gas transmission pipeline and co-owns 59,000 miles of gathering pipeline with ConocoPhillips. (Pet. Ex. B, pp. 3-4.)

Mr. Osborne further explained that Duke Power is a division of Duke and is headquartered in Charlotte, North Carolina. Mr. Osborne described Duke Power as one of the largest U.S. investor-owned utilities, with 2.2 million electric customers in its 22,000 square-mile service territory encompassing central and western North Carolina and western South Carolina. He stated that Duke Power owns and operates a diverse portfolio of generating assets consisting of eight coal-fired stations (7,754 MW), three nuclear stations (5,020 MW owned, 6,996 MW operated), 31 hydroelectric stations, with two pumped storage facilities (2,819 MW), two combustion turbine stations and several additional combustion turbine units (2,446 MW). (Pet. Ex. B, p. 4.)

Mr. Osborne also described Duke's other principal businesses. He stated that Duke Energy Gas Transmission ("DEGT") transports natural gas through 17,500 miles of transmission pipelines throughout the northeastern and southeastern United States, as well as the Pacific Northwest and Canada. Mr. Osborne also stated that these transmission pipelines include facilities located in the State of Indiana. DEGT owns 250 billion cubic feet of natural gas storage facilities and also owns two liquid natural gas storage and regasification plants. Mr. Osborne testified that DEGT also owns Union Gas, an integrated natural gas storage, transmission and distribution company based in Ontario, Canada, with 1.2 million retail gas customers. (Pet. Ex. B, pp. 4-5.)

Mr. Osborne stated that Duke Energy Americas consists of Duke Energy North America ("DENA") and Duke Energy International ("DEI"). He explained that DENA owns and operates merchant power generating assets and markets electricity, natural gas and energy management services to North America wholesale customers. Mr. Osborne further stated that DEI owns and operates generating assets and sells power and natural gas in Latin America. (Pet. Ex. B, p. 5.)

According to Mr. Osborne, Duke's other principal businesses include Duke Energy Field Services, a joint venture between Duke and ConocoPhillips, which is the largest North American producer, and one of the largest North American marketers, of natural gas liquids. He described Crescent Resources as the aforementioned real estate company which manages and develops property throughout a nine-state region. Mr. Osborne also testified that DukeNet develops and manages fiber optic communication systems for wireless, local and long-distance communications companies and large customers in the southeastern United States. (Pet. Ex. B, pp. 5-6.)

4. **The Proposed Duke/Cinergy Merger.** Mr. James E. Rogers, Chairman, President and Chief Executive Officer of Cinergy, will be the President and Chief Executive Officer of the new holding company to be created by the Merger, to be named Duke Energy Corporation ("New Duke Energy"). Mr. Rogers testified that the Merger will be consummated via an all-stock transaction at the holding company level. Mr. Rogers stated that, as a result of the Merger, PSI will continue to be a wholly-owned subsidiary of Cinergy and will become an indirect wholly-owned subsidiary of New Duke Energy. (Pet. Ex. A, p. 6.) Mr. Rogers stated that Cinergy's shareholders will receive 1.56 shares of New Duke Energy common stock for each share of Cinergy common stock owned, amounting to a 13.4% premium for Cinergy shareholders based on Cinergy's and Duke's stock prices immediately prior to the May 9, 2005 Merger announcement. (Pet. Ex. A, p. 6.) Following the Merger, Mr. Rogers stated that New Duke Energy will be headquartered in Charlotte, North Carolina, and PSI will remain headquartered in Plainfield, Indiana. (Pet. Ex. A, p. 7.)

Ms. Kay Pashos, PSI's President, testified that the Energy Policy Act of 2005 ("EPAct of 2005") repealed the Public Utility Holding Company Act of 1935 ("PUHCA") effective six months after enactment of the EPAct of 2005. (Pet. Ex. D, p. 4.) Ms. Pashos explained that Cinergy is currently a registered public utility holding company under the PUHCA and is subject to the U.S. Securities and Exchange Commission's ("SEC") regulatory authority. She stated that Cinergy and Duke will not file for SEC merger approval under PUHCA, due to PUHCA's repeal. Nevertheless, Ms. Pashos stated that PSI will still enter into service agreements and other affiliate agreements, described below, similar to its present service agreements and affiliate agreements required under PUHCA. (Pet. Ex. D, pp. 4-5.)

5. **The Settlement Agreement.** A copy of the Settlement Agreement is attached to and incorporated into this Order. The Settlement Agreement's major provisions (which are discussed in more detail in further Findings below) include:

(a) **Additional Merger Commitments**: In addition to the other specific provisions of the Settlement Agreement, PSI agreed to 42 specific Merger commitments, as set forth in Attachment 1 to the Settlement Agreement.

(b) Rate Credit: PSI will provide a retail electric rate credit of $40 million dollars paid over one year after the Merger closing.

(c) Contributions to Community: PSI will contribute $2.5 million dollars to the Indiana Center for Coal Technology Research and $2.5 million dollars to the Low Income Home Energy Assistance Program ("LIHEAP") for low income electric customers in PSI's service territory.

(d) 1994 Cinergy Merger Costs: Starting June 1, 2008, PSI will reduce its retail electric rates by $11.552 million dollars annually, representing the annual amortization of costs from the 1994 Cinergy merger, and will not seek any future retail electric rate recovery of such costs.

(e) Duke/Cinergy Merger Costs: PSI will not recover transaction costs associated with the Duke/Cinergy Merger from Indiana retail electric customers, but may reflect such costs on its books below-the-line. PSI may retain Merger savings in excess of the rate credit and the $5 million dollars contribution to the community, subject to the Fuel Adjustment Clause ("FAC") earnings test of Ind. Code § 8-1-2-42(d). PSI shall reflect actual Merger savings and actual PSI retail jurisdictional costs to achieve Merger savings in PSI's FAC filings, except that, during the first two years after the Merger, PSI's FAC filings shall reflect the lesser of the actual PSI retail jurisdictional costs to achieve Merger savings or $42 million dollars. If PSI seeks to recover PSI retail jurisdictional costs to achieve Merger savings in its next base retail electric rate case, PSI must prove that such costs are prudent, reasonable and recurring.

(f) Affiliate Agreements and Audits: The Settlement Agreement provides for this Commission to approve the five affiliate agreements filed by PSI with its case-in-chief testimony in this proceeding. PSI agreed to fund and cooperate in a series of four independent audits of PSI's compliance with its Affiliate Standards (see item (k) below), including an audit of the Affiliate Standards training and controls PSI has in place to prevent cross-subsidization, plus an additional audit of the five affiliate agreements. The Settlement Agreement also details related procedures, such as selecting the auditor, funding the audits, audit timing and challenging audit results.

(g) Service Quality Reliability and Customer Service: PSI shall file quarterly reports with this Commission on its actual performance on SAIDI (*i.e.*, the System Average Interruption Duration Index), SAIFI (*i.e.*, the System Average Interruption Frequency Index), CAIDI (*i.e.*, the Customer Average Interruption Duration Index) and average speed of answer as described in the Settlement Agreement. If PSI exceeds two or more of the specified benchmarks during any quarter for the first five years after the Merger, PSI will implement a Commisson-approved remediation plan, after notice and hearing, at a cost of up to $5 million dollars, at stepped-in levels depending on the number of missed benchmarks. PSI is also required to provide 30 days advance written notice to the Commission and the Settling Parties of any decision to close or move the Plainfield Call Center out of the State of Indiana, which notice shall include the business criteria used to make the decision. If the Plainfield Call Center is closed within three years after the Merger closing, PSI must contribute $500,000 to the Indiana Economic Development Corporation or a successor fund with a similar purpose.

(h) Coordination of Regulation: After the Merger closing, PSI shall not challenge or seek review, based on a Federal Energy Regulatory Commission ("FERC") preemption theory, of an Order of this Commission that changes, for Indiana retail ratemaking purposes only, the allocation factors applied to PSI in the Merger-related affiliate agreements. The Settlement Agreement provides that it should be applied so as to avoid stranding reasonable utility costs among the various regulatory jurisdictions where PSI and its utility affiliates operate. Additionally, the Settlement Agreement acknowledges that the respective rights of PSI and this Commission under Section 1275 of Subtitle F, Repeal of the Public Utility Holding Company Act of 1935 in Title XII of the Energy Policy Act of 2005 ("PUHCA 2005") are expressly reserved.

