

APPEARANCES (Continued):

CRAIG R. BURGRAFF, Esquire
JAMES A. MULLINS, Esquire
1425 Strawberry Square
Harrisburg, Pennsylvania 17120
(For Office of Consumer Advocate)

KAREN OILL MOURY, Esquire
Assistant Small Business Advocate
Suite 1102, Commerce Building
300 North Second Street
Harrisburg, Pennsylvania 17101
(For Office of Small Business Advocate)

DAVID A. McCORMICK, Esquire
901 North Stuart Street, Room 713
Arlington, Virginia 22203-1837
(For U.S. Department of Defense)

USHER FOGEL, Esquire
One Columbia Place
Albany, New York 12207
(For Pennsylvania Petroleum Association and
Pennsylvania Plumbing, Heating and Cooling
Council, Inc.)

DEBORAH SWANSTROM, Esquire
901 Fifteenth Street, NW
Washington, D.C. 20005
(For Allegheny Power, d/b/a West Penn Power
Company)

MARY McFALL HOPPER, Esquire
2301 Market Street
Philadelphia, Pennsylvania 19101
(For PECO Energy Company)

TERRENCE J. FITZPATRICK, Esquire
Ryan, Russell, Ogden & Seltzer
800 North Third Street, Suite 101
Harrisburg, Pennsylvania 17102
(For GPU Energy)

Commonwealth Reporting Company, Inc.

700 Lisburn Road
Camp Hill, Pennsylvania 17011

APPEARANCES (Continued):

SCOTT J. RUBIN, Esquire
 3 Lost Creek Drive
 Selinsgrove, Pennsylvania 17870
 (For International Brotherhood of
 Electrical Workers, Local 1600)

JOHN J. ALZAMORA, Esquire
 Thomas, Thomas, Armstrong & Niesen
 P. O. Box 9500
 Harrisburg, Pennsylvania 17108
 (For Allegheny Electric Cooperative, Inc.)

RICHARD L. CAPLAN, Esquire
 STEPHEN M. HLADIK, Esquire
 Caplan & Luker
 40 Darby Road
 Paoli, Pennsylvania 19301
 (For Schuylkill Energy Resources, Inc.
 and Gilberton Power Company)

FRED ZALCMAN, Esquire
 ALAN J. BARAK, Esquire
 1417 Blue Mountain Parkway
 Harrisburg, Pennsylvania 17112
 (For Environmentalists)

WILLIAM HAWKE, Esquire
 TODD S. STEWART, Esquire
 Malatesta, Hawke & McKeon
 100 North Tenth Street
 P. O. Box 1778
 Harrisburg, Pennsylvania 17105
 (For Mid-Atlantic Power Supply Association)

DAVID M. KLEPPINGER, Esquire
 PAMELA C. POLACEK, Esquire
 McNees, Wallace & Nurick
 P.O. Box 1166
 Harrisburg, Pennsylvania 17108-1166
 (For PP&L Industrial Customer Alliance)

Commonwealth Reporting Company, Inc.

700 Lisburn Road
 Camp Hill, Pennsylvania 17011

APPEARANCES (Continued):

ALAN KOHLER, Esquire
ROBERT LONGWELL, Esquire
Wolf, Block, Schorr & Solis-Cohen
305 North Front Street, Suite 401
Harrisburg, Pennsylvania 17102
(For Enron Capital & Trade Resources, Inc.)

CRAIG A. DOLL, Esquire
214 State Street
Harrisburg, Pennsylvania 17101
(For Delmarva Power & Light Company
D/B/A Connectiv Energy)

ETHAN HALBERSTADT, Esquire
367 South Gulph Road
King of Prussia, Pennsylvania 19406
(For Quaker Oats Company and
Mount Joy Wire Corp.)

FREDERICK D. OCHSENHIRT, Esquire
Dilworth, Paxson, Kalish & Kauffman
305 North Front Street
Harrisburg, Pennsylvania 17101
(For American Association of Retired Persons)

JOHN P. LAVELLE, JR., Esquire
Hangley Aronchick
One Logan Square
Philadelphia, Pennsylvania 19103
(For New Energy Ventures)

Commonwealth Reporting Company, Inc.

700 Lisburn Road
Camp Hill, Pennsylvania 17011

C O N T E N T S

<u>WITNESSES</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>
Joseph P. Kalt				
By Mr. Kaplan	429	--	547	--
By Mr. Kohler	--	445	--	--
By Mr. Stewart	--	471	--	--
By Mr. Fogel	--	474	--	--
By Mr. Kleppinger	--	484	--	--
By Mr. Zalzman	--	493	--	--
By Mr. Caplan	--	515	--	--
By Mr. Rubin	--	545	--	--
 Robert M. Geneczko				
By Mr. Kaplan	551	--	587	--
By Mr. Kohler	--	555	--	--
By Mr. Stewart	--	566	--	--
By Mr. Fogel	--	567	--	--
By Mr. Caplan	--	576	--	--
By Mr. Mullins	--	580	--	--
 John Mayo				
By Mr. Kohler	588	--	638	--
By Mr. Rubin	--	591	--	--
By Mr. Kaplan	--	610	--	--

E X H I B I T S

<u>NUMBER</u>	<u>FOR IDENTIFICATION</u>	<u>IN EVIDENCE</u>
<u>PP&L Statements</u>		
19 ✓ No. 1 (J.P. Kalt)	430	550
20 ✓ No. 1-R (J.P. Kalt)	430	550
21 No. 13 (R.M. Geneczko)	552	588
22 ✓ No. 13-R (R.M. Geneczko)	552	588

FORM 2

E X H I B I T S (Continued)

2	<u>NUMBER</u>	<u>FOR IDENTIFICATION</u>	<u>IN EVIDENCE</u>
3	<u>PP&L Exhibits</u>		
4	✓ No. 1 (statement of reasons) ✓	417	417
5	✓ No. 2 (responses to filing requirements) ✓	417	417
6	✓ No. JPK-1 (J.P. Kalt) ✓	430	550
8	✓ No. JPK-2 (J.P. Kalt) ✓	430	550
9	Nos. RMG-1 through 4 (R.M. Geneczko)	552	588
10	<u>PP&L Cross Examination Exhibits</u>		
11	✓ No. 1 (PP&L-Enron-29) ✓	612	612
12	✓ No. 2 (PP&L-Enron-7) ✓	612	612
13	✓ No. 3 (PP&L-Enron-4) ✓	612	612
14	✓ No. 4 (PP&L-Enron-30) ✓	612	612
15	✓ No. 5 (PP&L-Enron-17) ✓	621	621
16	<u>Environmentalists Cross Examination Exhibits</u>		
17	✓ No. 1 (excerpt, "Reestablishing the Regulatory Bargain in the Electric Utility Industry") ✓	501	515
20	<u>Enron Cross Examination Exhibits</u>		
21	✓ No. 1 (Enron III-16) ✓	466	514
22	✓ No. 2 (Chapter 6 from Economic Report to President) ✓	468	514

E X H I B I T S (Continued)

<u>NUMBER</u>	<u>FOR IDENTIFICATION</u>	<u>IN EVIDENCE</u>
<u>Enron Statements</u>		
No. 2 (J. Mayo)	590	639
No. 2.1 (J. Mayo)	590	639
<u>IBEW Cross Examination Exhibits</u>		
No. 1 (MAPSA-JPK-2)	545	546

NOTE: The Afternoon Session begins on page 493

Any reproduction of this transcript
is prohibited without authorization
by the certifying reporter.

1 counsel an opportunity to address the record before we
2 start, my first concern is, I believe it was, Thursday or
3 Friday, I sent out a list of what I felt were the grouping
4 of the parties as I visualize your interests in this
5 particular matter. And along that line I also designated
6 lead counsel for each particular group in those interest
7 groups. I've had a rash of objections to that particular
8 proceeding, and by and large, I will say a pox on the rash.

9 (Laughter.)

10 The concept is well established at the federal level
11 and before FERC where there is a multiplicity of parties of
12 the assignment of the counsel.

13 I, in fact, understand some of the concerns that have
14 been expressed individually by counsel relating to conflict
15 of interest with other parties in their particular group.
16 And that's my fault then for putting you in a particular
17 group.

18 Secondly, some of the more mundane concerns about
19 fees and things like that, I'm not too sure I'm all that
20 concerned about that. That's something that I always leave
21 to counsel, and I'm sure they can all work that out.

22 However, with the concerns of counsel in mind, with
23 the idea that this proceeding is going to be kept as simple
24 as possible, I am still going to pursue the idea of lead
25 counsel much more in the sense of a coordinator than as a

1 be-all, end-all take over the proceeding for the entire
2 particular group.

3 So the people who have been designated as lead
4 counsel on that fax that I sent out, other than for
5 Mr. Hawke, Mr. Hawke called and said that he was unable to
6 perform that particular duty, and so I have nominated and
7 designated Mr. Kohler.

8 What we will do is attempt to get through the cross
9 examination as best we can with the lead counsel
10 coordinating the efforts of everyone to make sure that we're
11 going to stay on time.

12 There will be no duplicative questioning. If you've
13 got some burning issue that pertains to your particular
14 client, we're going to go ahead with it. But we're not
15 going to get bogged down with it.

16 I expect that we're going to be here five hours a
17 day. And one of lead counsel's function is going to be to
18 make sure that, in fact, that particular group of his that
19 is doing cross examination that day is, in fact, going to
20 stay on time with it.

21 If, in fact, anybody has further questions that they
22 would like to take a look at on the concept of lead counsel,
23 I would refer them to Judge Benkin, Isaac D. Benkin. He's
24 an administrative law judge with Federal Energy Commission,
25 and the Law Review article at the Harvard Law School, as far

1 as appointment of lead counsel where there are a
2 multiplicity of parties.

3 Be that as it may, there is one outstanding matter
4 that was not taken care of in that order. There were two
5 petitions that were filed, one by Mount Joy, and the second
6 by Quaker Oaks. Those petitions were petitions to join as
7 parties certain intervenors in this particular matter, and
8 essentially then went ahead and filed for requests for
9 admissions, and we've had motions to compel, etcetera,
10 etcetera. And unfortunately, their horse ran away. The two
11 parties that they were attempting to join, that being Metal
12 Industries and Caradon Mideast Aluminum, filed a petition
13 with me on Friday, I believe it was, Thursday or Friday, to
14 withdraw their petition to intervene, with prejudice.

15 I granted that petition. Having granted the
16 petition, there is nothing for Quaker Oats and Mount Joy to
17 join to. And therefore their petitions are going to be
18 denied as moot. The petition to join being denied as moot,
19 their requests for admissions, etcetera, etcetera, are not
20 necessary to even go to.

21 Yes, sir.

22 MR. HALBERSTADT: Good morning, Your Honor. My name
23 is Ethan Halberstadt. I'm here today on behalf of Mount Joy
24 and Quaker Oats Company.

25 May I be heard briefly with respect to that issue?

1 JUDGE KASHI: Very briefly.

2 MR. HALBERSTADT: Your Honor, the petitions to join
3 included as an alternative as a petition to intervene, as
4 well. And we feel that in order to protect their rights,
5 they need to be parties to this proceeding. The relief was
6 and/or; and join as a party, or to intervene in their own
7 right.

8 JUDGE KASHI: Then they're untimely.

9 MR. HALBERSTADT: Would Your Honor consider a motion
10 for reconsideration with respect to that?

11 JUDGE KASHI: Yes, please. And you can set it forth
12 in writing.

13 MR. HALBERSTADT: Thank you, Your Honor.

14 JUDGE KASHI: All right. Shall we hear from counsel
15 this morning?

16 Mr. Russell?

17 MR. RUSSELL: Thank you, Your Honor.

18 Basically I have three or four housekeeping matters
19 I'd like to address before we begin with the witnesses. The
20 first is a suggestion, Your Honor, that in order to save
21 hearing time that we agree to stipulate to the foundation
22 for written testimony right today, and rather than ask each
23 witness to go through the litany of did he or she prepare
24 the testimony, is it true and accurate, etcetera, that we
25 would all be willing to stipulate that the testimony is

1 proper and has a proper foundation.

2 I have not had an opportunity to discuss this
3 suggestion with other counsel, so I'm not aware of whether
4 there's objection.

5 JUDGE KASHI: Can we ask if there is objection by
6 counsel to that particular stipulation?

7 MR. BURGRAFF: We have no objection, Your Honor.

8 JUDGE KASHI: Does anyone have an objection to
9 waiving questions regarding foundation of testimony?

10 (No audible response.)

11 JUDGE KASHI: Hearing none, we will note that counsel
12 have agreed and stipulated to foundation of testimony.

13 MR. RUSSELL: Thank you, Your Honor.

14 The second thing I have, we have prepared over the
15 last two weeks a schedule of witnesses in a matrix of
16 anticipated cross examination. The most recent version of
17 that was sent out to all the parties by fax on Friday. I
18 have extra copies here if there are any counsel, or the
19 reporter, who need copies.

20 In that vein, Your Honor, as we look at the matrix,
21 it appears to us that no one has identified cross
22 examination for four witnesses; Mr. Rooney on behalf of
23 PLICA, Mr. Schneider on behalf of PLICA, Mr. Tabor on behalf
24 of Enron, and Mr. Coles on behalf of Enron. The company has
25 no cross for these witnesses.

1 The second change to the schedule, or what we've
2 noticed on the schedule, the company had indicated it had
3 brief cross examination for Mr. Bradford, sponsored by the
4 environmentalists, and Mr. Prisco, sponsored by the army.

5 After further review, we have decided we do not have
6 cross for either of those witnesses. So at least from the
7 company's perspective, the six witnesses that I've
8 identified do not need to appear at the hearings, and their
9 testimony could be moved in by counsel.

10 JUDGE KASHI: Can you go through that list one more
11 time, please?

12 MR. RUSSELL: Yes, sir. Mr. Rooney, who is a witness
13 sponsored by PLICA.

14 JUDGE KASHI: Right.

15 MR. RUSSELL: Mr. Schneider, also of PLICA;
16 Mr. Tabor, a witness sponsored by Enron; Mr. Coles, also
17 Enron; Mr. Bradford, the environmentalists; and Mr. Prisco,
18 the army.

19 JUDGE KASHI: The last one, sir, was?

20 MR. RUSSELL: Mr. Prisco, for the army. I think he
21 is -- let me see where he is on the schedule.

22 JUDGE KASHI: I may be looking at a different list.
23 I'm looking at an August 5th matrix.

24 (Pause.)

25 JUDGE KASHI: All right, he was an intervenor, and

1 his testimony was filed on the stranded calculation issue;
2 yes?

3 MR. RUSSELL: Mr. Prisco?

4 JUDGE KASHI: Yes.

5 MR. RUSSELL: Yes.

6 JUDGE KASHI: All right. Are there any counsel who,
7 in fact, having heard those witnesses, and having perhaps
8 not responded as were requested to whether or not you had
9 cross examination of those people, is there anyone here who,
10 in fact, would have cross examination for any of those
11 witnesses?

12 MR. RUBIN: Your Honor?

13 JUDGE KASHI: Yes, Mr. Rubin.

14 MR. RUBIN: I don't have cross for those witnesses,
15 but there's one more I think we can add to that list. And
16 that is Ms. Day, who filed testimony on behalf of New Energy
17 Ventures. I had indicated I would have cross examination
18 for her, but I do not. And I think I was the only party
19 that indicated cross for her. She was scheduled on the
20 28th.

21 MR. RUSSELL: Your Honor, actually, we had been
22 notified by counsel that Ms. Day was out of the country and
23 not available to appear, and that her testimony would be
24 adopted by Mr. Boonin.

25 But Mr. Rubin is correct, there is no cross shown for

1 Ms. Day either.

2 JUDGE KASHI: Okay.

3 Now, would it be by stipulation that the parties will
4 agree that that testimony will come in, and therefore the
5 witnesses need not show?

6 MR. RUSSELL: That would be our proposal, Your Honor.

7 JUDGE KASHI: Is there any disagreement with that
8 stipulation?

9 (No audible response.)

10 JUDGE KASHI: Hearing none, the witnesses that have
11 been named will be excused, their testimony will be, in
12 fact, admitted by stipulation.

13 Next, Mr. Russell?

14 MR. RUSSELL: Just two more items, Your Honor.

15 Next, I would like to request that as witnesses
16 appear for the intervenor groups and are cross-examined,
17 that PP&L have an opportunity to cross last; that the other
18 parties cross first, and then we would do our cross
19 examination at the end of the cycle. And I wanted to raise
20 that up front and have it discussed and resolved.

21 JUDGE KASHI: Mr. Simms?

22 MR. SIMMS: I have no objection to that.

23 JUDGE KASHI: Does any other counsel have any
24 objection to that?

25 MR. BURGRAFF: We don't, Your Honor.

1 JUDGE KASHI: Hearing no objections, we'll let you
2 cross last, Mr. Russell.

3 MR. RUSSELL: Thank you, Your Honor.

4 And my final item is the mechanics of introducing our
5 filing for the record. Do you want me to do that now or
6 wait to hear from other counsel and do that just before we
7 begin the witnesses?

8 JUDGE KASHI: Why don't we do that now since we've
9 got you on your feet, and get it done.

10 MR. RUSSELL: Okay.

11 Your Honor, PP&L's filing in this case consists of in
12 the first instance of two exhibits that have been pre-
13 identified and pre-marked. The first is PP&L Exhibit No. 1,
14 which is in a blue book, which is the company's statement of
15 reasons in the filing.

16 PP&L Exhibit No. 2 is in green volumes, four volumes.
17 And those are the company's responses to the Commission's
18 filing requirements.

19 Beyond those two exhibits, the remainder of the
20 filing consists of the direct testimony of PP&L's witnesses
21 and the exhibits that accompany that testimony.

22 What I would propose, Your Honor, is that the
23 testimony and the exhibits that accompany the testimony
24 would be identified and moved as the witnesses appear.

25 What I would like to request at this time is that

1 PP&L Exhibit No. 1 and PP&L Exhibit No. 2 be identified and
2 admitted into the record, subject to cross.

3 JUDGE KASHI: That which has been identified will be
4 marked for identification as Exhibit No. 1 and Exhibit No.
5 2; and that which has been so identified will be received
6 into the evidentiary record, subject to any timely motions
7 and/or objections pending cross examination.

8 (Whereupon, the documents were marked
9 as PP&L Exhibit Nos. 1 and 2 for
10 identification and received in evidence.)

11 MR. RUSSELL: Thank you. And we have also made two
12 copies of the filing available to the court reporter, Your
13 Honor.

14 JUDGE KASHI: Thank you.

15 MR. RUSSELL: And that's all I have.

16 JUDGE KASHI: Mr. Kohler.

17 MR. KOHLER: Yes, Your Honor.

18 JUDGE KASHI: Do you have anything that you would
19 like to at this time state either on behalf of Enron or on
20 behalf of the alternative suppliers?

