CASE

1426 S. Polk
Dallas, Texas 75224

(CITIZENS ASSN. FOR SOUND ENERGY)

214/946-9446
214/941-1211, work, usually
Tuesdays and Fridays only

December 14, 1981

Secretary
U. S. Nuclear Regulatory Commission
Washington, D. C. 20555

Attn: Chief, Docketing and Service Section

Dear Secretary:

Subject: Docket Nos. 50-445 and 50-446
Application of Texas Utilities Generating Company, Et Al. for an Operating License for Comanche Peak Steam Electric Station Units #1 and #2 (CPSES)

Attached are the following original documents, copies of which are attached to certain copies of CASE's 12/14/81 Transmittal of Documentation As Agreed Upon At 12/1/81 Prehearing Conference:

All of the following have been certified by Martha M. Bartow, Director of Record Services, Public Utility Commission of Texas, Austin, Texas:

The direct testimony of Joe D. Karney, September, 1980 (including exhibits and affidavit); a portion of the direct testimony of Max H. Tanner, Jr., September, 1980 (pages 1, 2 and affidavit only, for the limited purpose of showing qualifications, and subject of testimony); a portion of the direct testimony of Max H. Tanner, Jr., from the transcript of the November 24, 1980 City of Dallas Hearing (pages 85 through 89); all from Public Utility Commission Docket No. 3460.

A portion of the cross examination of Charles E. Olson from the transcript of the December 9, 1980 Hearing from Public Utility Commission Docket No. 3460 (pages 270, 271, and 307).

A portion of the transcript of the hearing for July 9, 1979 and July 10, 1979 from Public Utility Commission Docket No. 2572 (cross-examination of Max H. Tanner, pages 91 through 93, 138, 139; and cross-examination of Erle A. Nye, pages 364, 365, 377, 392, 397, 398).

These items correspond to the following items in CASE's 11/18/81 Motion to Allow Testimony To Be Admitted On Affidavit Only, respectively:

Item 6 (CASE Attachment E of CASE's 11/18/81 Answer to NRC Staff's Motion for Summary Dispos[illegible] of Contention 25);

Item 7 (CASE Attac[illegible]ent I of our 11/18/81 Answer to Staff's Motion);

Items 10 and 8 (CASE Attachments L and J, respectively, of our 11/18/81 Answer to Staff's Motion);

Item 11 (CASE Attachment M of our 11/18/81 Answer to Staff's Motion);

Item 9 (CASE Attachment K to our 11/18/81 Answer to Staff's Motion).

Respectfully submitted,

CASE (Citizens Association for Sound Energy)

Juanita Ellis

(Mrs.) Juanita Ellis
President

cc: Service List

50-445,446

DOCKET NUMBER
PROD. & UTIL. FAC.

Public Utility Commission of Texas

'81 DEC 15 P4:13

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SECRETARY
ING & SERVICE
BRANCH

George M. Cowden
Chairman

H. M. Rollins
Commissioner

Garrett Morris
Commissioner

I, Martha M. Bartow, certify that this is a true and correct copy of the direct testimony of Joe D. Karney, September, 1980; a portion of the direct testimony of Max H. Tanner, Jr., September, 1980; a portion of the cross examination of Max H. Tanner, Jr., from the transcript of the November 24, 1980 City of Dallas Hearing, from Public Utility Commission Docket No. 3460.

ISSUED UNDER MY HAND AND SEAL on this the 9th day of December, 1981.

SEAL

Martha M. Bartow

Martha M. Bartow
Director of Record Services

DIRECT TESTIMONY OF

JOE D. KARNEY

FOR

DALLAS POWER & LIGHT COMPANY

SEPTEMBER 1980

DIRECT TESTIMONY OF JOE D. KARNEY

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Joe D. Karney. My business address is 1506 Commerce Street, Dallas, Texas 75201.

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

A. I am employed by Dallas Power & Light Company, hold the position of Treasurer & Assistant Secretary and have responsibility for the financial, accounting, and internal audit activities of the Company.

Q. PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL QUALIFICATIONS.

A. I graduated from Southern Methodist University in 1961 with a Bachelor of Business Administration degree in accounting. I have been employed by Dallas Power & Light Company since July, 1952 and have worked in various areas of the Accounting Department prior to becoming Head of the General Accounting Division in 1964. I was elected Assistant Treasurer of the Company in 1971, Assistant Treasurer and Assistant Secretary in 1975, and Treasurer and Assistant Secretary in 1977. In addition, I headed the Company's Accounting Department from 1970 through 1978. I am a Certified Public Accountant in the State of Texas and hold memberships in the American Institute of Certified Public Accountants, the Texas Society of Certified Public Accountants, the Financial Executives Institute, and the Edison Electric Institute Financial Committee. I have testified previously in rate proceedings before the City of Dallas and the Public Utility Commission of Texas (PUC).

Q. TO WHAT DEGREE DO YOU HAVE CONTACT WITH THE INVESTMENT AND FINANCIAL COMMUNITY?

A. I have extensive involvement in and responsibility for the financial affairs of the Company. My contacts with the financial community include regular meetings and discussions with representatives of commercial banks, investment banking firms and rating agencies, as well as consultation with individual and institutional investors and security analysts.

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

A. My testimony will discuss: (a) the importance of the Company's ability to attract capital; (b) the Company's current financial condition, including fixed charge coverages, internal generation of cash, return on common stock equity, and quality of earnings; (c) the basis for the Company's request to include construction work in progress (CWIP) in the rate base; (d) the adjusted value rate base for the Company; (e) the capital structure of the Company; and (f) the Company's composite cost of capital.

Q. PLEASE EXPLAIN THE SOURCES OF FUNDS AVAILABLE TO THE COMPANY AND THE IMPORTANCE OF THE COMPANY'S ABILITY TO ATTRACT CAPITAL AT REASONABLE COSTS.

A. In addition to funds generated internally, the Company traditionally has obtained permanent capital principally through the sale of long-term debt, preferred stock and common stock. In recent years, however, the Company has had to resort to a higher level of short-term debt and the sale, through private placement, of intermediate-term debt.

Electric utilities are generally conceded to be the most capital intensive of all industries. Therefore, they must enter the capital market on a regular basis. Since capital costs represent a significant portion of total costs, and continue to increase in an inflationary environment such as we have experienced over the past several years, it is extremely important to maintain a high credit rating in order that capital may be obtained at the lowest possible cost. The Company's ability to keep its capital costs low in the past has helped to maintain reasonable electric rates for its customers.

As pointed out in Mr. Tanner's testimony, the Company is engaged in a continuing construction program to provide facilities that will bring the cost benefits resulting from the use of lignite and uranium fuels to its customers. The Company's regulatory authorities have acknowledged the benefits the customer receives from the conversion to lower cost alternate fuels in the Company's past two rate proceedings. Based on current estimates, the Company's construction expenditures will average approximately $130 million per year for the next several years. It should be noted that a construction program of this size represents annual expenditures equal to approximately 19 percent of the net cost of all the plant currently in service. It is therefore important, and to the direct benefit of the customer, that the substantial quantities of capital that will be required to provide these facilities be available at the most reasonable cost.

Q. CONSIDERING THE COMPANY'S NEED TO ACQUIRE CAPITAL TO FINANCE THE CONSTRUCTION PROGRAM, WHAT IS THE SIGNIFICANCE OF THE FIXED CHARGE COVERAGE?

A. One of the most important indicators of the financial integrity of a utility company is the extent to which earnings will cover its fixed charges on debt. The fixed charge coverage that the Company maintains over a period of years has a substantial impact on the ratings the agencies assign the Company's bonds. It is generally recognized throughout the financial community that for an electric utility, a fixed charge coverage, including all applicable debt, of at least 4.0 times is the minimum requirement to maintain a triple A bond rating.

Q. WOULD YOU EXPLAIN THE TERM "SUPPLEMENTAL FIXED CHARGE COVERAGE"?

A. The computation of the supplemental ratio of earnings to fixed charges is made pursuant to Securities and Exchange Commission (SEC) Accounting Series Release No. 122, the purpose of which is to include, for interest coverage purposes, interest requirements on debt which is not on the Company's balance sheet but which the Company has guaranteed or is in some manner obligated to assume in case of default. In the case of Dallas Power & Light Company, the supplemental coverage calculation includes the Company's proportionate obligations for senior notes issued by Texas Utilities Fuel Company (TUFCO) and Texas Utilities Generating Company (TUGCO).

Q. MR. KARNEY, WHAT HAS BEEN THE RECOMMENDATION OF THE COMPANY'S REGULATORY AUTHORITIES AS TO AN ADEQUATE FIXED CHARGE COVERAGE FOR DALLAS POWER & LIGHT COMPANY?

A. The staffs of the regulatory authorities exercising jurisdiction over the Company have recognized the need for a 4.0 times coverage to maintain a triple A bond rating.

Q. WHAT HAVE BEEN THE COMPANY'S FIXED CHARGE COVERAGES AND SUPPLEMENTAL FIXED CHARGE COVERAGES IN RECENT YEARS?

A. They have declined substantially. As shown in JDK Exhibit No. 1, prior to 1974 the Company's fixed charge coverage was generally in excess of 4.0 times. For the test year ended June 30, 1980, the fixed charge coverage was 3.12 times and the supplemental fixed charge coverage was 2.76 times. These coverages are obviously below the minimum needed to retain the triple A rating and have been for several years. Since capital costs are such a major portion of the Company's expenses, retention of the triple A rating is vitally important to the Company and its customers.

Q. HAS DALLAS POWER & LIGHT COMPANY BEEN ABLE TO ACHIEVE A 4.0 TIMES SUPPLEMENTAL FIXED CHARGE COVERAGE AS A RESULT OF RECENT RATE ORDERS?

A. As shown in JDK Exhibit No. 2, the Company's supplemental fixed charge coverage is substantially below the minimum 4.0 times coverage needed. Although recent rate orders of the Company's regulatory authorities' have addressed the need to restore the Company's financial integrity, the amount of rate increase granted in each case has been inadequate to accomplish this objective.

Q. MR. KARNEY, WILL DP&L'S CUSTOMERS BENEFIT IF THE COMPANY IS ABLE TO MAINTAIN ITS TRIPLE A FIRST MORTGAGE BOND RATING?

A. Yes. The triple A rating allows the Company to borrow funds at the lowest possible cost. This is reflected in JDK Exhibit No. 3 which shows Moody's average of yields on long-term public utility bonds for the years 1969 through 1979. For example, the spread between triple A and double A was, on average, approximately 30 basis points from 1974 through 1979. During periods of greatest financial strains, the spreads are even wider. With a difference in financing rates of 30 basis points, the savings over the 30-year life of a $75 million bond issue would be over $6.7 million. The spread to lower rated bonds is even greater. With a high credit rating there are additional savings in the cost of short-term debt, pollution control bonds, and preferred and common stock.

Q. IN ADDITION TO THE SAVINGS OF INTEREST AND DIVIDENDS, ARE THERE OTHER REASONS FOR MAINTAINING THE TRIPLE A BOND RATING?

A. Yes, other benefits of maintaining the triple A rating are the greater availability and flexibility of capital financing. Strong credit indicators lead to better financial health at a lower cost to the ratepayer. Investors will generally accept a lower return on their investment if the Company is financially strong, which results in a lower cost of capital. The magnitude of the Company's construction program and the required external financing necessitates that the Company have ready access to the capital markets at reasonable cost.

Q. IF DALLAS POWER & LIGHT COMPANY WERE TO LOSE ITS TRIPLE A RATING, WHAT WOULD BE NECESSARY TO REGAIN THAT BOND RATING?

A. It would take many years of sustained financial performance above the established minimum requirements before the rating agencies would consider upgrading the Company's bond rating. Therefore, retention of the Company's favorable bond rating is extremely important at this time.

Q. TO WHAT EXTENT ARE INTERNAL SOURCES OF FUNDS AVAILABLE TO MEET THE COMPANY'S CAPITAL NEEDS?

A. A portion of the Company's net earnings are reinvested in the Company in support of the construction program. JDK Exhibit No. 4 shows retained earnings, combined with other internally generated funds, as a percentage of construction expenditures for the period January, 1978 through June, 1980, as compared to the range of 40 to 60 percent recommended by the PUC Staff in Docket 2572. As shown in the exhibit, the percentage for the Company has fluctuated during the past several years, but has averaged less than 40 percent during this period. For the test year, the level of internally generated funds as a percentage of construction expenditures was 32.1 percent. JDK Exhibit No. 4 further illustrates that the rate increases granted in the Company's last two rate orders have been insufficient to provide the level of internal cash generation recommended by the PUC staff for the maintenance of financial integrity.