(i) Books and Records: PSI may continue to locate its books and records outside the State of Indiana. PSI shall make its records and personnel available in the State of Indiana for any required audits or, in the alternative, shall pay travel expenses for the staffs and designated experts of this Commission and the OUCC.

(j) Integrated Resource Planning: PSI agrees to follow the procedures set forth in the Settlement Agreement for PSI's planning for additional generating facilities and for obtaining this Commission's approval for such generating facilities, including the use of clean coal technology and PSI's environmental compliance plans. Under the terms of the Settlement Agreement, PSI shall also obtain Commission approval for any purchase of firm power or unit power from an affiliate for a term of five years or longer.

(k) Affiliate Standards: PSI shall follow the Affiliate Standards set forth in Attachment 2 to the Settlement Agreement, which shall replace PSI's current Affiliate Guidelines effective immediately upon the Merger closing. After the Merger closing and finalization of the FERC's PUHCA 2005 Final Rules in FERC Docket RM05-32-000, the Settling Parties shall work together to implement any necessary changes to PSI's Affiliate Standards.

(l) Rate Design: The Settlement Agreement provides that in its next retail electric base rate case, PSI shall provide and fully support a cost of service and rate design for production plant using a four coincident peak ("4 CP") methodology.

6. Commission Jurisdiction and Standards for Approval of the Settlement Agreement. This Commission has no jurisdiction to review or approve stock transactions at the holding company level, such as the Duke/Cinergy Merger; however, this Commission has jurisdiction to review the Merger's impacts on PSI's retail electric customers. *Indiana Bell Tel. Co. v. Indiana Util. Reg. Comm'n*, 715 N.E.2d 351 (Ind. 1999); *In re the Commission's Investigation, under IC §§ 8-1-2-58 and 59, into the Proposed Termination of the 1951 Operating Agreement Between American Electric Power, Inc. and Indiana Michigan Power Company*, Cause No. 42045-S1 (Opinion and Order) (*Ind. Util. Reg. Comm'n*, April 28, 2004).

"It is the policy of the Commission to review and accept appropriate settlements." 170 IAC 1-1.1-17(a). The Commission may approve a settlement agreement if it is supported by substantial evidence, and the Commission finds it to be in the public interest. In this case, the Commission is reviewing a Settlement Agreement entered into by PSI, the IURC Testimonial

Staff, the OUCC, and PSI-IG. It is a settlement of fewer than all the parties to this proceeding and fewer than all the parties that participated in the negotiations. Settlement agreements by less than all the parties may be submitted to this Commission pursuant to 170 IAC 1-1.1-17(b). This Commission may reject, in whole or in part, any proposed settlement if we determine the settlement is not in the public interest. 170 IAC 1-1.1-17(c).

Settlements presented to this Commission are not ordinary contracts between private parties. *United States Gypsum, Inc. v. Indiana Gas Co.,* 735 N.E.2d 790, 803 (Ind. 2000). When this Commission approves a settlement, that settlement "loses its status as a strictly private contract and takes on a public interest gloss." *Id.* (quoting *Citizens Action Coalition v. IPL Energy,* 664 N.E.2d 401, 406 (Ind. Ct. App. 1996)). Thus, this Commission "may not accept a settlement merely because the private parties are satisfied; rather [the Commission] must consider whether the public interest will be served by accepting the settlement." *Citizens Action Coalition,* 664 N.E.2d at 406.

Furthermore, any Commission decision, ruling, or order – including the approval of a settlement – must be supported by specific findings of fact and sufficient evidence. *United States Gypsum,* 735 N.E.2d at 795 (citing *Citizens Action Coalition v. Public Service Co.,* 582 N.E.2d 330, 331 (Ind. 1991)). This Commission's own procedural rules require that settlements be supported by probative evidence. 170 IAC 1-1.1-17(d). Therefore, before this Commission can approve the Settlement Agreement, we must determine whether the evidence in this proceeding sufficiently supports the conclusion that the Settlement Agreement serves the public interest and the customer rate credit is reasonable, just and not inconsistent with the purpose of the Indiana Public Service Commission Act, Ind. Code 8-1-2.

7. **Additional Merger Commitments.** The Settlement Agreement contains in Attachment 1 a list of 42 specific Merger commitments by PSI in addition to those set forth in the main part of the Settlement Agreement. These Merger commitments deal with areas such as reliability, customer service, ratemaking and accounting, affiliate transactions, financial insulation, the Midwest Independent Transmission System Operator, Inc., integrated coal gasification combined cycle generating facility, local presence/economic development, corporate governance/environmental stewardship and integrated resource planning. (Pet. Ex. K, p. 2.) These Merger commitments are intended to replace the merger commitments from the 1994 Cinergy merger, so that PSI's Merger commitments will be clearly known and understood by all parties in the future. (Pet. Ex. K, p. 8.)

CAC witness Mr. Robert M. Fagan, Senior Associate at Synapse Energy Economics, Inc., testified that these additional Merger commitments do not adequately protect PSI's customers, and that additional measures are necessary to adequately protect customers from incurring higher rates from the Merger. (CAC Ex. RMF-S, p. 19.) This practice of establishing conditions to protect a public utility from adverse financial impacts from its parent company's and affiliates' non-regulated businesses is sometimes called "ring-fencing." Mr. Fagan raised several ring-fencing concerns. First, Mr. Fagan voiced concern about the impact of the Merger on future ratemaking outcomes in Indiana, including especially the capital structure and associated capital costs on which PSI earns a regulated return. He reasoned that PSI's proposed Merger commitments were inadequate because, during PSI's next rate case, New Duke Energy's non-regulated businesses could cause PSI to have a higher cost of capital. (CAC Ex. RMF-S, pp. 20-21.) Second, Mr. Fagan recommended that PSI provide assurances that PSI's customers will not

be exposed to any costs associated with non-jurisdictional investments made by PSI or its affiliate or parent companies. (CAC Ex. RMF-S, p. 21.) Third, Mr. Fagan claimed that the proposed additional Merger commitments did not adequately specify the manner in which this Commission can truly retain cost disallowance authority over PSI for costs intended to be allocated to ratepayers that this Commission may deem unreasonable, imprudent or unjust. (CAC Ex. RMF-S, pp. 22-23.)

Mr. Fagan stated that the larger scope and greater risk of New Duke Energy's non-regulated businesses will require investors to demand a higher return. (CAC Ex. RMF-S, p. 20.) He recommended that the Commission should aggressively ring-fence PSI from the adverse impacts of its affiliate relationships, and should adopt the regulatory conditions imposed by the North Carolina Utilities Commission Public Staff ("North Carolina Public Staff") in the corresponding North Carolina proceeding regarding the Cinergy/Duke Merger. (CAC Ex. RMF-S, pp. 19-20 and 23-25.) Mr. Fagan proposed that PSI should make additional commitments involving various matters such as financially insulating PSI from the adverse effects of: its affiliate relationships; PSI's power purchases from affiliates; the integrated resource planning process; generation acquisition; and allocation of purchased power costs to PSI's retail electric customers. (CAC Ex. RMF-S, pp. 25-28.) Mr. Fagan also proposed that PSI should affirmatively assert that this Commission is authorized to take various actions to protect PSI's customers from possible adverse effects from the Merger. (CAC Ex. RMF-S, p. 21.) Mr. Fagan contended that the Settlement Agreement provision addressing coordination of regulation is confusing and provides inadequate protection for customers. (CAC Ex. RMF-S, pp. 22-23.) Mr. Fagan provided a list of "hold harmless" Merger conditions, which he said were adapted from the settlement agreement between Duke Energy Corporation and the North Carolina Public Staff. (CAC Ex. RMF-S, pp. 25-26.) Mr. Fagan also provided a number of commitments relating to preemption, which primarily deal with wholesale market transactions, and which he adapted from the North Carolina settlement agreement. (CAC Ex. RMF-S, pp. 26-28.)