21 MR. KOHLER: No, Your Honor. And I would turn to
22 anyone who's in my group. As I understand, the
23 modifications in your original memo, just to clarify, Your
24 Honor, that the lead counsel will essentially be the
25 timekeeper for the group; is that a fair summary?

1 JUDGE KASHI: That's a fair summary.

2 MR. KOHLER: And that comprises the objection as part
3 of the matrix?

4 JUDGE KASHI: Yes.

5 Ms. Hopper?

6 MS. HOPPER: My name is Mary McFall Hopper, I'm
7 attorney for PECO Energy Company and as the coordinator for
8 the electric distributor.

9 JUDGE KASHI: Okay.

10 Mr. Rubin?

11 MR. RUBIN: Nothing to add, Your Honor.

12 JUDGE KASHI: Mr. Kleppinger?

13 MR. KLEPPINGER: Just so I'm understanding the
14 modification of the memo, are you suggesting that the lead
15 counsel do the initial cross, and if there are areas not
16 covered, that the other members in the group could ask other
17 questions?

18 JUDGE KASHI: If, in fact, someone in the group feels
19 that there is something so particular that lead counsel has
20 not covered, or is so proprietary that he hasn't shared the
21 information with lead counsel, or something to that effect,
22 we will hear from that counsel. But I want to hear from
23 lead counsel.

24 MR. KLEPPINGER: All right.

25 JUDGE KASHI: Is there anything that you would like

1 to add?

2 MR. KLEPPINGER: I believe one of the members of my
3 group would like to speak.

4 JUDGE KASHI: Mr. McCormick?

5 MR. McCORMICK: Yes, Your Honor. Two items. One, on
6 the stipulated testimony, are we to furnish two copies to
7 the court reporter?

8 JUDGE KASHI: Yes, sir.

9 MR. McCORMICK: Secondly, on the issue of the
10 determination as to lead counsel and so on, I do have a
11 brief comment that I did want to put in the record, if I
12 could.

13 JUDGE KASHI: Certainly.

14 MR. McCORMICK: While I have very little, if any,
15 cross examination, and so on, and it appears that the
16 parties are not going to cross-examine my witness, so that
17 my role is not large, at least at the moment, I have been
18 instructed that the Department of Defense and federal
19 executive agency is not insensitive to the timing structure,
20 facing the Judge with a large number of parties and
21 witnesses.

22 However, we did make an effort to correspond with the
23 other parties on this issue on July 18th and July 21st, and
24 so on, expressing our views, citing for the benefit of the
25 other parties a case entitled United States vs. the Maryland

1 Public Service Commission, at 422 Fed Supplement, page 676.

2 DOD has also endeavored to work with the other
3 parties, or at least to the extent we can, we were a party
4 to the pilot program settlement in another related docket,
5 which is being contested by some of the other parties.

6 DOD did mention in its intervention petition that it
7 was opposed to grouping. And generally speaking, it is.
8 But we are ceding to Your Honor's approach to this, and
9 especially as has been clarified in your discourse with
10 Mr. Kleppinger this morning, and so on, and we will continue
11 to work within those boundaries.

12 Also, I wanted to point out that while the, I guess,
13 Pennsylvania statutory parties were not grouped, the federal
14 statute under which I appear here is probably another
15 statute that might come into consideration at some future
16 point in time.

17 That's all I had, Your Honor. We will try and work
18 with the parties and keep things moving.

19 JUDGE KASHI: Can you, for the record, state what the
20 holding is in U.S. vs. Maryland Public Service Commission at
21 422 Fed sub, 676? Or do I have to send someone out to get
22 it?

23 MR. McCORMICK: Oh. Well, that was a case in which
24 the Maryland Public Service Commission sought to limit the
25 cross examination by the Federal Government of some

1 witnesses in a proceeding before the Maryland Public Service
2 Commission. And the federal court, in a different circuit
3 -- this is the third circuit, that's the fourth circuit --
4 decided that that was probably something that could be
5 enjoined, and so on, because it may have violated the due
6 process rights of the Federal Government, because the
7 commission was probably acting as not in its legislative
8 function, as a rulemaking, but in a judicial type of
9 function, because it was case that affected cost recovery
10 rates and that sort of thing.

11 JUDGE KASHI: You understand that I am in no way, by
12 designating lead counsel, attempting to limit the cross
13 examination.

14 MR. McCORMICK: That certainly is my understanding
15 with your discourse with Mr. Kleppinger this morning.

16 JUDGE KASHI: I'm attempting to make it run
17 smoothly --

18 MR. McCORMICK: Yes, sir.

19 JUDGE KASHI: -- and produce a transcript that will
20 be simpler than if we have 36 lawyers asking questions.

21 MR. McCORMICK: Yes, sir; yes, sir.

22 JUDGE KASHI: Okay?

23 MR. McCORMICK: And then we are acceding to your
24 purpose.

25 JUDGE KASHI: Thank you, sir.

1 Mr. Kaplan?

2 MR. KAPLAN: Yes, sir. I have nothing to add for
3 clarification. Certainly I think it makes my role clear,
4 and I will abide by it.

5 JUDGE KASHI: Is Ms. Smith here?

6 MR. OCHSENHIRT: Your Honor, Fred Ochsenhirt. I'm
7 here for Linda Smith. We have nothing further to add; and
8 your comments addressed many of the concerns of AARP.

9 The only thing I would like to take the opportunity
10 to deliver the original letter that was faxed to you on
11 Friday.

12 JUDGE KASHI: I have it.

13 MR. OCHSENHIRT: You have the fax, I have the
14 original, if you want it. It doesn't really matter.

15 JUDGE KASHI: Well, you can drop it at my office.

16 MR. OCHSENHIRT: All right.

17 JUDGE KASHI: So Ms. Smith decided she's not coming?

18 MR. OCHSENHIRT: Oh, she had another appointment this
19 morning.

20 JUDGE KASHI: Oh, okay. I'm glad to hear that.

21 Ms. Simms?

22 MR. SIMMS: Just one item, Your Honor. There had
23 been some communication from the company's counsel as to
24 whether or not all the parties would present their testimony
25 and exhibits into the record this morning. I didn't know

1 whether or not that is your pleasure, or just have it done
2 at the time that we present the individual witnesses. The
3 court reporter may not like all that testimony at once.

4 JUDGE KASHI: I think that we probably may be better
5 off with the individual witnesses.

6 MR. RUSSELL: Okay. Thank you.

7 JUDGE KASHI: Mr. Burgraff?

8 MR. BURGRAFF: We have nothing further, Your Honor.

9 JUDGE KASHI: And Ms. Moury?

10 MS. MOURY: I have nothing further, Your Honor.

11 JUDGE KASHI: Is there any counsel that's missed?

12 Mr. Barak?

13 MR. BARAK: I thought I had been given an honor, and
14 now I've been ignored, I feel awful about it.

15 (Laughter.)

16 MR. BARAK: I have three brief things to say.

17 JUDGE KASHI: It's just the bifocals, Mr. Barak.

18 (Laughter.)

19 MR. BARAK: For the record, we have to enter an
20 objection as to our being designated lead counsel. Although
21 I understand everything you said today, we will do our best
22 to carry out the administrative, and I underline
23 administrative, tasks that you've given us.

24 I must say that we have not gotten together with this
25 diverse group, again on an administrative basis, or any

1 other, to find out what it is they want to ask any
2 particular witness. That would be an enormous task.

3 JUDGE KASHI: You would agree with me, sir, that I
4 mentioned this from the very first prehearing conference;
5 have I not?

6 MR. BARAK: Your Honor, you did. And I --

7 JUDGE KASHI: You didn't believe me; is that it?

8 (Laughter.)

9 JUDGE KASHI: Or was it just too much work to get
10 together?

11 MR. BARAK: No. Candidly, well, there are a couple
12 of reasons, Your Honor. One is, this Commission, not you,
13 this Commission has set out an enormous amount of work for
14 all the parties in this case. For instance, I think I know
15 why Ms. Smith is not here today, because it involves another
16 case which is extraordinarily important and precedent
17 sitting. And everybody here, it's just amazing that they're
18 in this room today, because they're all involved in a number
19 of other proceedings. A number of other proceedings.

20 So, we're all very sensitive to this, we've all
21 done our best to try to comply with your needs for this
22 case, as the administrative law judge. And by entering an
23 objection, I'm not trying to argue with you. I'm simply
24 preserving our rights on the record, because I haven't the
25 faintest idea of what will happen down the road with respect

1 to our interests and, again, your needs, as you've expressed
2 them, for this case.

3 But we heard the first time, and we hear you again.
4 And we were very concerned that, as Mr. McCormick stated,
5 there might be some effort in this agency's attempt to move
6 things smoothly that would have interfered with what we
7 consider our rights to due process.

8 I don't see that today, and I'm hoping that doesn't
9 happen. But I need to enter the objection for the record.

10 JUDGE KASHI: All right. I can assure that the due
11 process rights of each and every individual party will be
12 fully coordinated, and the concept of lead counsel and the
13 asking of questions by someone else does not violate those
14 rights.

15 Mr. Kohler?

16 MR. KOHLER: Your Honor, one point of clarification,
17 if I could, for Mr. Russell, if possible. I believe in
18 informal discussions, and since we're working off this
19 matrix, that's kind of the organizational structure for the
20 whole hearing. Most of the parties have responded, but not
21 all of the parties have responded.

22 Could he just identify essentially who responded, and
23 if we could check to see -- or perhaps Your Honor could
24 direct them that the parties that haven't responded, to
25 respond, so at least the designated counsel can know who

1 they have to keep in mind.

2 JUDGE KASHI: I'm looking at, what, the August 15th?

3 MR. RUSSELL: The August 15th letter, Your Honor.

4 And it has attached to it a matrix that shows the witnesses
5 down in the left-hand column, and the parties across the
6 top.

7 JUDGE KASHI: Do we know who has not yet responded to
8 this?

9 MR. RUSSELL: Basically, the best way to identify who
10 hasn't responded is to work across and find columns where
11 there's no --

12 JUDGE KASHI: Entry whatsoever.

13 MR. RUSSELL: -- information whatsoever. And just
14 looking at it quickly, it appears that we have not heard
15 from AARP, it appears we haven't heard from -- okay, I
16 apologize, I was wrong. We have heard; AARP has brief
17 cross.

18 And then you get towards the right-hand side of the
19 chart, and it appears that those parties have not responded.
20 But again, they have not been active parties up to this
21 point, and I guess it would be my expectation that there
22 would not be a lot of cross, if any, from the parties over
23 to that side of the chart.

24 JUDGE KASHI: All right. And this I'll direct you
25 from the Bench that all those parties who have not

1 responded, they will respond, and they will respond by the
2 close of business.

3 Do you have extra copies of that, sir?

4 MR. RUSSELL: Yes, I do.

5 JUDGE KASHI: Mr. Russell has extra copies of that.
6 If you need them, you can pick them up. And let's get it
7 in. It's going to make the job of coordinating counsel a
8 lot easier.

9 MR. OCHSENHIRT: Your Honor?

10 JUDGE KASHI: Sir?

11 MR. OCHSENHIRT: If I may clarify for the purposes of
12 the statement just made, AARP has said from the time we
13 filed out intervention that we do not intend to cross-
14 examine witnesses. So, I think the statement we've made now
15 is that we might be planning brief cross examination. I
16 just wanted to clarify that for the record.

17 JUDGE KASHI: And that fits in with Ms. Smith's
18 three-page document on the denial of due process? What am I
19 missing here?

20 MR. OCHSENHIRT: Well, we just wanted to put some
21 concerns in the record with the letter regarding due
22 process. And it does state in that letter that we didn't
23 intend to cross-examine anybody.

24 JUDGE KASHI: I understand that.

25 MR. BARAK: I had three points, Your Honor.

1 (Laughter.)

2 JUDGE KASHI: Sir?

3 MR. BARAK: The second point, just again for the
4 record, we make the same request in this case on behalf of
5 the environmentalists that I made on behalf of my clients in
6 the last PP&L rate case, that is for transcripts to be
7 provided by the Commission at the cost of reproduction. I
8 don't expect to argue with anybody about that here today,
9 it's up at the appellate courts. But for the record, Your
10 Honor, I would like to note that we do make that request.

11 And finally, I get to hand off first chair in this
12 case for the environmentalists to Mr. Zalzman, who is here
13 pro hoc vice. And the two of us are working closely. He
14 has primary responsibility for this case.

15 As I said, there are a number of cases every party
16 has here, and administratively, the way we have determined
17 with our group, which is a number of parties, is Mr. Zalzman
18 have first chair and primary responsibility for this case.

19 Thank you.

20 JUDGE KASHI: And in handing off to Mr. Zalzman, are
21 you going to still remain the coordinator, to make sure that
22 that group stays on time?

23 MR. BARAK: My sense is that you probably will
24 require me to remain the coordinator.

25 JUDGE KASHI: You got it.

1 (Laughter.)

2 JUDGE KASHI: All right.

3 Now, having heard from the folks who were nominated
4 and designated by myself as lead counsel and coordinators,
5 are there any counsel here today who feel the need to
6 address me this morning before we begin cross examination?

7 (No audible response.)

8 JUDGE KASHI: Seeing none, we will call the first
9 witness. Thank you very much.

10 Mr. Russell.

11 MR. KAPLAN: Mr. Kaplan, Your Honor.

12 JUDGE KASHI: Oh, Mr. Kaplan.

13 MR. KAPLAN: Thank you, Your Honor.

14 Pennsylvania Power & Light Company calls
15 Dr. Joseph P. Kalt.

16 **Whereupon,**

17 **JOSEPH P. KALT**

18 **having been duly sworn, testified as follows:**

19 **DIRECT EXAMINATION**

20 BY MR. KAPLAN:

21 Q. In light of our new procedure, Dr. Kalt, I simply
22 want to identify for the record first your prepared direct
23 testimony, PP&L Statement No. 1, a statement of 31 pages;
24 your JPK Exhibit No. 1, which is your curriculum vitae; PP&L
25 Statement No. 1R, which is your rebuttal testimony; your

1 statement of 69 pages and your rebuttal exhibit, JPK-, we
2 will designate that 2

3 JUDGE KASHI: They'll all be marked for purposes of
4 identification.

5 (Whereupon, the documents were marked
6 as PP&L Statement No. 1, PP&L Exhibit
7 No. JPK-1, PP&L Statement No. 1R, PP&L
8 Exhibit No. JPK-2 for identification.)

9 DIRECT EXAMINATION

10 BY MR. KAPLAN:

11 Q. Dr. Kalt, do you have any corrections or
12 additions to that testimony?

13 A. Just very briefly, several typographical errors
14 I'll just read into the record quickly.

15 In the rebuttal testimony, Statement No. 1R, at page
16 32, line 8, the word "of" should be "or".

17 On page 46, line 6, where it says "Professor Mayo
18 Thale", it should say "Mr. Dirmeier sales".

19 On page 48, line 12, there should be a right
20 parenthesis after the word "bawalts".

21 And on page 63, line 9, the word "direct" should be
22 "rebuttal", and the number "10" should be "3".

23 MR. KAPLAN: Your Honor, with those corrections,
24 and with the foundation laid by agreement, PP&L moves into
25 the record the direct and rebuttal testimony of

1 Dr. Joseph P. Kalt, and Exhibits JPK-1 and 2.

2 JUDGE KASHI: Subject to any timely motions and/or
3 objections pending the cross examination of that which has
4 been previously identified, it will be received into the
5 evidentiary record.

6 MR. KAPLAN: Your Honor, we have brief oral rejoinder
7 examination, direct examination, for Dr. Kalt.

8 JUDGE KASHI: Go ahead.

9 MR. KAPLAN: Thank you, Your Honor.

10 BY MR. KAPLAN:

11 Q. Dr. Kalt, have you read the surrebuttal testimony
12 of Messrs. Mayo, Dirmeier and Dirmeier concerning the
13 procedures and requirements for establishing a competitive
14 market for the generation of electricity?

15 A. Yes, I have.

16 Q. Do you have a response to that testimony, sir?

17 A. Yes. By way of overview, I put the testimony in
18 the following context: The parties are engaged here in
19 trying to design policy which will allow competition to
20 flourish in the supply of electricity in Pennsylvania.

21 And if you strip away the huff and puff that
22 witnesses engage in, I think that the debate on competition
23 policy boils down to a discussion of essentially how far,
24 how intense, how extensive is the regulatory reach
25 appropriately applied in setting forth a framework that will

1 allow competition to flourish.

2 I think that the proper framework is one that
3 recognizes that we are embarking on a system that will
4 deregulate or open to competition significant parts of the
5 industry in Pennsylvania, in particular the supply marketing
6 of electric power.

7 Meanwhile, certain significant components of the
8 industry will remain regulated, particularly transmission
9 and distribution, the so-called natural monopoly functions.

10 I think that the right framework for policy in this
11 context is to recognize that the crucial step for policy to
12 take, for the regulator to take, is to prevent the extension
13 of monopoly power from the continuing monopoly functions in
14 particular, the essential facilities of transmission and
15 distribution.

16 To prevent the extension of monopoly power from those
17 facilities into the non-monopoly functions that are being
18 opened up to competition, I think that we see in the
19 testimony and the surrebuttal testimony of a number of the
20 parties a slightly different view, which takes the view that
21 rather than simply or straightforwardly and aggressively
22 trying to block this extension of monopoly or the non-
23 monopoly functions, policy should take the step, at least
24 during the transition period according to some of the
25 witnesses, of handicapping or otherwise limiting advantages

1 that it sees the incumbent utility as having.

2 When those advantages are pro-consumer and do not
3 arise from the extension of monopoly, out of the continuing
4 monopoly functions, I think it's bad policy to limit the
5 ability of the incumbent to compete on the basis of what it
6 can offer the consumer. To do so is to tilt the competitive
7 playing field in a way that harms the consumer.

8 And so, I think that's an overview of the nature of
9 the debate that I guess you will hear from me and from
10 others.

11 Q. In reviewing the surrebuttal testimony, will you
12 state and explain the principal areas of concern this
13 Commission should keep in mind that could adversely affect
14 the development of a competitive market?

15 A. Sure. The development of a competitive market,
16 as I've already said, requires that the incumbent utilities
17 who have continuing monopoly functions, particularly those
18 extending from their transmission and distribution central
19 facilities, the central problem becomes preventing those
20 facilities and those continuing monopoly functions from
21 being used to stifle competition in the marketing and the
22 supply of electricity.

23 There are three basic ways in which that competition
24 might be stifled. There might be continuing barriers to
25 entry from the regulatory or legal side which prevent new

1 competitors from either accessing power in the wholesale
2 markets or accessing consumers in the retail markets.

