BEFORE THE

PUBLIC UTILITIES COMMISSION OF OHIO

THE DAYTON POWER AND LIGHT COMPANY

CASE NO. 12-426-EL-SSO

CASE NO. 12-427-EL-ATA

CASE NO. 12-428-EL-AAM

CASE NO. 12-429-EL-WVR

CASE NO. 12-672-EL-RDR

CONFIDENTIAL

ELECTRIC SECURITY PLAN (ESP)
REBUTTAL TESTIMONY
OF CRAIG L. JACKSON

REDACTED VERSION

- □ MANAGEMENT POLICIES, PRACTICES, AND ORGANIZATION
- ■ OPERATING INCOME
- □ RATE BASE
- □ ALLOCATIONS
- ■ RATE OF RETURN
- □ RATES AND TARIFFS
- ■ OTHER

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ON BEHALF OF
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I. INTRODUCTION

Q. Please state your name and business address.

A. My name is Craig Jackson and my business address is 1065 Woodman Drive, Dayton, Ohio, 45432.

Q. Are you the same Craig Jackson who previously filed testimony in this proceeding?

A. Yes, I am.

II. PURPOSE OF YOUR REBUTTAL TESTIMONY

Q. Have you read the testimonies of witnesses Kevin Murray, Edward Hess, Joseph Bowser, Michael Gorman, Jonathan Lesser, Roger Ruch, Sharon Noewer, Scott Rubin, Kenneth Rose, Lane Kollen, and Daniel Duann in this proceeding?

A. Yes, I have.

Q Have you read the testimonies of PUCO Staff witnesses Hisham Choueiki, Shahid Mahmud, and Timothy Benedict in this proceeding?

A. Yes, I have.

Q. What is the purpose of your rebuttal testimony?

A. The purpose of my rebuttal testimony is to discuss: (1) several witnesses' concerns about the early separation of the generation assets from DP&L; (2) witness Hisham Choueiki's recommendation for a 3 year ESP term; (3) several witnesses' testimony concerning financial integrity; (4) possible Operations and Maintenance (O&M) reductions in the future discussed by several witnesses; and (5) other points of clarification.

Q. Several parties have suggested through their testimony, that DP&L could separate its generation assets sooner than the Company's proposed date of December 31, 2017. Do you agree?

A. No. The Company is limited in how quickly it can legally separate its generation assets by two separate and distinct factors:

- First, the Company maintains a First and Refunding Mortgage, which creates a lien on all of the assets (transmission, distribution and generation) of DP&L for the purposes of securing approximately $884M of current indebtedness ("Secured Bonds"). So long as this First and Refunding Mortgage remains in existence in its current form, the Company is unable to effectuate a legal separation of the generation assets from the regulated assets. In fact, legal separation cannot occur until this First and Refunding Mortgage is either: a) defeased or; b) amended to permit the release of the generation assets from the First and Refunding Mortgage.

    a) Defeasement of First and Refunding Mortgage: defeasement cannot occur until all of the Secured Bonds are called (i.e. redeemed prior to maturity) by the Company and either refinanced or re-paid in cash. At that point in time, the First and Refunding Mortgage would be extinguished. Any debt being refinanced, would be refinanced separately by the regulated entity with the benefit of the regulated assets, or the generation entity with the benefit of the generation assets. Given certain "no-call" provisions on certain outstanding bonds, the earliest possible date that all the Secured Bonds could be called is September 1, 2016. Although one avenue to accomplish an earlier call would be to amend the bonds containing this "no-call" provision, this amendment would require consent of bondholders and would entail significant execution and financial risk.

b) Release of the generation assets from the First and Refunding Mortgage: if the First and Refunding Mortgage is not defeased, the only other way to enable a legal separation of the regulated and generation businesses is to amend the existing First and Refunding Mortgage such that the generation assets are released from the mortgage. In order to release the generation assets, the Company will require that existing bondholders - who currently have the benefit of this security – to willingly 'consent' to the release of the generation assets from the mortgage. The only certain way to obtain this consent is through calling and refinancing new bonds under an 'amended' DP&L First and Refunding Mortgage that has the benefit of only the regulated transmission and distribution assets. At that point in time, new bond-holders would be lending monies to the Company only in so much as they are comfortable with a lesser amount of security. Given the ability to obtain the required consent to amend the First and Refunding Mortgage is linked to the refinancing of all outstanding bonds, the earliest possible date this could occur is September 1, 2016 (the earliest date all outstanding bonds could be called and refinanced).