In her settlement supporting rebuttal testimony, Ms. Kay Pashos posited that Mr. Fagan's proposed additional Merger commitments and requirements are unnecessary because other provisions of the Settlement Agreement will adequately protect PSI's retail electric customers. (Pet. Ex. U, pp. 8-12.) Ms. Pashos pointed out that the Settlement Agreement's Affiliate Standards provide extensive protections against potentially harmful effects from PSI's affiliate transactions. (Pet. Ex. U, pp. 9-10.) Ms. Pashos stated that the Settlement Agreement also provides for PSI to make 42 additional Merger commitments in areas such as service reliability, customer service, ratemaking and accounting, and protecting PSI from the adverse effects of affiliate relationships. (Pet. Ex. U, pp. 10-11.) Ms. Pashos also noted that the Settlement Agreement contains additional Merger commitments in areas such as affiliate agreements and audits, service quality reliability and customer service, coordination of regulation and affiliate standards. (Pet. Ex. U, pp. 11-12.)

Ms. Wendy L. Aumiller, Cinergy's Vice President and Treasurer, also provided settlement supporting rebuttal testimony addressing Mr. Fagan's position relating to Merger commitments. As to Mr. Fagan's contention that New Duke Energy's larger scope and greater risk will require investors to demand greater returns, Ms. Aumiller noted that, in the instance of PSI and its current and prospective holding companies: (i) PSI operates (and will continue to operate) as legally separate from its holding company with PSI's creditors having priority claim over PSI's assets; (ii) no loans or guarantees exist (or will exist without this Commission's

approval) from PSI to its holding company; (iii) there are (and will continue to be) no cross-default provisions in PSI's loan agreements; (iv) PSI's holding company has provided (and will continue to provide) financial support, as needed, an especially important factor in light of the size of PSI's ongoing construction program. Ms. Aumiller observed that PSI raises its own capital, independent of its holding company and could access short-term borrowing markets if its holding company's financial condition deteriorates. (Pet Ex. V, pp. 3-4.)

Ms. Aumiller also responded to Mr. Fagan's recommendation that PSI should be aggressively ring-fenced or insulated from the financial risk arising from its affiliate relationships. Ms. Aumiller pointed out that this Commission submitted comments to the FERC, regarding the FERC's rulemaking on implementing the EPAct of 2005, and recommended various protections for utilities involved in mergers where the holding company will have large non-regulated businesses. (Pet. Ex. V, p. 5.) Ms. Aumiller noted that the Settlement Agreement provides for each of the applicable protections recommended by the Commission in its comments to the FERC. The only protections that were not adopted directly by PSI were those recommendations that were directed and discussed in the context of future rulemakings that may be undertaken by the FERC. (Pet. Ex. V, pp. 5-7.) She also stated that PSI derives additional financial protection from the Cinergy companies' FERC-approved Codes of Conduct (and that similar Codes of Conduct will be in place under the Merger); from PSI's new Affiliate Standards included in the Settlement Agreement, which expand PSI's currently effective Affiliate Guidelines; and from the Settlement Agreement requirement for PSI to conduct independent audits of its compliance with the new Affiliate Standards. (Pet. Ex. V, p. 7.)

Ms. Aumiller also testified that she believes that aggressive ring fence protections could be harmful to PSI's retail customers. She stated that PSI's stand alone credit quality would have been adversely impacted in the past without the support of its affiliate, The Cincinnati Gas & Electric Company, on dividend relief and low cost borrowing through the Cinergy Utility Money Pool. She noted that Moody's Investors' Service recognized this support in its May 22, 2005 Liquidity Assessment Report concerning PSI. (Pet Ex. V, p. 7.)

In response to Mr. Fagan's statement that New Duke Energy's non-utility businesses would cause concern for PSI's retail customers, Ms. Aumiller responded that Duke Energy has announced that it will substantially exit the DENA marketing and trading business, which will improve Duke Energy's credit quality. (Pet. Ex. V, pp. 7-9.) Specifically in her settlement supporting rebuttal testimony, Petitioner's Exhibit V, Ms. Aumiller testified that Standard & Poor's ("S&P") addressed Duke Energy's announced sale of the majority of its non-regulated generating assets (*i.e.,* the DENA assets) and its electric and gas contracts (*i.e.,* the DENA book) and S&P's assignment of a stable outlook as follows:

> The stable outlook reflects Standards & Poor's assessment that, once executed, Duke Energy's plan to sell 6,200 MW of merchant generation capacity in the western and northeastern U.S., along with the disposition of its book of electric and gas contracts, will improve Duke Energy's business risk profile, thereby providing support to its credit quality. The stable outlook also accounts for a measure of clarity in the combined company's corporate structure that alleviates earlier concerns arising from Duke Energy's assertion that the electric and gas businesses could be eventually separated.

Ms. Aumiller also testified that the January 10, 2006 announcement by Duke Energy Corporation that it had found a buyer (*i.e.*, LS Power Equity Partners) for 6,200 MW of merchant generation in the west and northeast United States (*i.e.*, DENA generating assets) resulted in the following favorable comments from S&P:

> Duke Energy Corp.'s announcement that it is selling 6,200 MW of merchant generation assets in the west and northeast U.S. to LS Power Equity Partners is positive for credit quality but does not affect the company's ratings.
>
> Duke's business risk profile improves to '6' (satisfactory) from '7' (weak) (business risk profiles are ranked from '1' (excellent) to '10' (vulnerable)).
>
> This revision reflects that the merchant-asset sale, combined with the sale of the derivative and physical contracts, significantly moderates business risk by eliminating earnings and cash flow variability, reducing Duke's collateral requirement and reducing or eliminating the imputation of off-balance-sheet debt.
>
> Given Duke's business-risk improvement, Standard & Poor's expects that, post-merger, the combined entity will likely also have a '6' consolidated business risk profile.

(Pet. Ex. V, pp. 8-9.)

Ms. Aumiller further testified that, in her opinion, the Merger will not have any material adverse impact upon the financial integrity of PSI. (Pet. Ex. G, pp. 22) Finally, Ms. Aumiller provided a point-by-point response to Mr. Fagan's recommendations for additional financial insulation for PSI. She noted that Mr. Fagan's recommendations which he adapted from North Carolina were not equally applicable to PSI due to the different regulatory environments in Indiana and North Carolina. (Pet. Ex. V, pp. 9-11.) Nevertheless, she identified the specific additional financial insulation commitments recommended by Mr. Fagan that PSI was willing to accept if so mandated by this Commission in this proceeding, in addition to the provisions of the Settlement Agreement. (Pet. Ex. V, pp. 11-13.)

Ms. Pashos testified that she believes that the Settlement Agreement, including Attachments 1 and 2, provides adequate protection of PSI's retail electric customers from potential adverse impacts of the Merger. Taking the three major components of the Settlement Agreement separately, she noted that the Affiliate Standards included as Attachment 2 to the Settlement Agreement are specific and detailed provisions addressing: (a) Cross-Subsidization Principles; (b) Access to Employees, Officers, Books and Records; (c) Accounting for Affiliate Transactions; (d) Precluded Affiliate Financial Undertakings; (e) Untariffed, Non-Utility Services Provided by PSI or the Service Company; (f) Goods or Services Provided by a Non-Utility Affiliate; (g) Independent Operations; (h) Precluded Property Ownership; (i) Market Information; (j) Use of Name or Logo; (k) No Tying or Conditioning; (l) Sharing of Office Space, Office Equipment, Computer Systems or Information Systems with Affiliated Wholesale Power Marketers; (m) Exception for Computer Systems and Information Systems; (n) Limitations on Corporate Support Services to Affiliates; (o) Availability of Goods or Service to Affiliates; (p) Documentation; (q) Contract for Affiliate Transactions and Personnel Information; (r) Contact for Service and Reliability; (s) Contact for State Regulatory Matters; (t) PSI's Affiliate Contract Filings; (u) Violations; (v) Independent Audits; (w) Public Utility Holding

Company Act of 2005; (x) No Impairment of Service Company Structure; (y) No Preclusion of Commission Approved Actions or FERC Pricing Requirements for Affiliate Transactions; and (z) Affiliate Firm or Unit Power Purchase by PSI for a Term of 5 Years or More. Ms. Pashos also noted that the Affiliate Standards include 36 individual definitions of terms used in the Affiliate Standards. She also stated that the Affiliate Standards include provisions for detailed Annual Informational Filings, Additional Annual informational Filings and Special Informational Filings with this Commission (with a copy to the OUCC). (Pet. Ex. U, pp. 8-10.)