3 There might be the possibility of discriminatory
4 access or denials of access or conditioning of access by
5 which an incumbent utility would block the effective entry
6 by competitors, preventing them from getting on your power
7 lines, which would block competition.

8 Third, there's a possibility of cross-subsidization
9 between regulated monopoly functions and largely deregulated
10 non-monopoly functions.

11 Cross-subsidization could be used by an incumbent
12 utility to advantage its non-regulated functions,
13 essentially high costs over in the regulated functions
14 jacking up tariff trades, potentially, if there are not
15 regulatory safeguards in the regulated functions.

16 Those are the three primary things, barriers to
17 entry, discriminatory actions, and cross-subsidization, that
18 form the ways by which competition could be effectively
19 impeded by this mixture of regulation and deregulation we're
20 embarking on.

21 Q. Dr. Kalt, the supplemental testimony of Dr. Mayo
22 and Dr. Dirmeier argue that PP&L has not gone far enough in
23 protecting competition. Do you agree?

24 A. No, I think that the combination of PP&L and the
25 steps taken under the act and by the Commission, and also by

1 the FERC, set up a system that provides for workable,
2 effective competition in the non-regulated, non-monopoly
3 functions that the act envisions.

4 In particular let me cite five attributes of the
5 system that is proposed by PP&L that is consistent with the
6 act, the policies of the Commission, and the FERC.

7 First, the company proposes functional separation of
8 its monopoly and non-monopoly functions, providing for the
9 separation of costs, accounting, people, information,
10 provision of services, etcetera.

11 This functional separation is crucial, because
12 without it there's the possibility of this extension of
13 monopoly from regulated functions into non-regulated
14 functions that I've already talked about.

15 Second, the proposals provide for the unbundled, non-
16 discriminatory access at both the wholesale and retail
17 level, to the continuing monopoly functions that the company
18 would continue to retain.

19 Third, there are provisions in these plans and in the
20 policies that will block any cross-subsidization of the time
21 that I described earlier. In particular, the company
22 proposes cost allocations based upon Commission policy, and
23 the rate cap itself will block cross-subsidization, since it
24 acts to prevent the loading of costs into the regulated
25 function.

1 Fourth, obviously the whole policy is designed in a
2 very significant way to remove the legal and regulatory
3 barriers to entry. That is essentially the exclusive
4 franchise that the utilities have enjoyed for most of the
5 last 75 years will be removed under the act.

6 This removal of these barriers to entry, coup-led
7 with the removal of wholesale barriers to entry, under the
8 regulations of the FERC, will allow competition to arise in
9 both the retail and wholesale markets.

10 And then fifth, the company proposes, and is adopting
11 codes of conduct for the oversight of all of these
12 functions. In particular, it proposes to adopt the same
13 code of conduct that is adopted under FERC Order 889 that
14 covers the transmission and wholesale functions, to extend
15 that to the transmission to retail, and also to adopt a
16 retail access code of conduct that will govern everything
17 from the rules of non-discriminatory access to the sharing
18 of information and people.

19
20
21
22
23
24
25

1 Q. Dr. Kalt, are there underlying principles that
2 guide and design these policies?

3 A. Yes. I think in designing these policies, the
4 fundamental goal ought to be to protect competition, not
5 competitors, not any of the competitors. I think that what
6 this boils down to, this rather standard anti-trust commerce
7 view of the world of protecting competition rather than
8 individual competitors, is a policy which says none of the
9 competitors should be handicapped by having advantages taken
10 away from them or costs imposed upon them that un-levels the
11 playing field on which they play when those advantages arise
12 from their ability to effectively compete to provide
13 consumers what they want.

14 What should be taken away from incumbent utilities is
15 the ability to extend monopoly from their essential
16 facilities and transmission and distribution into non-
17 monopoly functions.

18 What this means I think in terms of public policy and
19 the relative roles of the various parties who have
20 responsibility for implementing and overseeing the policies
21 we're about to implement here is that the problems of
22 extending monopoly functions and using them to stifle
23 competition in the non-regulated, non-monopoly functions is
24 a proper function of regulatory commissions such as the
25 Pennsylvania Public Utility Commission and the FERC. With

1 respect to activity and behavior and the non-monopoly
2 functions that do not arise from this extension of monopoly
3 from the regulated monopoly functions, of course, the anti-
4 trust authorities have a crucial role to play to make sure
5 that those behavior and actions of the non-regulated
6 activities of the incumbent utilities are consistent with
7 competitive markets.

8 JUDGE KASHI: Excuse me, Dr. Kalt. I seem to be
9 missing something. What I'm hearing, a lot of it is out of
10 your direct testimony. What am I missing here that this is
11 rejoinder?

12 MR. KAPLAN: I believe these were points made in
13 particularly Dr. Mayo and Dr. Dirmeier. We are finishing up
14 with a couple of specific items and we'll be done, Your
15 Honor.

16 JUDGE KASHI: All right. Go ahead.

17 BY MR. KAPLAN:

18 Q. Dr. Kalt, will you specifically distinguish
19 between advantages, competitive advantages and
20 disadvantages?

21 A. Yes. One kind of advantage that can arise is
22 the potential ability on the part of an incumbent utility to
23 use its essential facilities, its continued monopoly
24 functions to extend monopoly. As I've already stated, those
25 kind of advantages are properly removed from the hands of

1 the incumbent utility.

2 Other advantages, however -- I see a bunch of
3 discussion here, for example, about name recognition, for
4 example. Those kind of advantages provide benefits to
5 consumers. They provide consumers with information,
6 assurances, et cetera. Those kind of advantages, which may
7 be offset by other advantages that other parties bring to
8 the table, those kind of advantages are not properly
9 eliminated, handicapped or otherwise taken away from the
10 incumbent utilities. After all, competition is a process.
11 That process is a process of individual parties searching
12 out their respective advantages.

13 In the context that we face here, the competition
14 that we're going to embark upon will involve large and/or
15 very sophisticated competitors who will each be searching
16 for their own advantages in attempting to take customers
17 away from others. In some cases those competitors will have
18 more experience, more expertise than the incumbent utility.
19 The corporate culture of incumbent utilities in my
20 experience is a disadvantage because they've lived for 75
21 years not having to compete.

22 A searching out of those kinds of pro-competitive,
23 pro-consumer advantages is what competition is all about.

24 Q. And concluding, Dr. Kalt, can you just comment
25 on the renewed attack by Dr. Mayo and Mr. Dirmeier on the

1 ability of PP&L to continue to use its corporate name in the
2 competitive world, retail world?

3 A. Yes. Questions have been raised about whether
4 PP&L should be allowed to use its corporate name,
5 particularly in marketing in the non-monopoly functions. I
6 believe it is proper for PP&L to be able to use its name.
7 As I understand it, the Act does not prevent doing so.
8 Moreover, the corporate name is a valuable asset.

9 As we all know, public utilities can have either good
10 reputations or bad reputations. In this case, PP&L seems to
11 believe by its behavior that it is a valuable asset. This
12 valuable asset is not derived from the continued monopoly
13 functions in the T&D, the transmission and distribution, and
14 hence, is not a proper place to attack, but rather, this
15 corporate name, to the extent it is valuable to consumers,
16 is derived from a history of providing good service. That
17 history of providing good service is something over which
18 companies ought to be able to compete and which other
19 competitors ought to try to take away if they can.

20 MR. KAPLAN: Thank you, Dr. Kalt. Your Honor, Dr.
21 Kalt is available for cross-examination.

22 MR. KLEPPINGER: Your Honor, before we proceed, I
23 appreciate Dr. Kalt's comments, and he was not allegedly
24 making rejoinder testimony to any of PPLICA's, but the
25 purpose of rejoinder testimony is very limited to the extent

1 that there were items raised in the surrebuttal testimony of
2 the other parties that had not previously been addressed in
3 direct or rebuttal testimony of the company. And if we're
4 going to have to listen to 15 or 20 minutes of rejoinder
5 testimony that is repetitive of information already
6 contained in direct and rebuttal testimony, our days are
7 going to be longer than five hours.

8 JUDGE KASHI: That's why I in listening to Dr. Kalt's
9 testimony said it sounded strangely like what I have been
10 hearing in his direct testimony.

11 MR. KOHLER: Your Honor, since he was rebutting
12 Enron's witness, I have absolutely no problem with what Dr.
13 Kalt said, but with your emphasis on saving time in this
14 proceeding, I join in Mr. Kleppinger's statement.

15 MR. KAPLAN: I just want to make a commitment to Your
16 Honor. We received about six inches worth of surrebuttal
17 testimony, not all of it on Friday, the day you designated;
18 some which we did not get until Saturday. As the hearing
19 moves forward, we, of course, will be more careful in
20 specifically identifying pages and statement and exhibits
21 that we are rebutting, and we will make that commitment. We
22 got it in in ten minutes, and hopefully we'll keep it to
23 that or less. Thank you, Your Honor.

24 JUDGE KASHI: Thank you. Before I allow counsel to
25 have their opportunity, you brought something up about the

1 name recognition. That is something that I have heard a lot
2 about in the first round of public input hearings. One of
3 the questions when you were talking that came right out,
4 there was a gentleman in Bethlehem that used to be at one
5 time on the Consumer Advisory Council, and his name was
6 Butkys; and Mr. Butkys, after giving us a lesson, I asked
7 him the question: what telephone company do you use for
8 your long distance carrier? He said AT&T. I said to him:
9 why? He said because of the name recognition, and he knows
10 that he can buy the services less expensively from other
11 carriers, but in fact, he's going to buy from AT&T because
12 of the name.

13 How do we approach that, Mr. Kalt?

14 THE WITNESS: I think a couple of important points.
15 I don't know Mr. Butkys, but it sounds like from what you
16 just said, he knows he can buy other services perhaps at
17 lower prices from other companies. Why does a consumer
18 behave like that? As economists, we look at that problem
19 and it tells us the consumer apparently understands they can
20 choose, understands at least the general nature of the
21 option and could go search out those options, but instead
22 makes a choice based on the reputation of a particular
23 supplier for what presumably that customer regards as
24 quality service that perhaps offsets the price disadvantages
25 of that service. We all make decisions like that all the

1 time as we buy brand name products in the face of being able
2 to buy generic products.

3 JUDGE KASHI: In a similar vein, I was recently taken
4 by a consumer article that listed cellular phones. I have a
5 19-year-old daughter who is just dying to get her hands on a
6 cellular phone for those emergency situations, you know,
7 back and forth to college, and I've told her no way.

8 Doing the research on it, I came across an article in
9 Consumer Reports that amazed me to the extent that MCI's
10 cellular services throughout the country are almost double
11 the cost of everybody else's, and yet, they're doing
12 business like there is no tomorrow.

13 THE WITNESS: I think there are two other things to
14 add to this as well. One thing the Act has done that is
15 productive or whatever in this context is by providing this
16 transition period, remember at the transition period say at
17 the first year, parties self-select do they want to
18 participate in choice. So you're watching parties who by
19 the very nature of self-selecting into the process come into
20 that knowing that there is an alternative to the traditional
21 utility. That is a signal, of course, that you're dealing
22 with parties who understand that they are there to search
23 for choices.

24 At some point it is proper in that framework to
25 respect the wishes of the consumer to have the choice and in

1 your example to choose MCI since most consumers of cellular
2 phones understand there are other competitors out there that
3 are on the television and in the magazines all the time
4 advertising.

5 The other point to be made I think about the use of
6 the name is that the use of the name is one source of
7 potential advantage to a particular competitor in the
8 marketplace. The nature of competition is, of course, there
9 are lots of advantages and disadvantages that parties fight
10 over.

11 Our experience in other states has been that parties
12 have used different capabilities, including advertising to
13 build their own names, to provide expertise, and to use
14 their expertise in chasing customers; and competition is not
15 a process of finding everybody with exactly the same, quote
16 "advantages," in which case there are no advantages.
17 Competition is a process of letting each party try to find
18 what they can provide to the consumer to attract that
19 consumer, and that is the process of competition that
20 ultimately serves the consumer; and a textbook view, if you
21 will, which has everybody identical simply doesn't fit the
22 real world and doesn't fit public policy.

23 JUDGE KASHI: Thank you, sir. Cross, Mr. Kohler.

24 MR. KOHLER: Thank you, Your Honor.
25

CROSS-EXAMINATION

1
2 BY MR. KOHLER:

3 Q. Good morning, Professor Kalt. My name is Alan
4 Kohler. I represent Enron in this proceeding.

5 A. Good morning.

6 Q. In the interest of complying with the Judge's
7 directives, I'm going to try to move quickly. If Professor
8 Kalt has a problem with that, I would ask him to let me
9 know.

10 Dr. Kalt, I refer you to page 19 of your rebuttal
11 testimony and the discussion that goes on to page 20.

12 A. Yes.

13 Q. Can you tell me which witnesses you are
14 rebutting in that paragraph?

15 A. The one beginning on line 13?

16 Q. The paragraph that runs from 19 over to 20,
17 starting at line 13.

18 A. I would say this is rebuttal to themes and
19 issues that are raised in the testimony of Mr. Dirmeier,
20 Professor Mayo, I believe in the testimony of Mr. Johnstone,
21 and some of it goes to Mr. Biewald a little bit. I think
22 those would be the primary parties that this addresses, the
23 witnesses that this addresses.

24 Q. Professor Kalt, can you point to anywhere in Dr.
25 Mayo's testimony in which he asks the Commission to focus on

1 the number of competitors in the market?

2 A. Well, what I'm referring to there is the
3 attention to the potential size or you might say market
4 share of the incumbent utility and concerns that are raised
5 by Professor Mayo and the other people that I listed that
6 that share might be so large or the ability to attract
7 customers. I recall discussion of having a so-called large
8 customer base and so forth. That's what I was referring to.

9 Q. But as to the number of competitors and the idea
10 of subsidizing inefficient competitors, specifically as to
11 that notion, is it your position that there is anything in
12 Dr. Mayo's testimony which asserts that position?

13 A. I don't recall him saying that the Commission
14 should have a number of 99 competitors or something like
15 that, but rather what I'm pointing to is this concern that
16 the parties raise that if PP&L or another incumbent utility
17 in another area has a large share of the customer base, that
18 that somehow is an indication that competition has been
19 impeded; and that's just not proper economics.

20 Q. Professor Kalt, I believe it is your testimony
21 that PP&L's proposed code of conduct is sufficient to
22 prevent anti-competitive behavior. Is that right?

23 A. That would be mischaracterizing my testimony.
24 What I've said is that code of conduct, which, as I
25 understand, the company proposes as part of its proposal

1 would be adopted and enforced by the Commission -- indeed,
2 there are two codes of conduct; another one enforced by the
3 FERC -- that the combination of the code of conduct, its
4 force and the oversight within the jurisdiction of the
5 respective federal and state regulatory commissions coupled
6 with the other provisions of the Act which provide for
7 breaking down the barriers to entry, eliminating
8 discriminatory access and so forth, that combination of
9 functions and attributes is what I think creates a solid
10 policy to go forward with.

11 Q. I'm sorry for misstating your position. What I
12 wanted to get to is that you believe PP&L's proposed code of
13 conduct is an appropriate code of conduct in Pennsylvania?

14 A. In the context of all of the policies that it is
15 going to be embedded in, yes, I think it is an appropriate
16 code of conduct.

17 Q. And if I could refer you to pages 35 to 36 of
18 your rebuttal testimony, starting around lines 17 to 18.

19 A. Page 35?

20 Q. Page 35. It goes on to page 36.

21 A. I'm sorry. You mean the paragraph that starts
22 with line 14?

23 Q. That's right. I believe you testify that there
24 are a number of prohibitions which you believe are
25 appropriate for a code of conduct. Is that right?

- 1 A. Yes.
- 2 Q. Staring around line 17?
- 3 A. Yes.
- 4 Q. Now, are you familiar with PP&L's proposed code
5 of conduct, the state code of conduct which was attached as
6 RMG-4?
- 7 A. In Mr. Geneczko's --
- 8 Q. In Mr. Geneczko's rebuttal.
- 9 A. What the company refers to as the retail access
10 code of conduct?
- 11 Q. That's right.
- 12 A. Yes.
- 13 Q. Do you have a copy of that?
- 14 A. I don't have it with me.
- 15 MR. KAPLAN: We can provide a copy.
- 16 (Document handed to witness.)
- 17 BY MR. KOHLER:
- 18 Q. Do you have that in front of you?
- 19 A. I have it.
- 20 Q. Take a second to look at it.
- 21 A. I have it.
- 22 Q. Again, focusing on the reference on page 35 of
23 your rebuttal, I believe the first thing you mention is no
24 discrimination.
- 25 A. Yes.

1 Q. Which are the provisions you are relying on in
2 RMG-4 as to no discrimination?

3 A. Well, I would refer you to -- and I'm
4 interpreting these as an economist -- I would refer you to,
5 for example, the last paragraph on page 1, quoting, "Charges
6 for services between the generation supply group, electric
7 delivery group and other internal service organizations
8 would be provided at fair and non-discriminatory prices."

9 I'm also relying on the first paragraph of page 2,
10 quoting, "The electric delivery group will not favor the
11 generation supply group in any marketing of energy supply
12 products."

13 Each of the paragraphs under the category,
14 "Comparability" are part of what economists think of as the
15 comparability of the non-discriminatory aspects of product
16 provisions and offerings, and I would rely on that.

17 I think the last paragraph on page 2, No. 5, quote,
18 "As deemed appropriate, employees involved in the
19 administration of energy supply, alternative suppliers and
20 having access to competitive information will sign a
21 confidentiality agreement prohibiting improper disclosure of
22 competitive information," I think prevents discriminatory
23 conduct.

24 Those would be the key things.

25 Q. It is your testimony that taken together those

1 provisions mean no discrimination?

2 A. I think they are part of it. As I say, in the
3 paragraph you've referred to in my rebuttal testimony, I
4 say, quote, "The conduct and the regulations that stand
5 behind them." Of course, there is the state Public Utility
6 Commission and the Federal Regulatory Commission who also
7 oversee this process, and you need to I think read these
8 codes of conduct, as I've already stated, in the context of
9 that regulatory oversight.

10 Q. I think what you're saying there, sir, is you
11 are recommending that the codes of conduct have crisp
12 edicts, I believe those are the words you used. So your
13 testimony is that those provisions taken together are crisp
14 edicts?

15 A. I think they are fairly crisp, yes. They refer
16 to discrimination bluntly and don't shy away from the issue.

17 Q. Fair enough. I want to go to the next one, "No
18 cross-subsidization."

19 A. Yes.

20 Q. Which provisions in RMG-4 are you relying on for
21 the crisp edict of cross-subsidization?

22 A. Well, here I would, again in the context of the
23 regulatory framework, which also focuses on this, point you
24 to, for example, on page 1 under "Assignment of
25 responsibilities," where it says, quoting, "Employees in the

1 generation supply group directly involved in marketing
2 energy to customers choosing competitive generation service
3 will not be assigned any responsibilities within the
4 electric delivery group and vice-versa."

