

BEFORE THE  
PUBLIC SERVICE COMMISSION  
OF MARYLAND

IN THE MATTER OF THE )  
CURRENT AND FUTURE )  
FINANCIAL CONDITION OF ) Case No. 9173, Phase II  
BALTIMORE GAS AND )  
ELECTRIC COMPANY )

DIRECT TESTIMONY OF JEFF HOOKE  
ON BEHALF OF INTERVENOR  
MARYLAND TAX EDUCATION FOUNDATION

August 28, 2009

1 **Q. Please state your name and business address.**

2 A. My name is Jeff Hooke, 7504 Maple Avenue, Chevy Chase, MD 20815

3

4 **Q. Are you the same Jeff Hooke who submitted testimony on behalf of the**  
5 **Maryland Tax Education Foundation in Phase I of this proceeding?**

6

7 A. I am.

8

9

10

11 **Q. Have you previously testified in any other regulatory or governmental**  
12 **proceedings?**

13

14 A. Yes, I have testified on numerous occasions before state legislatures on valuation  
15 and financial matters. I testified in the Phase I proceedings as well.

16

17 **Q. What is the subject of your testimony?**

18

19 A. I will address

20 (i) How the transaction lacks substantial benefits for ratepayers and the State  
21 of Maryland, yet is a windfall for CEG;

- 1 (ii) How the ratepayers of Maryland prop up CEG financially;
- 2 (iii) How CEG ignores certain of its constituents;
- 3 (iv) How the transaction threatens the ability of the Baltimore Gas and Electric
- 4 Company (BG&E), the regulated utility subsidiary of Constellation
- 5 Energy (CEG), from supplying economical and reliable electricity to its
- 6 standard-offer-service (SOS) ratepayers; and
- 7 (v) How the transaction perpetuates, within the CEG corporate umbrella,
- 8 certain conflicts of interest that are untenable for a public utility operating
- 9 under Section 5-303 of the Public Utilities Article of the Maryland Code.

10

11 **Q. Are you familiar with the position of CEG and EDF in this regard?**

12

13 A. Yes, I have read portions of (i) the testimony of CEG, BG&E and EDF

14 employees, (ii) the transaction documentation, and (iii) the information provided

15 by CEG, BG&E and EDF.

16

17 **Q. The position of the EDF, CEF and BG&E representatives is that the EDF**

18 **transaction is a terrific deal for BG&E ratepayers and Maryland residents.**

19 **Do you agree with that assessment?**

20

21 A. No. The best way to expand on the response to this question is to note that Ken

22 DeFontes, Jr., CEO of BG&E, bluntly stated in his testimony of June 24, 2009

1 that BG&E realizes no cost-savings synergies from the transaction. He then goes  
2 on to testify (Defontes Phase II Direct at 7:9-15):

3 “BGE’s customers will still benefit greatly from the transaction.  
4 All of the benefits that I described earlier in my testimony – improving  
5 CEG’s and BGE’s financial strength, solidifying its headquarters in  
6 Baltimore and its role as a major employer, enabling the potential for new  
7 nuclear investment in the State, and making substantial contributions to  
8 both philanthropic efforts and the tax coffers of Maryland – will benefit  
9 BGE’s customers as well as other Maryland residents.”

10

11 I respond briefly to each of the four points set forth in that portion of Mr.  
12 DeFontes’ testimony:

13

14 1. Improving CEG’s and BG&E’s financial strength: This statement is true, but  
15 the benefit to ratepayers is questionable. If the transaction were not to close,  
16 CEG would likely fall below an investment-grade bond rating temporarily.  
17 However, CEG management has means at its disposal that could reverse the  
18 downgrade over 1-2 years. These means include selling more assets, selling  
19 common stock or reducing trading positions, all of which raise cash for debt  
20 repayment (and bond rating enhancement). Since S&P follows the “corporate  
21 parent ceiling” concept, BG&E’s rating from S&P would likely fall below  
22 investment grade as well on a temporary basis. Moody’s does not practice the

1 corporate parent ceiling concept; and, thus, BG&E might retain its investment  
2 grade rating from Moody's even if CEG were downgraded to junk bond status  
3 by Moody's and S&P.