- Second, notwithstanding the restrictions above, the Company has material financing market limitations. If DP&L could defease or amend its First and Refunding Mortgage such that the lien on the generation assets was released, the Company would then have to: a) maintain or refinance all $884M of indebtedness at the regulated business; b) call a portion of this indebtedness and repay it with cash; or c) call a portion of this indebtedness and refinance it with proceeds raised by the new non-regulated business. Option a) is problematic, since leaving the entire debt within the regulated business would result in a capital structure with excessive debt under current PUCO guidelines would increase business and financial risks and would increase financing costs attendant with excessive debt levels. Options b) is not practical given the Company would not have sufficient time to accumulate the necessary cash in order to pay down a material amount of this debt Options c) is not practical given the new non-regulated generation business could not raise debt in the capital markets to refinance currently outstanding indebtedness (primarily due to today's generally weak power markets).

Q. On Page 15 of his testimony, Witness Choueiki indicates "To the extent the Commission grants an SSR charge to DP&L, Staff recommends that the revenues collected stay with DP&L and not be transferred to any of DP&L's current, or future-formed, affiliates or subsidiaries." Is this reasonable?

A. I disagree with this proposal. DP&L has no intention of transferring cash received from its proposed ESP, including the Service Stability Rider (SSR), to fund the current or future operations of DPLER, DPLE or any other subsidiaries of DPL Inc. The revenues from the ESP, including the SSR revenues, are needed to ensure the financial integrity of DP&L, and are required to meet DP&L's own obligations and enable the Company to legally separate at December 31, 2017. Since cash is fungible, it is not necessary to isolate the SSR revenues. I therefore, disagree with this proposal and believe that it would add an unnecessary restriction to the Company or DPL Inc.'s ability to pay down its debts and restructure its balance sheet.

Q. Witness Hisham Choueiki stated on Page 5 of his testimony that a five-year period is not acceptable to staff. What effect would Staff's proposed 3-year term have on the financial integrity of the Company?

A. Staff's position on the term would significantly weaken the Company's financial integrity and restrict the certainty of future cash flows that are needed to separate its generation assets by December 31, 2017. As shown on Second Revised Exhibit CLJ-2, removing the [redacted] million Service Stability Rider in the fourth and fifth years substantially degrades the Company's financial outlook. Specifically, carving out the last two years of the SSR, the Company expects its net income to be [redacted] million and [redacted] million (line 41) and its annual ROEs to be [redacted] and [redacted] (line 45), respectively. From a cash perspective, the shorter term would reduce after-tax cash flow, on a cumulative basis, by approximately [redacted] million ([redacted] million x 2 years x [redacted] after tax rate). This negative impact focuses only on the effect of the reduced term of the SSR and does not take into account the exclusion of the switching tracker which would further reduce after tax earnings and cash flow by an additional [redacted] million ([redacted] million switching tracker impact x after tax rate of [redacted]) over the term of the ESP.

Q. Have you modeled the financial effect of the Staff's testimony?

A. Although the Company is not conceding to the terms proposed by Staff, we have modeled the financial effect of proposals set forth in Staff's testimony (from various witnesses), and this too, would have a significant negative impact on the overall financial integrity of the Company if adopted. Specifically, the key assumptions from Staff's proposal I have analyzed are as follows:

- Three-year term beginning June 1, 2013 and ending May 31, 2016;
- Market blending of 40% beginning June 1, 2013; 60% beginning June 1, 2014; and 100% beginning June 1, 2015;
- No switching tracker;
- Customer switch rates ranging from [redacted] to [redacted] over the 2013, 2014 and 2015 period. For purposes of our analysis, we assumed [redacted] in 2013, [redacted] in 2014, and [redacted] in 2015;
- Adjusted generation operating margin in 2013, 2014 and 2015 respectively; and
- Target three-year average ROE of [redacted].