5 In other words, you can't sort of share that employee
6 and hide the costs on one side or the other of the
7 functionally separate function.

8 Q. So it would be a cross-subsidy of information?

9 A. In that case, you'd do it through the labor.
10 Similarly, you will note that the first paragraph, No. 1,
11 under "Accounting Cost Allocations," refers to "The costs
12 associated with the generation, supply and electric delivery
13 groups will be kept separate."

14 Now, that, of course, is embedded in a whole set of
15 proposals and procedures being adopted by the company. I
16 know Dr. Tierney will testify about this and others, as to
17 how those cost allocations arise from what I understand to
18 be Commission precedent and so forth.

19 Similarly, with respect to the role of employees, if
20 you look at page 2, Item No. 5, quote, "It is deemed
21 appropriate employees involved in the administration of
22 energy supply by alternative suppliers and having access to
23 competitive information will sign a confidentiality
24 agreement prohibiting improper disclosure of competitive
25 information."

1 Of course, that has been backed up by holding
2 employees not only to the regulatory requirements, but to
3 the company's own internal codes of professional
4 responsibility.

5 There are also elements of this cross-subsidy issue
6 in the comparability block of RMG-4 which deals with
7 channeling and those kinds of issues, in which you
8 essentially incur the costs on one side of the boundary to
9 build up the business on the other side of the boundary.

10 Q. Where are you referring?

11 A. For example, No. 5 on page 2 on the
12 comparability block of items.

13 Q. On the point of channeling customers?

14 A. Yes, pointing out those comparability things go
15 to the cross-subsidy issue as well.

16 Q. Focusing more on costs than information, I
17 believe the one you identified was No. 1 under Accounting
18 Cost Allocations. Would you agree that cost segregation or
19 segregation of accounts in and of itself does not
20 necessarily prevent cross-subsidization?

21 A. You mean if people segregated accounts and they
22 ignored the segregation?

23 Q. No. That depends on how you allocate costs.
24 Just segregating the accounts between two entities, wouldn't
25 you agree that absent the proper allocation, that that

1 doesn't necessarily preclude cross-subsidization?

2 A. If a firm could find surreptitious ways, for
3 example, to move costs across the boundary, then they would
4 be violating the rule of no cross-subsidization.

5 Secondly, the crucial costs to be segregated, of
6 course, from a competition point of view are those that
7 affect competition, specifically those which affect the
8 ability to compete at the margin for business, hence the
9 segregation of those costs that are the important boundaries
10 for cross-subsidization policy.

11 Q. Also, couldn't cross-subsidization result as
12 allocation in the first instance -- as the result of
13 allocation of costs in the first instance?

14 A. In theory, it could, sure.

15 Q. In the interest of time, I'll skip going over
16 the rest of it. Professor Kalt, are you familiar with what
17 is commonly referenced to as an imputation requirement?

18 A. I'm sorry. I couldn't hear you.

19 Q. An imputation requirement.

20 A. I've heard it discussed. I'm not familiar with
21 it in detail.

22 Q. Do you have any understanding of what an
23 imputation requirement is?

24 A. I'd hesitate to say right now, no. I believe it
25 has to do with the imputation of costs, but I don't want to

1 be more specific.

2 Q. Are you aware that Dr. Kahn in his testimony
3 accepted the application of an imputation requirement?

4 A. I believe there is some discussion of that. I
5 think so. I'd have to go back and check.

6 Q. You're not really qualified to talk about
7 imputation?

8 A. As I say, I've not really studied that issue in
9 detail.

10 Q. Do you know enough about it to know whether it
11 is addressed in RMG-4?

12 A. I shouldn't offer an opinion at this time.

13 Q. Referring you to pages 39 to 41 of your
14 testimony, you talk a little about --

15 A. The rebuttal testimony?

16 Q. I'm sorry; of your rebuttal testimony.

17 MR. KAPLAN: I'm sorry. What page, Mr. Kohler?

18 JUDGE KASHI: Thirty-nine to 41.

19 MR. KAPLAN: Thank you.

20 BY MR. KOHLER:

21 Q. You talk a little about telecommunications
22 deregulation; is that right?

23 A. Yes.

24 Q. And you talk a little bit about the enactment of
25 the new federal law through telecommunications; is that

1 right?

2 A. Yes.

3 Q. Are you aware that the Telecommunications Act of
4 1996 imposes a structural separation requirement on the Bell
5 companies between their local and long distance operations?

6 A. What do you mean by structural?

7 Q. They're required to provide those services under
8 structurally separate affiliates.

9 A. But not separate ownerships.

10 Q. But not under separate ownership?

11 A. I'm going to be careful. I understand that
12 there are requirements for functional separation.
13 Structural separation separates people and so forth, but not
14 divestiture or divorcement.

15 Q. For these questions, let's separate out
16 structural separation from employee divestiture. Do you
17 believe that the Bell structural separation requirement is
18 inappropriate or unnecessary?

19 A. I have not studied it in detail. As I've
20 already said here, when you have continuing monopoly
21 functions and non-monopoly functions, I think some form of
22 functional separation is appropriate. I have not studied
23 the specific components of the 1996 Act with regard to your
24 question and its application here.

25 Q. If Congress had not required structural

1 separation and, for example, required functional separation

2 --

3 A. You're drawing a distinction between the two?

4 Q. Yes.

5 A. What is your distinction?

6 Q. Structural separation would involve corporate
7 reorganization; is that correct? Well, you tell me. Is
8 there a difference between structural separation and
9 functional separation?

10 A. To some extent. It is all functional separation
11 until you get to divorcement, and there are varying formats
12 along continuums that one might use, setting up corporate
13 subs, setting up different accounting, so forth and so on,
14 so it's a continuum.

15 Q. Let's define structural separation as separately
16 organized subsidiaries under a corporate umbrella, because I
17 believe that's what Congress talks about.

18 A. You mean like separate and chartered corporate
19 subs?

20 Q. No; as compared to functional separation without
21 structural separation. Wouldn't that be more efficient for
22 the Bell companies? Wouldn't that be more efficient for
23 anyone in those circumstances?

24 A. I don't think I can honestly answer either of
25 your questions in the sense that if one wants to go study

1 the telecommunications industry the way we are intently
2 studying right now this industry in Pennsylvania, I think
3 that would be the appropriate way to go about asking your
4 question as to whether, to roughly quote you, structural
5 separation is more efficient for the Bell system.

6 With respect to your second question as to something
7 to the effect in most situations wouldn't structural
8 separation be more efficient, I don't think you can provide
9 a general answer like that. We're dealing here with
10 economies of scope and scale that make the proper analysis
11 fact and industry specific. I've tried to provide that
12 analysis in this case applied to this industry. Beyond
13 that, I don't think you can generalize the way you are
14 implying.

15 Q. Are you aware that in Pennsylvania this
16 Commission has imposed restriction on the use of a monopoly
17 local exchange carrier's name by a carrier's long distance
18 affiliate?

19 A. I'm not aware specifically. I've heard some
20 discussion about that, but I'm not sure what the Commission
21 has done on that.

22 Q. Let me ask you as a hypothetical if in fact a
23 state commission included a bar on the use of a monopoly
24 logo and only permitted use of the name with an affirmative
25 disclosure that the utility is not the same company as the

1 monopoly, do you believe those types of policies are
2 appropriate or necessary?

3 A. In every possible context or do you mean for
4 this industry?

5 Q. Well, you talked a little bit about the
6 telecommunications industry and what might be appropriate
7 there and or what has occurred and what might be
8 appropriate. So let me ask you in the context of the
9 telecommunications industry.

10 MR. KAPLAN: If I can ask a question, Your Honor.
11 You say not the same company. What do you mean by not the
12 same company? No affiliation, totally independent, a
13 separate subsidiary?

14 MR. KOHLER: My understanding of the role is that the
15 corporate affiliate, if they are to mention the name of the
16 local exchange carrier, must have an affirmative disclosure
17 that they are not the same company as the local exchange
18 carrier; otherwise that they are structurally separate.

19 MR. KAPLAN: Are they prohibited from saying that
20 they are a subsidiary of Bell of Pennsylvania?

21 MR. KOHLER: No, but that's what the affirmative
22 disclosure is.

23 THE WITNESS: I'm sorry. You're asking me --

24 BY MR. KOHLER:

25 Q. That's the hypothetical that I'm asking about.

1 Do you believe that that is a necessary or appropriate
2 safeguard in the telecommunications industry in sharing a
3 competitive market?

4 A. The clarifying questions that Mr. Kaplan asked
5 you make it clear that there are layers to this issue as to
6 what people can say and not say. I have to say, as I told
7 you, I do not know precisely what the nature of the
8 Pennsylvania regulation was in this regard.

9 I can answer you as far as I can without having the
10 facts. I can say the following. First, it is inappropriate
11 to in any way deceive consumers and imply that they are not
12 getting service from some company. Taking information out
13 of a market is not plausibly a sound public policy. The
14 reason for that, as I have said, is that information to
15 consumers is valuable because they value such things as
16 peace of mind, assurance, et cetera, reputation.

17 The second thing I can say is one cannot argue, as
18 your witnesses have in surrebuttal, I think Mr. Dirmeier, in
19 particular, that a company should be in its non-regulated
20 functions denied the ability to inform consumers that it is
21 part of the incumbent because, according to Mr. Dirmeier,
22 that brand name was built up during an earlier period of
23 less competition and more blockades to competition.

24 If the use of a name took the form in some way -- and
25 I don't know how it would apply to telecom. I'm trying to

1 answer your question, but you've got to recognize you go in
2 and look at the facts of these situations. If the use of a
3 name was a mechanism by which a party was leveraging its
4 control over essential facilities, the ability to deny
5 access and so forth, to tie and do the leveraging that I
6 talked about, then it might be reasonable to restrict the
7 use of that name, but I can't beyond that go and analyze
8 specific facts that I don't have as to what they've done in
9 Pennsylvania on telecom.

10 Q. You talked about that consumers should not be
11 deprived of accurate information; is that right?

12 A. Yes.

13 Q. Would you agree with the notion that generally
14 speaking more information which is accurate is appropriate?

15 A. Generally, that's a good policy prescription,
16 yes.

17 Q. If I can refer you to page 45 of your rebuttal
18 testimony, lines 6 to 7.

19 A. Lines 6 and 7? Did you say 6 and 7?

20 Q. Six going on to line 7.

21 A. Okay.

22 Q. You use the term there "prevailing market
23 rates."

24 A. Yes.

25 Q. Is your reference to prevailing wholesale market

1 rates?

2 A. I'm trying to recall. I believe that this --

3 Q. Just so it's clear, in contrast to prevailing
4 retail market rates.

5 A. I'm trying to recall. I believe it would be
6 prevailing wholesale, but you'd have to ask a company
7 witness that. I'm just not recalling right now the answer
8 to that question.

9 Q. You said it in your testimony. I'm just asking
10 for clarification.

11 A. I'm sorry. I'd have to go back and ask somebody
12 at the company. I'm just not recalling at this time.

13 Q. I believe on line 7 going onto line 8 on that
14 page, you indicate that PP&L intends to pass through the
15 prevailing market rate to consumers. I won't put words in
16 your mouth.

17 A. That's what I say. I believe this was
18 wholesale, but I'd have to double check.

19 Q. Now, in that pass-through of the prevailing
20 market rate -- and let's, subject to check, accept that it's
21 a wholesale market rate. Is that okay?

22 A. We can discuss it that way, if you'd like.

23 Q. What costs will PP&L recover in the rate to
24 consumers who choose not to choose?

25 A. It would recover the cost of that power, subject

1 to the rate cap, of course, cost of that power. It would
2 recover the cost of its transmission and distribution and
3 other services to the tariffs.

4 Q. Now, if it were a prevailing wholesale market --

5 A. Again, subject to the rate cap and the accuracy
6 of those tariffs and so forth.

7 Q. If it were a prevailing wholesale market rate,
8 would it recover any retail costs that might be incurred?

9 A. Like the distribution of retail. It would
10 recover the billing and the distribution, those costs, yes.

11 Q. A prevailing market rate would recover those
12 costs?

13 A. Not that part of it, but the overall price paid
14 by the consumer. As I indicated, they would recover the
15 costs of the power plus the ancillary services, T&D,
16 whatever is needed.

17 Q. Would, for example, the prevailing wholesale
18 market rate contribute to recovery of overhead?

19 A. If it was done on a direct pass-through, which
20 is dollar for dollar, no, it would not.

21 Q. Is it possible, Professor Kalt, that at any
22 point in time the rate for generation charged by the
23 delivery group to the choose not to choose customer would be
24 less than the generation rate charged by PP&L's generation
25 supply group to the customers who affirmatively choose PP&L?

1 A. I think that would be possible under the rate
2 cap, yes.

3 Q. Do you think it is likely to occur?

4 A. That the company would hit the rate cap?

5 Q. Do you think it is likely to occur that the rate
6 charged -- the prevailing market price passed through by the
7 delivery group would be less than the generation rate
8 charged by the generation supply group to the customers who
9 choose?

10 A. Well, again, if the company bumps up against the
11 rate cap, then of course it wouldn't be able to engage in
12 the pass-through, so the effective price by the structure of
13 that argument would be below the prevailing market price.

14 Q. Let's assume it doesn't bump up against the rate
15 cap. Doesn't the generation group have an overhead cost and
16 retail cost to recover?

17 A. As I understand it, it would be recovering those
18 costs through tariffs on its transmission, distribution and
19 other ancillary services.

20 Q. We're talking about the generation supply group,
21 the competitive arm of the business. Aren't they going to
22 have some overhead?

23 A. If it's truly overhead and fixed costs, it
24 presumably wouldn't be reflected in prevailing market prices
25 of anybody, because that competition goes on on the basis of

1 marginal cost.

2 Q. You testified that it could occur. If it does
3 occur or if it does occur frequently, would customers have
4 any incentive to choose any generation supplier, including
5 PP&L's generation supply group?

6 A. They certainly could, yes.

7 Q. What would be their incentive? I know they
8 could. What would be their incentive?

9 A. As I understand it -- take the clearest case of
10 what I think you're trying to illustrate. PP&L is bumped up
11 against the rate cap and the market is pushing other prices
12 higher. In that situation, the relative price makes PP&L
13 look more attractive.

14 However, as I understand it and as we've looked
15 around not only this industry, but others, other competitors
16 in the market are also trying to provide different services,
17 different qualities of service, different reputation
18 effects, and they're competing on just those, and those
19 provide incentives for customers to go pick an alternative
20 supplier.

21 Q. But there would be no price incentive; is that
22 right?

23 A. In the sense of you say holding all else equal,
24 well then, by definition, the structure price is the only
25 thing that differs.

1 Q. And that would be also true if both prices were
2 below the cap but that the delivery group's price was lower?
3 Isn't that true, there would be no price incentive?

4 A. You mean if nothing else mattered to consumers
5 and Party A had lower prices than Party B?

6 Q. There is no price incentive. There might be
7 another incentive.

8 A. I think people would pick Party A if Party A has
9 lower prices and nothing else matters to consumers.

10 MR. KOHLER: I'm in danger of, I guess, breaking my
11 own time limitation, Your Honor.

12 MR. KAPLAN: Perhaps, Your Honor, since it is now
13 11:30 -- I don't know what your schedule is -- we could give
14 Mr. Kohler a chance to collect his notes and we could take a
15 morning break.

16 JUDGE KASHI: We'll take a morning break in 15
17 minutes. Then we'll go till 12:30, at which time we will
18 recess for lunch.

19 MR. KOHLER: I can move pretty quickly, Your Honor,
20 and hopefully in a more organized fashion.

21 I'd like to mark as Enron Cross Exhibit 1, if that's
22 how we're marking documents, an interrogatory response from
23 PP&L to Enron.

24 JUDGE KASHI: So marked for purposes of
25 identification.

1 (Whereupon, the document was marked
2 as Enron Cross-Examination Exhibit
3 No. 1 for identification.)

4 BY MR. KOHLER:

5 Q. Professor Kalt, that is an interrogatory
6 response that is noted at the top was answered by Mr. Krall.
7 Is that right?

8 A. Yes.

9 Q. I'd ask you to focus on Answer 16(b), if you
10 could read that quickly.

11 (Witness perusing document.)

12 A. Yes.

13 Q. I'd like to quickly refer you to page 46 of your
14 rebuttal. I believe you corrected the name of the witness
15 you were rebutting. I want to refer you to the line which
16 originally said Professor Mayo, but now says Mr. Dirmeier.
17 That's line 6.

18 A. Yes.

19 Q. I believe that says what Mr. Dirmeier failed to
20 understand is that no services of the EDC will be de-
21 tariffed. Is that right?

22 A. That's correct.

23 Q. Now, in answer 16(b), there is a line, isn't
24 there, that says, "However, because supply will be at market
25 prices, Chapter 13 of the Public Utility Code may not

1 apply"?

2 Are those two statements consistent?

3 MR. KAPLAN: Your Honor, clearly, Dr. Kalt did not
4 participate in answering this interrogatory. It involves
5 the detail of Pennsylvania Public Utility law. Mr. Krall,
6 who will be a witness indeed tomorrow, if we keep on
7 schedule, is the witness listed as responsible for that
8 answer, and I think we are just wasting time.

9 MR. KOHLER: Let me ask it a different way so it's
10 not wasting time.

11 BY MR. KOHLER:

12 Q. When you use the word "de-tariffed," did you
13 mean that it was a regulated rate subject to Chapter 13
14 procedures?

15 A. I didn't necessarily mean it was subject to
16 Chapter 13. My understanding was that the company
17 anticipated it would be sold under tariffs, whether it was
18 under Chapter 13 or some other provision or some
19 modification of Chapter 13 in light of the Act, but that the
20 company anticipates that it would be sold as a tariffed
21 service.

22 Q. Quickly, one final question. If I can refer you
23 to page 43 of your testimony, Footnote 10, I believe -- your
24 rebuttal testimony. I'm sorry.

25 A. Yes.

1 Q. You recite a quote there from the Economic
2 Report to the President on electric regulatory reform; is
3 that right?

4 A. Well, it refers to air transport, trucking,
5 natural gas, and long distance telecom.

6 Q. But it is a quote from the Economic Report to
7 the President in 1996; is that correct?

8 A. But not about electric.

9 Q. Okay. I'm sorry.

10 MR. KOHLER: Your Honor, I'd like to mark as Enron
11 Cross Exhibit 2 what purports to be a chapter from that
12 report.

13 (Whereupon, the document was marked
14 as Enron Cross-Examination Exhibit
15 No. 2 for identification.)
16
17
18
19
20
21
22
23
24
25

1 MR. KAPLAN: Mr. Kohler, are you done with Cross-
2 Examination Exhibit No. 1?

3 MR. KOHLER: Yes, I am.

4 (Pause.)

