BEFORE THE

PUBLIC UTILITIES COMMISSION OF OHIO

THE DAYTON POWER AND LIGHT COMPANY

CASE NO. 19-0162-EL-RDR

EXTENSION OF DISTRIBUTION MODERNIZATION RIDER

DIRECT TESTIMONY
OF GUSTAVO GARAVAGLIA M.

PUBLIC VERSION

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

BEFORE THE

PUBLIC UTILITIES COMMISSION OF OHIO

DIRECT TESTIMONY OF

GUSTAVO GARAVAGLIA M.

ON BEHALF OF
THE DAYTON POWER AND LIGHT COMPANY

TABLE OF CONTENTS

I. INTRODUCTION 1

II. BACKGROUND OF ESP AND THE IMPORTANT LINK TO DP&L'S APPLICATION TO MODERNIZE ITS GRID 3

III. DP&L HAS COMPLIED WITH THE TERMS OF THE ESP III STIPULATION 4

IV. ADDITIONAL STEPS DP&L HAS TAKEN TO IMPROVE ITS FINANCIAL CONDITION 7

V. CHANGES IN DP&L'S FINANCIAL CONDITION SINCE THE ESP III STIPULATION 10

VI. DP&L'S FINANCIAL CONDITION THROUGH 2028 21

VII. CONCLUSION 25

I. INTRODUCTION

Q. Please state your name, employer and business address.

A. My name is Gustavo Garavaglia M. I am employed by AES US Services, LLC, which provides services to The Dayton Power and Light Company ("DP&L" or the "Company"). My business address is One Monument Circle, Indianapolis, IN 46204.

Q. What is your position and professional relationship with DP&L?

A. I am DP&L's Chief Financial Officer and Chief Financial Officer of AES US Services, LLC.

Q. How long have you been in your present position?

A. I have been CFO of DP&L since January 2019.

Q. What are your responsibilities in your current position?

A. In my current position, I report to the President of AES US Services. I have direct responsibility and oversight for accounting, tax, financial planning & analysis, treasury, and risk management functions of DPL and DP&L and other AES affiliates.

Q. Will you describe briefly your educational and business background?

A. I received a Bachelor's degree in Electrical Engineering from University of Campinas ("Unicamp") in Brazil in 2009 and a Master's degree in Business Administration from FGV Brazil in 2012 and I am a CFA Charterholder.

I joined AES in Brazil in January 2010 as a finance trainee. In November 2011, I moved to Business Development as a Senior Analyst. In June 2012, I took a new role as Strategic Planning Specialist. Starting in May 2013, I did a 6-month assignment with the Mergers and Acquisitions team at the AES Global Headquarters in Arlington, Virginia and at the end of 2013, I returned to Brazil as Manager for Investment Analysis and Risk Management. In March 2015, I moved to Panama to be the Head of Transactions and Developments for AES in Mexico, Central America and Caribbean and while still in Panama, I expanded my role, and became the Director for Financial Planning & Analysis and Development & Transactions for AES in Mexico, Central America and the Caribbean. In January 2019, I accepted my current position.

Q. What are the purposes of this testimony?

A. The purposes of this testimony are to:

a. Explain the background facts that support DP&L's application to extend its Distribution Modernization Rider ("DMR-E") and the important relationship to the Company's grid modernization application.

b. Demonstrate that DP&L has complied with the terms of the Amended Stipulation and Recommendation from DP&L's third Electric Security Plan ("ESP III Stipulation") in Case No. 16-395-EL-SSO ("ESP").

c. Provide an overview of the additional steps that DP&L has taken to improve its financial condition;

d. Summarize the changes in DP&L's financial condition since the ESP III Stipulation was signed, including new challenges that DP&L faces; and

e. Support exhibits that forecast DP&L's financial condition through 2028, and describe the process the Company undertook to develop this projection.