As shown on Exhibit CLJ-6, Line 33, in order to allow the Company the opportunity to realize a three year average ROE of [redacted] if the Staff proposals above are implemented, we have estimated the service stability rider would have to be at a level of approximately [redacted] million per year compared to the [redacted] million per year noted in Witness Choueiki's testimony.

Q. Is a five year ESP term critical to the Company?

A. Yes. As noted earlier, the five-year term is critical for the Company to have the necessary cash flows needed to separate its generation assets by December 31, 2017. Included in DP&L's ESP filing were average ROE's as follows:

- Five-year average ROE: [redacted] (See Second Revised Exhibit CLJ-2, Line 36)
- Three-year average ROE of [redacted] (average of 2013, 2014 and 2015 ROE as shown on Second Revised Exhibit CLJ-2, Line 35)

Although the Company's proposed filing resulted in a five-year average ROE of [redacted] which is [redacted] the 7% to 11% range recently approved by the PUCO in the AEP Ohio ESP proceeding, the Company proposed a lower average ROE in exchange for more certainty of future cash flows over a 5-year ESP period. As the [redacted] ROE was predicated on a 5-year term, it should not be considered relevant or adequate to a 3-year ESP.

Q. On Pages 10 and following in Witness Jonathan Lessers' Direct Testimony, he discusses the Company's proposed SSR and on Page 11 indicates that "If a company is told its financial integrity is guaranteed, then the economic incentive to improve its operations and reduce costs is reduced." Please comment on his assertion and the SSR.

A. DP&L has not and is not requesting that its financial integrity be guaranteed. DP&L is only requesting the opportunity, not the guarantee, to earn a reasonable rate of return on its operations. DP&L does not have the opportunity to earn a reasonable rate of return on operations if it does not recover revenues from the SSR proposed in this proceeding.

Even with the SSR requested, the Company's projected average return on equity will be [redacted] of what the Commission has deemed to be reasonable in the AEP case. The SSR is vital to the continued financial health of DP&L.

If DP&L collects the full amount of the SSR requested, other events, such as changed economic conditions within the service territory, increased costs of materials and supplies, changes in financial markets, unexpected operational challenges and other factors, can still reduce the Company's earnings materially. I strongly disagree that the SSR requested in this proceeding will "guarantee" the financial integrity of the Company. Instead, it is the minimum that DP&L needs to allow it to satisfy its obligations, operate efficiently so as to provide adequate and reliable service and otherwise continue operating as an ongoing entity.

Q. Witness Kevin Murray, throughout his testimony, states that the SSR and ST ("Switching Tracker") would provide an anticompetitive subsidy to DP&L's generation business. Do you agree?

A. I disagree. The SSR and ST are not subsidies and Mr. Murray has not provided any basis for this claim. The SSR and ST are critical components of DP&L's ESP filing that allow the enterprise, which consists of its transmission, distribution and generation businesses, to maintain its financial integrity.

Q. Witness Kevin Murray stated throughout his testimony that DP&L's financial integrity claims are the result of a self inflicted condition and its improper business relationship with DPL Energy Resources (DPLER). Do you agree?

A. No. There is nothing improper about DP&L's business relationship with DPL Energy Resources ("DPLER") and Mr. Murray has not demonstrated any factual basis for this claim. DP&L sells power to DPLER at arm's length and at market costs. This is consistent with how DP&L would sell power to any affiliated or unaffiliated CRES provider. Additionally, although administrative and other overhead costs are not included in the transfer price between DP&L and DPLER, such costs are fully allocated to DPLER through DP&L's Cost Allocation Manual ("CAM") process.

Q. **In an environment where market prices are higher than DP&L's fully loaded embedded costs, would it be appropriate for the transfer price from DP&L to DPLER to be based on fully loaded embedded costs?**

A. No. If DP&L's transfer price to DPLER was set at fully loaded embedded costs at a time of high market prices, DPLER would have an advantage over competitors buying at market prices. Therefore, the only transfer price that makes sense under the ORC 4928.17 (A)(3) is the market price, which is the basis of the current transfer pricing.