Ms. Pashos next noted that Attachment 1 of the Settlement Agreement includes 42 separate Additional Merger Commitments. The primary topics addressed by these 42 Additional Merger Commitments are identified above in the first paragraph of this Finding No. 7. (Pet Ex. U, pp. 10-11.) Ms. Pashos next addressed the Settlement Agreement document itself (not including Attachments 1 and 2). She listed 14 of the specific major topics addressed by the Settlement Agreement document. Twelve of these major topics are outlined above in the first paragraph of Finding No. 5, and many of those topics are discussed in further Findings below. (Pet. Ex. U, pp. 11-12.)

Ms. Pashos testified that she believed that the above lists of topics addressed in the Settlement Agreement (the substance of which provisions are addressed in PSI's settlement supporting testimony), clearly show that the Settlement Agreement in its entirety constitutes an integrated and comprehensive resolution of the issues before this Commission in this proceeding. Ms. Pashos further testified that the provisions of the Settlement Agreement are designed to address the specific facts, circumstances and retail electric rates of PSI, in the context of the specific Indiana statutory and regulatory environment. She concluded that, while PSI has expressed a willingness to accept certain provisions suggested by Mr. Fagan if the Commission determines that such action is appropriate, she did not believe that it is either necessary or appropriate to now "bolt on" the additional provisions that Mr. Fagan has "adapted" from North Carolina and is proposing. (Pet. Ex. U, p. 12.)

Based on the testimony presented, while we do not accept all of the suggested changes presented by Mr. Fagan in his testimony, we are convinced that the inclusion of certain additional requirements presented by the CAC are important and applicable to the state of Indiana. Accordingly we hereby approve the following additional Merger requirements in this Cause:

> PSI shall manage its business with the intention of maintaining at least an investment grade debt rating on all of its rated debt issuances with all of its debt rating agencies. If PSI's debt rating falls to the lowest level still considered investment grade at the time, PSI shall provide notice to the Commission and OUCC within five (5) days of such change and provide an explanation as to why the downgrade occurred. Within 45 days of such notice, PSI shall meet with the Commission and the OUCC and provide information regarding the steps it intends to take to maintain and improve its debt rating.
>
> PSI shall limit cumulative distributions paid to Duke Energy Corporation subsequent to the Merger to (i) the amount of Retained Earnings on the day prior to the closure of the Merger, plus (ii) any future earnings recorded by PSI subsequent to the Merger.

PSI shall not invest in a non-regulated utility asset or any non-utility business venture exceeding $50 million in purchase price or gross book value to PSI unless it provides 30 days' advance notice to the Commission. Purchases of assets, including land that will be held with a definite plan for future use in providing Electric Services in PSI's franchise area shall be excluded from this Advance Notice Requirement.

By April 15 of each year, PSI shall provide to the Commission and the OUCC a report summarizing PSI's investment in exempt wholesale generators (EWGs) and utility assets or companies in foreign countries in relation to its level of consolidated retained earnings and consolidated total capitalization at the end of the preceding year. (To be revised if the FERC does not continue to determine EWG status.)

Duke Energy Corporation and PSI shall adequately fund and maintain PSI's current and future generation, transmission, and distribution systems and otherwise meet the service needs of PSI's customers.

PSI may borrow short-term funds in the financial markets or through the "Utility Money Pool Agreement" (Utility MPA), provided that the Utility MPA (a) is modified to exclude Tri-State Improvement Company; and (b) continues to provide that no loans through the Utility Money Pool will be made to, and no borrowings through the Utility Money Pool will be made by Duke Energy Corporation and Cinergy Corporation. If, after December 31, 2008, certain of The Cincinnati Gas & Electric Company's generation assets are not dedicated to serving retail load in its service territory and are not subject to the rate stabilization plan (as approved in Case 03-93-ATA) or traditional regulation, then PSI shall obtain Commission approval to continue to participate in the Utility MPA. PSI shall acquire its long-term debt funds through the financial markets, and shall neither borrow from nor lend to, on a long-term basis, Duke Energy Corporation or any of its other Affiliates. To the extent that PSI borrows on short term or long-term bases in the financial markets and it is feasible to obtain a debt rating, its debt shall be rated under its own name.

If an Affiliate of PSI experiences a default of an obligation that is material to Duke Energy Corporation or files for bankruptcy, and such bankruptcy is material to Duke Energy Corporation, PSI shall notify the Commission in advance if possible, or as soon as possible, but not later than ten days from such event.

Accordingly, consistent with these additional requirements we find that the Merger commitments contained in the Settlement Agreement are fair, just and reasonable, and are in the public interest. Therefore, we approve the Merger commitments in the Settlement Agreement consistent with the additional requirements set forth herein.

8. **Rate Credit.** PSI presented detailed evidence in its case-in-chief on the estimated savings arising from the Merger, and on how the Merger savings and costs would be allocated among New Duke Energy's non-regulated businesses and regulated businesses, including PSI.

Mr. Thomas J. Flaherty, Senior Vice President with the Booz Allen Hamilton consulting firm, explained how the areas of savings were identified, how the amounts of estimated Merger savings and Merger costs were determined, and how the estimated savings and costs were developed. (Pet. Ex. C, pp. 11-12 and 16.) Mr. Barry F. Blackwell, Cinergy's Director of Management Reporting and Analysis, reviewed the proposed new Service Company Utility Service Agreement ("Service Agreement"), and discussed how the Merger savings and the Merger costs will be allocated to the various companies, including PSI. (Pet. Ex. I, pp. 4.)

Mr. John P. Steffen, Cinergy's Vice President Rates, testified that the $40 million rate credit paid over one year after the Merger closing will reduce PSI's average retail electric rates by 2.6% for one year. (Pet. Ex. T, p. 4.) He opined that the terms of the Settlement Agreement relating to Merger savings and costs are reasonable because PSI's retail electric customers would immediately benefit from lower rates, which they would not receive absent the Settlement Agreement. (Pet. Ex. T, p. 4.) Ms. Pashos stated that the $40 million rate credit and the $5 million in contributions for coal technology research and LIHEAP provide for PSI to share 42% of net Merger savings with customers, and is consistent with the Merger savings sharing provisions approved by the South Carolina, Kentucky and Ohio utility commissions. (Pet. Ex. R, p. 6.) Ms. Pashos also testified that the settlement terms are reasonable and within the regulatory mainstream when viewed against recent merger settlements and orders as presented in the rebuttal testimony, Petitioner's Exhibit O, of Mr. Steven M. Fetter, President of the Regulation Unfettered consulting firm. (Pet. Ex. R, p. 10.) Mr. Robert M. Endris, the OUCC's Assistant Director of the Electric Division, testified on behalf of the OUCC supporting the settlement. Mr. Endris stated that the Settlement Agreement as a whole is fair and in the public interest because it fairly distributes Merger savings to customers and provides other important benefits. (Pub. Ex. S-1, p. 2.)

Mr. Fagan testified in response that the he believes the rate credit is not fair as the Settlement Agreement provides no guarantee that PSI will file a rate case in a specified time period, which would allow customers to capture all the Merger savings attributable to PSI. As a result, he claimed that the rate credit could produce a worse result for customers than if PSI filed a rate case one or two years after the Merger. (CAC Ex. RMF-S, pp. 9-10.) Mr. Fagan also criticized the Settlement Agreement because it did not provide any mechanism for sharing Merger savings with customers during years six through ten after the Merger, absent a base rate case by PSI. (CAC Ex. RMF-S, p. 9.) He recommended that customers should receive 100% of the regulated Merger savings for the five-year period after the Merger and that this Commission should re-visit the issue at year six. (CAC Ex. RMF-S, p. 8.)