4  
5 Even if BG&E were temporarily to fall to junk bond status, it would take  
6 several years before such a downgrade would have any significant impact on  
7 BG&E's financial status. The potential downgrade only affects the interest  
8 rates on new BG&E bond issuances, not on outstanding bonds of \$2.2 billion.  
9 Assuming \$400 million of new bond issuances each year, a drop to junk bond  
10 status costs BG&E another 4% in interest costs, or \$16 million annually  
11 (assuming debt rates of 7% for investment grade bonds vs. 11% junk grade).  
12 This equates to only one-half of one percent of BG&E's annual revenues.  
13 Obviously, this expense is mildly damaging to BG&E, but it is hardly the  
14 financial calamity painted by CEG. In any case, the PSC, in a future rate  
15 determination, could simply adjust BG&E's allowable return on equity to  
16 make up the difference for ratepayers.

17  
18 A drop to junk bond status would be far more problematic for CEG, which  
19 would have to post more collateral for its trading positions and pay higher  
20 rates on its short-term debt rollovers, including over \$2 billion in rollovers in  
21 2009. CEG's interest penalty could easily be \$100 million per year by 2010,

1 or \$0.50 per share, which would negatively impact CEG's stock price by  
2 several dollars.

3  
4 2. Solidifying its headquarters in Baltimore: Having a Fortune 500 firm  
5 headquartered in Baltimore has public relations value for the state, but CEG  
6 (absent BG&E) is not a major employer, with parent company employees  
7 totaling less than 1,000 in Maryland. Given the amount of profit that CEG  
8 extracts from the state each year, a corporate headquarters is the least  
9 residents can expect from CEG. It is at best unclear how strongly Maryland's  
10 image as "business friendly" is connected to CEG's headquarters, let alone  
11 how such an image directly benefits ratepayers.

12  
13 3. New nuclear investment in the state, related employment and taxes: Calvert  
14 Cliffs is one of the few nuclear sites in the country where new nuclear plant  
15 construction is ready to begin. If the third plant site is not developed by an  
16 EDF/CEG joint venture because this transaction does not close, it is logical to  
17 assume another operator would have an interest, particularly given the  
18 possibility of federal loan guarantees. In other words, if this transaction  
19 doesn't take place, that doesn't spell the end of the third plant. The new  
20 investment, if any, can be done by another large company with a nuclear  
21 business. Exelon, for example, just dropped its \$7.7 billion bid for NRG

1 Energy, a power generation firm with nuclear interests, after NRG refused to  
2 negotiate.

3

4 Because the new plant is planned as a merchant facility, it is unclear whether  
5 ratepayers will benefit from its construction since there is no guarantee that  
6 power will be sold in Maryland or will be sold cheaply at all. CEG, EDF,  
7 CENG and other generators in the PJM grid will want to preserve their high  
8 rates of return on generating assets, which, in turn, lead to higher electricity  
9 rates than might normally be the case. Recent studies by Edward Bodmer  
10 (American Power Association, May 2009) and McCullough Research (March  
11 3, 2009) are instructive in this regard.

12

13 The employment and property taxes paid by the plant should be favorable to  
14 the state's economy, but again there is no direct benefit to ratepayers here. In  
15 any case, some entity besides EDF could be expected to help to build the new  
16 Calvert Cliffs nuclear plant if the transaction under consideration here does  
17 not close.