5 JUDGE KASHI: Mr. Kohler?

6 BY MR. KOHLER:

7 Q. Professor Kalt, is this the chapter of that
8 report that you quoted from?

9 A. Yes. The quote in the footnote occurs on page
10 159.

11 Q. And if I could refer you to page 163 of that
12 same chapter, the first full paragraph. Could you read that
13 first sentence?

14 A. "The difficulty posed by such a mixture of
15 regulation and deregulation is that a price-regulated
16 bottleneck monopolist has strong incentives to provide its
17 own affiliates in unregulated segments better access to the
18 bottleneck than it offers to rivals."

19 Q. And then if you could skip the part that's in
20 the parentheses and read in the next sentence?

21 A. Starting with "Such"?

22 Q. Yes.

23 A. "Such discrimination can inefficiently exclude
24 rivals from the potentially competitive segments, harming
25 both the would-be rivals and consumers."

1 Keep going?

2 Q. No. Why don't we go down to the next full
3 paragraph, if you will?

4 A. Okay.

5 Q. Skip the first sentence, and the sentence that
6 starts with "Firms can devise..."

7 A. "Firms can devise many clever technological
8 games to circumvent regulation, such as varying the quality
9 of connections provided to competitors."

10 Q. Do you agree with all those statements?

11 A. With their essence? These are comments. I used
12 to work with the CEA. We're all saying the same thing.
13 It's just what I've just said. We've not ducked the issue
14 here, but the regulated monopoly functions can be used to
15 lever and stifle competition over the non-monopoly
16 functions, and it's proper for policy to focus on preventing
17 that leveraging or stifling of competition in the non-monopoly
18 functions.

19 MR. KOHLER: Nothing further, Your Honor.

20 JUDGE KASHI: Thank you very much, sir. Do you want
21 to move the exhibits?

22 MR. KAPLAN: Before we proceed, Your Honor, do you
23 have the entire report with you, Mr. Kohler?

24 MR. KOHLER: I do, Your Honor.

25 MR. KAPLAN: May I examine it?

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

(Document handed to Counsel Kaplan.)

MR. KAPLAN: Thank you. I'll return it to you then.

MR. KOHLER: Your Honor, I'm sorry. As you directed, we coordinated with MAPSA over the weekend. None of these questions will repeat in any way questions that I had. I would request that Mr. Stewart be allowed to go through it quickly; he can do it faster than I. If Your Honor insists, I can do it, but I think that's appropriate. I think also Mr. Fogel has some questions, but again, I could read them to the witness, but they're not repetitive and it would go more quickly if he read them.

JUDGE KASHI: All right.

CROSS-EXAMINATION

BY MR. STEWART:

Q. Good morning, Professor Kalt. My name is Todd Stewart and I represent the Mid-Atlantic Power Supply Association.

A. Good morning.

Q. Mr. Kalt, on page 10 of your direct testimony, at lines 10 and 11, --

A. Of my direct testimony?

Q. Your direct testimony.

A. Hold on; I'm going to catch up with you.

(Witness perusing documents.)

A. Yes.

FORM 2

1 Q. You state that one of the principal provisions
2 of Chapter 28 is the reliance upon market forces to
3 establish the price mix and performance characteristics of
4 power production capacity; is that correct?

5 A. Yes.

6 Q. Do you consider the term "market forces" to mean
7 the same thing as competition?

8 A. Market forces is broader than competition. We
9 mean things like profit incentives and so forth, so it's
10 broader than competition. Competition is one of the market
11 forces in the marketplace.

12 Q. As I understand it, the new regulatory scheme
13 for Pennsylvania envisions competition as a means of
14 controlling the price of electric generation and supply; is
15 that correct?

16 A. I think it's generally correct, yes. I mean
17 obviously, on the generation side, the FERC plays a major
18 role in that. It's not just the Act, in other words.

19 Q. And in order to have a competitive market for
20 retail sales of electricity, it would be necessary for PP&L
21 to lose market share; is that correct?

22 A. In what market? I don't think it's generally --

23 Q. In the retail electric market, in order to have
24 a competitive market, it would be necessary for PP&L to lose
25 market share?

1 A. I don't think you can directly conclude that in
2 the presence of low barriers to entry, because the threat of
3 competition, in a standard economist's framework, says
4 look -- looking at market share can be a starting point, but
5 what we want to know is whether the process of competition
6 is vital or not. The crucial element to that is barriers to
7 entry.

8 Q. One more question. On page 15 of your direct
9 testimony, beginning at line 17 and continuing on to the
10 next page, you make a statement --

11 A. I'm sorry; I need to catch up with you.

12 Q. I'm sorry. Page 15 of your direct testimony, at
13 line 17.

14 A. Okay.

15 Q. You state that the CTC cannot be raised. Did
16 you mean to say that the CTC cannot be changed or that the
17 rate cap cannot be changed?

18 A. My understanding was that the CTC could not be
19 raised as a result of market prices which turn out to be
20 lower than those that are employed to calculate the stranded
21 costs and hence the CTC. That was my understanding.

22 MR. STEWART: I have nothing further, Your Honor.

23 JUDGE KASHI: Thank you very much.

24 We're going to break at this time. Do you wish to
25 move your exhibits at this time, Mr. Kohler?

1 MR. KOHLER: I can, Your Honor, or I can wait till
2 the end of my group.

3 JUDGE KASHI: All right. We'll wait till the end of
4 your group.

5 We're going to recess until noon. We'll come back
6 and begin with Mr. Zalzman at noontime for the
7 Environmentalists.

8 MR. FOGEL: Your Honor, I have a few questions.

9 MR. KOHLER: Your Honor, the PPA also is a member of
10 my group. Again, these won't be repetitive questions.

11 JUDGE KASHI: You have a few questions?

12 MR. FOGEL: No more than ten minutes, Your Honor.

13 JUDGE KASHI: We'll pick it up when we get back. We
14 stand in recess.

15 (Recess.)

16 JUDGE KASHI: Mr. Fogel, PPA.

17 MR. FOGEL: Thank you, Your Honor.

18 **CROSS-EXAMINATION**

19 BY MR. FOGEL:

20 Q. Good morning, Professor Kalt.

21 A. Good morning.

22 Q. I'm counsel for the Pennsylvania Petroleum
23 Association. I'll try to keep this as brief as possible.

24 Directing your attention to page 35 of your rebuttal
25 testimony, line 20, you have those bullets of what a good

1 structure should have, and you identify --

2 A. Page 34?

3 Q. -- no discriminatory transfers.

4 A. Do you mean page 34?

5 Q. Page 35 of your rebuttal.

6 A. I don't have any bullets. I have bullets on
7 page 34.

8 Q. No. Line 20. You include no discriminatory
9 transfers.

10 A. Oh, I see. I was looking for bullets. I'm
11 sorry.

12 Q. I'm sorry. Do you see that?

13 A. Yes.

14 Q. Now, are you aware that under the restructuring
15 proposal as put forth by the company in this proceeding, the
16 electric delivery group, in addition to supplying
17 electricity, will also be marketing and supplying other
18 products, which include such competitive products as
19 electronic thermostats, power watch devices and heat comfort
20 controls?

21 A. I have not done an analysis to know whether
22 they're competitive, but I understand they can be. They
23 will market such things, yes.

24 Q. To your knowledge, would information, customer-
25 related information, be an important asset in the use of

1 marketing those devices?

2 A. Well, I would suspect that some customer
3 information would be useful, yes.

4 Q. Now, would you also agree that the customer
5 lists that have been developed by the company and related
6 customer information that the utility has obtained is an
7 asset that was acquired through its monopoly status?

8 A. You mean its current customer base arises out of
9 the past? Yes.

10 Q. And in addition, if PP&L, which would then in
11 the new world be the electronic delivery group, if they
12 would undertake a marketing program and secure marketing
13 leads, would those marketing leads also be a possible
14 beneficial asset used in marketing those types of devices we
15 discussed before?

16 A. Asset to whom?

17 Q. To the utility in marketing those devices.

18 A. Those devices? It would depend on whether that
19 information went to the parties that were doing the
20 marketing.

21 Q. Now, to your knowledge, will that type of
22 customer information be made available to alternate
23 suppliers as it will be made available to the electronic
24 delivery group in its marketing of those items?

25 A. You mean customer lists, for example? I'm not

1 sure. You'd have to ask one of the company witnesses on
2 that.

3 Q. Speaking as the company's expert in terms of
4 constructing a proper competitive environment, you would
5 agree that that customer information was obtained by the
6 company through the provision of its monopoly service;
7 correct?

8 A. It's just obtained from the past when it was a
9 monopoly; yes.

10 Q. Would you believe it would be appropriate for
11 that information only to be made available to the electronic
12 delivery group and not be made available to competitors
13 under similar terms and conditions and at a contemporaneous
14 time?

15 A. Again, if the information is acquired as a
16 result of the continuing monopoly in these essential
17 facilities, which includes the T&D, and that information is
18 transferred only to the company, I think that would be
19 inappropriate. However, the distinction that I'm drawing is
20 between information -- it's like the brand name of the
21 company. Information or a brand name that was acquired as a
22 result of the past but is not arising from continued
23 monopoly control over the essential facilities of
24 transmission and distribution, those kinds of pieces of
25 advantage or assets are not necessarily subject to full

1 disclosure.

2 Q. Under the rules of conduct that are being
3 proposed in this proceeding, focusing primarily upon the
4 sale of electric generation, to your knowledge, will that
5 customer information list be made available only to the
6 utility's competitive marketing group?

7 A. That's not my knowledge, no.

8 Q. Would you consider that to be an appropriate
9 activity under the rules of conduct we are trying to
10 establish for fair and open competition?

11 A. Which?

12 Q. To only provide this information to the
13 utility's marketing group. Talking now past, all the
14 customer stuff developed up until the date the Homestead Act
15 is opened up and everyone goes out after it?

16 A. Well, I would think that certain customer
17 information would -- you say all the customer stuff. I
18 would think that some of that information would not be
19 appropriate to share only with the non-regulated arm of the
20 business.

21 Q. Do you know of any aspect of the company's
22 proposed rules of conduct that deal with the situation of
23 the other competitive services that they will be offering in
24 the new world in contrast to solely only on the electric
25 generation?

FORM 2

1 MR. KAPLAN: Your Honor, we've been somewhat patient,
2 but these other services are way beyond the scope of Dr.
3 Kalt's direct or rebuttal testimony, and there are other
4 witnesses who are more familiar with these services and
5 would be in a much better position to address Mr. Fogel's
6 questions. Indeed, the statement of company policy is in
7 this area.

8 MR. FOGEL: If I may respond, Your Honor?

9 JUDGE KASHI: Sure.

10 MR. FOGEL: I haven't been very impressed with the
11 witness' qualifications and standards, and in terms of
12 testimony which he addressed, he identified general rules
13 that should be established and followed by the company in
14 order to insure that we have a fair and open competitive
15 environment. I believe it's quite relevant and appropriate
16 then to apply those principles to the construct that the
17 company has submitted in this proceeding, which he is
18 testifying to. Now, I realize there may be little details
19 and certain factors that some other witness could better
20 explain, but I don't think I'm dealing in such a detailed,
21 micro-managed level at this time; I'm dealing with fairly
22 broad concepts.

23 JUDGE KASHI: All right. We'll overrule the
24 objection.

25 Go ahead.

1 MR. FOGEL: That's the great thing about those
2 objections, I forget the question.

3 (Laughter.)

4 MR. FOGEL: I remember the question.

5 BY MR. FOGEL:

6 Q. To your knowledge, can you identify or point me
7 to any provision of the company's proposed rules of conduct,
8 either at the transmission or retail level, that address the
9 provision of customer-related information in connection with
10 the marketing and distribution of competitive products, such
11 as the thermostats, et cetera, in addition or beside merely
12 the competitive sale of electric generation?

13 (Witness perusing document.)

14 A. I would refer you to, for example, the exhibit
15 that we looked at earlier this morning, RMG-4, which is the
16 retail access code of conduct. In there, there is a
17 discussion of the segregation of information, indications
18 that the electric delivery group will release information to
19 a supplier only after approval from the consumer. There's
20 also discussion there of various aspects and attributes of
21 the consumer that would be subject to these confidentiality
22 and consumer approval lists.

23 Q. Could you just be more specific, Professor Kalt?
24 Are you speaking now under the heading entitled -- this is
25 in reference to RMG-4 -- "Segregation of and Restricted

1 Access to Information"? Is that what you're referring to?

2 A. Yes.

3 Q. Just for the sake of time, is that the section
4 that you're referring to in answer to my question?

5 A. Yes. That was what I was just referring to.

6 There is also discussion of segregation of information in
7 the section labeled "Communications to Employees and
8 Enforcement," in particular, the confidentiality provisions
9 provided by item number 5, number 4, which enforces the
10 code. I don't have in front of me the FERC Order 8-89 Code
11 of Conduct, but, as best I recall, there are also provisions
12 there with respect to -- I don't have it in front of me, but
13 the essence of it, as I understand it, is provisions for
14 non-discriminatory disclosure of competitive lists and such
15 information; that depending upon how policy evolves may have
16 applicability to the marketing of the activities that you're
17 talking about.

18 Q. Taking what you've said, assuming it's correct
19 for the moment and for the sake of time, however, under
20 these codes of conduct, this information, almost by
21 definition, will be retained by and made available to the
22 electric delivery group; correct?

23 A. Well, if it's subject to non-disclosure and non-
24 discrimination criteria, I think what you're saying is
25 accurate, that it would reside within the electric delivery

1 group.

2 Q. Now, in the brave new world, however, the
3 alternate supplier will also be competing against the
4 electric delivery group, will they not?

5 A. Well, the electric delivery group will primarily
6 have responsibility for selling -- I'm sorry; the phrasing
7 that's been used, the electric delivery group, would have
8 primary responsibility for the regulated monopoly functions,
9 T&D. The generation supply group would be competing against
10 the alternative suppliers.

11 Q. But in order for the competitor to be
12 successful, he's going to have to convince that customer to
13 leave the utility?

14 A. Not the T&D, they stay with the -- not the
15 electric delivery group.

16 Q. Fine. Just two follow-up, quick questions,
17 Professor. You indicated before, you had discussion and in
18 your testimony, about barrier entries.

19 A. Barriers to entry.

20 Q. Would you agree that the barrier to entry for an
21 alternate supplier with respect to residential customers
22 could be more difficult than the barrier to entry to serve
23 commercial customers, larger volume customers?

24 A. I don't think that you can generalize in that
25 way.

1 Q. Have you had any experience in examining what
2 the entry barriers would be to a new marketer vis-a-vis
3 residential as compared to large commercial?

4 A. Yes, I've acquired information on that in my
5 experience; yes.

6 Q. Would one of the facets of going after the large
7 volume residential customers be telemarketing?

8 A. That might be a strategy that the incumbent or
9 any of the suppliers might try to use.

10 Q. Are you familiar with the deregulation efforts
11 in the natural gas industry that have been going on in
12 various jurisdictions?

13 A. Yes.

14 Q. Would you agree that the experience to date has
15 been that the marketers have gone first after the larger
16 commercial customers rather than the residential customers?

17 A. I think that's generally a true statement. The
18 basic reason it has arisen in my experience has been because
19 the larger customers have been successful before state
20 commissions in allowing open access to such customers, in
21 some cases, with direct hook-up customers; that happens
22 under the FERC provisions. Whereas at the retail level, for
23 the most part most jurisdictions have maintained barriers to
24 protect the local gas distribution company, and so there's
25 simply been a regulatory barrier to entry. I know in my

1 state they can't come market directly to me; there's still a
2 barrier to entry.

3 Q. For example, in New York there is no such
4 barrier. Are you aware of data there?

5 A. I haven't studied it specifically. I know New
6 York has been undertaking some deregulation efforts. I
7 don't know the exact state of them at this point.

8 MR. FOGEL: I have nothing further. Thank you.

9 JUDGE KASHI: Thank you very much.

10 Mr. Kleppinger, you only have brief cross-
11 examination. Can you do it in 15 minutes?

12 MR. KLEPPINGER: I'll make every effort, Your Honor.
13 That all depends on Dr. Kalt, himself.

14 **CROSS-EXAMINATION**

15 BY MR. KLEPPINGER:

16 Q. Good afternoon. I'm David Kleppinger. I
17 represent the PP&L Industrial Customer Alliance.

18 A. How do you do?

19 Q. Referring to your rebuttal testimony on page 60
20 where you begin your discussion of Mr. Baron's approach to
21 stranded cost recovery, at line 10 you use the term
22 "limited" in terms of how Mr. Baron had limited stranded
23 cost recovery in his proposal. Is it your understanding
24 that his limitation does allow the utility to recover its
25 stranded cost but not a return on that stranded cost?

1 A. I think that's basically right. There's other
2 details, but I think that's basically accurate; yes.

3 Q. So in the vernacular of utility regulation, we
4 hear return of, return on, Mr. Baron's proposal would allow
5 a return of but not a return, equity return, on the stranded
6 costs; correct?

7 A. I believe that's a generally accurate statement
8 of Mr. Baron's position.

9 Q. On the next page of your rebuttal testimony you
10 discuss the used and useful concept. Dr. Kalt, is it your
11 understanding that when a utility's investment in generating
12 plant has been deemed used and useful and included in rate
13 base, that the utility is assured that that plant will
14 continue to be included in rate base as used and useful for
15 the duration of the life of the asset?

16 A. I don't think you can conclude that across all
17 state jurisdictions, no.

18 Q. So that there are occasions that you apparently
19 are familiar with where a state commission, after having
20 found a plant to be used and useful at one point in time,
21 subsequently found that plant to no longer be used and
22 useful; is that correct?

23 A. I don't know the precise nature of the legal
24 arguments. I think the flavor of what you're describing
25 I've seen, certainly.

1 Q. Next, on page 64 of your rebuttal testimony you
2 again are discussing the used and useful concept at lines 10
3 to 13 and assert that Mr. Baron made an arbitrary
4 distinction between non-utility generating power contracts
5 and utility generation assets. Do you see that reference?

6 A. Yes.

7 Q. Now, have you had an opportunity to review the
8 piece of legislation that caused us all to be here today?

9 A. Yes.

10 Q. Are you aware that the Act itself makes a
11 distinction between non-utility generation contracts and
12 utility generation assets for purposes of stranded cost
13 recovery?

14 A. I recall a specific discussion of those two
15 separate items, and the Act seemed to be making some
16 distinction; yes.

17 Q. Do you recall enough from the statute as to
18 whether or not there is a difference in terms of the
19 latitude given to the Commission in determining what level
20 of stranded cost can be recovered by a utility for its own
21 generation assets versus non-utility generation contracts?