Mr. Fagan testified that this Commission would establish a poor precedent if it approved a Merger sharing mechanism which provides less than 50% of Merger savings for customers, and that this would be less than the proportion of Merger savings for customers approved in other merger cases as he described in this initial testimony at Exhibit RMF-4. (CAC Ex. RMF-S, pp. 8-9.) Mr. Fagan stated that the risk is low that New Duke Energy will not achieve the estimated Merger savings. (CAC Ex. RMF-S, pp. 9-10.) He noted that a due diligence document relating to the Merger suggests that an equitable sharing of Merger savings would be a 50/50 sharing of corporate and regulated savings with customers. (CAC Ex. RMF-S, p. 11.) Mr. Fagan pointed out that the same document provides for 65% regulated savings for Cinergy and 57% of the regulated savings for Duke Energy – for a total of 59% regulated gross savings. (CAC Ex. RMF-S, pp. 11-12.) Mr. Fagan claimed that this indicates that the Merger savings

allocated to PSI may be too low, because PSI has not established that this higher share of the regulated savings for Cinergy has been flowed through to PSI. (CAC Ex. RMF-S, pp. 11-12.)

In her settlement supporting rebuttal testimony, Ms. Pashos explained that the Settlement Agreement must be viewed as a whole, as part of a comprehensive negotiation among the Settling Parties, and that the rate credit was reasonable as part of an overall settlement which provides manifold customer benefits. (Pet. Ex. U, pp. 2-3.) Even if viewed in isolation, Ms. Pashos stated that the rate credit is well within the regulatory mainstream, as discussed in Mr. Fetter's rebuttal testimony, Petitioner's Exhibit O. (Pet. Ex. U, pp. 2-3.)

Addressing Mr. Fagan's claim that a pre-Merger document supported a 50/50 sharing of Merger savings with customers, Ms. Pashos testified that many changes have occurred since that time. For example, the merging companies have now omitted significant change in control costs from the calculation of net Merger savings. (Pet. Ex. U, pp. 3-4.) Second, the rate credit provides for customers to receive the Merger savings from the first five years on an up-front basis, in the first year after the Merger, which provides additional benefits that may not have been contemplated in the pre-Merger document. (Pet. Ex. U, p. 4.) Finally, Ms. Pashos noted that PSI will have certain earnings test exclusions for Merger-related costs and cannot defer transaction costs or recover costs to achieve Merger savings unless such costs fall within the test year of a rate case and are proven to be fair, just and reasonable. (Pet. Ex. U, p. 4.)

Upon cross examination, Mr. Flaherty made clear that the 50/50 assumption in the early Merger documents was a preliminary high level assumption only, and did not take into account all the other terms of a comprehensive settlement, such as that filed in this proceeding.

Mr. Barry F. Blackwell also provided settlement supporting rebuttal testimony on PSI's behalf. Mr. Blackwell testified that the actual allocation of Merger savings to the Duke/Cinergy regulated businesses was 63%, which is slightly higher than the 59% noted in the pre-Merger document relied upon by Mr. Fagan. (Pet. Ex. W, p. 2.) Mr. Flaherty testified on cross-examination that the original 59% estimate of corporate and shared service Merger savings going to the regulated businesses was simply a high level estimate using one allocation factor (*i.e.*, operation and maintenance expenses) and that subsequently Cinergy and Duke Energy performed additional analysis using the more comprehensive cost causation factors included in the proposed Service Company Utility Service Agreement ("Service Company Agreement") to come to a more accurate and detailed allocation. Mr. Blackwell also noted that 76% of the gross Merger savings attributable to corporate and shared services were allocated to the Cinergy regulated businesses in formulating the Settlement Agreement's rate credit, which is significantly better for PSI's customers than the 65% allocation noted in the pre-Merger document cited by Mr. Fagan. (Pet. Ex. W, pp. 2-3.)

9. <u>Contributions to Community</u>. The Settlement Agreement requires PSI, after the Merger closing, to make annual contributions of $500,000 to the Indiana Center for Coal Technology and $500,000 for LIHEAP to benefit low-income retail electric customers in PSI's service territory for a period of five years. (Pet. Ex. R-1, Section II(C).) No party offered any testimony opposing this provision of the Settlement Agreement.

10. <u>Resolution of 1994 Cinergy Merger Issues</u>. This provision of the Settlement Agreement requires PSI to reduce its retail electric base rates starting June 1, 2008 by $11.552

million dollars annually, which represents the annual amortization of costs in PSI's current retail electric base rates relating to the 1994 Cinergy merger. (Pet. Ex. R-1, Section II(D).) No party offered any testimony opposing this provision of the Settlement Agreement.

11. **Merger Costs.** The Settlement Agreement provides that PSI will not defer or amortize any transaction costs related to the Merger. PSI is barred from reflecting transaction costs in the earnings and expense test calculations of its FAC filings. PSI is, however, permitted to book transaction costs below-the-line for financial accounting purposes. The Settlement Agreement also restricts PSI's ability to defer and to recover costs to achieve Merger savings. Regarding costs to achieve Merger savings, PSI has agreed to cap at $42 million the amount of such costs that will be permitted to be reflected in the FAC earnings and expense tests for the first two years after consummation of the Merger. If PSI seeks to recover costs to achieve Merger savings in its next retail electric base rate case, the Settlement Agreement requires PSI to establish that such costs were prudent, reasonable and recurring. (Pet. Ex. R-1, Section II(E).) No party offered any testimony opposing this provision of the Settlement Agreement relating to PSI's accounting and ratemaking treatment of Merger costs.

12. **Affiliate Agreements and Audits.** The Settlement Agreement provides for PSI to fund and participate in four independent audits relating to its compliance with PSI's new Affiliate Standards. (Pet. Ex. R-1, Section II(F).) The Settlement Agreement also provides for this Commission to approve the five Merger-related affiliate agreements submitted with PSI's case-in-chief testimony. The Settlement Agreement further provides for an audit of the five affiliate agreements for reasonableness, including a review of the allocation factors in the Service Company Agreement, and details a procedure for presenting any issues arising from the audit to the Commission for review. Additionally, the parties agreed that any changes in the affiliate agreements as a result of the audit shall be for retail ratemaking purposes only, and not require actual changes in these multi-state agreements themselves, unless otherwise agreed to by the Settling Parties.

Mr. Blackwell testified that, after the Merger, New Duke Energy will form a subsidiary, Duke Services, to provide administrative, management and support services to the regulated operating companies, including PSI. (Pet. Ex. I, p. 3.) Ms. Pashos noted that, with the repeal of PUHCA, a service agreement between regulated operating companies and the service companies of utility holding company is no longer required. (Pet. Ex. D, pp. 4-5.) Ms. Pashos explained that PSI nevertheless will enter into the Service Company Agreement with Duke Services to govern these services. The Service Company Agreement provides for services from New Duke Energy Shared Services to the regulated operating companies to be priced at fully embedded cost for ratemaking purposes, the same transfer pricing methodology formerly required under PUHCA, except for purposes of Internal Revenue Code Section 482. (Pet. Ex. D, pp. 4-5 and 25; and Pet Ex. I, pp. 4-5.)

In addition to the Service Company Agreement discussed above, Ms. Pashos and other PSI witnesses described the following affiliate agreements which PSI requested this Commission accept for filing and approve, to the extent necessary: (1) Operating Company/Nonutility Companies Services Agreement; (2) Operating Companies Service Agreement; (3) Money Pool Agreement; and (4) Tax Sharing Agreement. (Pet. Ex. D, pp. 24-29.) Ms. Pashos explained that these agreements formerly were approved by the SEC under PUHCA, but SEC approval is no longer required due to the repeal of PUHCA. Ms. Pashos stated that the Operating

Company/Nonutility Companies Services Agreement allows PSI and various non-regulated affiliated companies to provide services to each other at fully embedded cost for ratemaking purposes. Ms. Pashos stated that the Operating Companies Service Agreement will allow PSI and its affiliated utility operating companies to provide services to each other at fully embedded cost for ratemaking purposes. (Pet. Ex. D, pp. 26-27.) Ms. Aumiller explained that the Money Pool Agreement is similar to the current Cinergy Money Pool Agreement, and will allow PSI and its affiliated utility operating companies and their subsidiaries, New Duke Energy and Duke Services, to make short-term loans to each other at lower rates than commercial short-term borrowing rates, yet higher than the lender would earn on a short-term investment. (Pet. Ex. G, pp. 15-17.) Ms. Lynn J. Good, Cinergy's Executive Vice President and Chief Financial Officer, stated that the Tax Sharing Agreement is similar to the current Cinergy Tax Sharing Agreement, and will allocate the consolidated income tax liabilities and benefits among the members of New Duke Energy participating in the consolidated income tax return. (Pet. Ex. F, pp. 9-10.)