II. BACKGROUND OF ESP AND THE IMPORTANT LINK TO DP&L'S APPLICATION TO MODERNIZE ITS GRID

Q. Can you provide an overview of DP&L's ESP III proceeding?

A. Yes. DP&L filed its Application in that case on February 2, 2016, and filed an Amended Application on October 11, 2016. Among other things, DP&L's Amended Application sought a DMR of $145 million per year for seven years.

On March 14, 2017, DP&L, Staff and numerous intervenors signed the ESP III Stipulation. That Stipulation provided that DP&L could collect a DMR of $105 million per year for three years, and could apply for a two-year extension in an amount to be determined in a future case. ESP III Stipulation, § II.2.a. That Stipulation also provided that DP&L would file a comprehensive Distribution Infrastructure Modernization Plan to implement grid modernization. Id. § II.3.a.

The Commission approved the DMR, stating "testimony during the hearing shows that the Company cannot fund grid modernization investments without the DMR" and that the DMR "would provide an incentive to DP&L to focus its efforts on grid modernization." October 20, 2017 Opinion and Order, pp. 26-27.

Q. Has DP&L filed an application to implement grid modernization?

A. Yes, on December 21, 2018, DP&L filed an application to implement grid modernization in Case No. 18-1875 ("Distribution Modernization Plan" or "DMP").

Q. Is this case related to that case?

A. Yes. As demonstrated in DP&L's DMP application and the supporting testimony, modernization of DP&L's distribution grid will lead to significant benefits for DP&L's customers and society as a whole.

However, as demonstrated in the testimony of DP&L Witness Malinak in this case, DP&L's financial condition remains weak, and DP&L cannot afford to modernize its distribution grid unless the DMR-E is approved in this case. The DMR-E is a foundational component that will enable DP&L to implement its vision for grid modernization, which will provide meaningful customer benefits through a robust, modernized electric grid, with improved reliability. The DMP combined with the DMR-E represents a carefully crafted package that will allow DP&L to provide transformative technology and services to DP&L's customers, assist the Company in continuing to resolve its financial integrity issues, while creating a sustainable business model going forward. Absent approval of the DMR-E, and related grid modernization through the DMP, customers in DP&L's service territory will be left out of the vision set forth for Ohio through the Commission's PowerForward Roadmap. The two cases are thus linked, and DP&L reserves its right to withdraw its application to implement grid modernization if its application in this case is denied or modified substantially.

III. DP&L HAS COMPLIED WITH THE TERMS OF THE ESP III STIPULATION

Q. Have AES, DPL Inc. and DP&L complied with the DMR conditions in the ESP III Stipulation that were intended to improve DP&L's financial condition?

A. Yes. Among other things, since that ESP III Stipulation was signed:

a. DPL Inc. has made no dividend payments to AES (ESP III Stipulation, ¶ II.1.a);

b. DPL Inc. has made no contractually-required tax-sharing payments to AES and the tax-sharing liability has been converted into an equity investment in DPL Inc. (id. at ¶ II.1.b). Shortly after the ESP III Stipulation was approved, $107.5 million in tax sharing liabilities were converted into equity; since then, the amount of tax-sharing payments that have been foregone and converted to equity is [redacted]; based on this filing, [redacted] in tax sharing liabilities are projected to be converted into equity through the end of the DMR term (October 31, 2022). These amounts represent a significant equity investment in DPL Inc. by AES;

c. DP&L transferred its generation assets and non-debt liabilities to AES Ohio Generation (id. at ¶ II.1.c);

d. DPL Inc., through its subsidiary AES Ohio Generation, commenced a sales process for Conesville, Miami Fort and Zimmer Stations (id. at ¶ II.1.c). Miami Fort and Zimmer Stations were sold in December 2017 for approximately [redacted] in net proceeds and those proceeds were used to retire debt at DPL Inc.;

e. DP&L established a separate account to appropriately track the DMR and its uses, and has subsequently deposited cash from the DMR funds into that account to:

   i. Pay interest obligations on existing debt at DPL Inc. and DP&L;

   ii. Make discretionary debt prepayments at DPL Inc. and DP&L; and

   iii. Position DP&L to make capital expenditures to modernize and/or maintain transmission and distribution infrastructure (id. at ¶ II.1.e).

