

R-00973953, R009739530001
Statement No. 10-R 0007
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Phillips 11/17/97
L. Holben

Petition of Enron Energy Services Power Inc. for approval
of an Electric Competition and Customer Choice Plan and
for authority pursuant to Section 2807(e)(3) of the
Public Utility Code to serve as the Provider
of Last Resort in the service territory
of PECO Energy Company

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Rebuttal Testimony

of

Michael D. Dirmeier

on behalf of

Enron Energy Services Power, Inc.

concerning

Proposed Competitive Safeguards and

Code of Conduct

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1 **I. SCOPE AND PURPOSE OF REBUTTAL TESTIMONY**

2 **Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?**

3 A. The purpose of this rebuttal testimony is to respond to the testimonies of PECO witnesses
4 Sidak and Crowe concerning my positions on competitive safeguards and the appropriate
5 code of conduct that should be adopted by the Pennsylvania Public Utility Commission
6 ("Commission" or "PUC") in the transition from a monopoly to competitive structure for
7 electric generation. This PECO testimony was directed specifically to the Code of
8 Conduct proposed to be applied to PECO as part of Enron's Choice Plan.

9

10 **Q. WAS THIS TESTIMONY PREPARED BY YOU OR UNDER YOUR DIRECT**
11 **SUPERVISION?**

12 A. Yes, it was; and, I was assisted by Richard J. Koda, a Senior Consultant at Georgetown.

13

14 **II. CONCLUSIONS AND RECOMMENDATIONS**

15 **Q. WHAT HAVE YOU CONCLUDED REGARDING PECO'S TESTIMONY FILED**
16 **NOVEMBER 7, 1997?**

17 A. I have concluded that PECO still seeks to advance its own interests and the interests of
18 the incumbent electric utilities in Pennsylvania. PECO implores the Commission to
19 maintain the inherent advantages of the Electric Distribution Companies ("EDC") over
20 their potential competitors and erroneously characterizes Enron's position and the
21 regulatory theory supporting it. PECO's inherent advantages are derived from its historic
22 and continued monopoly position, not from a competitive process. The focus of the

1 Commission should be on the long-term benefit of customers and which processes and
2 requirements provide this benefit.

3

4 **Q. DO YOUR RECOMMENDATIONS DIFFER FROM THOSE YOU ORIGINALLY**
5 **RECOMMENDED IN THIS PROCEEDING?**

6 A. No. The Commission should still adopt a code of conduct that goes beyond the principles
7 adopted by the Competitive Safeguards Working Group which appear in their Final
8 Report to the Commission dated October 6, 1997 and embody the additions and
9 enhancements recommended in this testimony. The Code of Conduct proposed by Enron
10 as part of its Choice Plan is a reasonable basis for establishing such a code.

11

12 ***III. DISCUSSION OF ISSUES RAISED BY PECO WITNESSES***

13 **Q. WHAT CONCLUSIONS DOES MR. SIDAK REACH IN HIS TESTIMONY (PECO**
14 **STATEMENT NO. 10-E) REGARDING YOUR PREVIOUS TESTIMONIES IN**
15 **THIS PROCEEDING?**

16 A. Mr. Sidak opposes the recommendation contained in the Choice Plan Code of Conduct
17 (and supported in my earlier testimony) which would have the Commission prohibit a
18 competitive supplier from using the trade name, trade mark or logo of its affiliated utility
19 distribution company. On page 5 of his testimony Mr. Sidak opines that my positions
20 evidence a "hostility to, and proposal for the deprivation of, the private property of
21 regulated utility is an extreme and unsupportable position that would harm consumers."
22 He then proceeds to provide the bases for his conclusion.