CAC presented testimony opposing the Service Company Agreement, but did not offer any testimony opposing the other affiliate agreements. Mr. Fagan recommended that the proposed Service Company Agreement should incorporate various terms contained in the current service agreement which he asserted protected PSI's Indiana retail electric customers from being allocated unreasonable costs. (CAC Ex. RMF, p. 31.) Mr. Fagan also recommended that this Commission should implement a cost cap to ensure that no material shift of administrative, managerial and support costs will occur under the new Service Company Agreement. (CAC Ex. RMF, p. 31.) Mr. Fagan also stated that the new Service Company Agreement included cost of capital as a component of the at-cost pricing, but, failed to reference the old PUHCA provision which provided for such pricing. (CAC Ex. RMF, p. 30.)

Mr. Blackwell responded to Mr. Fagan's concern that the Service Company Agreement refers to a "cost of capital," by stating that the definition of costs used in the New Service Company Agreement includes the same components provided for under the old PUHCA – namely direct costs, indirect costs and costs of capital. The at-cost pricing will not result in Duke Services earning a profit on the services it provides to PSI. (Pet. Ex. P, pp. 7-8.) Mr. Blackwell and Ms. Pashos addressed Mr. Fagan's concerns about the extent of this Commission's oversight of the Service Company Agreement by pointing out that any amendments to the Service Company Agreement will be subject to Commission approval, and that PSI will participate in independent audits to assure that no cross-subsidization occurs. (Pet. Ex. P, pp. 8-9; and Pet. Ex. K, p. 5.) Mr. Endris testified that the Settlement Agreement's audit requirements will protect Indiana customers from potential abuse of affiliate relationships. (Pub. Ex. S-1, pp. 2-3.) He also testified that the Settlement Agreement as a whole contained adequate protections to mitigate the OUCC's earlier concerns about the potential that PSI would incur a higher cost of capital due to the Merger. (Pub. Ex. S-1, p. 4.)

13. **Service Quality Reliability and Customer Service.** The Settlement Agreement provides for PSI to file quarterly SAIDI, CAIDI, SAIFI, and Average Speed of Answer reports for the first five years following Merger closing. (Pet. Ex. R-1, Section II(G)(1) – (3).) PSI will calculate these indices for the prior twelve-month period, excluding major events (*e.g.*, Category 3 storms and above). The Settlement Agreement establishes the following reliability benchmarks:

Performance Measure	Benchmark
SAIDI	175 Minutes
CAIDI	115 Minutes
SAIFI	1.65 Interruptions
Average Speed of Answer	60 Seconds

These benchmarks are based on PSI's recent reliability performance, excluding major events. (Pet. Ex. R-1, Section II(G)(2).) The benchmarks will be updated based on rolling 12-month averages of PSI's performance. (Pet. Ex. R-1, Section II(G)(2).) If PSI does not meet two or more of these benchmarks for any quarter during the first five years following Merger closing, PSI must implement a Commission-approved remediation plan and spend up to $5 million annually to correct identifiable reliability problems arising from causes within PSI's control.

Mr. John C. Procario, Cinergy's Senior Vice President and Chief Operating Officer, in his settlement supporting testimony explained that these benchmarks are based on PSI's actual reliability scores during the past ten years. (Pet. Ex. S, p. 3.) PSI has generally exceeded these reliability scores during the past ten years, but occasionally PSI has failed to meet one of the benchmarks during a given quarter. Mr. Endris stated that these reliability targets provide meaningful financial commitments from PSI and meaningful protection to customers against any possible degradation of service arising from the Merger. (Pub. Ex. S-1, p. 4.) Mr. Thomas L. Bernardi, Hoosier's Senior Vice President and Chief Financial Officer, testified that Hoosier believes that PSI has demonstrated that, post-Merger, PSI will continue its commitment to reliability concerning its transmission system and its commitment to cooperating with Hoosier on the "one system" approach which has historically been engaged in between Hoosier and PSI. (Hoosier Ex. A, pp. 6-7.) Mr. Fagan criticized PSI's earlier proposal for assuring reliable service following the Merger, and recommended certain minimum standards for reliability, but offered no testimony opposing the Settlement Agreement's reliability metrics and corresponding commitments relating to remedial measures. (CAC Ex. RMF, p. 37).

While the Settlement Agreement identifies minimum service levels and remedial steps, including a requirement that PSI implement a Commission-approved remediation plan and spend up to $5 million annually to correct identifiable reliability problems, we note that any expenditures that may be necessary under an approved remediation plan must be independent of expenditures necessary for PSI to maintain adequate electric service in its territory. Accordingly, our approval of this provision of the Settlement Agreement should not be interpreted to shield PSI from the requirement to undertake any additional expenditures that may be necessary to fully address service quality issues that may arise. With this caveat, we find that these provisions of the Settlement Agreement are in the public interest, and are hereby approved.

14. **Coordination of Regulation.** Section II(H) of the Settlement Agreement prohibits PSI from challenging or seeking review of any Commission order that changes (for Indiana retail ratemaking purposes only) the allocation factors contained in the Merger-related affiliate agreements. The Settlement Agreement further provides that it should be applied so as to avoid stranding reasonable utility costs among the various New Duke Energy jurisdictions.

Finally, the Settlement Agreement provides that PSI and the Commission expressly reserve their respective rights under Section 1275 of Subtitle F, Repeal of PUHCA in Title XII of the EPAct of 2005 or any successor provision. (Pet. Ex. R-1, Section II(H).)

Ms. Pashos testified in her settlement supporting testimony that this provision is necessary to coordinate regulation between state and federal authorities. (Pet. Ex. R, p. 7.) She explained that the Settlement Agreement goes beyond requirements under existing law by requiring PSI to waive review on FERC preemption grounds of any Commission decision that changes (for state retail ratemaking purposes only) the allocation factors in the Merger-related affiliate agreements. (Pet. Ex. R, p. 7.) Mr. Fagan testified that this provision could be interpreted, when read together with other provisions of the Settlement Agreement, to require PSI's customers to pay for costs incurred by PSI's affiliates. (CAC Ex. RMF-S, p. 22.) In response, Mr. Pashos stated that a similar Merger commitment was agreed to by CAC in the 1994 Cinergy merger. (Pet. Ex. U, p. 14.) Ms. Pashos noted that PSI is not claiming that this Commission is precluded from finding costs unreasonable and imprudent in future regulatory proceedings. Rather, these provisions provide that costs that are found to be reasonable should not be left stranded between jurisdictions and therefore not recoverable.

15. Books and Records. The Settlement Agreement authorizes PSI to continue maintaining its books and records outside of the State of Indiana. PSI is required to make its records and personnel available for inquiry in Plainfield, Indiana for all audits in any type of regulatory proceeding. If PSI does not make its books and records or personnel available in Plainfield, then PSI must pay travel expenses for the staffs and outside consultants of this Commission and the OUCC. Neither the CAC nor any other party offered any testimony opposing this provision of the Settlement Agreement.

Pursuant to our May 26, 2004 Order in Cause No. 42594, PSI has been keeping its books and records outside of the State of Indiana, provided that PSI grants access to its books and records in the State of Indiana or, in the alternative, pays the reasonable expenses for this Commission and the OUCC to inspect PSI's books and records located outside of the State of Indiana.

16. Integrated Resource Planning. This provision of the Settlement Agreement requires PSI to follow certain procedures in planning for additional generating facilities and for obtaining Commission approval for such generating facilities, including the use of clean coal technology and PSI's environmental compliance plans. PSI is also required to obtain Commission approval for any purchase of firm power or unit power from an affiliate for a term of five years or longer. (Pet. Ex. R-1, Section (J).