Q. In its Opinion and Order approving the ESP III Stipulation, did the Commission find that the provisions that you identify above would benefit customers?

A. Yes, the Commission found that those commitments would benefit customers and were "analogous or equivalent to AES infusing equity into DPL Inc." October 20, 2017 Opinion and Order, ¶¶ 48-51.

Q. Has DP&L complied with the other commitments in the ESP III Stipulation that benefited customers?

A. Yes. The ESP III Stipulation created significant customer benefits. Those benefits include:

a. Economic Development incentives (ESP III Stipulation, ¶ IV)
b. Economic Development Grant Fund - $1 million per year (id. ¶ V)
c. Commitments to the City of Dayton, including payments for residential energy education and reduction programs in the City; and payments to assist the City in providing economic development programs and essential city services to low-income residents - $400K per year (id. ¶¶ X.2.b,c & .i)
d. Payments to Edgemont/Ohio Partners for Affordable Energy to benefit consumers at or below 200% of the federal poverty line - $565K per year (id. ¶ X.3.)
e. Payments to Ohio Hospital Association to promote and obtain energy/demand savings among their members - $200K per year (id. ¶ 5.a.)
f. Payments to People Working Cooperatively to fund their programs to assist low-income, elderly and disabled customers - $200K per year (id. ¶ 6).

Q. Is the DMR-E necessary to allow DP&L to continue to provide those customer benefits?

A. Yes. The customer benefits that were established in the ESP III Stipulation are linked to the DMR and would cease without the DMR-E.

IV. ADDITIONAL STEPS DP&L HAS TAKEN TO IMPROVE ITS FINANCIAL CONDITION

Q. Since the ESP III Stipulation was signed, have AES, DPL Inc. and DP&L taken any additional steps beyond what was required by the ESP III Stipulation to improve DP&L's and DPL Inc.'s financial condition?

A. Yes. In addition to the items described above, since the ESP III Stipulation was signed, those entities have taken other significant steps to improve the financial condition of DP&L and DPL Inc., including:

a. DP&L settled its distribution rate case (Case No. 15-1830-EL-AIR), which has resulted in an increase in DP&L's base rates, the recovery of certain vegetation management costs, the implementation of a Distribution Investment Rider ("DIR"), a continuation of the decoupling rider, and the implementation of a storm rider. However, as discussed below, the increased revenue from the distribution case was significantly below what was projected when the company entered into the ESP III Stipulation and the rate increase came later than projected.

b. DP&L reduced O&M expenses through workforce reductions.

c. DPL Inc., through its subsidiary AES Ohio Generation, sold 100% of its interest in merchant peaking generation assets (Hutchings Unit 7, Tait, Montpelier, Sidney, Yankee, and Monument generating stations) for approximately [redacted] in net proceeds in March 2018. The net proceeds from the sale were kept within the DPL Inc. complex and were used to reduce outstanding debt, pay related accrued and unpaid interest, and early redemption premiums on the redeemed debt.

d. DPL Inc., through its subsidiary AES Ohio Generation, closed 2,936MW of generation assets, which would have required significant environmental capital investment if they continued to operate.

e. AEP, the operator of Conesville Unit #4, plans to close the unit. DPL Inc., through its subsidiary AES Ohio Generation, is a minority owner of the plant.

Q. Since the ESP III Stipulation was signed, has DP&L taken steps to improve its capital structure?

A. Yes. Among other things, DP&L has:

a. Continuously monitored its outstanding debt obligations to identify the appropriate time to pay those down;

b. Addressed near-term obligations and continued to amortize the DP&L Term Loan B. On December 4, 2018, DP&L filed an Application seeking approval to refinance the Term Loan B in PUCO Case No. 18-1795-EL-AIS;

c. Started infrastructure investment recovery via the approved DIR, to benefit customers through better reliability and improve DP&L's long-term financial stability;

d. Prepared a grid modernization strategy consistent with the Commission's PowerForward Roadmap, which will benefit customers through a robust, modernized electric grid, with improved reliability and result in a transformed and financially stable utility in the long-run; and

e. Begun investment in PJM Regional Transmission Expansion projects.