Also, from 1969 to the end of 1979, construction expenditures have increased more than four times. This means that the Company must attract additional capital. In order to obtain new capital in an inflationary and recessionary environment, internally generated cash must be maintained at a level adequate to ensure investor confidence.

Q. WHAT PERCENTAGE OF DALLAS POWER & LIGHT COMPANY'S CAPITAL REQUIREMENTS SHOULD BE MET THROUGH INTERNALLY GENERATED FUNDS ?

A. Dallas Power & Light Company should generate on a consistent basis 50 percent of its capital needs internally. In view of the prevailing rate of inflation and the size of our construction program, this level is the minimum requirement.

Q. ANOTHER TEST OF FINANCIAL PERFORMANCE IS RETURN ON COMMON STOCK EQUITY. WHAT HAS BEEN DALLAS POWER & LIGHT COMPANY'S RETURN ON COMMON EQUITY SINCE 1969?

A. The return on equity has declined dramatically since 1969, as shown by JDK Exhibit No. 5. This exhibit shows return on common stock equity, including and excluding Allowance for Funds Used During Construction (AFDC), for the period 1969 through the test year ended June 30, 1980. This decline has occurred in a period which has seen the cost of high quality debt issues increase from just above 6 percent to over 14 percent, approximately 3 percent above the Company's actual equity earnings of 11.0 percent for 1978 and 1979 and 11.3% for the test year ended June 30, 1980. The level of earnings for the Company has simply been inadequate for several years. Reasonable investors will not continue to accept the risk of an equity security at 11 percent when they can earn 13 to 14 percent on a low risk mortgage bond.

Of even greater concern is the trend in return on equity excluding AFDC. The sophisticated analyst, particularly rating agencies and institutional investors, considers calculations of return on equity both including and excluding AFDC. Earnings are discounted when a significant portion is attributable to AFDC. In the case of Dallas Power & Light Company, over one-third of its test year earnings were non-cash. With such a large portion of non-cash earnings, the Company's earnings are subject to substantial discounting by investors. At the end of the test year the cash return on equity, that is, the return excluding AFDC, was 7.2 percent. If allowed to continue, this condition will not permit capital to be attracted at reasonable costs.

Q. WHAT DO YOU CONSIDER NECESSARY TO IMPROVE THE COMPANY'S FINANCIAL INTEGRITY?

A. In addition to obtaining an adequate return on common equity, the inclusion of all Construction Work in Progress (CWIP) in rate base is necessary.

Q. IS THE COMPANY REQUESTING CONSTRUCTION WORK IN PROGRESS IN RATE BASE?

A. Yes, the Company proposes to include $308,313,988 of CWIP in rate base. This represents all CWIP at June 30, 1980 with the exception of a noncurrent payable related to Martin Lake SES Unit 4.

Further, it should be understood that the amount of CWIP requested to be allowed in the rate base is substantially less than will be invested in CWIP before the proposed rates are in effect. At an average monthly investment of $10 million, an additional $70 to $80 million will be added to CWIP after the end of the test period and before these rates are in effect.

Even with 100 percent of test year CWIP in rate base the Company's actual investment in CWIP will be substantially more during the period when the rates are in effect. In Docket 1526, $87.7 million of CWIP, approximately 48 percent of a requested $182.3 million, was allowed in rate base. By the time new rates were in effect, the amount in rate base represented only 36 percent of the Company's actual investment in construction and the average during the period covered by those rates was only 28 percent. In Docket 2572, the Company was allowed $194.6 million of CWIP in rate base, which was approximately 80 percent of a requested $243.2 million. However, after the new rates were in effect only nine months, CWIP in rate base as a percent of the total CWIP for the period was only 62 percent. This is estimated to decrease to 51 percent by December, 1980. The Company is presently requesting that 100 percent of adjusted CWIP at June 30, 1980 ($308,313,988) be included in rate base. As shown on JDK Exhibit No. 6, the percent of CWIP in rate base will have been reduced to approximately 77 percent by the time the rates could reasonably be expected to be placed in effect and further reduced to 58 percent by the end of the first year the new rates are in effect. This exhibit graphically reflects the capital attrition problem which exists when rates are set on a historical test year basis and substantiates the need for all CWIP at the end of the test year to be included in rate base.

DP&L's ongoing construction program assures that the Company will in the future, as it has in the past, incur substantial additional investments in CWIP after the end of the test year. Since a cash return has not been allowed on this portion of the Company's investment in CWIP, the Company is virtually assured that its earnings will be inadequate to recover on a current basis the full carrying costs associated with the construction program, a program which the Company undertakes for the benefit of its customers. Thus, it is extremely important from the standpoint of the Company's financial integrity that the full requested amount of CWIP be allowed in rate base. Any lesser amount will only result in additional non-cash earnings, further eroding the Company's financial integrity.

Q. ARE THERE OTHER REASONS FOR REQUESTING THAT CWIP BE INCLUDED IN RATE BASE?

A. In addition to enhancing the financial integrity of the Company, it is the best alternative for the customer. When the construction of a facility covers an extended period of time, interest costs for the funds necessary for the construction program are incurred. These costs must be borne by the customer whether they are capitalized and recovered over the life of the project or recovered currently. When CWIP is included in rate base, the costs of construction are paid as they are incurred. When these costs are capitalized, they add to the cost of the facility being constructed and earn a return over the life of the plant. It is better to pay the costs currently rather than to pay interest on interest.

Q. IS THE COMPANY'S ABILITY TO ATTRACT CAPITAL ENHANCED BY THE INCLUSION OF CONSTRUCTION WORK IN PROGRESS IN THE RATE BASE?

A. Yes. The engineering and construction periods for major projects such as power plants range from eight to twelve years. During these extended periods the Company is required to obtain large amounts of capital to finance the projects and, therefore, must pay for the use of these funds in cash. Including CWIP in rate base results in a recovery of these costs currently, providing higher quality earnings, which helps the Company maintain its financial integrity. Conversely, capitalizing these costs defers their recovery by the Company, leaves the quality of earnings at an inadequate level, and increases the overall cost of providing service to the customer.

Q. HOW CAN COMPLETION OF A CONSTRUCTION PROJECT AFFECT THE COMPANY'S ELECTRIC SERVICE RATES IF CWIP IS NOT ALLOWED IN RATE BASE?

A. To the extent that CWIP is excluded from rate base, completion of a major project will cause revenue requirements to increase dramatically at the time the project is included in rate base. This is the result of accruing AFDC which is capitalized and becomes part of the cost of a project. Upon completion of a project, AFDC is discontinued, the project is placed in service, and revenue requirements must subsequently be increased sufficiently to cover the return on the full amount of the project, including the capitalized AFDC. By allowing CWIP in rate base, rate increases tend to be more gradual which again is in the best interest of customers.

Q. IF CWIP IS NOT INCLUDED IN RATE BASE, WHAT EFFECT DO AFDC EARNINGS HAVE ON THE COMPANY'S FINANCIAL INTEGRITY?

A. When non-cash AFDC makes up a large part of earnings, the amount of cash earnings available to pay common dividends can be inadequate to pay those dividends. At the end of the test year, the dividend payout ratio, excluding AFDC from earnings, was 123.3 percent. This ratio is unacceptably high and must be reduced. The inclusion of CWIP in rate base will have a positive effect in reducing this ratio to more acceptable levels.

Q. HOW IS THE QUALITY OF THE COMPANY'S EARNINGS AFFECTED BY INCLUDING CWIP IN RATE BASE?

A. As shown in JDK Exhibit No. 7, the construction program to convert to alternative fuels has caused CWIP to increase rapidly in relation to electric plant. CWIP has increased from approximately 9 percent of electric plant in 1969 to almost 24 percent at the end of the test year. As a result, the portion of the Company's earnings attributable to AFDC has increased significantly. JDK Exhibit No. 8 shows that AFDC has increased from less than ten percent of earnings in 1969 to a high of 43.2 percent in 1978 and 36.7 percent for the test year ended June 30, 1980. The reduction from the higher level in 1978 results principally from the sale of portions of the Comanche Peak Steam Electric Station. AFDC earnings have a negative influence on the Company's financial integrity and its credit rating. The income statement reflects AFDC as income, when in fact it is a non-cash item which cannot be used in meeting the Company's capital requirements. Actually, AFDC represents a cost which cannot be fully recovered until the plant with which it is associated is fully depreciated. The Company's regulatory authorities have recognized the impact of AFDC on the quality of earnings and the PUC staff, in the Company's most recent rate case, has recommended that rates be set such that AFDC not exceed 20 percent of earnings. JDK Exhibit No. 9 shows that the Staff's recommendation for AFDC as a percent of earnings has never been attained during the periods of time following the implementation of rates resulting from the Company's last two rate proceedings. The amounts of CWIP allowed in rate base in those proceedings have been inadequate. As a result, the Company's AFDC as a percent of earnings has not dropped below 34 percent. Even with the requested $308 million of CWIP in rate base, additions to CWIP subsequent to the test year will result in additional AFDC earnings. For all of the above reasons the Company is requesting that the amount of CWIP shown in Schedule B, page 3, be included in rate base.

Q. DOES THE INCLUSION OF CWIP IN RATE BASE AFFECT THE FIXED CHARGE COVERAGE?

A. Again, to the extent that AFDC is included in earnings, the quality of those earnings is reduced. In evaluating a company's financial condition most financial analysts, the rating agencies and the sophisticated investor will consider the fixed charge coverage ratio excluding earnings attributable to AFDC. As shown in Schedule H-7, the Company's supplemental fixed charge coverage, excluding AFDC, has dropped to 2.42 times for the test year ended June 30, 1980. This coverage is inadequate and underscores the importance and necessity of including the requested amount of CWIP in the rate base.

Q. WHAT WEIGHTINGS WERE GIVEN TO CURRENT COST AND ORIGINAL COST IN CALCULATING THE COMPANY'S ADJUSTED VALUE RATE BASE?

A. Sixty percent original cost and forty percent current cost.

Q. WHAT FACTORS WERE CONSIDERED IN DETERMINING THESE WEIGHTINGS?

A. The need to attract capital, quality of service, the growth in the Company's service area, and inflation, as it has affected and will continue to affect the Company's construction program were considered. As discussed in Mr. Tanner's testimony, the Company is engaged in a substantial construction program to convert from the use of scarce and costly fuels such as natural gas and oil to cheaper, more abundant fuels such as lignite and uranium. As can be seen in MHT Exhibit No. 2, construction expenditures have increased dramatically in the past ten years. Our construction expenditures over the next three years are estimated to be almost $400 million, which is approximately 58 percent of the net cost of all the plant currently in service. The Company must be in a position to attract large sums of money from the investment community if it is to carry out its required construction program.

As to quality of service, the Company has met and is meeting the needs of its customers by providing dependable electric service within its service area. In order to continue to provide quality service, the construction of facilities to utilize alternate fuels must be maintained. Thus, the maximum current cost weighting of 40 percent is appropriate in view of the need to support this construction program and to continue the record of high quality service.

Inflation continues to have a serious impact on the Company's operations, as well as its construction program, since inflation increases the costs of all goods and services purchased. Also, interest rates continue to be high compared to our present embedded rates. Current interest rates for higher quality long-term debt are in the 13 percent range compared to our present embedded interest rate of 6.96 percent, as shown on Schedule H-6. Each new dollar of long-term debt or preferred stock increases our embedded cost of money, whether it is issued to finance our construction program or to refund maturing bonds and debentures originally issued 25 or 30 years ago.

In view of these factors, a 60 percent weighting for original cost and a 40 percent weighting for current cost is reasonable and should be allowed.

Q. WOULD YOU BRIEFLY DESCRIBE THE CAPITAL STRUCTURE OF DALLAS POWER & LIGHT COMPANY AT THE END OF THE TEST YEAR?

A. At the end of the test year the capitalization was composed of 41.6 percent long-term debt, 12.7 percent preferred stock and 45.7 percent common stock equity.

Q. PLEASE DESCRIBE THE COMPANY'S LONG-TERM DEBT.

A. At June 30, 1980, the Company had three basic types of long-term debt outstanding. The majority of this debt is first mortgage bonds. As reflected in Schedule H-6, the Company had thirteen series of first mortgage bonds outstanding in the principal amount of $305 million. These series range in principal amounts from $9.0 million to $50.0 million and have maturity dates from 1983 through 2005. Interest rates range from a low of 3 1/8 percent to a high of 9 3/8 percent.