1 Q. ARE THERE FLAWS IN MR. SIDAK'S ANALYSIS?

2 A. Yes, Mr. Sidak states that the benefits that a brand name can create for a firm flow from
3 investment in the reputation, not from a state conferred monopoly. What he fails to
4 mention is that the utilities' investment to provide safe and adequate service was a
5 response to the mandate of the Commission for the franchise holder to provide safe and
6 adequate service. The established reputation, goodwill and brand loyalty of an incumbent
7 electric utility is the direct result of its providing regulated monopoly service under
8 quality of service guidelines established in this jurisdiction by the Pennsylvania Public
9 Utility Commission. As I have previously testified; these assets were not obtained by
10 PECO in the competitive marketplace, but were financed virtually entirely by ratepayers.

11 While a franchise monopoly is not necessary for a firm to create a valuable brand
12 name, that fact that the electric utility has the only brand name to which most of the
13 electric customers in the franchise area have been exposed over the last 75 years has been
14 crucial in establishing the utility's brand name in the minds of its customers. In fact, the
15 brand name, goodwill and sales channels of PECO all have been established through the
16 provision of monopoly electric service in its Pennsylvania service territory and paid for
17 by Pennsylvania ratepayers over the past multitude of years. Potential entrants cannot
18 simply overcome, in an advertising blitz, what took the incumbent electric utility almost a
19 century to develop. The day-in and day-out provision of quality electric service for many
20 customers for decades solidifies the position of the incumbent utility in the view of many
21 of its jurisdictional customers. This recognition creates a reluctance in customers to try
22 an alternative provider. This was true in the transition to competition in the
23 telecommunications and gas industries and it will be even more so with regard to the

1 electric industry because of the importance of electric service in today's environment.
2 Moreover, the utility's continued monopoly provision of distribution and transmission
3 service - and its ability to manipulate access to service - will only enhance that incumbent
4 advantage.

5 Mr. Sidak questions whether in theory or practice a particular utility's brand name
6 will necessarily be a net benefit. He also maintains that the practical effect of Section
7 23.10 of Enron's proposed tariff, coupled with my proposed restrictions on PECO's
8 continued use of its brand name, only would be to raise PECO's marketing costs and that
9 consumers would suffer if the PECO brand name were a valuable signal of quality to
10 consumers. While I do agree with Mr. Sidak that brand names can contain valuable
11 information and that through their brand names, firms can signal quality to consumers, I
12 disagree with his implication that PECO's competitive affiliates and customers would be
13 disadvantaged or harmed by the prohibition on the use of the PECO name, logo, service
14 mark, trade mark or trade name.

15 My position does not handicap anyone; rather, it is intended to place all competitors
16 on the same initial footing recognizing that, in reality, PECO has a decided initial
17 advantage resulting from its monopoly position, which it seeks to prolong. It is also
18 necessary to protect electric consumers from the likely confusion that will be created
19 when competitive services are marketed under the EDC name. I recommend that the
20 Commission take actions to ensure the development of a competitive market and protect
21 consumers. It should be reiterated that my concern is what the regulators should do
22 *before* the markets become competitive.

1 Without competitive safeguards and a code of conduct that will effectively deal with
2 the issue of trade name, competition may not survive the transition stage. The transition
3 period is critical for competition to obtain a foothold and nurture itself to the point where
4 it is fully robust.

5 The last basis for Mr. Sidak's conclusion is his perception that my testimony seems
6 to imply that an electricity customer in PECO's service territory has acquired an
7 ownership interest in PECO's brand name by virtue of paying regulated rates for service
8 from that investor owned electric utility. My position is not based on a claim of property
9 interest in the utility name but on the recognition of the special advantage that the
10 incumbent utility will have if it is permitted to keep the benefit of having its affiliated
11 ESP market under the EDC trade name.