Q. Prior to the ESP III Stipulation, had DPL and DP&L made efforts to cut costs and to maintain DP&L's financial integrity?

A. Yes. Before the ESP III Stipulation, DPL and DP&L had taken strategic actions to improve DP&L's financial integrity, including:

(1) Asset Sales: In addition to the transactions discussed above, DP&L sold its ownership interests in East Bend generating station in December 2014 and sold its competitive retail businesses (MC Squared Energy Services, LLC in April 2015 and DPL Energy Resources, LLC in January 2016), which sale proceeds totaled [redacted]. The net proceeds were used to pay debt at DPL Inc. and DP&L;

(2) Operational Actions: DP&L implemented cost controls, travel restrictions and other measures to reduce its ongoing operating expenses;

(3) Financing Actions: DP&L lowered its consolidated interest expenses by selectively refinancing with short-term variable-rate instruments at relatively low cost; and

(4) Additional AES commitments: DPL has not paid any dividends or made tax sharing payments to AES since the end of 2012, allowing those funds instead to be used to service debt at DPL and DP&L.

Q. How much debt have DPL Inc. and DP&L paid down as a result of the actions that you describe?

A. The actions listed above, along with the use of existing operating cash flows, enabled DPL and DP&L to pay down approximately $1.1 billion in consolidated indebtedness between January 1, 2012 and December 31, 2018. Since the DMR was approved, DPL Inc. and DP&L have paid down approximately $338 million in consolidated debt.

V. CHANGES IN DP&L'S FINANCIAL CONDITION SINCE THE ESP III STIPULATION

Q. Since the ESP Stipulation was signed, have the financial prospects of DP&L changed in any way?

A. Yes. There have been changes in actual and projected cash flows since the ESP III stipulation was signed.

Q. **What were the changes in actual cash flows?**

A. During 2017 and 2018, DPL's net cash flows [redacted] due to:

1. The sale of Miami Fort, Zimmer, and the merchant peaking generation assets previously discussed that provided [redacted] in net proceeds, offset by:

2. A change in the timing and level of the DP&L distribution rate case outcome. The financial models prepared by Witness Malinak to support the ESP III Stipulation assumed that DP&L would receive a [redacted] However, the distribution rate case resulted in a rate increase of only $29.8 million, beginning November 2018. For 2017 and 2018 this resulted in [redacted]

Q. What are the changes in cash flows that are projected from 2019 through 2022?

A. In total, cash flows are now projected to be [redacted] compared with the projection made to support the ESP III Stipulation from 2019 to 2022. This is caused by:

[redacted]

---

[1] Revenue and expense figures provided above exclude the effect of [redacted] in matching revenues and expenses related to Universal Service Fund, Storm Rider, Energy Efficiency Rider, and Regulatory Compliance Rider, which are all pass-through items.

[redacted]

Q. What is the combined effect of the 2017 to 2018 actual changes and the 2019 to 2022 forecast changes?

A. [redacted]

Q. Is there any additional change in financial condition projected compared with the forecast made for the ESP III Stipulation?

A. Yes. As a result of the Tax Cuts and Jobs Act ("TCJA"), DP&L lowered its request in the distribution rate case (mentioned above) and committed to file an application no later than March 1, 2019 regarding the TCJA refund. DP&L has already agreed to refund to customers no less than $4.0 million per year for five years certain amounts associated with excess accumulated deferred income taxes as a result of that Act. In addition, DP&L transmission rates were adjusted for the TCJA effective March 21, 2018, lowering DP&L's rate by approximately $2 million annually. Each of these TCJA impacts result directly to lower available funds to be used to service DPL Inc. and DP&L's remaining debt, since AES has waived DPL Inc.'s contractually-required tax-sharing payments and those amounts would otherwise have been converted into an equity investment in DPL Inc.