At June 30, 1980, the Company had approximately $23.3 million of sinking fund debentures outstanding. This debt is not secured by any lien on the Company's property, but is issued on the basis of the Company's general credit. As reflected in Schedule H-6, there are two separate issues of 25-year debentures outstanding with maturity dates of 1989 and 1993. The interest rates are 4 1/2 percent and 6 3/4 percent, respectively.

Also reflected in Schedule H-6, is other unsecured debt consisting of three series of 30-year pollution control revenue bonds of approximately $16.7 million, net of funds on deposit with the trustee. These three series were sold by the Sabine River Authority, a governmental agency of the State of Texas, for the purpose of constructing pollution control equipment to be installed at certain jointly-owned generating stations of the Company, Texas Electric Service Company and Texas Power & Light Company. Interest on the bonds is exempt from federal income taxes to the holder. By agreement with the Authority, the Companies contract for the repayment of the bonds sold for the purchase of the equipment installed at the generating stations. The Company is obligated for $8,590,000 of the 6 1/4 percent series,

$7,125,000 of the 5.70 percent series and $2,025,000 of the 6.60 percent series. The bonds are due in 2006, 2007 and 2008, respectively. This type of security is similar to the sinking fund debentures in that they are based on the Company's general credit and are not secured by property of the Company.

The Company's embedded interest cost on long-term debt has steadily increased to 6.96 percent. This represents a 63 percent increase from the embedded cost of 4.26 in 1969.

Q. WHAT RATINGS HAVE BEEN ASSIGNED TO THE COMPANY'S FIRST MORTGAGE BONDS, SINKING FUND DEBENTURES AND POLLUTION CONTROL REVENUE BONDS?

A. The Company's first mortgage bonds have been designated triple A by both Moody's Investors Service, Inc. and Standard & Poor's Corporation. The sinking fund debentures and pollution control revenue bonds have been assigned a double A rating by both agencies since they are not secured by property but are based on the general credit of the Company.

Q. PLEASE DESCRIBE THE NOTES PAYABLE INCLUDED IN THE COMPANY'S CAPITAL STRUCTURE.

A. The notes payable, amounting to an adjusted $202,821 as shown in Schedule H-5, page 2, were issued as partial payment for land acquired for plant sites, lignite reserves and water rights.

Q. WOULD YOU DESCRIBE THE COMPANY'S PREFERRED STOCK?

A. At June 30, 1980, the Company had seven preferred stock issues outstanding as detailed in Schedule H-4. The amount outstanding was approximately $104.7 million with annual dividend rates ranging from $4.00 per share to $7.48 per share. The preferred stock is cumulative, without par value, and entitled to $100.00 per share upon liquidation. The embedded annual dividend rate for all of the series is currently 6.27

percent, as shown in Schedule H-4. The Company's preferred stock, like the sinking fund debentures and pollution control revenue bonds, is rated double A by both Moody's Investors Service, Inc. and Standard & Poor's Corporation.

Q. PLEASE DESCRIBE THE COMPANY'S COMMON STOCK.

A. At June 30, 1980, there were 14 million shares of common stock outstanding, 99.9 percent of which were owned by Texas Utilities Company. The common stock equity on the books of the Company at this date amounted to $377.9 million.

Q. ARE THERE ANY OTHER ADJUSTMENTS NECESSARY TO DETERMINING THE PROPER CAPITAL STRUCTURE OF THE COMPANY FOR THIS PROCEEDING?

A. Yes. A pollution control revenue bond issue is scheduled to take place in October of 1980 in which the Company will be obligated for $6,334,000 of the issue. This adjustment more accurately reflects the Company's capital structure and is shown in Schedule H-6, page 1, of the rate filing package.

Q. HAVE YOU CALCULATED THE COMPANY'S WEIGHTED COST OF CAPITAL AT JUNE 30, 1980 AS ADJUSTED?

A. Yes. Schedule H, page 2, shows the outstanding capital, as adjusted, at the end of the test year. The weighted cost of capital is the composite cost of the various classes of capital used by the Company. The cost of long-term debt is the embedded cost of debt taken from Schedule H-6. Notes payable are detailed in Schedule H-5, page 2. The cost of preferred stock capital is its annual dividend requirement as shown in Schedule H-4. The cost of common stock equity capital is the amount necessary to yield a fair return as described by Dr. Charles E. Olson and is reflected in Schedule H, page 2. The cost of equity was determined from Dr. Olson's recommended range of return on common equity of 17.0 to 18.0 percent. In view of current circumstances, I believe a 17.0 percent return is appropriate. Although the 17 percent return is the minimum of the range recommended by Dr. Olson, such return together with the inclusion of 100 percent of the test year balance of CWIP which the Company is also requesting should be adequate to allow the Company a reasonable opportunity to improve its financial integrity. However, it is apparent that with the inclusion of less than 100 percent of CWIP in rate base, a higher return on common equity would be necessary and appropriate.

Q. WHAT IS THE COMPANY'S WEIGHTED COST OF CAPITAL?

A. The weighted cost of capital is derived by taking each cost element expressed as a percentage rate as shown on Schedule H, page 2. This results in an 11.44 percent weighted cost of capital on a total adjusted capitalization of $886,029,596.

Q. MR. KARNEY, WHY DO YOU CONSIDER 17.0 PERCENT RETURN ON COMMON EQUITY TO BE REASONABLE?

A. Since the equity component is the foundation of the capital structure and the common shareholder bears the most risk, the return to the common shareholder must be higher than the return to either the bondholders or the preferred shareholders. Currently the return on high quality corporate bonds with little or no risk is approximately 13 percent. The return to the risk bearing equity investor must be substantially higher. With the Company's present depressed level of earnings and interest coverage, the recommended return on equity is justified and necessary to assure its financial integrity.

Q. WILL YOUR PROPOSAL GUARANTEE THE COMMON EQUITY INVESTOR THAT HIS RETURN WILL BE 17.0 PERCENT?

A. No. Recent history shows that the allowed return on common equity has not been earned. This results from the use of a historical test year to determine the Company's rate base and cost of service. In our last proceeding it was nine months after the end of the test year before the Company was able to begin billing a portion of the requested rate increase under bond, and it was eleven months before current rates were billed under an interim rate order. During this period, the Company's costs continued to increase and the investment continued to grow, making the test year out of date well before the rates went into effect. This assured that the Company would be unlikely to earn the rate of return granted based on a historical test year. Although some adjustments have been made for post-test year events, these adjustments do not fully offset the effects of attrition on the Company. Unless the Company's regulatory authorities recognize the reality of attrition, the Company will be denied the opportunity to earn the return granted.

Q. MR. KARNEY, WILL THE REVENUE INCREASE REQUESTED IN THIS CASE ALLOW THE COMPANY A REASONABLE OPPORTUNITY TO RESTORE ITS FINANCIAL INTEGRITY?

A. An analysis of the Company's projected results of operations based upon rate increases resulting from various levels of return on equity and CWIP in rate base clearly indicates that the Company has virtually no chance of earning the 17 percent return on equity requested, unless all of the CWIP requested is included in rate base. If such amount of CWIP is included in rate base, there is a reasonable opportunity to earn the requested return on equity by the end of the first year the new rates will be in effect; however, the return declines significantly thereafter. Although return on equity on a twelve month basis reaches 17 percent at one point in time (the twelve months ended December 31, 1981), the return for any other twelve month period is below this level. It should be noted that such results are based upon receipt of the full amount of rate increase requested by the Company; anything less cannot be expected to produce these results.

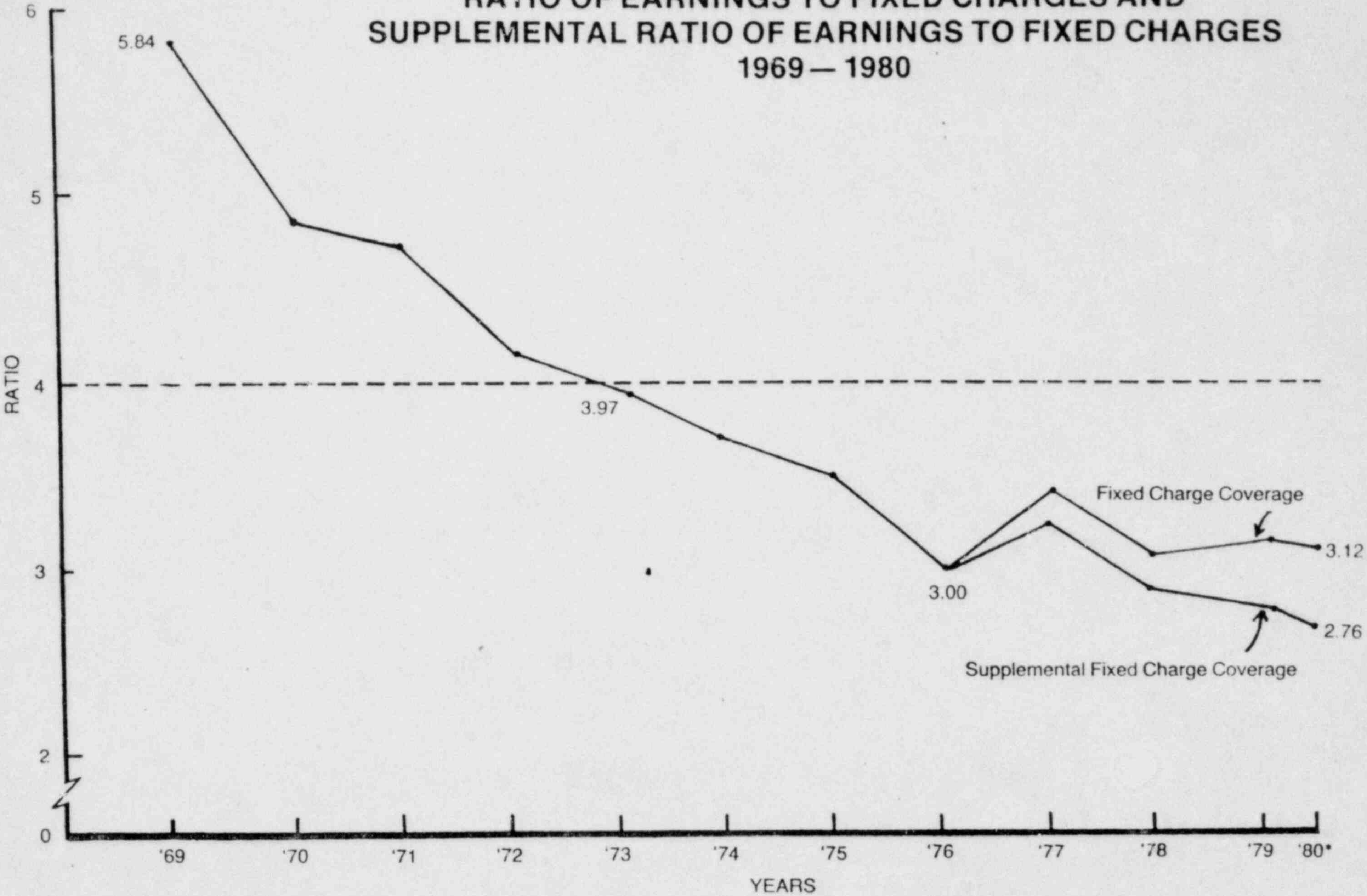
Q. WHAT HAS BEEN DALLAS POWER & LIGHT COMPANY'S RETURN ON EQUITY SINCE JANUARY 1, 1978?