18

19 4. Philanthropy: CEG likes to highlight the \$36 million charitable contribution  
20 in both its PSC and its legislative testimony. Each grant made from the  
21 contribution, assuming the deal closes, will no doubt subject Maryland  
22 residents to a public relations onslaught from CEG. The company's

1           generosity is barely noteworthy; the \$36 million is a tiny fraction (2%) of the  
2           estimated \$2 billion in benefits for CEG stockholders that would flow from  
3           consummation of the EDF/CEG transaction under consideration in this case.  
4           Thus, given that 98% of the benefits of the Transaction as proposed would go  
5           to CEG stockholders, any claim of benefit flowing from the Transaction to the  
6           people of the State of Maryland rings more than a little hollow.

7

8   **Q.   How do BG&E ratepayers prop-up CEG financially?**

9

10  A.   Earnings before interest, taxes, depreciation and amortization (EBITDA) is a  
11       popular measure of corporate profitability and cash flow production.  CEG's  
12       annual EBITDA is approximately \$1.9 billion, according to the Company's SEC  
13       filings and equity research reports.

14

15       BG&E supplies \$560 million of CEG's annual EBITDA (according to SEC  
16       filings) and CEG's Maryland generating plants provide another \$570 million  
17       (according to my calculations).  Based on SEC filings, most of the Maryland  
18       power generation is sold through the PJM network back to BG&E, which uses it  
19       to service SOS customers, although the exact percentage is not disclosed by CEG  
20       publicly.  Based on consolidating accounting entries in the SEC filings, my  
21       analysis assumes 80% of the Maryland power generation is consumed by BG&E  
22       ratepayers, who thus provide 80% of the \$570 million in annual generating

1 profits, or \$456 million (80% x \$570 = \$456). Thus, BG&E ratepayers likely  
2 represent \$1.0 billion, or 53% of CEG's annual \$1.9 billion of EBITDA (\$560 +  
3 \$456 = \$1,016).

4

5 The steady, reliable earnings stream from BG&E ratepayers supports CEG's  
6 forays into more speculative trading operations, which almost led to the firm's  
7 collapse in 2008.

8

9 **Q. Is CEG being fair to its corporate constituents, which include stockholders,**  
10 **customers, lenders, suppliers and others?**

11

12 A. Rather than act reasonably toward the BG&E ratepayer constituency (a course of  
13 action that might be suggested by many business theorists) by (i) approving re-  
14 regulation, (ii) fighting high PJM prices, and (iii) offering rate concessions in this  
15 proceeding, CEG follows the tenets espoused by Milton Friedman in his famous  
16 article (1970) for the New York Times Magazine: "The Social Responsibility of  
17 Business is to Increase Its Profits." The views espoused by this article might  
18 please CEG stockholders and provide a foundation for the EDF transaction, but it  
19 is inconsistent with CEG's responsibility not to interfere with BGE's obligation to  
20 "furnish equipment, services, and facilities that are safe, adequate, just,  
21 reasonable, economical, and efficient, considering the conservation of natural

1 resources and the quality of the environment” to its ratepayers under Section 5-  
2 303 of the Public Utility Companies Article.

3

4 **Q. Do you believe the EDF transaction brings benefits to the State and CEG?**

5

6 A. The EDF transaction brings benefits to the State, but those benefits are minor  
7 relative to the windfall benefits to be enjoyed by CEG stockholders. As noted,  
8 benefits are split 2% to the public (in the form of a charitable contribution) versus  
9 98% to CEG’s stockholders.

10

11 The stockholders of CEG have seen a stock price jump due to the proposed deal,  
12 and will see another rise in the stock price, should the PSC approve the  
13 Transaction and the Transaction closes. Consider the following:

14

15 I estimate that the transaction enhances CEG’s stock value by \$10 per share or \$2  
16 billion. This \$10 per share results from (i) risk reduction (i.e., a lower discount  
17 rate on future earnings): \$6 per share; and (ii) premium price paid by EDF for  
18 entry into the nuclear energy business: \$4 per share (see Attachment A).