Q. If the Commission does not approve the Company's recommended DMR-E, what impacts will such a ruling have on DPL and DP&L's financial integrity?

A. Without the proposed DMR-E, DP&L's investment grade credit rating would be threatened throughout the forecast period, as shown by Witness Malinak. In addition, [redacted], rendering the ability of the Company to make needed investments to maintain and improve reliability difficult, if not impossible.

Without approval of the Company's proposed DMR-E, both DPL and DP&L would: (a) [redacted]; (b) have insufficient cash flow to implement grid modernization; (c) face the threat of a downgrade of their credit ratings to non-investment grade level; (d) be unable to pay down debt to appropriately capitalize the business; and (e) be unable to provide a reasonable return to equity holders.

Q. Can you describe DPL Inc.'s and DP&L's current debt and any material terms of that debt?

A. Yes. DPL Inc. has the following outstanding long-term debt as of December 31, 2018:

[redacted]

DPL Inc. also has a revolver. That revolver currently has a cap of [redacted] but that cap is projected to [redacted]

The material covenants in the revolver include:

- Interest Coverage Ratio (Consolidated EBITDA/Consolidated Interest) – shall not be less than 2.10 to 1.00 and increases to 2.50 to 1.00 effective 1/1/2019
- Debt to EBITDA – shall not be more than 7.25 to 1.00 and then decreases over time as follows below:
    - January 1, 2019 – June 30, 2019 - 7.00 to 1.00
    - July 1, 2019 – December 31, 2019 – 6.75 to 1.00
    - January 1, 2020 and afterward – 6.50 to 1.00 (credit agreement matures 7/31/20)

DP&L has the following outstanding long-term debt as of December 31, 2018:

[redacted]

[redacted] [redacted]

[redacted] [redacted]

[redacted] [redacted]

DP&L also has a revolver, which has a cap of [redacted]. The material covenants in those debt issuances and revolver include:

- Interest Coverage Ratio (EBITDA/Interest) – shall not be less than 2.50 to 1.00
- Debt to Total Capitalization shall not be greater than 65% (but suspended if any Agency rates at utility Investment Grade Stable)

[redacted]

Q. Is the financial integrity of DP&L and DPL Inc. equally essential?

A. Yes. They are equally essential for several reasons: DP&L must maintain its financial integrity to ensure that it can (a) make the necessary capital investment and operating expenses that are required in the normal course of business; (b) access debt markets to refinance existing debt obligations; (c) attract debt and equity to finance the investments required to maintain reliability and modernize its transmission and distribution infrastructure; and (d) maintain reasonably priced debt and equity capital to ensure reasonable rates to customers.

If DPL Inc. cannot maintain its financial integrity, it will (a) need to minimize capital and operating expenditures at DP&L (that otherwise would be necessary to ensure safe and reliable service) in order to ensure that its own financial obligations can be met; (b) not have funds, or access to funds, that may be required to invest in DP&L and to ensure that DP&L can maintain its existing infrastructure; (c) not have funds, or access to funds, that will be required to invest in DP&L to provide the ability to modernize DP&L's distribution grid and the associated benefits for DP&L's customers and society as a whole; and (d) adversely affect its own credit ratings and the credit ratings of DP&L (all of the major credit ratings agencies "notch" the utility and the utility holding company, so that the utility credit ratings are directly linked to that of the utility holding company), which will increase the borrowing costs for DP&L and DPL Inc. and decrease cash available to operate and maintain DP&L's assets, or to invest in infrastructure modernization projects.

Q. Is it important that DP&L have an investment grade credit rating?

A. Yes. With an investment grade credit rating, DP&L can finance its debt in a low-cost bond market. If DP&L had a rating that was below investment grade, then it would be forced to finance its debt in the junk bond market, which would be much more expensive for DP&L and its customers.