22 A. I don't recall specifically a difference in the
23 latitude. The point I was trying to make here was that the
24 exclusion of non-utility generation assets as compared to
25 non-utility generation assets was arbitrary; that part of it

1 was all I was focusing on.

2 MR. KLEPPINGER: May I approach the witness, Your
3 Honor?

4 JUDGE KASHI: Yes.

5 MR. KLEPPINGER: Counsel, I'd like to just show the
6 witness Section 2808(c)(2) and (3) of the Act. It is a
7 printed version. Section (2) and (3) are right here.

8 (Document handed to witness.)

9 BY MR. KLEPPINGER:

10 Q. Will you agree --

11 A. Let me take a quick look at it.

12 Q. Sure. Go ahead.

13 (Witness perusing document.)

14 Q. The distinction I would like to have you
15 acknowledge, Dr. Kalt, is that with respect to non-utility
16 generation contracts, the Act requires the Commission to
17 permit recovery, and the use of the word "shall" is included
18 in Section 2808(c)(2).

19 A. Well, I'm certainly not qualified as a lawyer,
20 but as a layman --

21 Q. That's what it says?

22 A. -- that seems to be accurate; yes.

23 Q. Now, will you agree with me then that in Section
24 2808(c)(3), the Act indicates that recovery may be allowed
25 by the Commission. The word "may" is used in that section.

1 A. Yes; that's correct.

2 Q. So that the Act itself makes some distinction
3 between non-utility generation contracts and utility
4 generation assets for purposes of stranded cost recovery?

5 A. Yes. I indicated that to you earlier. That was
6 my understanding.

7 Q. And along that line, is it your understanding of
8 the Act that it's up to the Commission to determine the
9 appropriate amount of recovery for a utility to receive with
10 respect to stranded costs?

11 A. I think that's generally a fair statement.

12 Q. And that the Commission would employ a just and
13 reasonable standard as to what the appropriate amount to
14 recover from ratepayers would be?

15 A. I think that's generally right. I mean that
16 standard, of course, occurs in the context of all the other
17 objectives of the Act from rate stability to protection
18 against cost shifting in rates and so forth.

19 Q. One last area. Page 67 of your rebuttal
20 testimony, here you're discussing Mr. Baron's objection to
21 the rate design approach which places 50 percent of the CTC,
22 if you will, into a fixed charge.

23 A. What line?

24 Q. Line 7 through the end of the page, roughly.

25 A. Okay.

1 Q. At lines 14 to 16 you indicate that a usage-
2 based CTC charge are avoidable to the extent that usage is
3 reduced and price-sensitive customers would be particularly
4 able to avoid the CTC were it entirely loaded in usage
5 charges. Is that only true if the customer ends up buying
6 no energy whatsoever?

7 A. No. It would be a function of the demand
8 elasticity, as this statement is trying to -- it's probably
9 a little awkward, but what I'm trying to say here is more
10 elastic demand consumers, upon seeing a higher usage-based
11 charge, if you loaded the CTC in the usage charge, would cut
12 back their demand more; lower demand elasticities would do
13 it less. What I'm trying to point out is that there's a
14 differential impact then depending upon the demand
15 elasticities of the customers.

16 Q. But the only way the entire CTC would be avoided
17 is if the end-user shuts down the plant completely and is no
18 longer buying any kilowatt-hours from PP&L or from an
19 alternative supplier?

20 A. Just not using any electricity?

21 Q. Right.

22 A. I suspect you're right. That's true whether the
23 CTC is put in a usage charge or partially in demand charges.

24 Q. I just wanted to make sure that you weren't
25 implying here that a customer not purchasing any kilowatt-

1 hours could somehow avoid the CTC. They cannot do that.
2 The level of CTC payments they make may change depending on
3 their usage sensitivity --

4 A. I think you and I are saying the same thing,
5 yes.

6 Q. Okay. Now, are you familiar enough with PP&L's
7 current rate design of its tariffs to know whether or not
8 100 percent of its capacity costs are collected in the
9 demand charges of the rates?

10 A. You mean the proposed rates?

11 Q. No. Existing rates.

12 A. No. I've not done a detailed study of existing
13 rates. I'm afraid I couldn't answer.

14 Q. Would you know enough generally whether it is --
15 -

16 A. I would suspect that -- I'm sorry; I think I've
17 heard discussions, so I would suspect they are not.

18 Q. So that even under existing regulated rates
19 today, you would agree that there are capacity costs of
20 generation that are collected in the energy charges of the
21 rates?

22 A. I think that's generally the case in
23 Pennsylvania and in some other states as well.

24 Q. Insofar as that is occurring today on PP&L's
25 system, if we take some of those, again, capacity or

1 generation costs and define them as stranded costs, is it
2 your understanding of PP&L's rate design proposal that some
3 of those costs would then be moved into the fixed charge CTC
4 as opposed to leaving them to be collected in the energy
5 charges of the existing rate design?

6 A. To the extent that the costs that are stranded,
7 which is calculated, as you know, as a residual between the
8 level of recoverable costs and the forecasted market price,
9 to the extent that those include costs associated with, say,
10 capital used in building generation, then, as I understand
11 it, the rate design proposal of the company would put some
12 of those costs -- in the case of industrial use, the rate
13 design would put 50 percent of those generation-related
14 costs into the so-called fixed or demand component of the
15 CTC and 50 percent of it into the usage charge.

16 Q. So there's a movement of those costs from energy
17 charge into fixed CTC charge?

18 A. I think that's right. The only thing I'm trying
19 to stress is that the stranded costs that are being
20 calculated are in fact a mixture of just a statement of
21 essentially the company's total costs, recoverable costs,
22 versus forecasted market revenues, and so whatever the
23 source of the company having costs which might become
24 stranded, whether they are high variable costs or high fixed
25 costs, capital charges or whatever, they're all captured in

1 that, in a sense. I'm sorry; the variable costs would not,
2 but it wouldn't necessarily -- the sort of tracing back of a
3 particular cost to a particular machine is not where the
4 stranded cost is arising from.

5 MR. KLEPPINGER: Thank you. That's all I have.

6 JUDGE KASHI: Thank you very much.

7 MR. KLEPPINGER: Right on time, Your Honor.

8 JUDGE KASHI: As always, Mr. Kleppinger.

9 We'll recess at this point until 1:30. We'll come
10 back and begin with Mr. Zalzman for the Environmentalists.

11 We stand in recess until 1:30.

12 (Witness temporarily excused.)

13 (Whereupon, at 12:30 p.m., the hearing was adjourned,
14 to be reconvened at 1:30 p.m., this same day.)

15
16
17
18
19
20
21
22
23
24
25

AFTERNOON SESSION

(1:30 p.m.)

JUDGE KASHI: Going back on the record.

Mr. Zalcman.

MR. ZALCMAN: Thank you, Your Honor.

Whereupon,**JOSEPH P. KALT****having previously been duly sworn, testified further as follows:****CROSS EXAMINATION**

BY MR. ZALCMAN:

Q. Good afternoon, Dr. Kalt. My name is Fred Zalcman, and I represent the Environmentalists in this matter.

I'd like to ask you to turn to your Exhibit JPK, the qualifications that are attached to your prepared direct testimony.

A. Okay.

Q. And on page 2 you list, the beginning of page 2, you list the various proceedings in which you've testified. Am I correct that this testimony is listed in reverse chronological order?

A. I don't know what reverse is. The most recent is listed first.

Q. And up to this point in 1997 you've testified on

1 four occasions; is that correct?

2 (Pause.)

3 A. I think that's accurate. I think since this was
4 prepared I've also -- I see a March date on it. I believe
5 I've also testified in another matter involving gas
6 extraction, CO² gas extraction in New Mexico, submitted
7 written testimony.

8 Q. So of these five proceedings, would it be fair to
9 say that of those, one dealt with matters related to
10 electricity energy?

11 A. Of those five, yes, that would be accurate.

12 Q. And similarly, looking at the matters identified
13 as testimony, in 1996 you participated in eight matters; is
14 that correct?

15 A. Yes.

16 Q. And of these, would it be fair to say that one
17 related to electricity energy?

18 A. No, in addition to the obvious one on
19 restructuring in New Hampshire, the top of page 3, the
20 Burlington Northern Santa Fe case actually ends up involving
21 quite a bit of issues related to electricity and electricity
22 restructuring, because the Burlington Northern Railroad and
23 the Santa Fe Railroad are major carriers of coal to electric
24 power companies, particularly in the southwest. And there
25 are quite a few issues in that case that were included in

1 part of my testimony as well as other people's testimony
2 dealing with electricity.

3 Q. Let's go back just a bit further. Have you --

4 A. I'm sorry. That would also apply to both
5 Burlington Northern citations there that you see in 1996.
6 One is the UPS pre-merger and one is the BNSF merger.

7 Q. Okay. Were I to extend this analysis to 1995, of
8 the six matters you identify in your testimony, would it be
9 fair to say that two pertain to electric energy?

10 A. Again, you'd have to add the Burlington Northern
11 one, so that would be another one. So those three were in
12 that year, three out of the -- well, three out of the four.

13 Q. Perhaps it would speed things along if you would
14 just take this subject to check. For 1993, would you agree,
15 subject to check, that one of the eight matters in which you
16 testified related to electric energy?

17 A. 1993?

18 Q. Yes.

19 A. No, I think in addition to the obvious one there
20 for PSI, on the bottom of page 4, the case labeled SAGASCO
21 Holdings, Ltd. was a merger in the national gas industry in
22 Australia, and electricity matters were quite prominent in
23 that case.

24 Q. And then finally, for 1992, can you tell me which
25 of the matters listed as testimony, which of those matters

1 related to electricity energy?

2 A. 1992?

3 Q. Yes.

4 A. The 1992, the matter, again, the one labeled
5 Burlington Northern Railroad Company, this was a case
6 involving Wisconsin Power & Light on electricity fuel
7 procurement.

8 Q. And of this testimony, can you tell me in which
9 of these instances you've asserted a regulatory compact
10 between regulated utilities and the government?

11 A. I discuss the uses of the regulatory compact on
12 page 2, the third item, Public Service Company of New
13 Hampshire; on page 2, the bottom, next from the bottom,
14 Northeast Utilities; page 3, in the middle, the
15 Massachusetts restructuring. I believe also on page 3 on
16 the bottom, Houston Lighting and Power.

17 I don't recall, it's been a while. There may have
18 been some discussion of the issue in the case next to the
19 bottom on page 4, the CINergy merger.

20 Q. Going back to the --

21 A. I think that would be a direct response, an
22 accurate response.

23 Q. Your reference to the New Hampshire case; what
24 were you recommending in that case with respect to
25 regulatory compact?

1 A. Well, the themes were very similar to what we're
2 presented with here. In particular I talked about the role
3 of regulation in establishing investors' expectations, the
4 implications of standard cost recovery mechanisms, including
5 rate design mechanisms for stranded cost recovery.

6 As far as it relates to regulatory compact issues,
7 they're parallel to what we have here.

8 Q. Are you aware of what the New Hampshire
9 Commission, in fact, adopted as its policy with respect to
10 regulatory compacts?

11 A. My understanding is that it's still being fought
12 over.

13 Q. I'm sorry; it's still being --

14 A. Being fought over, or discussed, etcetera.

15 Q. And do you know what level is being fought over?

16 A. I know there's still ongoing discussions at the
17 Commission, as I understand it, as well as concern, or focus
18 in the courts.

19 Q. Do you know whether the New Hampshire Commission
20 has set forth preliminary findings related to regulatory
21 compacts?

22 A. I believe I heard -- I've heard that they have.

23 Q. But you don't know what those policies are?

24 A. I don't recall specifically.

25 Q. Referring to page 11 of your direct testimony.

1 A. Uh-huh.

2 Q. On line 10, there you refer to the regulatory
3 compact; correct?

4 A. Yes.

5 Q. And you discuss the regulatory compact as an
6 historical relationship between the utility company;
7 correct?

8 A. Yes.

9 Q. Now, is it your testimony that this so-called
10 regulatory compact has continued uninterrupted since
11 regulators began regulating the rates charged by public
12 utilities?

13 A. Well, the essence of it has been there. It's
14 been rate of return regulation. There are, of course,
15 constant debates going on with respect to the opening up of
16 retail franchises. In most states that's been
17 uninterrupted, that component of those rules of the game,
18 the regulatory compact.

19 Q. And is it your testimony that this so-called
20 regulatory compact has been applied with equal vigor across
21 the country?

22 A. Oh, I think states have varied in the stability
23 of their policies. So I would say there's been variation.

24 Q. Do you recall having addressed the issue of the
25 regulatory compact as part of your research, in particular a

1 1987 study in --

2 A. Sure, sure.

3 Q. And you co-authored that study with Henry Lee and
4 Herman Leonard?

5 A. Yes.

6 Q. And the title of that 1987 study was
7 "Reestablishing the Regulatory Bargain in the Electric
8 Utility Industry"?

9 A. Yes. And it has a colon and then a longer --
10 something about Boston Edison, in the title. It was a study
11 done around Boston Edison.

12 Q. And can you tell me what the genesis of what
13 study was?

14 A. I believe it was the Seabrook, New Hampshire
15 plant, nuclear plant, either had come on stream or was about
16 to come on stream. There was considerable debate in New
17 England, in particular Massachusetts for Boston Edison, as
18 to the recoverability of Seabrook Nuclear costs, which like
19 many of the nuclear costs, you know, were -- there were
20 overruns relative to original forecasts. And so the study
21 grew out of the policy issues that were being raised at that
22 time.

23 Q. And then the particular problem that you were
24 addressing in your 1987 study was the breakdown of the
25 so-called regulatory compact; isn't that correct?

1 A. Well, we were looking at the issue of allowance
2 of nuclear costs into rate base. And then the thrust of the
3 analysis was that changing the rules in the middle of the
4 game as to what would be allowed in the rate base with
5 respect to nuclear costs and nuclear cost overruns, would be
6 a breakdown of at least that part of the regulatory compact
7 against this focus that you see in the title of the paper.

8 Q. And were you just warning of the breakdown of the
9 regulatory bargain, or were you, in fact, looking at some
10 specific case studies in which regulatory agencies may have
11 already --

12 A. Well, the thrust of it was really warning, that
13 is, they're describing consequences and the implications of
14 changing the rules in the middle of the game.

15 We did focus on what we termed as the breakdown in
16 specific instances, particularly the allowance of nuclear
17 cost.

18 I did not reach the conclusion that you all imply in
19 some of your filings that somehow the bargain was broken and
20 it was gone, and all parts of it were gone. That's just a
21 misrepresentation that you all have made in my testimony, in
22 my writings.

23 MR. ZALCMAN: May I approach the witness, Your Honor?

24 Your Honor, if I may, I'd like to have this marked as
25 Environmentalists Cross Exhibit 1.

1 JUDGE KASHI: So marked for identification.

2 (Whereupon, the document was marked as
3 Environmentalists Cross Examination
4 Exhibit No. 1 for identification.)

5 (Document handed to witness.)

6 BY MR. ZALCMAN:

7 Q. Do you recognize the document I've just handed
8 you, Dr. Kalt?

9 A. It seems to be an excerpt of the paper we've been
10 talking about.

11 Q. In fact, it includes the title, the table of
12 contents, the executive summary in chapter one of that
13 report; is that correct?

14 (Witness perusing document.)

15 A. When you call it chapter one, it looks like --
16 you mean the introduction?

17 Q. Yes.

18 A. Yes.

19 Q. And looking at page 2 of the executive summary,
20 would you read the last line from the first full paragraph
21 on that page?

22 A. "This perceived a symmetry, specifically
23 referring to the decision by the Massachusetts DPU, and
24 financial returns is at the heart of the breakdown of the
25 regulatory bargain."

FORM 2

1 Q. Turning to page 5 of this report.

2 (Pause.)

3 Q. Do you have that, Dr. Kalt?

4 A. Page 5?

5 Q. Yes.

6 A. Yes.

7 Q. Referring to the third alternative; and I believe
8 the third alternative is the pre-approval process that you
9 recommend, isn't that correct, related to generation
10 capacity?

11 A. I think we refer to it as a pre-approval approach
12 to prudence.

13 Q. And there you say that the third alternative,
14 restoring the regulatory bargain remains the best option for
15 assuring that future consumers will receive reliable power
16 supplies at reasonable prices; is that correct?

17 A. You've read the sentence correctly, yes.

18 Q. You identify a regulatory trend in which it was
19 to be sufficient to --

20 (Unintelligible.)

21 A. I couldn't hear you.

22 Q. I'm sorry. The study identifies a trend in
23 regulation in which it's not sufficient to simply prove
24 prudence in order to earn a return on investment in
25 generation plant; isn't that correct?

1 A. What we identify is this tendency to disallow
2 nuclear cost overruns contrary to, in some cases, original
3 prudence decisions or in contravention, apparently, that the
4 prudent standards in operation at the time that the
5 investment decisions were made on the nuclear power plants.

6 Q. And as we've established previously, this study
7 relied on case studies; is that correct?

8 A. We did some case studies, yes.

9 Q. Was one of the states that you examined for
10 purposes of this study Pennsylvania?

11 A. I don't know if we did a case study. We did look
12 at information on Pennsylvania, yes.

13 Q. And you interviewed regulators as part of this
14 process?

15 A. I think so. It's been a long time since we did
16 that. I'm not sure if we did in Pennsylvania or not.

17 Q. Do you know whether you interviewed utility
18 management with respect to Pennsylvania?

19 A. I don't know. Maybe the study -- does indicate
20 that we did, that I checked?

21 Q. Referring to page 10 of the study, would you mind
22 reading the paragraph beginning, "It matters little"?

23 A. "It matters little which side wins this
24 unfortunate debate, for nothing can change the fact that
25 utility managements and investors feel, and will act on the

1 feeling, that the traditional regulatory bargain has
2 collapsed. The financial markets now distinguish sharply
3 between companies with construction programs and those
4 committing no new capital to the electric business. Boards
5 of directors might agree small additions -- might agree to
6 small additions to capacity, and then only reluctantly, when
7 demonstrable needs emerge. But they've had billions of
8 dollars of their investment wiped from the books, and know
9 that some of those billions represented may have represented
10 monies spent on coal, not nuclear plants. They fear too
11 that the hostility to nuclear power in the 1980s may become
12 pollution induced hostility to coal plants in the 1990s,
13 forcing regulators to renew ex post consideration of those
14 in investments in the manner of recent years.

15 Q. Thank you. Dr. Kalt, is it fair to say that the
16 purpose of your testimony here is to provide the economic
17 policy framework for restructuring?

18 A. Here in this --

19 Q. In this --

20 A. In this proceeding?

21 Q. In this proceeding.

22 A. Yes, I think that's fair.

23 Q. Now, would you turn to page 5 of your direct
24 testimony?

25 You speak generically there of utility construction

1 programs and the factors that influence investment
2 decisions; is that correct?