A. JDK Exhibit No. 10 clearly illustrates that the Company has not earned the rate of return allowed. The Company's authorized return was increased from 13.75 percent in Docket 1526 to 14.5 percent in Docket 2572, represented by the horizontal lines near the top of the exhibit, yet the return actually earned has continued to fall below the amount authorized. Further, the deficiency between the earned and authorized return is increasing. This indicates that previous rate orders have been inadequate and that in determining the amount of revenue deficiency, the Company's regulatory authorities must more carefully appraise the impact of economic and other factors that will exist during the period the rates will be in effect.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

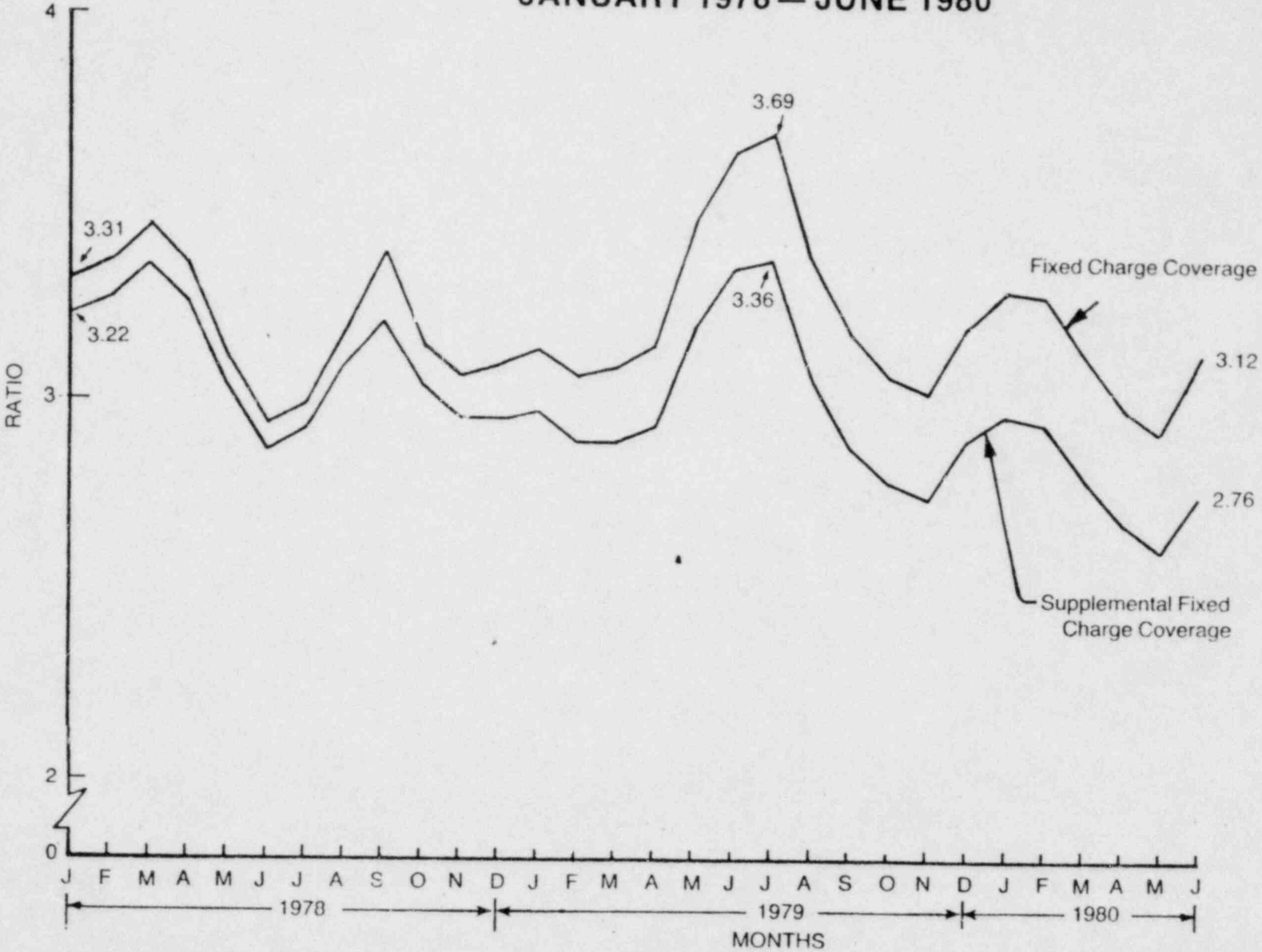
DALLAS POWER & LIGHT COMPANY
RATIO OF EARNINGS TO FIXED CHARGES AND SUPPLEMENTAL RATIO OF EARNINGS TO FIXED CHARGES
1969 — 1980



*TEST YEAR ENDED JUNE 30, 1980

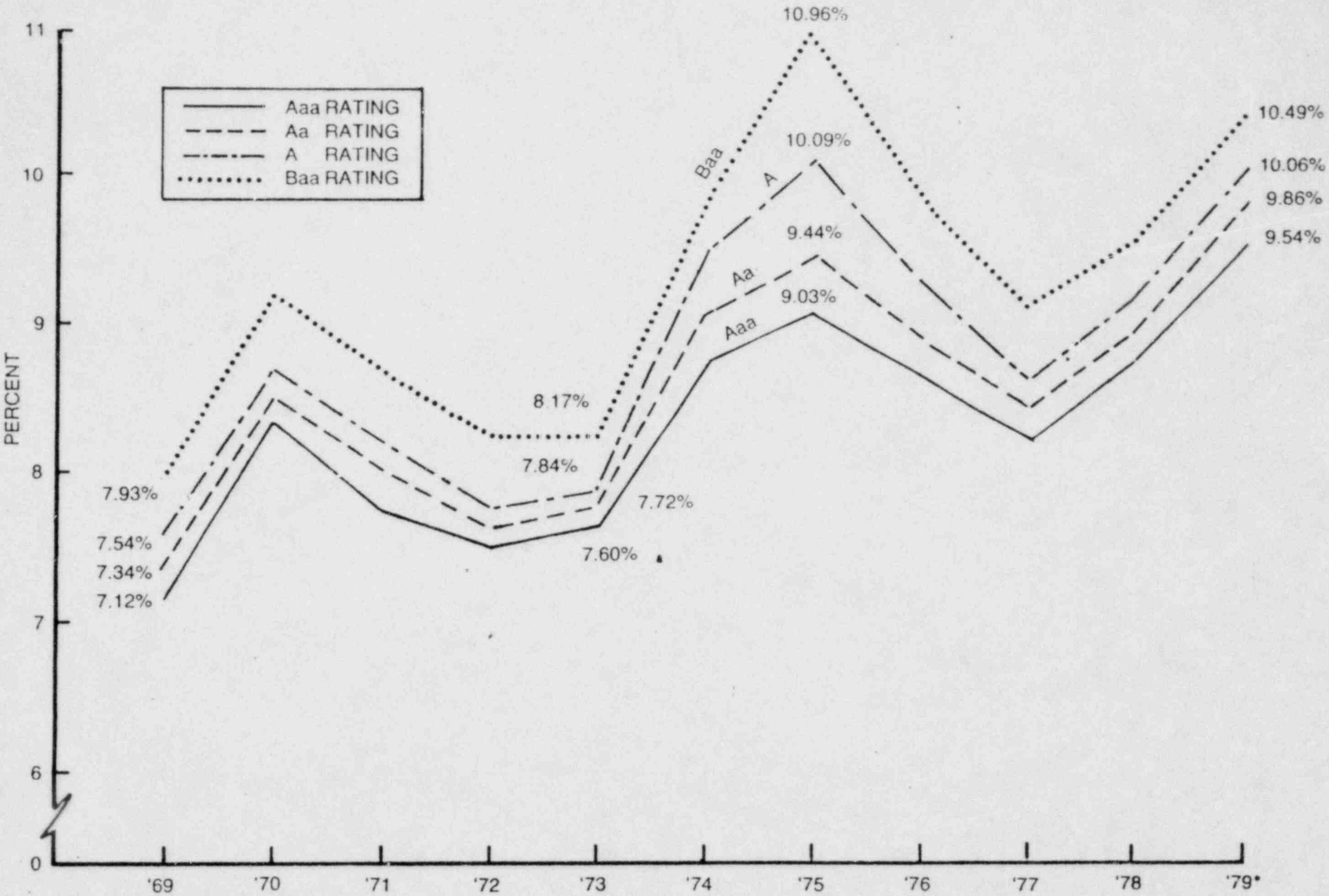
JDK Exhibit No. 1
Page 1 of 1

DALLAS POWER & LIGHT COMPANY
RATIO OF EARNINGS TO FIXED CHARGES AND SUPPLEMENTAL RATIO OF EARNINGS TO FIXED CHARGES
JANUARY 1978 — JUNE 1980