Mr. Fagan's testimony recommended various restrictions on PSI's right to purchase power from affiliates, and on PSI's integrated resource planning process, and he proposed a protocol for allocating PSI's system generating and purchased power resources. (CAC Ex. RMF-S, p. 26.) Ms. Pashos responded by noting that Mr. Fagan's recommendations are unnecessary or irrelevant to the Merger. (Pet. Ex. U, p. 7.) She explained that this Commission and the FERC have certain authority over affiliate power and capacity purchases, and resource adequacy, such that actual transactions are better addressed in the future when the actual facts of the transactions are known. (Pet. Ex. U, p. 7.) She asserted that issues relating to the matters raised by Mr. Fagan should be dealt with in the appropriate regulatory proceeding, such as a PSI

Certificate of Public Convenience and Necessity ("CPCN") proceeding, an FAC proceeding, or a summer reliability tracker proceeding. (Pet. Ex. U, pp. 7-8.) Finally, Ms. Pashos noted that the Settlement Agreement's integrated resource planning commitments are essentially identical to the corresponding commitments from the 1994 Cinergy merger, and have adequately protected customers since that time. (Pet. Ex. U, p. 8.)

17. **Affiliate Standards.** The Settlement Agreement provides for PSI to adopt new Affiliate Standards and also provides for PSI to work with interested stakeholders to modify these standards as necessary, following the FERC's issuance of new rules in FERC Docket RM05-32-000, which deals with FERC's new rules arising from the repeal of PUHCA and enactment of the EPAct of 2005. The Settlement Agreement also provides for PSI to meet with this Commission's Staff after the FERC's rulemaking is finalized, to discuss whether PSI should be required to issue any additional reports to this Commission, in light of FERC's final rule. (Pet. Ex. R-1, Section (K); and Pet. Ex. R-1, Attachment 2.)

Ms. Pashos testified that the Settlement Agreement's Affiliate Standards are the same as proposed in Attachment K-2 to Ms. Pashos' rebuttal testimony, and reflect a combination of PSI's existing Affiliate Guidelines and certain affiliate provisions adopted from the settlement of the AEP/CSW merger. (Pet. Ex. R, p. 4.) Mr. Endris testified that the Settlement Agreement's Affiliate Standards and audit requirements will protect Indiana customers from potential abuse of affiliate relationships. (Pub. Ex. S-1, pp. 2-3.)

Neither CAC nor any other party offered any testimony opposing this provision of the Settlement Agreement specifically addressed to the Affiliate Standards or audits. Mr. Fagan did generally testify to the need for certain additional measures to financially insulate PSI from its affiliates, which could be construed as requesting additional protections in PSI's Affiliate Standards. (CAC Ex. RMF-S, pp. 23-31.)

18. **Rate Design**. The Settlement Agreement requires PSI to file and fully support a 4 CP methodology for the rate design for production plant in its next retail electric base rate case. (Pet. Ex. R-1, Section II(L).) The Settlement Agreement also provides that the OUCC will not object to the use of the 4 CP methodology for production plant in PSI's next retail electric base rate case. Mr. Fagan objected to this provision on the grounds that this Commission should not approve the rate design for PSI's next rate case in this Merger proceeding. (CAC Ex. RMF-S, p. 32.) Ms. Pashos, in response, noted that the 4 CP methodology for production plant is reasonable because PSI's monthly loads are now consistently higher in the four summer months. She also pointed out that the Settlement Agreement does not request Commission approval of the 4 CP methodology in this case, but merely binds PSI to propose this methodology in its next rate case. Further, pursuant to the Settlement Agreement, PSI will provide a comparable 12 CP methodology to allow stakeholders and the Commission to compare the impacts of both approaches. (Pet. Ex. U, pp. 17-18.).

While the Settlement Agreement sets forth an agreed upon framework under which certain parties intend to address rate design issues in PSI's next rate case, we agree with Mr. Fagan that as the issue is sufficiently unrelated to the matter presented to us for approval in this Cause it is not necessary or appropriate for the Commission to affirm this understanding and approach as part of this proceeding.

19. Miscellaneous Issues. CAC raised two miscellaneous issues in Mr. Fagan's settlement opposing testimony related to five gas-fired plants comprising 3,600 MW owned by DENA in the Midwest ("the DENA Midwest assets") and to energy efficiency.

Mr. Fagan relied on various confidential documents and a Morningstar report, that make statements about using the DENA Midwest assets to serve Cinergy load in Indiana and Ohio, to support his conclusion that PSI will purchase power from these plants or put them into rate base in the future. (CAC Ex. RMF-S, pp. 13-18).[2] He expressed concern that these plants' costs exceed their market value, and that PSI has an open generic CPCN case that could allow for expedited treatment for PSI to purchase one of the facilities. (CAC Ex. RMF-S, pp. 18-19.) Mr. Fagan therefore recommended that this Commission should: (i) cap the price of any future PSI capacity purchases at market; (ii) mandate careful scrutiny of the market valuation of any plant that serves PSI load because the costs of the DENA assets may be greater than market; and (iii) exclude the DENA Midwest assets from the generic CPCN proceeding. (CAC Ex. RMF-S, pp. 18-19.)

Ms. Pashos rebutted Mr. Fagan by noting that there is no existing plan to transfer the DENA Midwest assets to PSI or to use these plants to serve PSI's customers. (Pet. Ex. U, pp. 4-5.) Ms. Pashos also indicated on cross examination that any transaction that may yet occur under pending Cause No. 42469 would not involve an affiliate, which would exclude consideration of the DENA Midwest assets. (Tr. G-31.) She noted that, in the Duke/Cinergy Merger proceeding at the FERC, FERC approved the transfer of these plants to The Cincinnati Gas & Electric Company ("CG&E"). (Pet. Ex. U, p. 5.) Ms. Pashos also explained that, if PSI desired to purchase these plants from CG&E in the future, then PSI would need to obtain both FERC and Commission approval. (Pet. Ex. U, p. 5.) Ms. Pashos also noted that CG&E's FERC-approved market-based tariffs provide that CG&E may only sell power to PSI at a price no greater than the Midwest Independent Transmission System Operator, Inc.'s Day 2 Markets locational marginal price. (Pet. Ex. U, p. 6.)

We have considered Mr. Fagan's concerns relating to these plants and we conclude that this issue is not directly related to the Merger transaction. We also note that other regulatory protections and requirements exist, which would allow the Commission to directly review and consider the issues presented by the CAC in the context of a separate proceeding filed with the Commission. We therefore, find it unnecessary to adopt Mr. Fagan's recommended conditions relating to the DENA Midwest assets as part of our consideration of the issues presented in this Cause.

Mr. Fagan also made recommendations related to energy efficiency and demand-side-management. Mr. Fagan testified that PSI is responsible for aggressively promoting energy efficiency because Mr. Rogers is co-chair of the Energy Efficiency Action Plan, and the U.S. Environmental Protection Agency's "Energy Efficiency Fact Sheet" states that members of the Leadership Group, such as Mr. Rogers, "will also commit to take action within their own spheres of influence in the near term, as well as participate in a broader communications strategy to share business cases and create additional leadership opportunities during the summer of 2006." (CAC Ex. RMF-S, p. 32-33.) He therefore recommended that PSI should increase its demand-side

[2] We note that the confidential documents relied upon by Mr. Fagan pre-dated PSI's acquisition of the Wheatland Generating Station as approved by this Commission in Cause No. 42469 (*Ind. Util. Reg. Comm'n,* August 3, 2005).

management programs, with a goal of reducing forecasted retail sales by 1%. (CAC Ex. RMF-S, pp. 34.) Ms. Pashos stated that PSI has and will continue to aggressively pursue energy efficiency and demand-side management; however, she also indicated that she believes that these issues are irrelevant to this case.