19

Corroborating opinions include:

20

21 Wall Street Equity Research: In February, 2009, four equity analysts predicted a  
22 drop in 2009 CEG’s earnings when the stock was at \$18 per share. The firms were

1 Credit Suisse, Standard & Poor's, Citicorp, and Jefferies. Normally, when a firm's  
2 earnings are expected to fall, the stock price should decline. However, based on  
3 the pending EDF deal, these four investment banks predicted a jump in the stock  
4 price from \$18 to \$27. That is a \$9 per share increase, which MTEF, in its Phase I  
5 testimony before this Commission, ascribed to the EDF deal.

6

7 In its April 22, 2009 report, Citicorp affirmed a target price of \$34 per share when  
8 the CEG stock traded at just \$22 per share. This \$12 difference represented a 55%  
9 increase when 2010 earnings were forecast to go up just 9%. The huge gain in the  
10 stock price is attributable to the impact of the EDF deal.

11

12 On July 8, 2009, Jefferies & Company predicted a stock price of \$32.50 when  
13 CEG was trading at \$26.07, a \$6.43 per share or 25% increase, despite a minor  
14 rise in forecast earnings. This \$6.43 gain is just part of the \$10 per share in  
15 benefits; an estimated \$3.57 of the benefits is now embedded in the stock price, as  
16 Wall Street predicts approval and few adverse concessions from the PSC (\$6.43 +  
17 \$3.47 = \$10.00).

18

19 Hedge Fund Analysis: MTEF corroborated its analysis with two hedge funds that  
20 hold large positions in the CEG stock and that talk to CEG regularly.

21

1 We thus have the ratepayers realizing zero benefits, the state realizing a paltry \$36  
2 million charitable contribution, and CEG realizing \$2 billion in increased equity  
3 value.

4

5 **Q. Should the PSC address this huge disparity in benefits?**

6

7 A. I believe that the disparity of benefits is a symptom of an underlying problem that  
8 PSC should address, notwithstanding that EDF and CEG would like the PSC to  
9 approve the EDF transaction with minimal conditions.

10

11 If this deal were a utility to utility merger with \$2 billion in long-term synergies,  
12 the PSC might reasonably target 50%, or \$1 billion, of the synergies for  
13 ratepayers. Here, as an asset sale of a related business, the situation has little  
14 precedent, and the PSC's goal should be (1) to protect ratepayers from a company  
15 (CEG) with a checkered track record, and (2) to resolve the disparity, given that  
16 ratepayers provide most of CEG's profits anyway.

17

18 **Q. How does the transaction potentially threaten the ability of BG&E to supply**  
19 **economical and reliable SOS service?**

20

1 A. CEG's history indicates that top management's risk management abilities are  
2 suspect, and that the Board is either unwilling, or unable, to discipline  
3 management in this regard, thus setting the stage for another debacle in the future.

4

5 It is almost impossible to predict exactly what series of events (involving CEG,  
6 EDF and CENG) could occur and negatively affect BG&E and ratepayers. One  
7 possibility: If EDF denies CENG the ability to upstream cash dividends to CEG,  
8 then CEG might use BG&E as a greater cash flow source, by cutting capital  
9 expenditures to bare-bone levels, or by maximizing dividends and thus  
10 endangering the utility's health (and ability to provide reliable and economical  
11 electricity). Alternatively, CEG might feel pressure to obtain more cash through  
12 its intercompany charges to BG&E. These charges total approximately \$170  
13 million per year and are stipulated as "fair" by CEG executives and CEG's  
14 independent accountants, but the PSC has no ability to audit these stipulations.  
15 Overcharges will lead to higher SOS rates.

16

17 The EDF transaction brings CEG new cash and a strengthened balance sheet.  
18 Subsequently, given its history, CEG could go on an acquisition binge, plunging  
19 CEG into unknown and risky businesses. A more onerous, and perhaps, more  
20 likely outcome of the transaction, would be CEG and EDF working together to  
21 preserve the anti-consumer nature of the PJM market arrangements, which, as

1 noted earlier, result in premium rates of return for merchant generators and  
2 higher-than-expected rates for SOS customers.