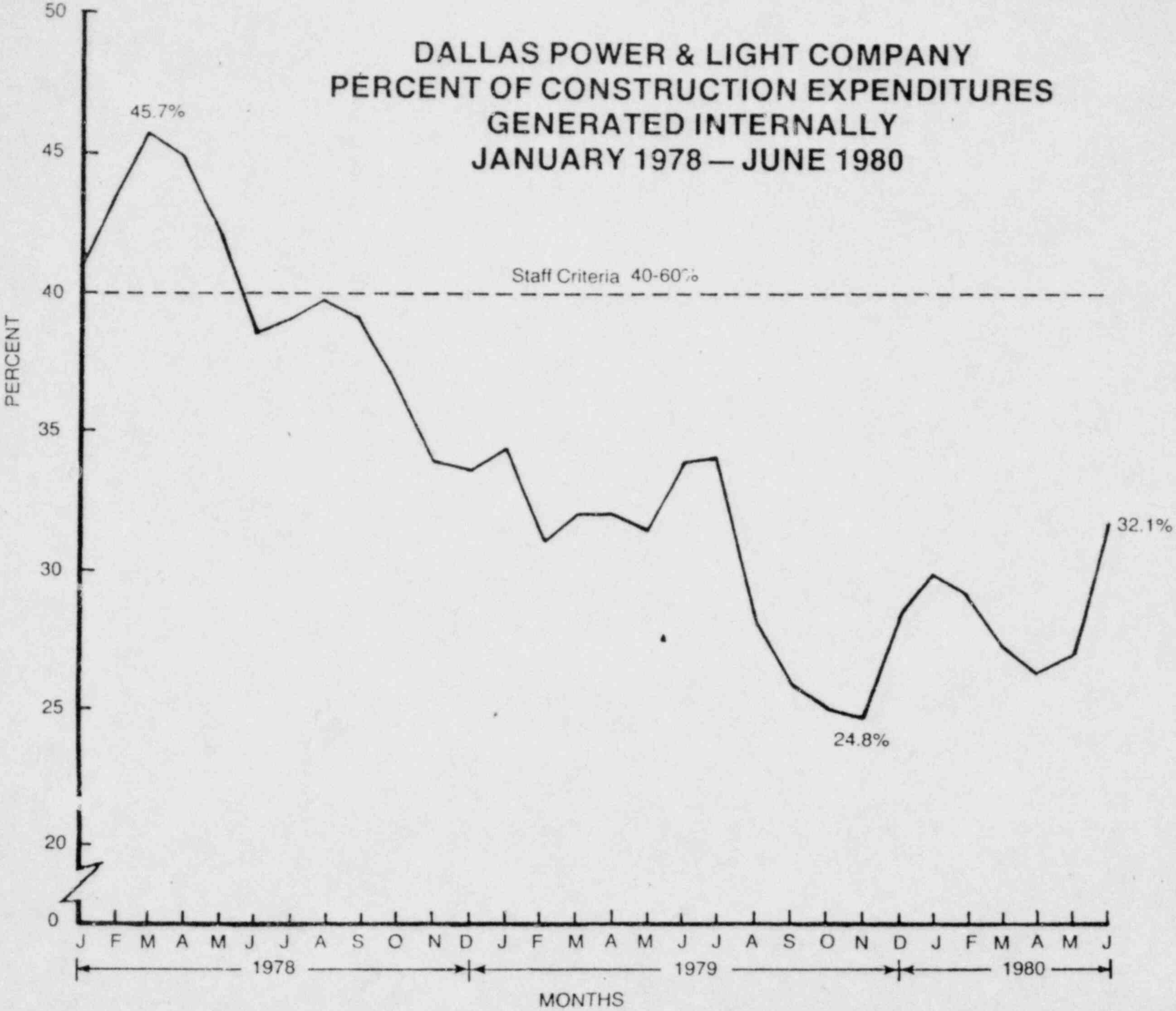
JDK Exhibit No. 2
Page 1 of 1

MOODY'S AVERAGE PUBLIC UTILITIES BOND YIELD BY RATING GROUP 1969 — 1979



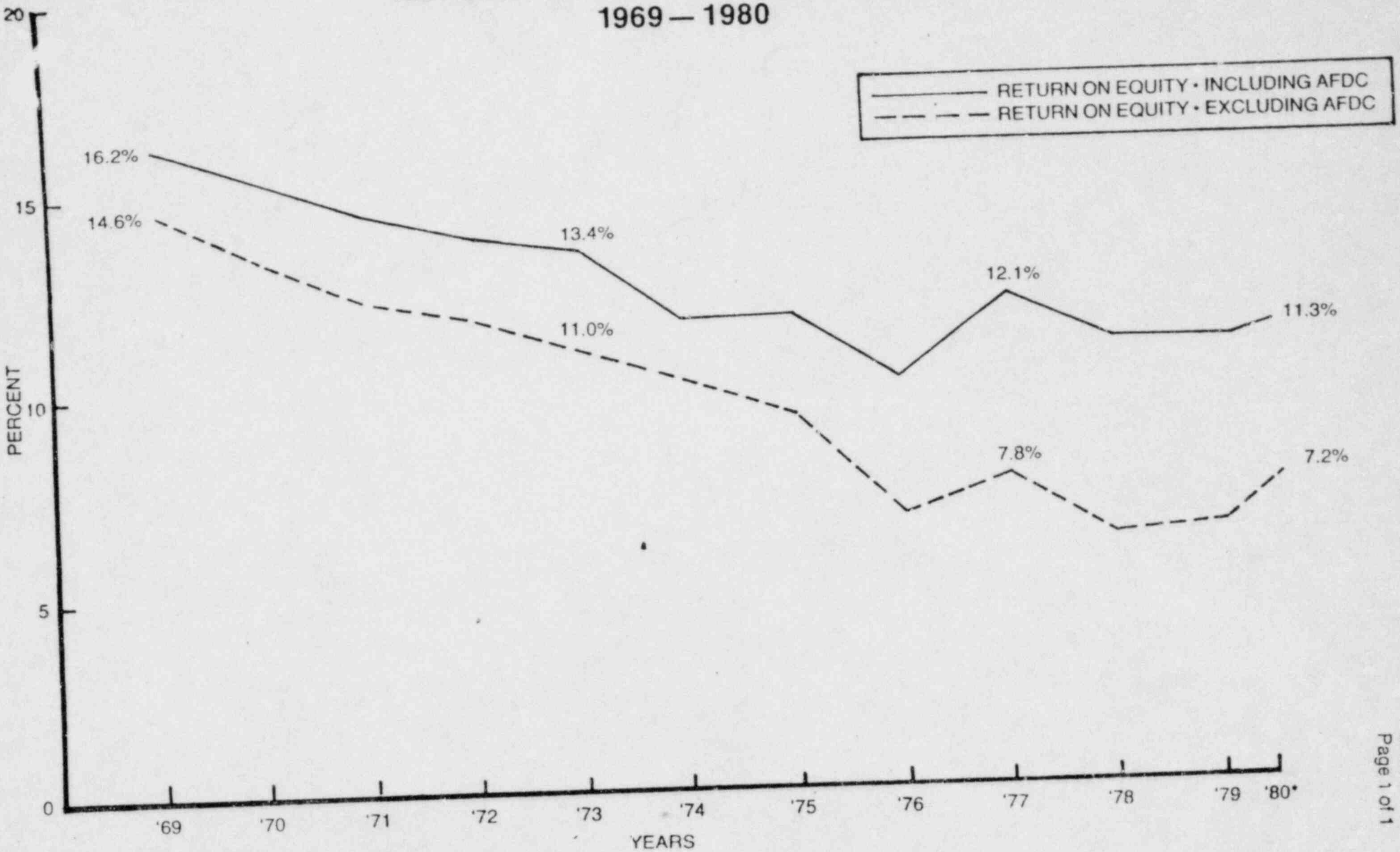
*EIGHT MONTHS ENDED AUGUST, 1979

JDK Exhibit No. 3
Page 1 of 1



JDK Exhibit No. 4
Page 1 of 1

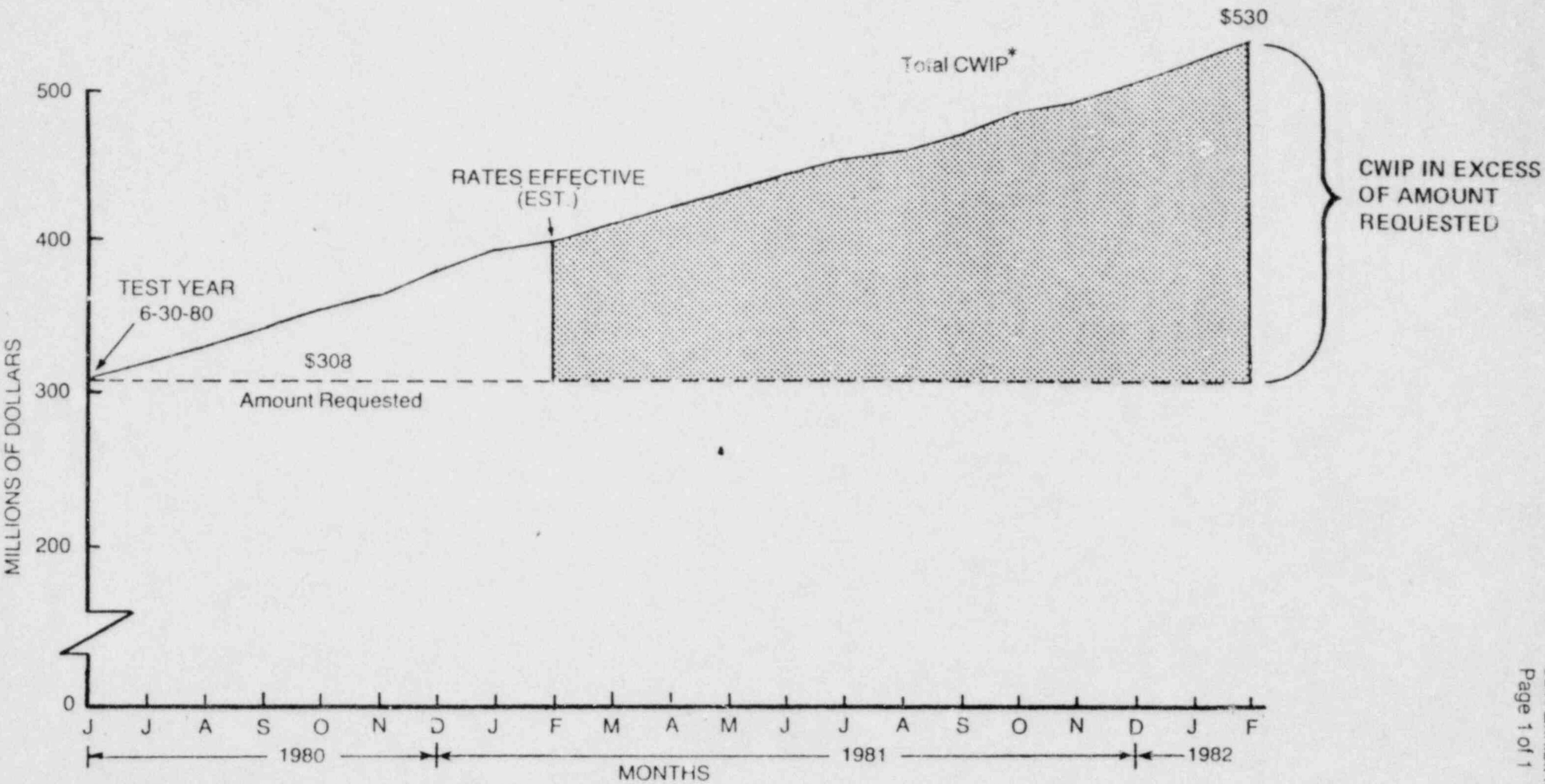
DALLAS POWER & LIGHT COMPANY
RETURN ON COMMON STOCK EQUITY
1969 — 1980