Mr. Fagan also recommended that PSI should be required to incorporate its best forecast of carbon dioxide emissions credit prices into its base case or reference case planning assumptions. Mr. Fagan testified that while there is considerable uncertainty about the specifics of future regulation of carbon dioxide emissions, that uncertainty can be addressed by sensitivity analysis using low and high case assumptions. Mr. Fagan recommended that, at a minimum, PSI should update its IRP modeling processes with respect to the consideration of carbon dioxide issues. In response to this issue Ms. Pashos indicated that PSI has committed to continue to factor environmental issues into its IRP process going forward. According to Ms. Pashos, how PSI does this will naturally change as new federal and state environmental regulations are proposed and finalized. Ms. Pashos indicated that in PSI's recent environmental compliance plan case, PSI performed and presented a sensitivity analysis using carbon emission credit prices, and in future cases PSI will use its professional judgment on how to incorporate relevant environmental issues into its IRP. (Pet. Ex. U, p. 17.)

Energy efficiency, demand side management, and carbon dioxide emission issues, while important, are not directly related to the Merger presented to us for consideration in this Cause. PSI has indicated that it has and will continue to pursue energy efficiency and we accept this as an objective that the company must continue to pursue consistent with prior determinations of the Commission. We also anticipate and expect that PSI will actively focus on carbon dioxide emission issues in future proceedings in a manner that considers the possible future regulation of these emissions. However, in reaching these conclusions, we do not find that these issues are sufficiently related to the issues presented in this Cause to warrant modification of the Settlement Agreement in the manner proposed by the CAC.

20. **Findings, Conclusions and Approval of Settlement Agreement**. While this matter was resolved by agreement, or not disputed, by most of the parties to this proceeding, several specific issues were raised by the CAC which were considered as part of our review of the Settlement Agreement. Based on the findings set forth in this Order we find that the Settlement Agreement when taken as a whole, consistent with the additional findings recommended by the CAC and adopted by the Commission, is in the public interest and should be approved. In reaching this conclusion we note that the Settlement Agreement provides a credit to ratepayers that would not exist absent the merger. The Settlement Agreement establishes service quality standards that provide some protection to ratepayers against a reduction in service quality. The Settlement Agreement includes several specific affiliate standards that provide further protections to Indiana ratepayers. Further, the Settlement Agreement provides for certain audits of affiliate agreements that will provide the parties and this Commission with information that should facilitate the continued protection of Indiana ratepayers. Therefore, we find that the Settlement Agreement provides a reasonable balancing of interests and note that the Commission continues to have jurisdiction over PSI and therefore retains the authority to address any issues that arise in the future.

Based upon all of the evidence presented at the Evidentiary Hearing in this proceeding, and based upon the foregoing Findings of this Order, we find that the Settlement Agreement in its entirety constitutes an integrated and comprehensive resolution of the relevant issues before us in this proceeding, and is designed to address the specific facts, circumstances and retail electric rates of PSI, in the context of the specific Indiana statutory and regulatory environment. We also find that the Settlement Agreement provides adequate protection for PSI's retail electric customers from the potential material adverse impacts of the Merger. We recognize that the Settlement Agreement was the product of negations and constitutes a compromise by all the Settling Parties that involved give and take, and that, as a whole, the Settling Parties believe it is a just and reasonable resolution of the issues raised in this Cause. We find that the Settlement Agreement is just and reasonable, in the public interest, and not inconsistent with the purpose of the Indiana Public Service Commission Act. Accordingly, we find that the Settlement Agreement should be approved, consistent with the findings set forth herein.

The Settlement Agreement provides that the acceptance and approval of the Settlement Agreement by this Commission in accordance with its terms shall not establish any principles or precedent, or be cited as precedent by any Settling Party, except if necessary to enforce its terms before this Commission, or any state court of competent jurisdiction. We find that this provision of the Settlement Agreement is reasonable. With regard to future use, citation, or precedent of the Settlement Agreement, we find that our approval of the terms of the Settlement Agreement should be construed in a manner consistent with our finding in *In Re Richmond Power & Light*, Cause No. 40434 (*Ind. Util. Reg. Comm'n,* March 19, 1997).

21. **Request for Confidential Treatment.** PSI filed two Motions for Protection of Confidential and Proprietary Information, with Affidavits of Ms. Kay Pashos, and Messrs. Richard Osborne and William Tyndall, on August 13, 2005 and December 9, 2005, respectively. The Affidavits indicate that such confidential information has actual or potential independent economic value to competitors, the disclosure of the confidential information could provide competitors with an unfair advantage, and PSI and Duke and their affiliates have taken all reasonable steps to protect the confidential information from disclosure. No party objected to PSI's August 13, 2005 request for confidential treatment concerning certain coal contract information. In a September 8, 2005 Docket Entry the Presiding Officers found that such information should be subject to confidential procedures on a preliminary basis.

The CAC objected to PSI's request for confidential information which was the subject of PSI's December 9, 2005 Motion. The Presiding Officers granted preliminary confidential treatment in a January 6, 2006 Docket Entry and ordered an *in camera* review of the disputed documents. PSI and CAC worked to resolve the confidentiality dispute and were successful in coming to an agreement on various redacted versions of most documents, and maintaining confidential treatment for the remaining information, except for one document which remained in dispute. On January, 20, 2006, the Presiding Officers heard argument on the remaining confidential document and found that it was properly considered confidential trade secrets and entitled to confidential treatment.

Accordingly, pursuant to Ind. Code § 5-14-3-4(a)-(4), we find that the data concerning the confidential information presented in this proceeding constitutes "trade secrets" and should be afforded confidential treatment and continue to be held as confidential by this Commission.

We will note that where possible the confidential documents have also been produced and entered into evidence as cross-examination exhibits in public redacted form.

IT IS THEREFORE ORDERED BY THE INDIANA REGULATORY COMMISSION that:

1. The Settlement Agreement, including Attachments 1 and 2, is hereby, approved consistent with the findings set forth herein.

2. PSI is hereby, authorized to enter into the Service Company Agreement, the Operating Company/Nonutility Companies Service Agreement, the Operating Companies Service Agreement as set forth in Petitioner's Exhibit I, and subject to the modifications to the Service Agreement identified in Petitioner's Exhibit P. PSI should be, and is hereby, authorized to enter into the Money Pool Agreement as set forth in Petitioner's Exhibit G, and the Tax Sharing Agreement as set forth in Petitioner's Exhibit F. PSI shall submit copies of these agreements with the Electricity Division of this Commission within 30 days of executing the agreements following the Merger.

3. PSI is hereby authorized and directed to adopt the Affiliate Standards attached to the Settlement Agreement as Attachment 2. PSI shall file with this Commission's Electricity Division its revised Section 2 of its Retail Electric Tariff, containing these Affiliate Standards, within 30 days of Merger closing.

4. PSI is hereby authorized and directed to share Merger savings with its retail electric customers by providing a retail electric rate credit of $40 million paid over one year following the Merger closing. PSI shall further file with this Commission's Electricity Division new tariffs reflecting the rate credit no later than ten days after the Merger closing.

5. PSI is hereby authorized and directed to reduce its retail electric rates by $11.552 million annually to remove the annual amortization of costs from the 1994 Cinergy merger, beginning June 1, 2008. PSI shall file with this Commission's Electricity Division a new rider to its Retail Electric Tariff, containing the rate reduction, at least 30 days prior to June 1, 2008.

6. PSI is hereby authorized to locate its books and records outside of the State of Indiana, subject to the provisions of the Settlement Agreement.

7. The Merger commitments set forth in the Settlement Agreement and in Attachment 1 to the Settlement Agreement consistent with the findings set forth in this Order are hereby approved to take effect 30 days following the Merger closing. These Merger commitments shall replace the merger commitments agreed to by PSI in Cause No. 39897.

8. The Settling Parties are directed to begin discussions as soon as practicable as to whether the FERC's final rulemaking in Docket No. RM05-32-000 will require any changes to PSI's Affiliate Standards.

9. The confidential information presented in this proceeding is found to constitute trade secrets and is therefore excepted from public access.

10. This Order shall be effective on and after the date of its approval.

HARDY, HADLEY, SERVER, LANDIS AND ZIEGNER CONCUR:

APPROVED: MAR 1 5 2006

I hereby certify that the above is a true and correct copy of the Order as approved.

Brenda A. Howe

Brenda A. Howe
Acting Secretary to the Commission