3

4 BG&E's service obligation is defined by Section 5-303 of the Public Utility  
5 Companies Article of the Maryland Code as follows: "A public service company  
6 shall furnish equipment, services, and facilities that are safe, adequate, just,  
7 reasonable, economical, and efficient, considering the conservation of natural  
8 resources and the quality of the environment." CEG management does not seem  
9 to understand this provision. The PSC tries to deal with the inherent conflict of  
10 interest involved in a regulated utility (BG&E) doing business with its  
11 unregulated affiliates (CEG Merchant Power Division) by standards of conduct,  
12 ring fencing, and similar prescriptive rules.

13

14 The problem is that, in utility regulation, the structural (vs. the behavioral)  
15 remedy is almost always more dependable at protecting consumers. The  
16 inclination of the regulated party to evade or circumvent the intent of behavioral  
17 regulations, and the tendency of the ratepayer (and the courts) to blame the  
18 regulator for being insufficiently prescriptive when new evasion strategies emerge  
19 among the regulated entities, are both well known and frequently observed. One  
20 of the most glaring examples of this phenomenon occurred in convection with the  
21 merger of San Diego Gas & Electric Co. and Southern California Gas Co. to form  
22 Enova Corp. in 1998. The California Public Utilities Commission rejected

1 interveners' pleas for structural remedies (divestiture), saying "We will not  
2 presume that officers of the merged company are prepared to conspire to violate  
3 criminal statutes and Commission regulation." *Joint Application of Pacific*  
4 *Enterprises, Enova Corp., et al.* (D.98-03-073), 79 CPUC2d 343, 184 P.U.R.4<sup>th</sup>  
5 417 (1998). Within five years, Sempra Energy Trading, the marketing arm of the  
6 merged San Diego Gas & Electric Co. and Southern California Gas stood accused  
7 by the Federal Energy Regulatory Commission of engaging in such conduct, and  
8 contributing in a substantial way to the meltdown that was the California Energy  
9 Crisis of 2000-2001. *American Electric Power Svc. Corp. et al.*, 103 FERC ¶  
10 61,345 at pp. 62,342-62,344 (2003).

11

12 **Q. How is the conflict of interest manifested now to the detriment of BG&E**  
13 **ratepayers?**

14

15 A. If BG&E was a stand-alone entity, unaffiliated with CEG, it could use its  
16 substantial financial strength, political acumen and lobbying power to promote  
17 new regional generating plants, and a PJM market design and structure more  
18 favorable to the interests of BG&E ratepayers as consumers. As a subsidiary of  
19 CEG, which realizes premium profits from Maryland generating plants, BG&E  
20 has no motive to fight for its ratepayers in this regard.

21

1 The research studies by Edward Bodmer and McCullough Research cited earlier  
2 in this testimony explain the “deregulation premium” extracted from consumers  
3 by “organized” wholesale markets such as PJM.

4

5 A stand-alone BG&E might even push for re-regulation of CEG’s Maryland-  
6 based power plants (or a long-term power purchase contract based on regulation),  
7 since MTEF’s calculations indicate a substantial savings to SOS ratepayers from  
8 such an action. However, CEG (and BG&E) have strenuously fought this idea in  
9 the legislature and in the media.

10

11 **Q. How does the transaction perpetuate the CEG/BG&E conflict of interest and**  
12 **permanently impair the interests of BG&E’s ratepayers?**

13

14 A. CEG is one of the most powerful organizations in the state. With its vast financial  
15 resources, it unduly influences the media, the business community, the state  
16 legislature and the state executive branch.