Q. **Several witnesses have stated, through testimony, that the O&M cost reductions identified offset the need for the SSR. Do you agree?**

A. I do not agree for multiple reasons:

First, the potential costs savings for the years [redacted] are still under review and have not been approved by DP&L.

Second, the potential cost savings identified have not been risk adjusted, have not been demonstrated, and are inconsistent with the historic operating experience of the Company. In short, these potential savings represent a best case scenario, with significant risk that they will not be realized.

Third, approximately [redacted] of the potential savings measures identified are generation related. If all of the savings measures were implemented, the operational performance of the Company's generation fleet would deteriorate, resulting in: (a) lower wholesale revenue and gross margin attributable to those plants; (b) potential PJM RPM capacity penalties; and (c) higher future operational and maintenance costs due to unforeseen and unplanned outages.

Fourth, the Company's filed ESP proposal, as shown on Second Revised Exhibit CLJ-2, results in a five-year weighted average ROE of [redacted] which is [redacted] the 7% - 11% range approved by the PUCO in AEP Ohio's recent ESP order. That said, assuming all other factors were equal and the Company were able to achieve all of the potential savings that have been identified, the Company would save on average approximately [redacted] per year over the term of the ESP. This level of savings would increase DP&L's 5 year weighted average ROE to approximately [redacted] as shown on Exhibit CLJ-7, which is still [redacted] of the 7% - 11% range approved by the PUCO in AEP Ohio's recent ESP order.

Last, I believe the Company's O&M projections, as shown on Second Revised Exhibit CLJ-2 are reasonable especially considering the actual O&M costs incurred in 2011 and 2012. Exhibit CLJ-8 provides a bridge from DP&L's actual 2011 O&M costs of $364.8 million to its projected 2013 O&M costs of [redacted] million. The increases are largely driven by energy efficiency programs and the low income (or Universal Service Fund) program, both of which are offset by increased revenues which compensate DP&L for the cost of these programs. The Company has included both the expense and offsetting revenues in its financial projections.

Q. Witness Michael Gorman stated, on page 5 (Lines 17-20), in his direct testimony that DP&L's financial projections included DP&L as well as the non-regulated subsidiaries, including DPL Energy Resources (DPLER) and DPL Energy, LLC (DPLE). Do you agree?

A. No. The financial projections provided in Second Revised Exhibits CLJ-2, CLJ-3 and CLJ-4 reflect DP&L results only. DPLER and DPL Energy, LLC are subsidiaries of DPL Inc. and therefore the financial projections of those entities are not included anywhere in this case.

III. CONCLUSION

Q. Does this conclude your rebuttal testimony?

A. Yes, it does.

The Dayton Power and Light Company
Case No. 12-426-EL-SSO
Projected Statements of Income (unaudited) ($ in millions)
2013 - 2017

Data: Forecasted
Type of Filing: Second Revised
Work Paper Reference No(s).: None

Exhibit CLJ-2
Page 1 of 1
Witness Responsible: Craig Jackson

Line No.	Description	2013	2014	2015	2016	2017	Source
(A)	(B)	(C)	(D)	(E)	(F)	(G)	(H)
1	Operating Revenues						
2	Retail	[redacted]					Internal Documents
3	Service Stability rider*						Internal Documents
4	Wholesale						Internal Documents
5	RTO Capacity and Other RTO Revenues						Internal Documents
6	Other Revenues						Internal Documents
7	Total Revenues						Sum Lines 2 thru 6
8							
9	Fuel and Purchased Power						
10	Fuel Costs	[redacted]					Internal Documents
11	Purchased Power						Internal Documents
12	Total Fuel and Purchased Power						Line 10 + Line 11
13							
14	Gross Margin	[redacted]					Line 7 - Line 12
15							
16	Operating Expenses						
17	Operation and Maintenance	[redacted]					Internal Documents
18	Depreciation and Amortization						Internal Documents
19	General Taxes						Internal Documents
20	Total Operating Expenses						Sum Lines 17 thru 19
21							
22	Operating Income	[redacted]					Line 14 - Line 20
23							
24	Interest Expense	[redacted]					Internal Documents
25	Other Income (Deductions)						Internal Documents
26							
27	Earnings Before Income Tax	[redacted]					Line 22 + Line 24 + Line 25
28							
29	Income Tax	[redacted]					Internal Documents
30							
31	Net Income	[redacted]					Line 27 - Line 29
32							
33	Common Shareholder's Equity	[redacted]					Second Revised Exhibit CLJ-3, Line 1
34							
35	Average Annual Return on Equity (ROE)	[redacted]					Line 31 / Line 33**
36	5-Year Weighted Average Return on Equity						Sum of Line 31 / Sum of Line 33
37							
38	***Service Stability Rider Sensitivity***						
39	Earnings Before Income Tax, excluding Service Stability Rider	[redacted]					Line 27 - Line 3
40							
41	Net Income, excluding Service Stability Rider	[redacted]					Line 39 x (1 - 35.8%)
42							
43	Common Shareholder's Equity, excluding Service Stability Rider	[redacted]					Line 33 - (Line 31 - Line 41)
44							
45	Average Annual Return on Equity (ROE), excluding Service Stability Rider	[redacted]					Line 41 / Line 43***
46	5-Year Weighted Average Return on Equity, excluding Service Stability Rider						Sum of Line 41 / Sum of Line 43
47							