3 A. You mean right at the top?

4 Q. Yes. It actually begins at page 4, line 11, and
5 carrying over to page 5.

6 (Witness perusing document.)

7 A. I see where you're asking. What's the question?

8 Q. Would you agree that there you're attempting to
9 identify historically the factors which led utility
10 investors to make certain resource commitments?

11 A. Just a general discussion of that nature.

12 Q. Now, in that section of your testimony, you're
13 not referring to any analysis you've done of PGL's decision-
14 making with respect to any of its generation capacity
15 constructed during this period; are you?

16 A. Well, I'm aware that PP&L has been subject to
17 some of the forces that are mentioned here; rapidly
18 accelerating inflation during the beginning of the 1970s,
19 etcetera. So I didn't mean it not to imply, but it's not to
20 describe PP&L specifically. I'm talking about forces in the
21 industry in general.

22 Q. But you conducted no analysis of PP&L's decision-
23 making with respect to, for example, it's Susquehanna
24 nuclear plant?

25 A. No, I have not investigated that specifically.

1 Well, to some extent, I have. I'm aware that they undertook
2 investments in consonant with what they viewed as their
3 responsibilities as a franchised utility. But beyond that
4 I've not tried to go back and reconstruct the Susquehanna
5 decision.

6 Q. And you're not testifying here that the
7 Pennsylvania PUC required PP&L to initiate and carry through
8 the construction of the Susquehanna plant?

9 A. I wouldn't say it that way.

10 Q. Nor are you testifying that the Pennsylvania PUC
11 induced PP&L to initiate and carry through the construction
12 of the Susquehanna?

13 A. Well, in a general way, it does in a general way,
14 that the regulatory commission is properly concerned about
15 supply reliability, etcetera, portfolio mix. And my
16 understanding is that those are considerations that went
17 into the company's decision, as I indicated to you a minute
18 ago; that is that they made the decisions cognizant of and
19 in the framework provided by the regulatory setting. Which
20 to a large extent, of course, is implemented by the
21 Commission.

22 Q. But there's no explicit mandate from the
23 Commission, for example --

24 A. You mean to go build the plant?

25 Q. To go build the plant.

1 A. Not that I'm aware of.

2 Q. Nor did the Commission constrain PP&L's
3 management discretion as to whether new capacity was needed,
4 its determination of whether new capacity was needed?

5 A. I don't think that would be an accurate
6 description.

7 Q. Can you explain how it's inaccurate?

8 A. Well, as I understand it, Pennsylvania, like most
9 states, has standards for what can go in rate base or what
10 cannot. And of course, that constrains decisions, to use
11 your phrase. So that would be a part of the decision-
12 making.

13 Again, my understanding is -- I have not tried to go
14 in and look through all the numbers on Susquehanna, but my
15 understanding is that that decision and related decisions
16 were made in the context of a regulated utility providing
17 capacity in order to meet service obligations, etcetera.

18 Q. The PUC didn't mandate to PP&L management as to
19 the resource choice; for example, to choose a nuclear
20 facility over coal or some other fuel sources; is that
21 correct?

22 A. I'm not aware that they did.

23 Q. Nor did the Commission dictate to PP&L management
24 where to site the plant?

25 A. I'm not exactly sure where the siting licensing

1 power lies within the state of Pennsylvania. I know that,
2 of course, sites do have to be approved. I'm not sure
3 whether it's the Commission; I know that someone else, if it
4 wasn't the Commission, must have had that power.

5 Q. And in terms of equipment vendors, would the --

6 A. I'm sorry? Equipment what?

7 Q. In terms of equipment vendors, would the
8 discretion in the first instance be with PP&L management
9 vendors to select for contract purposes the construction of
10 plant?

11 A. I'm sorry; would you repeat it, please?

12 A. In terms of management discretion on which
13 contractors to contract with for purposes of building
14 Susquehanna nuclear plant or any other facility, would that
15 decision have been in the first instance at PP&L management
16 discretion?

17 MR. KAPLAN: Your Honor, I think we're going way
18 beyond the scope of direct, way beyond the relevant issues
19 in this proceeding. I believe there was a Susquehanna
20 prudency proceeding. Maybe Your Honor had the fortunate
21 ability to sit on that proceeding, or not; I don't know.
22 This is not relevant to this case.

23 There's discretion of the management as to which
24 contractor to use to new plant that's been in operation for
25 ten years, and has no direct relationship to the stranded

1 cost issue. I think it's not a relevant issue. And it's
2 certainly far beyond the scope of the testimony of Dr. Kalt.

3 JUDGE KASHI: Well, doesn't the stranded cost issue
4 go somewhere to the extent that the reason that we're
5 talking about stranded cost is because the poor company was
6 forced into doing this by the Federal Government or the
7 state governments, and now that the governments have changed
8 the rules of the game in the middle that stranded costs
9 would be allowed?

10 MR. KAPLAN: Well I'm not objecting to that
11 statement, Your Honor. And while I think the matter of two
12 or three questions that were asked maybe skirted along the
13 edge of relevancy, we are beyond that. The question here
14 involved the choice of the contractor. It had nothing to do
15 with the amount they spent or whether they were required to
16 build a plant.

17 And the issue, at best, is, were they required to
18 build Susquehanna by an obligation to Pennsylvania. The
19 issue is not the manner in which they built the Susquehanna,
20 in terms of the selection of contractors. Unless he can --

21 JUDGE KASHI: Isn't that part of the issue as to the
22 discretion that the company had?

23 MR. ZALCMAN: Your Honor, if I may?

24 JUDGE KASHI: Go ahead.

25 MR. ZALCMAN: The witness's testimony at page 5, line

1 7, is that the regulatory process induced and required many
2 utilities to initiate and carry through large construction
3 programs. I'm simply probing the extent to which this
4 Commission induced and required the company to carry through
5 on the Susquehanna.

6 MR. KAPLAN: My only request, Your Honor, is we can
7 tie questions such as management discretion as to which
8 contractors to use to the issue of whether or not this is a
9 properly stranded cost.

10 But I see no relationship. As I said, we seem to
11 have gone off way -- we've gone off into the issue, which is
12 traditionally the subject of a prudency case, but not the
13 subject of whether or not there was state pressure or state
14 encouragement in building Susquehanna. These questions are
15 directed to how the company went about doing it.

16 If he can tie that question specifically to the
17 decision to build it in terms of spending and cost, then we
18 might have a relevant question. Might.

19 But I do point out there was a prudency proceeding on
20 Susquehanna, Your Honor.

21 JUDGE KASHI: Yes, I understand that. I don't think
22 that that wipes out the issue that's before us, the mere
23 fact that there was a prudency proceeding on Susquehanna.

24 The gentleman's testimony, in effect, says that many
25 jurisdictions operated to induce or require many utilities

1 to initiate and carry through large construction programs.
2 And I think counsel is entitled to see where that goes with
3 PP&L. I'm going to overrule your objection, Mr. Kaplan.

4 But, now, we're not going to do a prudency review
5 here.

6 MR. ZALCMAN: No. Let me just state that this is the
7 last of my questions along this line.

8 BY MR. ZALCMAN:

9 Q. To what extent has the Commission restrained PP&L
10 management with respect to its choice of vendors in building
11 Susquehanna plant or any other plant?

12 A. Well, I've not done a specific study or review of
13 the prudence of those decisions. As a general matter, the
14 extent would arise from the prudence requirements and the
15 recognition on the part of management that they're operating
16 in a regulated environment in which their ability to recover
17 costs would, in part, be a function, potentially, of their
18 choice of vendors. And were they, for example, to
19 imprudently select an unqualified vendor, that might well
20 cause their investments to be disallowed from rate base.

21 So, that would be the key role, and the
22 constraintive, to use your word, that would be played by
23 Commission policy.

24 Q. If I understand your testimony, it's the threat
25 of post hoc prudence disallowance that acted as a

1 constraint, rather than an explicit directive from the
2 Commission?

3 A. To hire a particular vendor?

4 Q. To hire a particular vendor.

5 A. My experience has been very are the Commission
6 would ever -- in fact, I don't know of any case where a
7 commission would say you have to hire a particular vendor.
8 In addition to the other -- I mean, I don't mean to be
9 facetious about this. Of course, there'd be other
10 constraints as well beyond the issue of rate disability of
11 an investment related to, if you took a vendor on a bribe or
12 something, you'd have all sorts of problems as well.

13 Q. For purposes of your testimony in this case, have
14 you analyzed the Pennsylvania regulatory decisions for
15 articulation of the regulatory compact?

16 A. Well, I've read some on that, and seen some
17 discussion in the record on this case on that.

18 Q. I'm sorry; you've seen?

19 A. Seen some discussion of those kinds of issues in
20 the record of this case.

21 Q. And can you point to any specific decision in
22 Pennsylvania which articulates the regulatory compact?

23 A. Well, I mean if you look at, I think it's -- I'm
24 not a lawyer, so I don't cite these. But the key segment of
25 the laws of Pennsylvania, I think it's Chapter 13, or

1 Section 13, that lays out the criteria for ratemaking, sets
2 forth standards of just and reasonable and related matters
3 that go into establishing a regulated utility's rate base
4 and the prices that it can charge.

5 As I understand it -- I can't cite exactly where this
6 is, but I've read it somewhere. As best I understand it,
7 and I believe I've read it, Pennsylvania has also had a
8 policy prior to the passage of the act which effectively
9 constituted exclusive territory for the main line utilities
10 in the provision of electric power. And obviously the act
11 is changing now because of one of its simple components.

12 In addition, I've seen some information and studied
13 some information I believe referred to in the research that
14 you asked me about before related to used and useful
15 standards in Pennsylvania.

16 In addition to that, I've done some research on
17 reliability in the industry and state of Pennsylvania
18 policies and related PJM policies were part of that
19 research. And I understand there to be requirements that
20 continue under the act through supply of last resort kind of
21 criteria for reliable service; and of course universal
22 service, as well.

23 Q. Is it your interpretation of Pennsylvania's
24 application of the used and useful standards that that
25 represents an articulation of the regulatory compact?

1 A. I think it would be interpreted as part of the
2 rules of the game that the state of Pennsylvania has tried
3 to discuss and articulate.

4 Q. Okay.

5 MR. ZALCMAN: Thank you, I have no further questions,
6 Your Honor.

7 JUDGE KASHI: Thank you very much.

8 Ms. Moury?

9 MS. MOURY: I have no questions, Your Honor.

10 MR. KOHLER: Your Honor, I know that, per your
11 instructions, I had agreed to move my exhibits into evidence
12 after my group was up. And I realized halfway through this
13 cross that the Environmentalists are outside of my group.

14 So if Your Honor would permit me, I would move Enron
15 Cross Exhibits 1 and 2 into the evidence at this time.

16 JUDGE KASHI: Without objection, they're received
17 into the evidentiary record.

18 **(Whereupon, the documents marked as**
19 **Enron Cross Examination Exhibit Nos. 1**
20 **and 2 were received in evidence.)**

21 MR. ZALCMAN: Your Honor, would it be appropriate for
22 me to move my cross exhibit at this time?

23 JUDGE KASHI: Environmentalists' Cross Examination
24 Exhibit No. 1 is received into the evidentiary record
25 without objection.

1 MR. KAPLAN: No objection, Your Honor.

2 JUDGE KASHI: All right.

3 (Whereupon, the document marked as
4 Environmentalists Cross Examination
5 Exhibit No. 1 was received in evidence.)

6 MR. KAPLAN: I do request if they have a complete
7 copy of the study available that they make it available to
8 us now, and we will return it to them a little bit later.

9 Do you have that copy?

10 MR. ZALCMAN: I do not.

11 MR. KAPLAN: Well, Your Honor, I would like to make a
12 reservation to have the opportunity to put other parts of
13 the study in evidence when we've had a chance to examine the
14 entire study.

15 JUDGE KASHI: All right.

16 MR. KAPLAN: Thank you, Your Honor.

17 Mr. Caplan?

18 MR. CAPLAN: Thank you, Your Honor.

19 **CROSS EXAMINATION**

20 BY MR. CAPLAN:

21 Q. Dr. Kalt, my name is Richard Caplan, and I
22 represent a number of independent power producers, including
23 Schuylkill Energy Resources and the Gilberton Power Company,
24 in this proceeding as intervenors.

25 I want to ask you some philosophical questions which

1 your testimony and rebuttal testimony raised for me. And
2 you'll excuse the fact that I am not an economist, and
3 therefore will be couching this in language which you may
4 find less than precise. And if so, please ask me to
5 rephrase it, or correct me if I say something that doesn't
6 comply with your expertise.

7 I see in the general tenor of your rebuttal
8 testimony, in particular, some disagreement with experts
9 proffered by intervenors with regard to the level of, shall
10 we say, strictures to be imposed on PP&L in its effort to
11 compete as an independent supplier in a deregulated market.
12 Is that fair to say so far?

13 A. That's fair. Thank you.

14 Q. And they seem -- and by they, I mean the
15 intervenor expert -- to be suggesting more structural rules,
16 more structural changes, more overt impediments upon the
17 free exercise of PP&L's discretion with regard to
18 competition in the retail market than you are proposing or
19 supporting; is that fair to say?

20 A. It's not just a question of counting up. I think
21 the disagreement, as I tried to say at the start of this
22 morning, centers on what actions, activities, assets,
23 structural characteristics promote, or potentially promote,
24 the leveraging of monopoly power from the continuing
25 monopoly functions, particularly the essential facilities of

1 T & D, transmission and distribution, into a stifling of
2 competition, a potential stifling of competition in non-
3 monopoly functions. And I've tried to be very clear that
4 those kinds of things are precisely what policy should go
5 after and it should be vigilant in protecting against.

6 The disagreement arises because even if there's none
7 of that leveraging that I'm talking about, it appears that
8 other intervenors are desirous of in one way or another --
9 and I use the word "handicapping." We don't have to get
10 into semantic distinctions. But one way or another, at
11 least during, I think what one of the intervenors calls it,
12 a transition period, inhibiting the ability of the incumbent
13 utility to compete, even when the sources of the competitive
14 vigor of the company are not related to this leveraging of
15 market power.

16 Q. Let me ask you this question, because it troubles
17 me. Are some of the inherent competitive advantages that
18 PP&L would enjoy in a competitive marketplace a product of
19 the regulatory compact? The very same regulatory compact
20 which you believe requires the reimbursement to PP&L of
21 prudently incurred stranded costs?

22 A. Well, the key one that people seem to focus on is
23 the brand name, apparently, PP&L.

24 Q. Well, let me give you a hypothetical.

25 MR. KAPLAN: Excuse me. Dr. Kalt was still answering

1 the question.

2 MR. CAPLAN: I'm sorry, excuse me. I apologize.

3 THE WITNESS: I'll try to answer the question this
4 way. Let me give you a hypothetical, if I could; the brand
5 name issue. We're all aware that some utilities around the
6 country have good brand names, some of them have real bad
7 brand names. And that fact suggests, of course, that it's
8 not a function of their ownership of essential facilities
9 T & D, the natural monopoly function that's generating the
10 brand name. Otherwise they'd all have great brand names.
11 See the logic of that?

12 And it's sort of running a hard counter-factual to
13 say, well, if we hadn't had this long history of the kind of
14 regulation that we've had, the regulatory compact, rate of
15 return regulation and all of that, would there be a company
16 called PP&L with a good brand name. And the evidence says
17 that already in the electricity market companies get good
18 brand names and can transfer good brand names, even if they
19 haven't been an incumbent utility.

20 So I think as a matter of strict logic, of sort of
21 causation of -- you want to talk philosophy -- you want to
22 talk about causation, I think you cannot conclude that the
23 good brand name's a function of the natural monopoly
24 attributes or just a fact of regulation over the last 75
25 years.

1 BY MR. CAPLAN:

2 Q. What about capability to generate electricity at
3 low cost? I'll give you the hypothetical I have in mind.
4 Atomic power plants. You will admit, will you not, that
5 generally speaking in the United States -- and I can't say
6 this categorically, because I haven't done the research --
7 atomic power plants are owned by regulated electric
8 utilities, not by private power companies?

9 A. Either that or by public enterprises like TVA.

10 Q. But basically, you would concede that they are
11 quasi-regulated entities owned by somebody?

12 A. Sure.

13 Q. And you have suggested, if you will, that to some
14 degree at least the regulatory compact was the driving force
15 for the acquisition of those atomic power plants; correct?

16 A. I've tried to say in both this and in my
17 testimony, and my discussion earlier was that as part of the
18 regulatory framework companies have effectively, with some
19 variation here and there with municipalization, exclusive
20 franchises. And as part and parcel of that they incurred
21 obligations. I use the word "requirement" here, now. To
22 make sure that the power flowed to the customers. And they
23 bore penalties if there were blackouts and so forth. And
24 that created a framework in which then it was expected; and
25 indeed, they did go out and build generation capacity.

1 Q. Now, let's assume that if we're talking about an
2 atomic power plant, that it has an energy only avoided cost
3 of something less than one cent per kilowatt hour. Would
4 you agree with that?

5 A. Well, I've seen numbers like that, yes.

6 Q. Yes. So, to all intents and purposes, if the
7 only asset, generating asset, that the utilities own,
8 including PP&L, were atomic power plants, and the market
9 price for energy in the retail market approached energy only
10 avoided cost, all of those utilities could sell power in
11 your paradigm of the competitive market at below one cent;
12 correct?

13 A. If I understand your question, and I am an
14 economist, I think of it in terms of supply and demand. You
15 mean, for example, demand is just so totally collapsed that
16 the only thing, the lowest marginal cost units are the only
17 ones that need to be run, then the lowest marginal cost
18 units would add up to the supply and set the price, and you
19 can draw the demand curve in far enough that the price could
20 be down there below one cent.

21 Q. Fine. And the fact is that these utilities, by
22 virtue of the compact that they have with regulators over
23 the 75-year period are the exclusive owners of those
24 generating facilities; isn't that true?

25 A. I'm sorry, I don't understand your question,

1 because you've linked it to the previous question. There
2 doesn't seem to be any link.

3 Q. What I'm interested in knowing is -- well, let me
4 give you a hypothetical, and maybe this will clarify where
5 I'm going.

6 Let us assume that in the retail market, the only
7 economically viable competitors turn out to be regulated
8 utilities; okay?

9 Now, this is my hypothetical. My hypothetical is
10 this. When the smoke clears, the only parties playing the
11 game for the retail customer are regulated utilities.

12 A. Playing the game --

13 Q. Not just Pennsylvania, but everybody else.

14 A. And just to keep me focused, you're talking about
15 the generation of electricity?

16 Q. Yes, right.

17 A. Yes.

18 Q. The only competitors for the generation and sale
19 of electricity.

20 A. Okay.

21 Q. Are regulated utilities. And that's because they
22 have the capacity, as demonstrated, for example, by the PJM
23 spot market, the wholesale market that PP&L has been using
24 to forecast the energy cost component in the future. Are
25 you familiar with the fact that they've been using PJM --

1 A. Yes, I am.

2 Q. -- wholesale prices for that purpose?

3 A. They make some --

4 Q. And you're aware that until very recently the
5 only parties that could trade in that wholesale market were
6 regulated utilities? Isn't that so?