17

18 By way of example, in 2008 electricity price increases caused widespread protest  
19 and ratepayer suffering. A proposal to re-regulate CEG’s Maryland-based power  
20 plants (directly or through long-term contract) would have cut SOS rates by 10%  
21 to 15% immediately, and would likely have been popular with voters. The impact  
22 of re-regulation on CEG’s annual EBITDA was minus 10%, but re-regulation

1 would have made a sizeable portion of the earnings stream more reliable, thus  
2 neutralizing part of the negative earnings impact on CEG's stock price. (Full re-  
3 regulation cuts EBITDA by 12%, but SOS re-regulation by 10%.) Reflective of  
4 CEG's lobbying power, even in its damaged state, a much-watered-down proposal  
5 barely passed the Senate Finance Committee and the legislation was buried in the  
6 House Economic Matters Committee by a lopsided 21-2 vote, without a hearing.

7

8

9

10 If the transaction closes, CEG will be on a much firmer financial, media and  
11 political footing. Its ability to assist in the preservation of the anti-consumer PJM  
12 market structure will be enhanced, and it will have a gigantic, well-heeled partner  
13 in this endeavor—EDF. Only the PSC stands in the way of the CEG/EDF  
14 juggernaut to be created by this transaction.

15

16 **Q. How would you suggest the PSC protect ratepayers from the profit-seeking**  
17 **CEG/EDF/CENG monolith?**

18

19 A. The PSC should make one condition of the deal the following: CEG/EDF/CENG  
20 provide 100% of the SOS energy load to BG&E, under long-term contract, on a  
21 cost-of-service basis (i.e., as if the Maryland plants supplying the power were  
22 doing so under a regulated regime).

1

2 CEG will complain, as it has in the past, that such a requirement would cripple the  
3 company, but the financial impact (i) to CEG EBITDA is only minus 10%; and  
4 (ii) to the stock price is just minus \$4 per share, or 40% of the \$10 per share  
5 benefits. CEG is still ahead by \$6 per share ( $\$10 - \$4 = \$6$ ) and the bond rating  
6 impact is negligible.

7

8 To mitigate any claimed negative impact on CEG's shareholders from  
9 implementing this consumer protection measure, the PSC could suggest that CEG  
10 evaluate actions to recover a portion of the \$1.1 billion MidAmerican merger  
11 termination fee, which appears excessive. Normally, an outside shareholder  
12 would prompt such actions, but prominent shareholders are afraid of bucking  
13 CEG management (see Attachment B).

14

15 **Q. Do you have anything to add?**

16

17 A. At the time of this testimony, the "money people" on Wall Street believe the PSC  
18 approval is a "done deal," despite the obvious danger to BG&E ratepayers. The  
19 probability of (i) the PSC denying the transaction, or (ii) conditioning its approval  
20 of the transaction in a way that costs CEG and EDF significant money is seen as  
21 20% or less. The market's apparent assumption concerning regulatory  
22 acquiescence over this transaction significantly underestimates the extent of the

1 authority granted to the Commission by Section 6-105 of the Public Utility  
2 Companies Article. It also underestimates what I believe is the extent of this  
3 Commission's commitment to regulation in the public interest.

4

5 **Q. Does this conclude your testimony at this time?**

6

7 A. Yes, it does.

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

**Attachments**

- A. \$10 Per Share Calculation
- B. Op-Ed Relating to \$1.1 Billion Termination Fee

ATTACHMENT A

CALCULATION OF \$10 PER SHARE VALUE OF CEG/EDF TRANSACTION TO  
CONSTELLATION ENERGY GROUP COMMON STOCK

## **\$10 Value for CEG Common Stock From CEG/EDF Deal**

CEG stockholder value resides in two aspects of the transaction:

1. Premium price paid by EDF to enter the US nuclear market (\$4); and
2. Reduced risk associated with CEG (\$6) --once the deal is closed, the cash proceeds are received and CEG's financial situation is strengthened.

Premium Price	\$ 4 per share
Reduced Risk	<u>\$ 6 per share</u>
Total	\$10 per share

The cost per share of settlement options include 100% re-regulation for SOS customers (\$ 4.15 per share), one time \$170 rate credit (60 cents), clean energy ( 35 cents), BG&E distribution rate freeze ( 35 cents)and universal service subsidy ( 31 cents). The Governor's settlement proposal had a value of \$2 per share.