48 *The Service Stability Rider has been rounded from $137.5 million to $138 million in this schedule.
49 **For purposes of this calculation, the average of the current year and prior year common shareholder's equity value (Line 33) is used.
50 ***For purposes of this calculation, the average of the current year and prior year common shareholder's equity value (Line 43) is used.

Analysis of Staff's Proposed Modifications and Changed Assumptions in DP&L's ESP

Exhibit CLJ-6
Page 1 of 1
Witness Responsible: Craig Jackson

Line		PY 13/14	PY 14/15	PY 15/16	Total or Average	Source / Calculation
1	**DP&L Filed ESP & Assumptions**					
2	Service Stability Rider ("SSR") ($MM/yr)	[redacted]				*DP&L Revised ESP Application at 8*
3	Net Income ($MM)					*Estimate for Planning Year based on Ex. CLJ-2*
4	Common Shareholder's Equity ($MM)					*Estimate for Planning Year based on Ex. CLJ-2*
5	Return on Equity (%)					*Line (3) / Average Equity*
6						
7						
8	**Modifications and Assumptions Proposed by Staff**					
9	**Remove Switching Tracker**					
10	Lost Revenue Opportunity w/Company Blending ($/MWh)	[redacted]				*Line (45) - Line (40)*
11	Company Forecast of Incremental Switching (GWh)					*Line (55) - Line (50)*
12	Change in Pre-Tax Margin ($MM)					*-Line (10) * Line (11) / 10^3*
13						
14	**Accelerate Market Blending**					
15	Decrease in ESP Rate due to Accelerated Blending ($/MWh)	[redacted]				*Line (45) - Line (46)*
16	Company Forecast of Retained Load (GWh)					*Line (50)*
17	Change in Pre-Tax Margin ($MM)					*-Line (15) * Line (16) / 10^3*
18						
19	**Assume Lower Switching**					
20	Lost Revenue Opportunity w/Staff Blending ($/MWh)	[redacted]				*Line (46) - Line (40)*
21	Increase in Retained Load Forecast					*Line (53) - Line (50)*
22	Change in Pre-Tax Margin ($MM)					*Line (20) * Line (21) / 10^3*
23						
24	**Assume Additional Generation Margin ($MM)**					
25	Change in Pre-Tax Margin ($MM)	[redacted]			[redacted]	*Benedict Testimony at 10, by Planning Year*
26						
27	**Cumulative Effect of Staff Adjustments**					
28	Total Change in Margin ($MM)	[redacted]				*Lines (12) + Line (17) + Line (22) + Line (25)*
29	Decrease in Net Income due to Adjustments ($MM)					*Line (28) * (1 - 35.8%)*
30	Return on Equity after Staff Adjustments (%)					*(Line (3) + Line (29)) / Average Equity*
31						
32	Increase in SSR Needed to Target 7.0% Average ROE ($MM)	[redacted]				*(7% - Line (30)) * Line (4) / (1 - 35.8%)*
33	SSR Needed to Target 7.0% ROE ($MM/yr)					*Line (2) + Line (32)/3*
34	ROE w/SSR of $163.3MM/yr (%)					*[L(3) + L(29) + (L(33)-L(2)) * 64.2%] / Avg Equity*
35						
36						
37	**Load and Rate Assumptions**					
38	**Forecasted Auction Prices and SSO Rates**					
39	Current Generation Rate	[redacted]				*Malinak Testimony, Exhibit RJM-2, Line 52*
40	Forecasted CB Auction Rates					*Robb Testimony, Schedule 5B, Line 4*
41						
42	Company Proposed Auction Blending	[redacted]				*DP&L Revised ESP Application at 7*
43	Staff Proposed Auction Blending					*Strom Testimony, Exhibit RWS-1*
44						
45	Forecasted ESP Rate with Company Blending ($/MWh)	[redacted]				*Line (42)*Line (40) + (1 - Line (42))*Line (39)*
46	Forecasted ESP Rate with Staff Blending ($/MWh)					*Line (43)*Line (40) + (1 - Line (43))*Line (39)*
47						
48	**Load and Switching Assumptions**					
49	Company Forecast of Switching (%)	[redacted]				*Hoekstra Testimony at 8*
50	Company Forecast of Retained Load (GWh)					*(1 - Line (49)) * Line (57)*
51						
52	Staff Forecast of Switching (%)	[redacted]				*Exhibit HMC-1, Converted to Planning Year*
53	Staff Forecast of Retained Load (GWh)					*(1 - Line (52)) * Line (57)*
54						
55	Frozen Retained Load Forecast at Time of Filing (GWh)	[redacted]				*Workpaper 8B, p 1, Col (O), Line 8*
56						
57	Distribution Load (GWh)	[redacted]				*Workpaper 8A, p 1, Col (O), Line 8*