Further, debt that is issued in the junk bond market may include restrictive conditions. For example, the debt that DP&L issued before the Commission's Order in the ESP III case was issued in the junk bond market and included a condition that DP&L could not issue new debt. Such a restriction would preclude DP&L from pursuing grid modernization, as DP&L will need to issue debt to finance the needed investments.

Q. Can you describe how the credit ratings agencies reacted to the Commission's approval of the ESP III Stipulation?

A. Yes. Before the ESP III Stipulation was approved by the Commission, DPL Inc.'s and DP&L's credit ratings were either below investment grade or barely investment grade with negative outlooks. Specifically:

a. On July 12, 2016, Fitch Ratings affirmed an issuer rating for DPL Inc. of B+ (four notches below investment grade) and for DP&L of BB+ (one notch below investment grade). The outlook for both was negative.

b. On August 11, 2016, Moody's issued credit opinions for DPL Inc. and DP&L. DPL Inc.'s rating was Ba3 (three notches below investment grade), and DP&L's rating was Baa3 (the lowest investment grade rating). The outlook for both was negative.

c. On March 27, 2017, S&P Global lowered the issuer credit rating for DPL Inc. and DP&L from BB to BB-, with a negative outlook. Both ratings are below investment grade.

After the Commission approved the ESP III Stipulation on October 20, 2017, the ratings and/or outlooks improved:

a. On October 27, 2017, S&P Global affirmed its BB- issuer rating for DPL Inc. and DP&L, and switched its outlook from negative to stable.

b. On October 30, 2017, Fitch Ratings upgraded DPL Inc.'s issuer rating from B+ (four notches below investment grade) to BB (two notches below investment grade). Fitch Ratings also upgraded DP&L's issuer rating from BB+ (non-investment grade) to BBB- (the lowest investment grade rating). All outlooks were revised to positive from negative. Among the "Key Rating Drivers" discussed by Fitch Ratings was the fact that "DP&L may apply for an additional two-year extension" of the DMR.

c. On October 31, 2017, Moody's affirmed the DPL Inc. senior unsecured credit rating of Ba3 (two notches below investment grade), and Moody's affirmed DP&L's issuer credit rating of Baa3 (the lowest investment grade rating). Moody's changed the outlook for DPL Inc. and DP&L to positive from negative. Moody's explained that its Rating Rationale was based in part on the fact that the DMR was "subject to an extension for an additional two years."

d. On December 20, 2017, S&P raised the issuer ratings for DPL Inc. and DP&L from BB- (three notches below investment grade) to BB (two notches below investment grade), and placed them on CreditWatch Positive.

More recently, the rating agencies have stated that their ratings assume that the DMR will be extended:

a. On March 30, 2018, S&P Global raised DPL Inc.'s and DP&L's issuer credit rating from BB (non-investment grade) to BBB- (the lowest investment grade rating). S&P stated that the upgrade "assumes that the DMR will be extended."

b. On October 9, 2018, Fitch Ratings upgraded DPL Inc.'s credit rating to BBB- (the lowest investment grade rating) and upgraded DP&L's credit rating to BBB (the second lowest investment grade rating). Its ratings said that "DPL Inc. and DP&L's long-term rating stability will depend on the extension of the Distribution Modernization Rider."

c. On December 17, 2018, Moody's issued separate Credit Opinions for DPL Inc. and DP&L. DPL Inc's credit rating was Ba1 (one notch below investment grade) and DP&L's credit rating was Baa2 (two notches above investment grade). Both Credit Opinions stated that Moody's has an "expectation that the PUCO will approve an extension of the Distribution Modernization Rider."

Q. What is the significance of those credit rating reports in this proceeding?

A. The most significant point is that while DP&L's rating is just barely investment grade for all three agencies, all three have made clear that their rating is based upon an assumption that the DMR will be extended.