### **Premium Price**

EDF is paying 10x operating cash flow for the 49% interest. The Exelon/NRG(nuclear) deal is priced at 6x and public merchant power firms trade at 5x. The 10x premium price is due to EDF's intense desire to build a presence in the US nuclear industry quickly. Assuming that 7x is 'fair value,' the \$ 4 billion is a 43% overpayment ( $10/7=143\%$ ). This translates into \$1.2 billion of excess price before taxes ( $4.0/2.8=143\%$ ) and the difference between 4.0 and 2.8 is 1.2). This after tax amount is \$800 million (\$ 4 per CEG share).

### **Reduced Risk**

High risk companies have higher investor returns. By way of illustration, today US Treasury bonds yield 4%, blue-chip corporate bonds yield 7%, and junk bonds yield 11%. The 11% difference between 7% and 11% shows the price investors charge for risk (CEG bonds yield 9%). Equity, or common stock, returns exceed bond returns.

When the EDF transaction closes, CEG will be a much 'safer' business. To calculate its share price, investors will use a lower discount rate (compared to today) in discounting its future earnings. The effect will be to increase the stock price. For example, discounting CEG's future earnings at 18% provides a \$26 share price. A post closing 14% discount rate (4% lower) indicates a \$32 price (i.e., \$6 per share).

### **Potential \$2 per Share Bonus from State Involvement**

CEG paid Buffett's company \$1.1 billion (\$5.50 per share) in termination fees, a 22% penalty when Delaware corporate law (which MD follows) sets a 4% maximum. A State settlement could require CEG to initiate legal action to recover a part of the fee. It is reasonable to assume that Buffett settles out of court for \$400 million, or \$2 per share. Thus, the 'pot of money' available for might total \$12 per share, or \$2.4 billion.

### **Confirmation of MTEF Analysis**

MTEF's Chairman is an experienced financial executive with an extensive Wall Street and international background. He also is the author of four books on finance and teaches courses on finance at various graduate schools.

Wall Street Equity Research: In February, 2009, four equity analysts predicted a drop in 2009 CEG's earnings when the stock was at \$18 per share. The firms were Credit Suisse, Standard & Poor's, Citicorp, and Jefferies. Normally, when a firm's earnings are expected to fall, the stock price should decline. However, based on the pending EDF deal, these four investment banks predicted a jump in the stock price from \$18 to \$27. That is a \$9 per share increase, which MTEF, in its testimony before the PSC, ascribed to the EDF deal.

In its April 22, 2009 report, Citicorp affirmed a target price of \$34 per share when the CEG stock traded at just \$22 per share. This \$12 difference represented a 55% increase when 2010 earnings were forecast to go up just 9%. The huge gain in the stock price is attributable to the impact of the EDF deal. See selected report pages.

On July 8, 2009, Jefferies & Company predicted a stock price of \$32.50 when CEG was trading at \$26.07, a \$6.43 per share or 25% increase, despite a minor rise in forecast earnings. This \$6.43 gain is just part of the \$10 per share in benefits; a portion of the benefits is now embedded in the stock price, as Wall Street predicts few adverse concessions required by the PSC.

Hedge Fund Analysis: MTEF corroborated its analysis with two hedge funds that hold large positions in the CEG stock: Rangle Capital and Catapult Capital. Both firms seem to be in regular contact with CEG. We can supply contact information at your request.

Mail Log # 118520

ATTACHMENT B

Opinion Editorial from *The Baltimore Sun* (February 1, 2009)

# Who's helping rich get richer

BY JEFFREY HOOKE

**M**aryland widows and orphans may soon start subsidizing billionaire Warren E. Buffett's corporate jet. Is it right? No. Legal? Maybe not. But whether anything can be done about it, at this point, is an open question.