The Dayton Power and Light Company
Case No. 12-426-EL-SSO
Projected Return on Equity with O&M Cost Savings (unaudited) ($ in millions)
2013 - 2017

Data: Forecasted
Type of Filing: Rebuttal
Work Paper Reference No(s).: None

Exhibit CLJ-7
Page 1 of 1
Witness Responsible: Craig Jackson

Line No. (A)	Description (B)	2013 (C)	2014 (D)	2015 (E)	2016 (F)	2017 (G)	Source (H)
1	Net Income from ESP filing	[redacted]					Second Revised Exhibit CLJ-2, Line 31
2	Potential O&M Savings (After-tax)*						$30M X (1-.358)
3	Adjusted Net Income						Line 1 + Line 2
4							
5	Common Shareholder's Equity from ESP filing	[redacted]					Second Revised Exhibit CLJ-3, Line 18
6							
7	5-Year Weighted Average Return on Equity	[redacted]					Sum of Line 3 / Sum of Line 5

The Dayton Power and Light Company
Case No. 12-426-EL-SSO
DP&L O&M Bridge (unaudited) ($ in millions)
O&M Bridge - Historicals to Filing

Data: Forecasted
Type of Filing: Rebuttal
Work Paper Reference No(s).: None

Exhibit CLJ-8
Page 1 of 1
Witness Responsible: Craig Jackson

Line No.	Description	2011A to 2012A*	2012A to 2013E	2011A to 2013E
1	Prior Year O&M	$ 364.8	$ 385.9	$ 364.8
2				
3	Merger Related costs	(19.4)	[redacted]	[redacted]
4	Low Income payment program	21.3	[redacted]	[redacted]
5	Energy efficiency programs	9.2	[redacted]	[redacted]
6	Generating facilities operating and maintenance expense	6.0	[redacted]	[redacted]
7	Maintenance of overhead transmission and distribution lines	(10.2)	[redacted]	[redacted]
8	Health insurance/ long-term disability	-	[redacted]	[redacted]
9	Pension	5.7	[redacted]	[redacted]
10	Legal and other consulting costs	3.1	[redacted]	[redacted]
11	Other	5.4	[redacted]	[redacted]
12				
13	Current Year O&M	$ 385.9	[redacted]	[redacted]
14				
15	*2011 and 2012 O&M expense as reported on DP&L's 2012 SEC Form 10k			