Q. If the DMR-E is approved, what would DP&L use the funds for?

A. DP&L would use the DMR-E funds for the same three purposes permitted for the DMR in the ESP III Stipulation, specifically, to:

i. Pay interest obligations on existing debt at DPL Inc. and DP&L;

ii. Make discretionary debt prepayments at DPL Inc. and DP&L; and to

iii. Position DP&L to make capital expenditures to modernize and/or maintain transmission and distribution infrastructure

Q. Will the DMR-E funds be used to support a generation business?

A. No. As mentioned above, DP&L has transferred all of its operational generation assets to an affiliate; all of those assets have been sold or retired (with the exception of Conesville, which is co-owned, and its operator has announced its scheduled retirement by May 31, 2020). As also mentioned above, the DMR-E funds will be placed in a separate account and used for the three identified purposes; none of the DMR-E funds will go to the affiliate to whom DP&L's generation assets were transferred. Thus, none of the DMR-E funds would be used to support generation.

Q. If the DMR-E is approved, what method does DP&L propose for calculating the significantly excessive earnings test ("SEET")?

A. DP&L proposes that a pro forma adjustment should continue to be made to exclude DMR-E funds from DP&L's SEET calculation, consistent with the methodology approved by the Commission in the ESP Stipulation. October 20, 2017 Opinion and Order, pp. 57-58.

Q. Why is this method reasonable?

A. The financial stability of DP&L, and its ability to fund future investments in accordance with Ohio energy policy and specifically with the Commission's PowerForward Roadmap, is dependent on the financial strength of its parent DPL. If the SEET included these funds, there would be no assurance that these funds would be available to

(a) [redacted], (b) [redacted], and/or (c) recapitalize its balance sheet and ensure the long-term viability of DPL and DP&L.

VI. DP&L'S FINANCIAL CONDITION THROUGH 2028

Q. Did you provide the underlying financial projections used by Witness Malinak in developing his financial model for this case?

A. Yes. I provided Witness Malinak the Company's financial projections for the period 2019 to 2028. Based on the various assumptions and input received in developing these projections, and the review completed by the Company, these underlying projections are DP&L's best estimates of expected results. After Witness Malinak refined the financing assumptions for his calculation of the required DMR-E, these projections ultimately served as the basis for the financial statements shown in the exhibits that he sponsors, specifically RJM-9A through RJM-10C and RJM-16A through RJM-17C.

Q. What methodology and associated processes were used to develop the financial statements?

A. The pro forma financial statements included in Exhibits 1 through 6 reflect the projected financial effect of the Company's filed ESP, including the proposed DMR-E, and were developed consistently with the methodology and process used by the Company for preparing its normal operating forecast. This methodology is a "bottom up" approach to forecasting that requires input and assumptions from a variety of areas within the Company. The assumptions, which include distribution sales, Standard Service Offer sales, operating cost projections, capital expenditures and financing assumptions, among others, are reviewed with the business areas to determine the most reasonable set of assumptions to be incorporated into the forecast. As we progress through the business year, we track and monitor actual results compared to the forecast. Based on actual results combined with potential changes in business and market conditions, the forecast is adjusted as needed. The process makes the forecast a reliable one.

Q. What are the major components of the financial forecast?

A. The inputs and assumptions received are used to derive the following major components of the forecast (1) Distribution baseline sales volumes; (2) Retail revenue estimates; (3) Operations and maintenance expense forecast; (4) Capital expenditures forecast; and (5) Financing Assumptions

Q. How are each of the above components developed?

A. The development and methodology for each of these major components are as follows:

(1) Distribution Baseline Sales Volumes — The distribution baseline sales volumes are in line with the Company's Long-Term Forecast.