When Constellation Energy canceled its \$5 billion merger with Mr. Buffett's company, Mid-American Energy Holdings, it was obligated to pay \$1.1 billion in termination fees. The fees, which amount to \$6 for each share, are paid directly by Constellation and indirectly by its shareholders, who now see the share price trade at \$27, or \$6 lower than a \$33 price without the fees.

Constellation Energy is the successor to Baltimore Gas and Electric Co., which was a conservative, dividend-paying electric utility. BGE's low-tech business and earnings consistency made its common stock a favorite of local trust departments, which prize capital preservation and steady income for clients who are vulnerable and unsophisticated. When BGE morphed into Constellation, many local institutions and individuals retained an exposure to the stock. We thus have a situation where a middle-income Marylander with only 200 shares is essentially paying \$1,200 (or \$6 per share) to a billionaire.

Legal research funded by the Maryland Tax Education Foundation concludes that the \$1.1 billion in termination fees is excessive, and likely illegal, under Maryland law. As one illustration: The fees total 22 percent of the deal's size, even though the maximum allowed in Maryland and other jurisdictions seems to be 4 percent. Getting this matter in front of a judge and jury, however, is problematic. Individual investors lack the resources to go against Mr. Buffett and his phalanx of lawyers and lobbyists. Standing in their place is the class-action bar — groups of trial attorneys who rush into almost every public merger transaction and accuse the buyer and seller of numerous infractions. Despite the merits of many cases, the defendants consider such lawsuits to be of the nuisance variety because the class-action bar tends to opt for quick negotiations to cover legal fees. Most settlements provide the supposedly aggrieved small stockholder with just a few cents on the dollar.

The natural opponents to the Constellation injustice should be the large, institutional funds that own millions of Constellation shares on behalf of their clients; however, such funds are reluctant to challenge such fees. Many lack experience in mergers and acquisitions, and others are unwilling to be perceived as anti-management in a marketplace where corporate executives hold sway in choosing which funds manage employee pension money. Also, the fight for lower termination fees can be costly, and the institution cannot recoup such expenses from its clients directly, even if a victory increases the value of client shareholdings by tens of millions of dollars. The institution's rewards in this regard come from higher assets under management (from the increased stock price) and enhanced performance, both of which provide it greater income over time rather than immediately.

The Maryland Tax Education Foundation contacted four institutions, including Baltimore-based T. Rowe Price, that collectively own 21 million Constellation shares. None has lifted a finger to stop the fees, despite the fact that reducing Constellation's payments to a normal level would save their clients \$100 million.

Our elected officials have yet to turn their full attention to this matter. Even if they do, their ability to intervene might be limited to "jawboning" the billionaire to do "what's right" for their constituents. The governor and attorney general have encouraged the Maryland Public Service Commission to assert authority to rule on the legality of the fees.

Whether the PSC is a match for the "Oracle of Omaha" remains to be seen, but many Constellation stockholders sure hope so.

*Jeffrey Hooke, a Baltimore native and Chevy Chase resident, is the author of four books on investment and finance. He is chairman of the Maryland Tax Education Foundation, a nonprofit that studies budget and tax issues. His e-mail is [jhooke@hookeassociates.com](mailto:jhooke@hookeassociates.com).*

BEFORE THE  
PUBLIC SERVICE COMMISSION  
OF MARYLAND

IN THE MATTER OF THE )  
CURRENT AND FUTURE )  
FINANCIAL CONDITION OF ) Case No. 9173, Phase II  
BALTIMORE GAS AND )  
ELECTRIC COMPANY )

**CERTIFICATE OF SERVICE**

The undersigned hereby certifies that one copy of the foregoing direct testimony of Jeff Hooke on behalf of Intervenor Maryland Tax Education Foundation has this day been served in accordance with the Commission's regulations on each person whose name appears on the attached current official service list compiled by the Secretary of the Commission in this proceeding.

*/s/ John P. Coyle*

---

John P. Coyle  
Duncan & Allen  
Suite 300  
1575 Eye Street, N.W.  
Washington, D.C. 20005

Dated: August 27, 2009.