*TEST YEAR ENDED JUNE 30, 1980

JDK Exhibit No. 5
Page 1 of 1

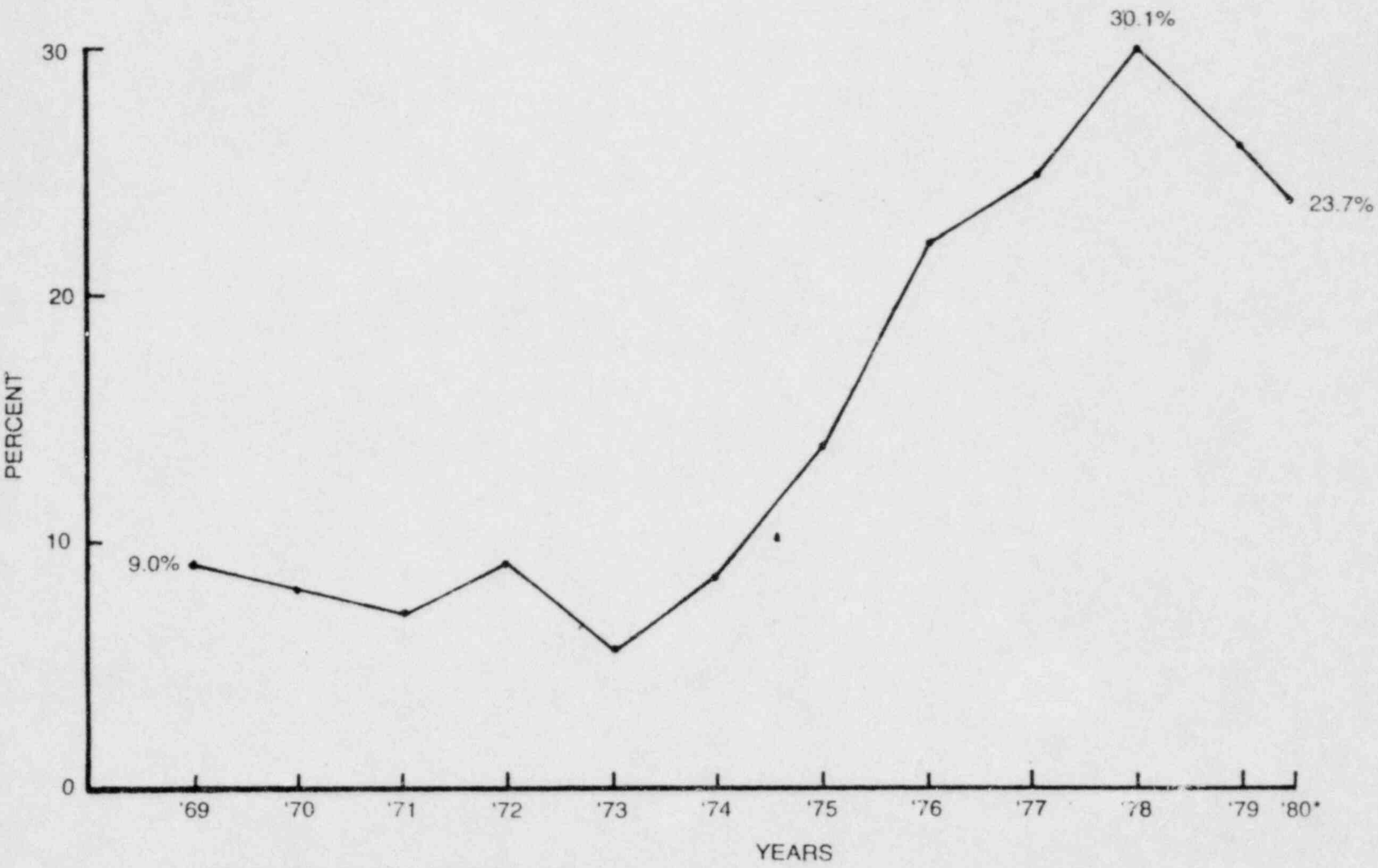
DALLAS POWER & LIGHT COMPANY
CWIP IN RATE BASE
ACTUAL VS. AMOUNT REQUESTED



*ACTUAL AT JUNE 30, 1980 AND ESTIMATED THEREAFTER

JDK Exhibit No. 6
Page 1 of 1

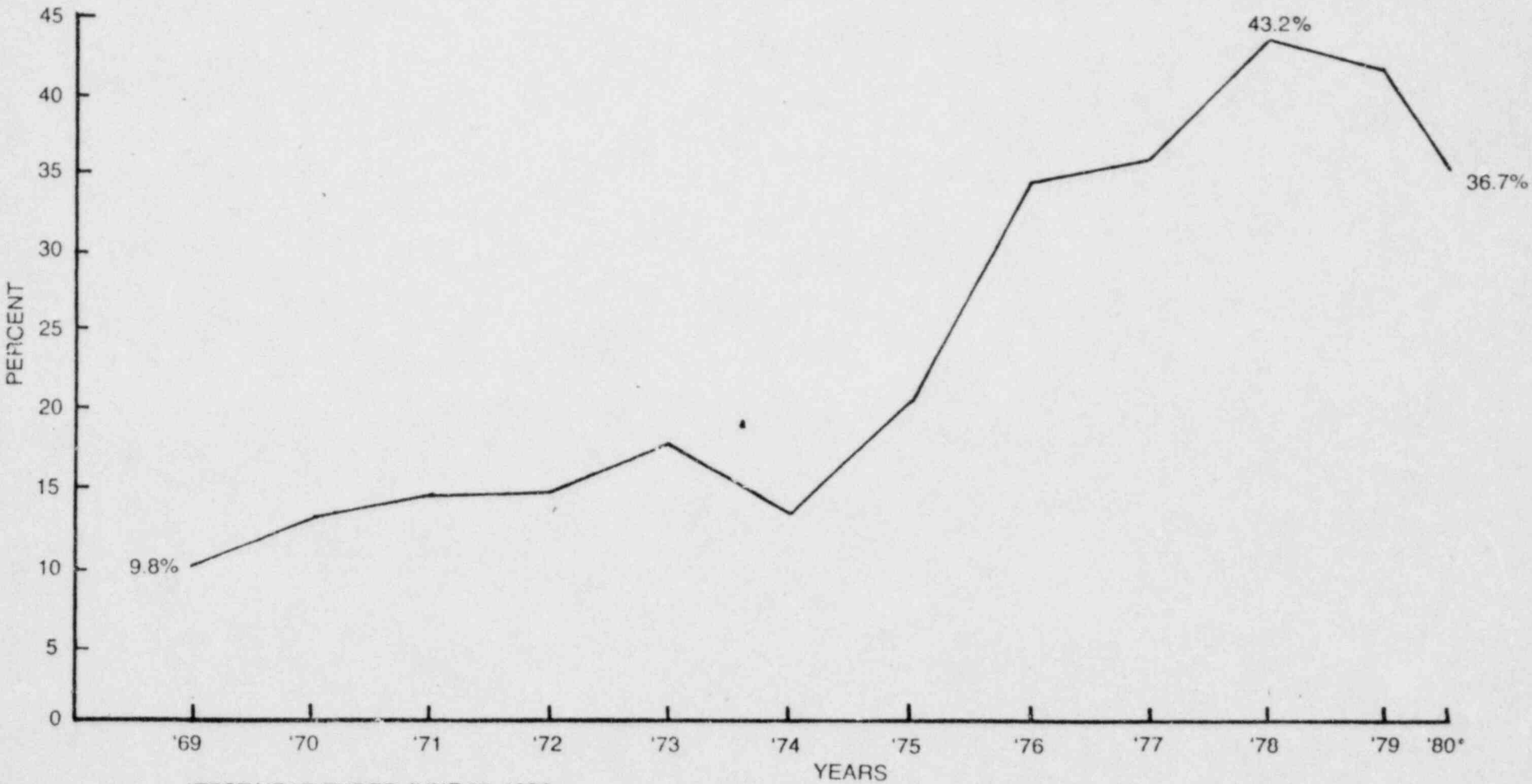
DALLAS POWER & LIGHT COMPANY
CWIP AS A PERCENT OF TOTAL ELECTRIC PLANT
1969 — 1980



*TEST YEAR ENDED JUNE 30, 1980

JDK Exhibit No. 7
Page 1 of 1

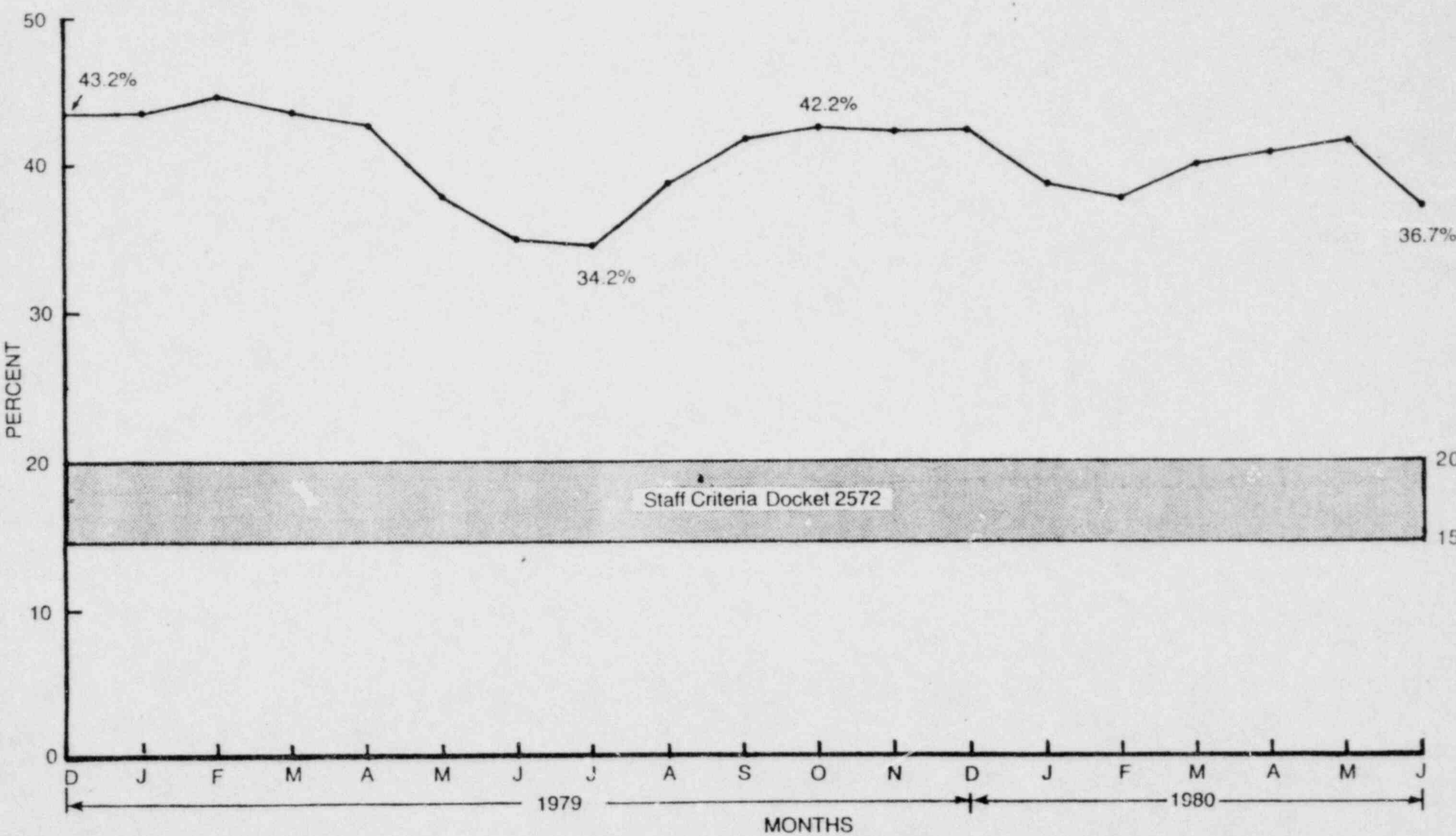
DALLAS POWER & LIGHT COMPANY
AFDC AS A PERCENT OF EARNINGS
1969 — 1980



*TEST YEAR ENDED JUNE 30, 1980

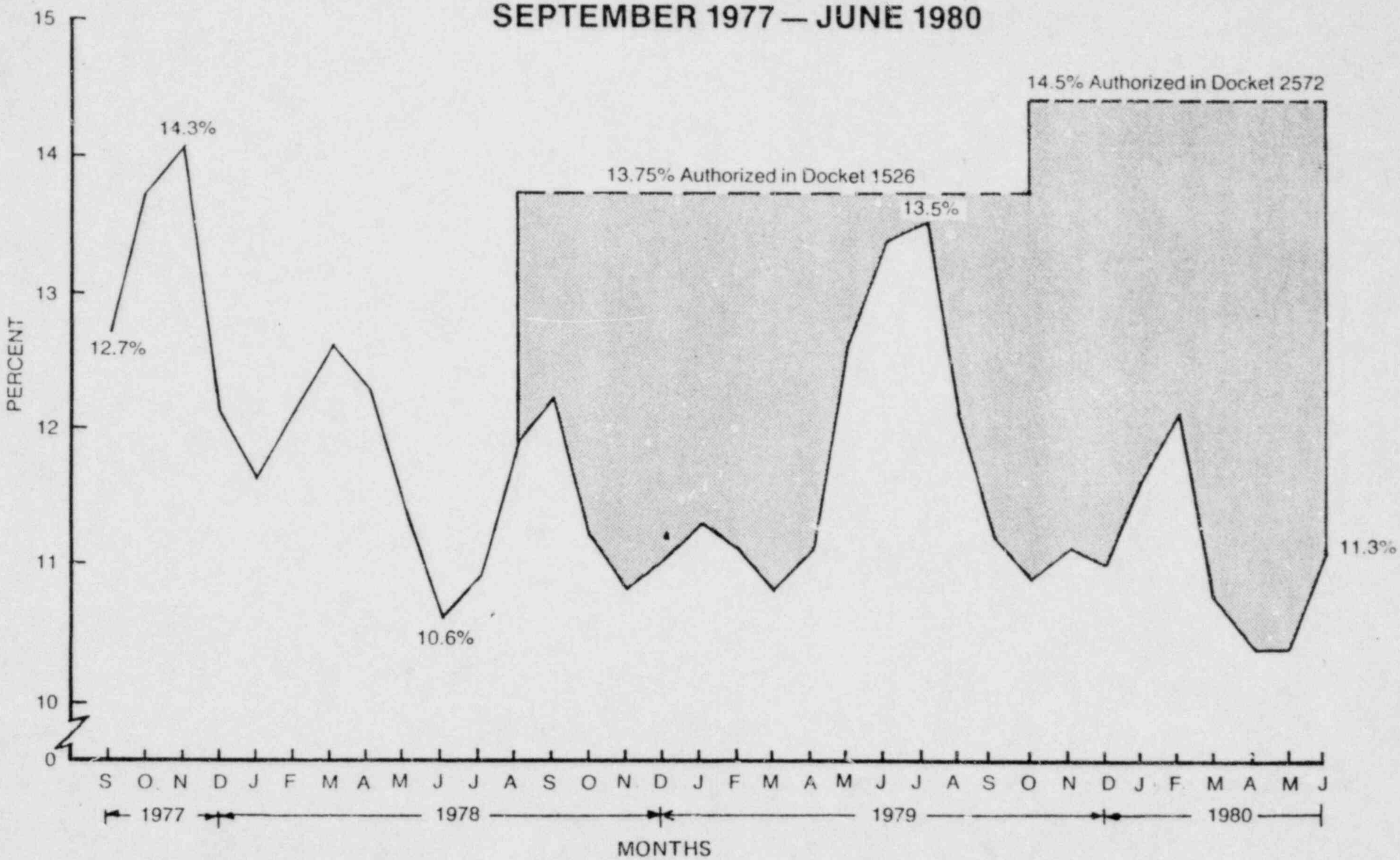
JDK Exhibit No. 8
Page 1 of 1

DALLAS POWER & LIGHT COMPANY
AFDC AS A PERCENT OF EARNINGS
DECEMBER 1978 — JUNE 1980



JDK Exhibit No. 9
Page 1 of 1

DALLAS POWER & LIGHT COMPANY
RETURN ON AVERAGE COMMON EQUITY
ACTUAL AND AUTHORIZED
SEPTEMBER 1977 — JUNE 1980



JDK Exhibit No. 10
Page 1 of 1

THE STATE OF TEXAS)

COUNTY OF DALLAS)

BEFORE the undersigned authority on this day personally appeared J. D. KARNEY, who, having been placed under oath by me, did depose as follows:

"My name is J. D. Karney. I am of legal age and a resident of the State of Texas. The foregoing testimony, and exhibits, offered by me on behalf of Dallas Power & Light Company, are true and correct, and the opinions stated therein are, to the best of my knowledge and belief, accurate, true, and correct."

J. D. Karney

J. D. KARNEY

SUBSCRIBED AND SWORN TO BEFORE ME by the said J. D. Karney this 23rd day of September, A. D. 1980.