(2) Retail revenue estimates — The retail revenues reflected in the Company's pro forma financial statements include tariff rates as proposed in DP&L's recently settled Distribution Rate Case (Case No. 15-1830-EL-AIR et al.), revenues associated with the Company's DMR-E in this case, revenues associated with the recently filed DMP (Case No. 18-1875-EL-GRD), and with the DIR approved in the distribution rate case. Additionally, retail revenues reflect the effects of future distribution and transmission rate increases to recover costs and investments expected to be incurred during the period 2019

through 2028. Finally, retail revenues incorporate the impacts from the Competitive Bid Process ("CBP"), which are completely offset by a corresponding expense.

(3) Operations and Maintenance ("O&M") Expense Forecast — O&M expenses are forecasted by (and reviewed with) all of the business areas within the Company. Underlying the O&M forecasts are assumptions for various items such as projected salary increases and inflationary factors. Each area's O&M forecast includes staffing plans, labor costs, and other operational costs necessary to perform the functions of the specific area.

(4) Capital Expenditures Forecast — Capital expenditures are forecasted by (and reviewed with) all of the business areas within the Company, although a substantial portion of the forecast is driven by the Company's operational groups: Transmission and Distribution. The forecast includes specific projects, as well as dollars to fund smaller projects under a blanket capital budget. Included in this forecast is the aforementioned expenditures related to the DMP, as well as transmission projects intended to improve the reliability of the PJM bulk power system. The capital expenditures are used to estimate depreciation (book and tax) and capitalized interest.

(5) Financing Assumptions — Financing assumptions, including but not limited to assumptions related to new financings, refinancings, debt retirements, and overall capitalization targets, are provided by DP&L's Treasury organization and reviewed by the finance leadership team. The forecasts include specific plans related to (a) known and measurable events, including the refinancing of near-term debt obligations, and

(b) targeted use of excess (or discretionary) cash flows for debt reductions / retirements. DP&L has also consulted with Witness Malinak on incorporating appropriate financing assumptions that are consistent with the proposed DMR-E in this case.

Q. Is the amount of the DMR-E proposed by Witness Malinak reflective of the distribution and transmission rate increases, Smart Grid Rider and DIR treatment noted above?

A. Yes. The proposed DMR-E was determined after including the cash flow effects of all of these revenue assumptions and projections. By incorporating these additional cash flows into the projections, DP&L maximized all sources of revenue before determining the proposed DMR-E amount in this case.

Q. Do you anticipate issuing incremental long-term debt at DP&L over the forecast period?

A. Yes, due to the capital investments made in the DMP, related to the DIR, and the Transmission system, the forecast projects new debt of [redacted]. This debt helps to finance these projects and is necessary to maintain the utility [redacted].

Q. Does your testimony and the testimony of Witness Malinak refer to information constituting trade secrets of DP&L and DPL Inc.?

A. Yes. Both Witness Malinak's testimony and my testimony refer to financial projections of DP&L and DPL Inc., including projected revenue, operating expenses, and capital expenditures, and to the proceeds of recent asset sales. Witness Malinak also projects the availability of capital via projected actions by credit rating agencies and lenders. Such information derives independent economic value from not being generally known to those outside DP&L and DPL Inc. who could obtain economic value from their disclosure. Moreover, DP&L and DPL Inc. internally limit the availability of such information to those who have a business need to know it, and do not disclose such information externally absent appropriate protective devices. This information is redacted in the publicly-available versions of my testimony and the testimony of Witness Malinak, but will be filed under seal with the Commission and will be available to parties who enter into protective agreements with DP&L.

VII. CONCLUSION

Q. Can you summarize your testimony?

A. Yes. Since the ESP III Stipulation was signed, DPL Inc. and DP&L have taken aggressive steps to improve its financial condition, including steps that were not required by that Stipulation. Despite those significant efforts, DPL Inc. and DP&L's financial condition remain weak, and DPL Inc. and DP&L will not be able to implement grid modernization without approval of the DMR-E. The Commission should thus approve the DMR-E to allow DPL Inc. and DP&L to return to solid financial footing and to implement grid modernization within the DP&L service territory.

Q. Does this conclude your direct testimony?

A. Yes, it does.

1322741.1