12 Another way to view this issue is in the context of stranded costs. PECO did not
13 include any value of the EDC trade name in its determination of its net stranded costs in
14 this proceeding. To the extent that the utility is to recover costs which originated in the
15 monopoly environment, the appropriate regulatory procedure would be to include an
16 offset or mitigation of the gross stranded costs by any additional value associated with the
17 remaining assets used to provide electric service. This includes the value of the brand or
18 trade name of the utility provider. If the affiliates of the EDC are not prohibited from
19 using the EDC's trade name, PECO would: 1) avoid reducing its stranded costs by
20 application of the value of the trade name; and, 2) retain for its competitive affiliates the
21 value of what was developed within its monopoly environment.

1 Q. ON PAGE 8 OF HIS TESTIMONY MR. SIDAK QUOTES FROM A U.S.
2 DEPARTMENT OF ENERGY REPORT REGARDING THE COMPETITIVE
3 EFFECTS OF THE USE OF A PARENT UTILITY'S BRAND NAME, INCLUDING
4 EXCLUSION FROM COMPETITION. PLEASE COMMENT.

5 A. The findings in the report pertain to the perceived effects of utilities marketing products
6 and services into already competitive markets in which the utility: 1) had no monopoly
7 franchise; and, 2) had not participated at all or had participated as one of many sellers
8 (e.g. appliance sales). Those circumstances have very little, if anything, to do with the
9 potential effects of allowing an electric utility affiliate to use the EDC name to market the
10 same product (electricity) in the same service territory while the EDC continues to
11 provide a related monopoly service.

12 Mr. Sidak's use of the above quote suggests that my position is that the Commission
13 should restrict PECO's entry into markets. This is certainly not the case. I am not
14 saying that PECO should not be allowed to compete or that PECO's unregulated
15 generation subsidiary should not be allowed to compete. In fact, it should be allowed to
16 enter any market it wishes. It simply should not be allowed to enter markets where it has
17 provided and continued to provide regulated monopoly service arm in arm with the
18 regulated T&D company resulting in decided advantages to the unregulated activities.

19

20 Q. MR. SIDAK DISAGREES WITH YOUR RECOMMENDATION FOR
21 REQUIRING THAT MONOPOLY AND NON-MONOPOLY ACTIVITIES
22 SHOULD BE AS SEPARATE AS POSSIBLE AND SUGGESTS THE ANTITRUST
23 LAWS AS A "DEFAULT" SAFEGUARD. PLEASE COMMENT.

1 A. Obviously Mr. Sidak and I disagree on this point and I refer the Commission to the well-
2 documented history of abuse by entities who have not had their monopoly and
3 non-monopoly activities adequately separated. With regard to the antitrust laws, reliance
4 on them is problematic. Proving violation of the antitrust laws is a difficult and time-
5 consuming undertaking. It is wrong to suggest that the Commission should rely on
6 reactive after-the-fact means to ensure the development of a competitive market,
7 particularly when it takes years to detect, prosecute and punish anti-competitive behavior.

8

9 **Q. WHAT "CODE OF CONDUCT" IS PECO NOW PROPOSING TO ADHERE TO?**

10 A. PECO now proposes to implement the Code of Conduct (with one addition) that was
11 produced by the "Competitive Safeguards Working Group" ("CSWG") (attached as
12 "BDC-1" to Mr. Crowe's testimony). Mr. Crowe implies that this Code should be
13 adopted because it represents the position of a broad cross section of stakeholders
14 participating in the electric restructuring debate.

15

16 **Q. IS IT CORRECT TO CHARACTERIZE THE "CSWG CODE" IN THIS WAY?**

17 A. Not in my opinion. I understand that Code suggestions produced by CSWG has not been
18 reviewed or approved by the Commission. The Report indicates that the "CSWG Code"
19 will be the subject of a Commission rulemaking. Moreover, the Report indicates that
20 several parties, including Enron and the OCA, dissented from several provisions of the
21 CSWG Code and have urged that additional provisions be added and that certain other
22 provisions need to be strengthened. Accordingly, it is more appropriate to characterize
23 this submission as the "PECO Proposed Code".