Carla F. Stroud

Carla F. Stroud
Notary Public in and for Dallas
County, Texas

My commission expires 3-31-84

DIRECT TESTIMONY OF

MAX H. TANNER, JR.

FOR

DALLAS POWER & LIGHT COMPANY

SEPTEMBER, 1980

dupe of

~~811240890~~

DIRECT TESTIMONY OF MAX H. TANNER, JR.

Q. PLEASE STATE YOUR NAME AND ADDRESS.

A. Max H. Tanner, Jr., 1506 Commerce Street, Dallas, Texas 75201.

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

A. I am a Vice President of Dallas Power & Light Company.

Q. HOW LONG HAVE YOU BEEN WITH THE COMPANY AND IN WHAT CAPACITIES?

A. I have been a full-time employee of DP&L since 1953 and have served in various technical and managerial capacities in the design, construction, operation and maintenance of the Company's distribution, transmission and production facilities, including fuel requirements. I served as Manager of DP&L's Production Department from 1968 until 1974 and as Manager of System Operation until 1976, when I was elected Vice President.

Q. WHAT IS THE NATURE OF YOUR RESPONSIBILITIES AS VICE PRESIDENT?

A. I am responsible for planning and engineering system facilities; managing the Company's power production, transmission and distribution activities; and securing fuel supplies for DP&L's plants. I am also responsible for coordinating operations with other Texas Utilities (TU) companies and other interconnected systems.

Q. WHAT ARE YOUR EDUCATIONAL AND PROFESSIONAL QUALIFICATIONS?

A. I have a Bachelor of Science Degree in Electrical Engineering from Texas A&M University and am a Registered Professional Engineer in the State of Texas.

Q. ARE YOU A MEMBER OF ANY INDUSTRY OR PROFESSIONAL ORGANIZATIONS?

A. I am presently active in the Texas Interconnected System (TIS), Electric Reliability Council of Texas (ERCOT) and the National Electric Reliability Council (NERC). In addition, I am a member of the Power Engineering Society of the Institute of

Electrical and Electronics Engineers (IEEE).

Q. MR. TANNER, PLEASE TELL US WHAT YOUR TESTIMONY WILL COVER.

A. I will review the Company's construction program, fuel utilization plans, operations, depreciation and related matters.

Q. HAVE YOU PREVIOUSLY TESTIFIED ON ANY OF THESE MATTERS BEFORE THE COMPANY'S REGULATORY AUTHORITIES?

A. Yes. I testified in the Company's last three rate applications before the City of Dallas and in Dockets 1526, 1903, 2572, and 3090 before the Public Utility Commission.

Q. WOULD YOU PLEASE DESCRIBE THE FACTORS WHICH IMPACT THE PLANNING OF FACILITIES NECESSARY FOR SUPPLYING ELECTRIC SERVICE?

A. Yes. There are many factors which affect the planning of facilities to meet the needs of our customers. These factors include: (1) the availability, cost and transportation of fuels; (2) the projected growth in both peak load and energy; (3) availability and location of water rights and plant sites; (4) availability and cost of capital; (5) the overall level of system reliability and (6) the time required to engineer, obtain regulatory approvals and construct new facilities. In view of the uncertainties associated with each of these factors, it is imperative, and in the best long term interests of our customers, to maintain viable options and flexibility in planning for additional facilities.

To supply electric service to the Company's service area, extensive facilities, resources and capital investments are necessary. In today's environment, the long lead times required to place new facilities in service and the high rate of inflation severely impact construction costs. Such parameters necessitate careful planning and engineering to provide facilities to meet the needs of our customers during a time when uncertainties prevail in every facet of the industry.

Q. MR. TANNER, WHY DOES IT TAKE SO LONG TO PLAN AND BUILD NEW GENERATING FACILITIES?

THE STATE OF TEXAS X

COUNTY OF DALLAS X

BEFORE the undersigned authority on this day personally appeared MAX H. TANNER, JR., who, having been placed under oath by me, did depose as follows:

"My name is Max H. Tanner, Jr. I am of legal age and a resident of the State of Texas. The foregoing testimony, and exhibits, offered by me on behalf of Dallas Power & Light Company, are true and correct, and the opinions stated therein are, to the best of my knowledge and belief, accurate, true, and correct."

Max H. Tanner, Jr.
MAX H. TANNER, JR.

SUBSCRIBED AND SWORN TO BEFORE ME by the said MAX H. TANNER, JR. this 17th day of September, A.D. 1980.

Kathy Wood
Notary Public in and for
Dallas County, Texas

My commission expires June 26, 1981

DALLAS POWER AND LIGHT COMPANY

APPLICATION FOR RATE CHANGE
SUBMITTED TO THE CITY OF DALLAS

- - -

APPEARANCES:

MR. THOMAS Z. JAMES

THE EXAMINER

DALLAS POWER AND
LIGHT COMPANY
Mr. Al Engelland
Mr. Robert A. Wooldridge

For the Applicant

MR. GALEN M. SPARKS

Assistant City
Attorney for the
City of Dallas

MS. PAM O'BRIEN

Assistant to the
Hearing Examiner

MRS. JUANITA ELLIS

President, CASE

MR. GEOFFREY GAY
MR. ROGER JOYNER
MS. FAITH SIMMONS

For ACORN

MS. KIM BATCHELOR

For CCEE

TRANSCRIPT OF PROCEEDINGS HAD ON THE 24TH DAY OF NOVEMBER, A.D., 1980, IN THE DALLAS CITY HALL, ROOM 6E SOUTH, CITY OF DALLAS, COUNTY OF DALLAS, STATE OF TEXAS, AT 9:00 O'CLOCK A.M.

- - -

Q Right. So you're saying, then, are you not, that as regards your lower growth projections, you reduced your interest in the nuclear plant?
A And some lignite plants and delayed some other lignite plants.
Q You postponed or rescheduled or reduced your interest in some of these lignite plants?
A (Witness nods head affirmatively)
Q Can you review the history of some of those transactions briefly for us, bring us up-to-date on what's transpired in regard to your interest in these joint projects?
A Well, we had in Comanche Peak, a third interest. It was agreed back in 1976 that a ten percent interest in that plant, which was required by the construction permit, to be sold to some third parties, would come from DP&L's portion. Because of the lengthy negotiations, that wasn't finalized till 1979. And then in 1980, early 1980, we sold an additional five percent to our sister companies. So we now have an eighteen and a third percent ownership in Comanche Peak, which is very close to our projected energy portion of the other operating companies. Or our subsidiary other operating companies.
Forest Grove, it's laid out until 1987,

Martin Lake 4 was scheduled at one time earlier and it's scheduled for '84. Martin Lake 4, also, we have a 20 percent interest now, we had a 25 percent interest earlier.

Q Did you change the percentage interest share in Forest Grove?

A No.

Q You just delayed?

A That's correct.

Q All right. Would you agree with me, Mr. Tanner, that the City of Dallas has generally been supportive of the construction program and the move away from gas as a primary fuel?

A Yes, very definitely.

Q And has Dallas also been, at least generally, somewhat supportive of the inclusion of a part of the CWIP in the rate base?

A Yes.

Q Let's look now at your Exhibit No. 4 where you show a projection of the relative fuel mix through 1989.

When did we hit the low point on gas, Mr. Tanner, was it in '79?

A That's the low point we hit so far.

Q And isn't that the low point that we're going to hit for a long time?

A. Well, looks like out through this part of the '80's, we're going to be in the 50 percent range or a little under 50 percent.

Q. And what was the percentage of gas in your fuel mix in '79?

A. Forty-eight percent.

Q. And then in '80, it jumps back up a little bit over 50 percent, does it not?

A. That's correct.

Q. Are we going the wrong direction?

A. Well, I don't think so.

Q. Well, as I recall, I believe we agreed that the objective of the construction program was to move away from gas.

A. That's correct, but we have had some changes which have caused us to shift that somewhat and delay it somewhat, because Docket 600 was repealed, the Fuel Use Act a owed us to burn gas in our existing units to a great r extent through the '80's. Natural Gas Policy Act caused more gas to come on stream so there -- and for peak and intermediate load purposes, the gas, even at a higher cost, low imbed cost and the capital expense of those units, it is more economical to go ahead and build replacement units.

Q All right. Well, what we see here on your Exhibit 4, isn't it correct that there is no substantial reduction in gas in your fuel mix on out until 1987 or '88, when the western coal plant comes on line?

A We're going to be at 40 percent in '86, looks like about the same amount in '85.

Q But in any event, it's a pretty flat curve until that western coal plant comes on line, isn't it?

A That's correct.

Q Okay. Can you tell us about TESCO and TP&L with regard to fuel mix? Will their percentage of gas be lower in the 1980's than DP&L?

A I do not know.

Q I believe you say in your testimony that DP&L now wants to reschedule the retirement of some of these gas/oil units.

A That's correct.

Q Okay. Can you compare for us the retirement plans you testified to last year in Docket 2572 against the present plans?

A By units or -- Dallas 3 has been delayed from '83 until '85. Dallas 9, from '82 to '85. Mountain Creek 2, from '79 to '83. Mountain Creek 3, from '80 to '83.

Q Parkdale?

A Parkdale 2, from '81 to '84.

Q So we're looking at three or four years delays on 1, 2, 3, 4, 5 gas units?

A Yes.

Q Well, we don't seem to be making much progress, Mr. Tanner, do we, during this decade of the '80's away from gas.

A That's by a conscious decision.

Q And is it consistent with what you represented to the regulatory authorities in the previous cases?

A No, because the fuel situations in regard to gas has changed since then.

Q All right.

A And our objective is still to shift off of gas and oil, but we're shifting at a slower pace than we were earlier.

Q Well, despite rate increases in, I believe it was '76, '78, '79, and the proposed application in this case, and despite all that CWIP in the rate base that the Dallas customers pay for, we're not making much progress, are we, towards getting away from gas here over in the near term?

A I think we are. And what we are doing is very beneficial to the customer, as is shown in my

DOCKET NUMBER
PROD. & UTIL. FAC. 50-445, 446

DOCKETED
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Public Utility Commission of Texas

'81 DEC 15 P4:14

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DOCKETING & SERVICE
BRANCH

I, Martha M. Bartow, certify that this is a true and correct copy of a portion of the cross examination of Charles E. Olson from the transcript of the December 9, 1980 Hearing from Public Utility Commission Docket No. 3460.

ISSUED UNDER MY HAND AND SEAL on this the 9th day of December, 1981.

Martha M. Bartow

Martha M. Bartow
Director of Record Services

SEAL

TRANSCRIPT OF PROCEEDINGS

BEFORE THE

PUBLIC UTILITY COMMISSION OF TEXAS

AUSTIN, TEXAS

IN THE MATTER OF THE	I	
APPLICATION OF DALLAS	I	DOCKET NO. 3460
POWER & LIGHT COMPANY	I	
FOR A RATE INCREASE	I	

PUBLIC HEARING ON APPLICATION

TUESDAY, DECEMBER 9, 1980

MORNING SESSION

VOLUME III

Pages 214 to 297

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THE RECORD NEVER FORGETS

TABLE OF CONTENTS

Q All right. Are you saying, then, that the increased revenues from--the increased revenues from TP&L, because of the hot summer, have helped, have they not?

A Yes, as DP&L's and TESCO's to the extent they contributed also helped.

Q All right. What I'm getting at is the need for rate relief now. Is this--Hasn't this alleviated part of the problem already? In other words, DP&L needs a rate increase based on this test year, but there have been factors which have come into play since the test year which have alleviated part of that problem, have they not?

A No. They haven't alleviated it. In spite of this record summer, in spite of the fact that Staff is recommending a higher return on equity than has probably ever been recommended for any Triple A public utility ever in the United States, we still see the common shares of Texas Utilities rating at less than 75 percent of book value. It's a long ways from 110.

Q And in spite of the fact that the--that Texas Utilities revenues for the first eight months of 1980 increased by 23 percent and DP&L's increased by 25 percent?

A In spite of all that, inflation is at record levels, interest rates are at record levels. Yesterday, Southwestern Bell, a Triple A company, sold long-term debt at a rate of 14.25 percent. That's higher than the returns on equity that this Commission was granting a couple of years ago, and the cost of debt, obviously, sets the floor for the return on equity, and there is just not very much spread between 14 and a quarter and 17.

Q So you don't think that--you don't think that this has alleviated the problem at all?

A It really hasn't. Interest rates are at high levels, and if the Company is going to have a capital attracting a rate of return that's going to be such that the shares will sell at a price equal to or, let's say, 110 percent of book value, they have to have more than they do right now. They just have to have more; otherwise, it's just going to be a continued situation of selling at less than book.

Q All right. I would like to talk to you for a minute about something which was said yesterday. I believe it was when I was discussing this with Mr. Tanner. He stated something to the effect that the sale of part of Comanche Peak does not affect the ratepayers. Do you recall that?

TRANSCRIPT OF PROCEEDINGS

BEFORE THE

PUBLIC UTILITY COMMISSION OF TEXAS

AUSTIN, TEXAS

IN THE MATTER OF THE	X	
APPLICATION OF DALLAS	X	DOCKET NO. 3460
POWER & LIGHT COMPANY	X	
FOR A RATE INCREASE	X	

PUBLIC HEARING ON APPLICATION

TUESDAY, DECEMBER 9, 1980

AFTERNOON SESSION

VOLUME IV

Pages 298 to 404

HKRS

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an increased role for the distribution activity of the electric utilities and a lesser production role.

Q All right. Could this also go back to what we were talking about, that perhaps there needs to be another method arrived at for rewarding the utilities rather than strictly by how much electricity they sell?

A I don't see how you make that link. There has been a great deal written that says that utilities are rewarded for the amount of rate base they have. But for the past five or six years, initially, DP&L and TU and other utilities have been penalized as they have added rate base. In other words, the more rate base they have added, the more rates have gone up, and the more the market-to-book ratio has fallen. So the shareholders haven't come out ahead by these expansions of rate bases and new issues of common shares at prices less than book value.

Q This goes back, too, to the large construction program, does it not?

A Yes, it does.

Q All right. I'm going to refer to the Dallas transcript of this year's hearings, if you would like to refer to it, also, on page 233, beginning about line 14, there.

Where you state that, "You don't find very

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OFFICE OF SECRETARY
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BRANCH

Public Utility Commission of Texas

George M. Cowden
Chairman

H. M. Rollins
Commissioner

Garrett Morris
Commissioner

I, Martha M. Bartow, certify that this is a true and correct copy of a portion of the Transcript of the hearing for July 9, 1979 and July 10, 1979 from Public Utility Commission Docket No. 2572.

ISSUED UNDER MY HAND AND SEAL on this the 11th day of December, 1981.

SEAL

Martha M. Bartow

Martha M. Bartow
Director of Records Services

2061

Q You testified to in response to a question by Mr. Bell about the level of residenti l bills for the companies of the Triple A and the Double A ratings. I think I heard you say that making tha comparison you dropped DP&L out.

A Yes.

Q Why was that?

A Well, I think there was a little bit of circular reasoning I'm trying to compare it against the others. I'll go a little further and be candid with you. I'm not sure whether we are Triple A or Double A. I haven't chanced it in awhile. The same results would--I think would come forward. Our rate for that particular month was a little higher than the average in that respect maybe I made an undue comparison. I don't remember the number exactly, but maybe if you add one dollar to the average that I gave you for the Triple A you could put it for all four companies. I can get you that number, but it's not--

Q I was just interested about why you dropped DP&L out. That was my only interest. And also in response to Mr. Bell you used a term that I'm not familiar with and I think some of the other folks here, perhaps, the Examiner may not be familiar with when you were talking about private placed bonds. And I believe I heard you make reference to SAMA bonds?

HRS

2062

A All right.

Q Could you define that term for us?

A Yes, sir. That's--I guess a colloquialism--
What we had there was a private placement bond.

Q Could you first define the term for us?

A Oh, SAMA, is the Saudi Arabian Monetary Agency, that was the purchaser.

Q And that was a private nonrated placement of how much?

A Total of 75 million dollars.

Q All right, sir.

A I might say that that whole transaction was discussed both with the PUC Staff and the Dallas Staff.

Q Just really wanted to know what the abbreviation meant, Mr. Nye.

A Yes, sir.

MR. SPARKS: We pass the witness.

MS. SHELLMAN: Thank you. Now are you ready?

MS. O'CONNOR: Yes.

CROSS EXAMINATION

BY MS. O'CONNOR

Q Mr. Nye.

A Yes, ma'am.

Q Is the Company's primary need for capital now

Q Mr. Saathoff. I wasn't sure how to pronounce it.

A Saathoff. Yes.

Q Now, he appears to state at one point in his testimony that Comanche Peak will not be less expensive to run than oil and gas plants for at least the first two years that they would be in service.

You also stated earlier this morning that you anticipate Comanche Peak would run at 70 percent capacity after the first three years.

A In the third year.

Q Or in the third year. Do you have an analysis of what capacity that Comanche Peak will be operating in the first two years?

A We are planning for fuel purposes 35 percent the first year, 50 percent the second year, and 70 percent the third year and thereafter. We hope that we can improve on that and all our objections would be to do so. But you plan on that and you might not have enough fuel sources to back it up.

Q Okay. So if I understand you correctly, you will not have enough fuel to fully utilize Comanche Peak during the first two years. Is that what you're saying?

A To replace Comanche Peak?

Q No. To utilize it.

A Oh, yes. We do have fuel, but just examining what has occurred on nuclear units as coal units, you have a period where they develop and are improved after they go in service. You have a maturity period. So, to figure it in a conservative mode, we've calculated on 35 percent the first year, 50, and then 70

Now, we would hope to do better than 35, and we have fuel to do better.

Q So you're just anticipati.g that the initial problems you might face with bringing it on line would cause you not to be able to utilize it at full capacity?

A That's correct.

Q Okay. With regard to the studies that the Company has done on cost amounts, the benefits of different programs, what studies have been done to cost out the relative benefits of a delay of bringing on Comanche Peak on line in 1981 and '83?

A Well, we had not made any details on that since around the '75-'76 period becaus: basically we're beyond the point and had so much commitments that it was obviously not something that was economically beneficial. I did, following review of testimony, review the delays that were suggested by Mr. Nichols, and if you delay Comanche Peak-1 for two years, and if you look at the first four-year operation and then present-worth it to

1981, it costs the customer $25 million to delay it for two years. That's assuming we can get gas to burn and projected gas cost.

Q Okay. Now, do you have that analyses--have you detailed that out, or is that just something out of your head?

A I've scribbled it down on a piece of paper. Yes.

Q Do you have that available for us?

A I've got it here on some notes. I could show it to you at the break or something.

Q Okay. So the last detailed analysis or alternative study by the Company was in '75-'76?

A I believe that was the last time. It was one of the options that we looked at seriously when we made a detailed analysis of our expansion plan.

Q What was the projected growth for the Company at that time?

A We were down around four percent, but at that time we were still having a very uncertain gas situation; Docket 600 had just come in, and we had had to anticipate if Comanche Peak wasn't there it was on oil, and oil was at around twelve or fourteen at that time. I forget just exactly when all the changes from OPEC occurred. But you were looking at some very high alternatives to replace

18b1

Q In regard to another question asked by Ms. O'Connor, you stated, I believe, that there h d been no studies made since the '75, '76 period to cost out the delay of Commanche Peak plant. Is that correct?

A It was not considered in detail. Now, we looked each year--as we are reviewing our system expansion plans we look at the various alternatives we could consider. It was obviously one that was considered, but it was not one that we elected to do a detailed analysis on.

Q All right. I believe you also stated that at that time you had costed out 25 million dollar costs for delaying Unit 1 for two years?

A I just did that here this week, or last week.

Q All right. You said, I believe, also that you were assuming gas and projected gas cost there. If you delayed the Commanche Peak plant it would be because you did not have as much load growth as had been anticipated. Is that correct? Was this why you made the analysis, was--

A I just assumed a two year delay on Unit 1 and the three year delay on Unit 2 because it was suggested by some other testimony, I just looked to see what that cost would be and I assumed that gas would be available. I considered the carrying cost, the O&M cost, and came up with an annual cost under those two scenarios, I present worthed it and the difference between those two on a

18b2

present worth basis is 25 million dollars for a four year period.

Q All right. Are you saying that--you are assuming that gas would be used to replace that--

A Generation.

Q All right. If the reason for delaying the Commanche Peak plant was that you did not need that generating capacity, why would you need to use the--assume that there would be a replacement cost using gas?

A Well, I'm not ready to conceive that we won't grow at the rates that we're projecting. That is our best estimates and we're planning on that basis and I don't think any analysis of considering two alternatives you're considering how you would supply certain amount of load and if you eliminate the load, well neither consideration is valid, I assume.

Q I'm sorry some of these are a little disjointed. My notes didn't tally a little bit here.

A I've got all afternoon.

Q Regarding another question by Ms. O'Connor, you were discussing the Department of Energy figures and mentioned that this was a fairly recent report, approximately last fall and that these figures were for '81, '82, and '83, were these for the same size units as the Commanche Peak?

question that you did not have a study showing, like, what kind of a rate increase you would need if you were going to be a Double A rated company and you needed 3.5 percent times interest coverage?

A John, I haven't made a study that if I fall out of that chair I'm going to hit the floor, I'm not going to hit the ceiling, and I don't think you need to study things that are apparent from examination. I'll go through it one more time. It's apparent to me that the bills are lower

Q Are you telling me that you just don't have a study of the nature that I've inquired about?

A I will describe my mental processes which allow me to conclude -- and I think most would agree -- that it is not more expensive to maintain a Triple A. And let me say it one more time. The factors that control in this case, it seems to me, would control anyway, independent of whether you maintain the financial indicators that I think are necessary for a Triple A, as they were in the last case.

It's important, it is vitally important, and I don't mean to diminish it. I think it's probably the most critical factor in this rate case. You made the point that we haven't lost our Triple A. We've asked for it three times. We haven't sold any bonds during that period of time. Now, we're going to sell bonds. We have put it off as long as we can. We sold SAMA bonds, we sold equity, we've sold plant, but we're going to sell bonds. There is no way to get around it.

Q But during this time, DP&L has raised the capital it needed to meet its needs and to meet its construction program?

A I believe I described that we sold BAMA bonds which do not require a rating. We sold equity which was from the holding company that thus far has been patient and provided us the capital. We've sold plant which I don't think is the best way to raise capital in a general sense. I don't believe most people would suggest, most experts would suggest, that's appropriate. Otherwise, I presume that you're suggesting that I go out and sell some more plant.

Q I'm not presuming anything. I'm asking questions.

A Mr. Fairchild has suggested that my equity ratio is too high. I don't believe that it is, but it clearly was an effort to avoid going to the bond market. Now, everybody ought to understand we have not had a public rating since financials for '74.

Q And you have not been hamstrung in your financing since '74, have you?

A I'd say we certainly have been hamstrung. I

99 percent certain of that.

A Is it your testimony that your Triple-A bond rating is less difficult to maintain today than it may have been last year in Docket 1526?

A I would say that if we had filed -- if we had sold bonds since 1526, we would have been derated. In that respect, the results that we got were simply not adequate. It's difficult for me to go back to relate to that case. I don't think that case provided sufficient coverage to take care of the bond rating and accordingly, I did not finance.

Q W , I'm not sure that answered the question.

A I'm sorry.

Q Let's go back to the case before that.

A Yes, sir.

Q You will recall in the previous case -- in other words just the third successive case in which the Company has come to the regulatory authority with testimony to the effect that the bond rating was in jeopardy.

A Yes, sir.

Q Is it your testimony today that your bond rating would be easier to maintain today than it would have been in either 1526 or the case before that?

A Mr. Sparks, I really can't relate that. I would

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Q If you were a bond rating analyst--this may be an unfair question--if you were a bond rating analyst, would you perhaps be more concerned with HL&P's eight or nine hundred million dollar construction budget in trying to raise funds and issue bonds for their construction budget and the lesser extent the smaller companies, GSU and El Paso Electric Company? Would you be more concerned about what's happening with those companies and more apt to be taking a harder look at their bond ratings than with DP&L?

A Frankly, Mr. Bell, Houston at this point, has substantially better financial indicators than Dallas Power, either on a current basis, on a five year average, almost any way you want to look at it. I believe they do look at your financials. I believe they do judge your record, and while Houston is a AA, I think they're a strong AA. And while Dallas Power is a AAA presumably, I am confident that we are a weak AAA. You know, you don't press the issue. If we haven't asked for a rating, it seems to me it's sort of problematical. I'd have to say that with respect to their construction program that 648 million in '79 is not nearly as substantial to a company the size of Houston as 168 million was for our '78.

Q How about El Paso Electric Company that serves