1 Q. WHAT ARE YOUR PRINCIPAL CONCERNS ABOUT THE PECO PROPOSED
2 CODE?

3 A. The principal deficiencies of the PECO Proposed Code are as follows:

- 4 • The PECO Proposed Code fails to require that competitive generation and other
5 related services be provided via an affiliate. This is a crucial requirement if the
6 PUC is to have any assurance that the EDC and Electric Generation Supplier
7 ("EGS") will be sufficiently divided so that operations and activities will be separate
8 and customers will recognize the distinction. Even if the competitive operation is
9 through a division, the division must be sufficiently separate and distinct that
10 customers will know that they are dealing with an entity that is not the traditional
11 provider of distribution and transmission. The EDC should be the provider of
12 default service to customers who choose not to choose as well as returning customers
13 (unless some other entity is chosen by the PUC to take on that role).
- 14 • The PECO Proposed Code fails to include meaningful restrictions on joint marketing
15 or promotion by the EDC of its affiliated supplier. While the Code prohibits the
16 EDC from stating or implying that an EGS has an "inherent" advantage it does
17 nothing to limit the EDC from participating in all sorts of joint promotion that other
18 suppliers will not be able to replicate. For example, PECO's proposal would not
19 prohibit an affiliate from allowing an EGS to place a bill stuffer advertising its
20 energy products in the distribution utility's bill for services. Unless all EGS would
21 have a similar opportunity, such an option would provide a significant advantage to
22 the affiliate. Similarly, the Code would not prohibit an EDC from engaging in joint
23 advertising of EDC and EGS products producing confused customers who

1 unintentionally sign up for an EGS product or service without realizing that EGS
2 and the EDC are separate and distinct operations.

3 • The PECO Proposed Code is not specific enough with respect to separation of EDC
4 and EGS activities. The separation should specify requirements for "separate"
5 books, personnel computer systems and other equipment. The ability to have access
6 to a "proprietary" customer record or billing system (access to which for other
7 suppliers might be extremely costly or impossible) could be a huge advantage for the
8 affiliated EGS.

9 • The PECO Proposed Code should require that the EDC and EGS costs must be
10 separately identified or kept in separate books. The Code produced by the CSWG
11 does not address this issue.

12 • The PECO Proposed Code does not include any provision for limiting the use of the
13 EDC name or logo in advertising and marketing. As I explained in different parts
14 of my earlier testimony, as well as in this testimony, this is an important provision
15 for any effective Code if customer confusion is to be minimized.

16 • The dispute resolution procedure needs to be more specific including a specific
17 process whereby all complaints (and the EDC's response) are logged and made
18 public.

- 1 • Other provisions of the PECO Proposed Code are too limiting in the conduct it
- 2 purports to prohibit:
- 3 (1) Paragraph A only prohibits giving a preference or advantage "in processing a
- 4 request by a distribution company customers for retail generation supply
- 5 service."
- 6 (2) Paragraph E prohibits only "illegal" tying arrangements, implying that the
- 7 Commission might need to make a finding that some tying arrangement
- 8 actually violates that antitrust laws, rather than simply being able to conclude
- 9 that the arrangement is unreasonable.

10

11 **Q. WHAT APPROACH SHOULD THE PUC TAKE IN DEALING WITH THE**
12 **CODES OF CONDUCT PROPOSED IN THIS PROCEEDING?**

13 A. The Commission should not adopt the CSWG Code as written for application to PECO.
14 It simply does not go far enough. In other areas the provisions are vague and hard to
15 reconcile in several key areas, as I have outlined. The Enron Code of Conduct proposed
16 as part of the Choice Plan, on the other hand, is a comprehensive package of provisions
17 that could be used to establish the relationship between an EDC and an affiliated EGS in a
18 fair way and, as such, is a reasonable alternative for PECO.

19

20 **Q. DOES THIS CONCLUDE YOUR PREFILED REBUTTAL TESTIMONY?**

21 A. Yes, it does.