7 A. I know that it's changed. You say until very
8 recently; I'm not sure of what --

9 Q. Within the last eight months, maybe.

10 A. Well, I don't think that's quite right.

11 Q. Well, in other words, we're talking about a
12 development that --

13 A. Relatively recent.

14 Q. -- was within the last year, let's say.

15 A. The FERC has been undertaking mechanisms for
16 several years to open up power pools and so forth.

17 Q. But in 1996, trading in the PJM market was all
18 between regulated utilities; true?

19 A. I'm not sure that that's accurate.

20 Q. But you don't know?

21 A. I'm not sure.

22

23

24

25

1 Q. If this paradigm that I've created
2 hypothetically in which regulated utilities, a number in
3 Pennsylvania and outside poachers from other states, are the
4 only competitors and that drove the price to the marginal
5 cost of producing units of power, would you not agree that
6 from your point of view, that would be a robust competitive
7 market?

8 A. I have not done a detailed study of your
9 hypothetical, but it is purely a factual matter. One could
10 find in a particular setting that there were lots of such
11 utilities. As in usual hypotheticals from attorneys, there
12 are lots of questions I could ask you, and I don't want to
13 bog things down.

14 If people have open access transmission, then that
15 tends to open up the market and there might well be so many
16 utilities, that that's a quite robust market. On the other
17 hand, it might be the case in a particular setting that for
18 whatever reason, absence of transmission, something like
19 that, or no open access to transmission, that there are only
20 one or two utilities and you start to worry more about
21 competition on the generation side.

22 Q. In my hypothetical, assuming that the only
23 parties that could compete because of their production
24 efficiencies are regulated utilities, in that circumstance,
25 the market that results, to the extent that it provides the

1 lowest price to consumers, would satisfy your vision of what
2 a robust competitive market would be; no?

3 A. No. As I said, that is a factual question. If
4 it turned out to be there was no transmission up in the
5 northern Rockies and Montana Power is the only utility and
6 by hypothesis in your hypothetical nobody else can come
7 compete, it doesn't sound to me like a competitive market.
8 It sounds like a monopoly.

9 In other words, it's a question of the factual
10 setting, and what you can say is the two premises that your
11 question requires seems to me to not be accurate. One is,
12 of course you do have open access transmission which allow
13 not only utilities, but others to reach the marketplace.

14 Second, I don't think the presumption in your last
15 opening to this line of questioning, the presumption that
16 utilities are the only ones who are efficient and can
17 compete, is accurate. That doesn't seem to be accurate at
18 all, factually, in terms of the real world out there.

19 Q. All I'm trying to suggest by my line of
20 questioning is whether in fact you can forget about the
21 positive benefits to the utilities as competitors which the
22 regulatory compact provided looking backward and only think
23 about it in terms of what is created going forward by cross-
24 subsidization or other leveraging.

25 Your view says we'll forget about the fact that the

1 regulatory compact created this entity, in other words,
2 built and allowed this entity to create excess capacity, has
3 allowed this entity to build atomic power plants which can
4 generate electricity at fractions of a cent per kilowatt-
5 hour, has given this company the opportunity to build the
6 infrastructure, to develop the 100 percent domination of the
7 customer base, all of these benefits that have been conveyed
8 by the regulatory compact and you've said, well, we'll
9 discount those going forward. Assume that they got them
10 through their own waivers without regard to the advantages
11 that regulation provided to accrue those benefits and only
12 worry about the use of the T&D monopoly in leveraging,
13 forgetting about the fact that they started with an
14 extraordinary advantage vis-a-vis the Enrons and the
15 independent power producers of the world.

16 Am I wrong in seeing it that way?

17 A. I think your question is not an accurate
18 characterization of my testimony. I discussed it with the
19 direct and rebuttal testimony, the fact that, for example,
20 the FERC has now provided provisional approval to market
21 based rates. What does that come out of? That comes out of
22 an analysis which looks at the kind of things your
23 hypothetical was getting at. Who's out there? How many
24 NUGs are there? How many utilities are there? What is the
25 transmission capability? Who can get into a particular

1 geographic part of the country?

2 That analysis -- and I endorse it in my reports --
3 appropriately says you find out that that market is not
4 competitive. Then you don't want to just turn it loose to
5 total deregulation.

6 Now, in doing that analysis -- and now this is just
7 sort of -- I don't want to sound like a typical FERC
8 economist, but it is a framework which says we will take
9 into account the installed base generation capacity of all
10 these utilities regardless of why they built it. In a
11 sense, regardless of whether it was prudent or dictated by
12 anyone else, we'll take that into account as part of the
13 supply that is in the market. Then we'll do a supply and
14 demand analysis.

15 That analysis implicitly says that if it were the
16 case that you found that there was one utility out there
17 that could flood the market with 1-cent power and everybody
18 else was up to 5 cents or something like that and you could
19 satisfy all the demand in that market, then you'd
20 potentially have a market power problem.

21 Now, the problem with your analysis from a market
22 power analysis point of view is that say I'm a utility and I
23 have some low-cost power. The fact that I have some low-
24 cost power does not in any way give me any market power,
25 because, a fairly familiar phrase, but it is a economist's

1 phrase, competition occurs at the margin. It is appropriate
2 to look at the margin where supply and demand are trying to
3 come into balance. Are there competitors?

4 If I come into a market with relatively low-cost
5 source of supply, I can make some money, perhaps, but it
6 doesn't give me market power unless I have the ability to
7 flood the market, be the monopolist and satisfy all of the
8 consumption out there.

9 To my knowledge, no utilities under the regime being
10 set up by the FERC have that capacity in the United States.

11 Q. Let me ask you about the significance of the
12 code of conduct and the other, shall we say, ethical
13 prohibitions against predatory behavior by a regulated
14 utility during the transition and beyond.

15 Your model it would seem to me presupposes the
16 availability of expeditious trained dispute resolution
17 mechanisms of one kind or another. Is that true?

18 A. No, I don't think that's accurate.

19 Q. In other words, you kept talking about the
20 oversight by FERC and the oversight by the PUC. Doesn't
21 that oversight capability translate into some kind of
22 adjudicative system that is both time responsive and
23 educated in the ways of competitive predatory behavior so
24 that in fact if there are violations claimed by the code of
25 conduct or there is conduct in the marketplace which is

1 anti-competitive it can be addressed promptly and curative
2 measures taken?

3 A. Let me address the first question you asked and
4 then the second question. When I say to you my testimony is
5 not that I am presuming or -- I think your word was
6 "presume" or "presuppose" -- what I say in my testimony
7 quite bluntly is -- I'm almost verbatim quoting, and we can
8 look at it. I think it's in the rebuttal testimony -- no
9 one should presume that this task of oversight is perfect,
10 without effort, without some investment and learning. These
11 are the real world problems that these participants in one
12 way or another in this process face.

13 So I'm not presuming some perfect regulator that
14 knows everything and zaps the company anytime they cross
15 over the boundary. That's not the case. That would be an
16 incorrect implication for any policy prescription of anybody
17 in this room to be implying.

18 Now, with respect to the second part of your
19 question, I think I can say it is the case that all else
20 equal, one would prefer to have experienced people rather
21 than inexperienced people. Yet, as we embark on the
22 restructuring of the electric power industry, that's what
23 we're doing is trying to provide the frameworks, the
24 intellectual mind sets, et cetera, that provide the setting
25 within which future regulators will enforce the company's

1 code of conduct, will zap them if they cross the line and so
2 forth.

3 Q. Isn't it correct that the less strictures that
4 are built into the operations of the marketplace, the more
5 vigilant the supervisory agencies have to be?

6 A. There is a sense in which that could be true,
7 but it's not a carte blanche truism to say that. I make a
8 remark again in my rebuttal testimony about I teach at a
9 school of public policy. There is lots of research. In
10 many context, the more detailed rules and regulations
11 become, they can become harder to enforce. The attempt to
12 detail creates the mind set or an approach of loopholes. So
13 you only said I could do that between the hours of 4:00 and
14 6:00. I did it at 6:01. And yet, you're breaking the
15 intent of the law.

16 Consequently, in many parts of this kind of law and
17 regulatory policy, we have adopted an approach in which we
18 have laid down very clear dos and don'ts. Don't
19 discriminate. Don't deny access. Don't engage in tying and
20 so forth. Those then provide the hammer, if you will, to
21 the enforcer to go out and enforce the rules, regulations
22 and laws.

23 Q. Have you done a study of the efficacy of
24 enforcement in this field by any agency at all? In other
25 words, have you looked to see if in fact there is a history

1 of successful enforcement of anti-competitive scrutiny at
2 the PUC here in Pennsylvania?

3 A. Let me answer the first part of your question,
4 which was have I done any of this kind of research. I have
5 done some research of this over my career, yes, both in a
6 systematic way, as well as by participating so much in the
7 electricity side, the gas side, telecom and so forth, I've
8 seen the evolution of policies.

9 Then with respect to your second question, in some
10 original research I did a number of years ago, Pennsylvania
11 was included, but I've never undertaken a specific,
12 systematic study of Pennsylvania's performance in terms of
13 limiting market power of regulated utilities.

14 Q. Are you aware of any area other than perhaps
15 trucking in which the PUC has any history of engaging in
16 such conduct?

17 A. I believe they're doing it in telecom. I
18 believe they've been a participant in a number of the
19 natural gas debates with respect to open access and
20 pipelines and so forth.

21 Q. I'm not interested in policy debates. I'm
22 interested in enforcing complaints by potential or current
23 competitors as to anti-competitive predatory or anti-trust
24 type behavior.

25 Are you familiar with the PUC's record in any area

1 other than potentially trucking involving this kind of
2 activities?

3 A. I'm aware that they are engaged in it in
4 telecom. What specific actions they may have now taken of
5 an enforcement nature -- I know they are involved in
6 rulemaking -- I have not done a detailed study of that.

7 Q. Are you aware of the fact that the FERC is so
8 backlogged that proceedings initiated even by PP&L itself in
9 which the allegations are that the ratepayers are losing
10 money at a million dollars a month have been sitting
11 unattended for more than a year by the FERC?

12 MR. KAPLAN: I object, Your Honor. There is
13 absolutely no foundation for that question and is indeed, as
14 a practicing FERC lawyer, untrue.

15 JUDGE KASHI: Do you want to rephrase the question,
16 Mr. Caplan?

17 MR. CAPLAN: Yes.

18 BY MR. CAPLAN:

19 Q. Are you familiar with the fact that there is now
20 as to many matters before the FERC an extraordinary level of
21 delay associated with the workload that the agency has to
22 meet on a day to day basis?

23 A. I don't know what FERC's backlog is at the
24 current time.

25 Q. Would you admit, sir, that in a competitive

1 marketplace, delayed adjudication of complaints by entrants
2 into the market or existing competitors with regard to
3 predatory conduct, that such delay would in fact potentially
4 undermine the validity of the remedy?

5 A. That is not necessarily the case. It certainly
6 could be the case. What I'm thinking is, of course, what
7 FERC has tended to do in my experience, as well as other
8 adjudicatory bodies, is to take precedential cases, cases
9 that will establish precedent, and thereby lay down the law,
10 if you will, as to where and how regulatory policy will be
11 enforced.

12 So accordingly, I know, for example, that electric
13 power companies very closely watch what FERC does on the gas
14 side, the decisions there, because it obviously sends a
15 precedent for how to think about if you're running a
16 company, for example, what actions are going to be
17 permissible and which will not.

18 Q. You yourself also have acknowledged in your
19 testimony, have you not, that the courts are not very good
20 at policing markets using anti-trust powers?

21 A. What I'm trying to say is that, of course,
22 they're not very good in being regulatory agencies of the
23 day to day monitoring of the behavior of companies going
24 through proceedings like we're doing right now. They're
25 dealing with lots of other matters.

1 Q. I just want to ask you one or two questions
2 about stranded costs. Am I correct that the lower the
3 forecasted energy market price that PP&L is able to convince
4 the PUC to be accurate, the higher the margin of stranded
5 cost recovery potential?

6 A. If I understand your question -- correct me if
7 I'm wrong -- you're describing the mathematics?

8 Q. Yes, the mathematics.

9 A. I think that is accurate.

10 Q. There has been an occasion --

11 A. The higher the calculation of stranded cost. It
12 doesn't tell you what actually gets collected.

13 Q. So it is a theoretical calculation; but the
14 lower the forecasted future market price, the larger the
15 interval of potential stranded cost recovery?

16 A. That's correct.

17 Q. Now, there was an opportunity in the 1980s for
18 PP&L to do forecasting of energy market costs, was there
19 not, presented by PURPA and the concept of levelized
20 contracts? Are you familiar with the fact that under PURPA,
21 which is the Public Utility Regulatory Policy Act, one of
22 the options available to the independent producer and the
23 utility buyer was to enter into a fixed rate of return
24 levelized contract for the duration of the contract, which
25 most of them were 20-year periods, and that required the

1 utilities to make a forecast of its energy-only avoided
2 costs for 20 years? Are you familiar with that fact?

3 A. Everything except the last statement you made I
4 think is generally accurate in my experience. That is, I
5 know and have seen levelized PURPA contracts. I believe
6 I've seen cases in which the need to forecast was shorter
7 than the term of the contract, considerably shorter, but
8 there was some forecasting that was done.

9 Q. And that was done by the utilities, not by the
10 independent power producer; isn't that correct?

11 A. Both sides probably were doing it.

12 Q. Well, the law required that the purchase be at a
13 price no higher than energy-only avoided cost of the
14 utility, not having anything to do with the power generated.

15 A. That's generally how PURPA works, yes.

16 Q. Are you familiar with the fact that PP&L did in
17 fact forecast in or around 1985 or 1986 for a period of 20
18 years an energy price of 6.6 cents?

19 A. I'm not aware of that, no. I've never seen that
20 particular number.

21 Q. Are you familiar with any of the contract prices
22 that currently exist in PURPA contracts involving PP&L as
23 the purchaser for the independent producer?

24 A. I've seen some discussions somewhere in the
25 course of the work on this matter, but I don't recall

1 anything specific.

2 Q. Are you familiar with utilities, including
3 Niagara Mohawk of New York and other utilities, who have in
4 effect essentially gone to FERC or to their state agency in
5 an effort to get out of contracts that they made because the
6 forecasts which they made in the 1980s of the energy price
7 going forward turned out to be grossly inaccurate?

8 MR. KAPLAN: Excuse me, Your Honor. First of all, we
9 may be getting far afield. Second of all, I think there is
10 a mischaracterization of the practice in Pennsylvania. As I
11 understand it, it was an energy and capacity avoided cost,
12 an avoided cost of constructing the capacity as well.

13 MR. CAPLAN: May I respond, Your Honor?

14 JUDGE KASHI: Yes.

15 MR. CAPLAN: Learned counsel is incorrect. I
16 happened to represent parties to this proceeding before the
17 FERC; and in general, there is not necessarily an energy and
18 capacity cost. It is in fact an energy-only avoided cost.

19 The reason I'm interested is to find out whether we
20 should have a high level of confidence in PP&L's ability to
21 forecast the energy price today which it would like to make
22 as low as possible when in fact in the 1980s it
23 overestimated the cost today by a factor of at least three
24 to five.

25 JUDGE KASHI: Are you prepared to put that into

1 evidence, sir?

2 MR. CAPLAN: It is a matter of public record. I
3 don't even have to put it into evidence. I can ask that you
4 take judicial notice of it. Virtually all of the contracts
5 involving the independent power industry under PURPA that
6 were entered into by PP&L are at prices between 5 and 7
7 cents per kilowatt-hour. I don't think counsel would deny
8 that and would stipulate to that.

9 MR. KAPLAN: First of all, I see no relevance to this
10 case. Secondly, counsel had an opportunity to offer
11 evidence and chose not to. Thirdly, we have an excellent
12 witness, Dr. Scott Jones, who did our market price analysis,
13 who will be testifying on Monday morning next week, who will
14 be happy to answer Mr. Caplan's questions. This is clearly
15 beyond the scope of Dr. Kalt's testimony.

16 MR. CAPLAN: Your Honor, it isn't in one respect, and
17 that is to the extent that the forecasted energy price turns
18 out to be erroneous and in this case to be a lower price and
19 the reality turns out to be higher, there is the opportunity
20 for an increased level of recovery of stranded costs, and
21 there are competitive implications to that which I would
22 like to ask the witness about very briefly just to establish
23 that the history of forecasting of energy prices going
24 forward has not been, shall we say, rocket science. I think
25 it is completely germane.

1 JUDGE KASHI: All right. Why don't you ask him on a
2 hypothetical basis and then go into how that involves the
3 competitive nature of the stranded costs?

4 MR. CAPLAN: Thank you very much.

5 BY MR. CAPLAN:

6 Q. Under the statute, the recovery of stranded
7 costs is to take place within a fixed period of time. I
8 think it is nine years or seven years, whatever. Correct?

9 A. Correct.

10 Q. To your understanding, would that be an
11 acceleration of the recovery of those costs over what would
12 have been recovered if deregulation had not ensued?

13 A. I've never done a detailed analysis of the exact
14 profile, but it could well be the case that some costs might
15 have longer lives, might have been in rate base for 20
16 years, for example, so you can get that kind of effect. For
17 other things, it is stretched out the other direction, so I
18 don't know what the net is.

19 Q. And there is no --

20 A. By the way, if I could just point out, by doing
21 the calculation on a present value basis the way the Act
22 requires, economically you're eliminating the spreading out
23 as an issue of concern because you're holding the present
24 value constant.

25 Q. Is there any limitation to your knowledge on

1 PP&L's use of the funds as specified in the statute, for
2 example?

3 A. I know they can't be used for cross-
4 subsidization, for example. I don't know if the Act uses
5 the word "cross-subsidization." I don't recall. But it
6 would be inconsistent with the thrust of pro-competitive
7 aspects of the Act.

8 Q. And would an independent producer be satisfied
9 that in fact those funds were not used to subsidize the
10 energy costs?

11 A. Well, the regulators and the company are putting
12 in place a set of policies that act to thwart any cross-
13 subsidization. I list a number of these in my testimony,
14 and let me just touch on them quickly for you.

15 First, the cost allocation mechanism that is being
16 created along with the functional separation and the related
17 attributes of functional separation that appear in the
18 company's code of conduct and the FERC code of conduct play
19 a direct role in that.

20 In addition, the rate cap, of course, provides a
21 mechanism. Since any incentive to cross-subsidize, that is
22 high costs that are really on the non-regulated side of
23 business, hide those in your regulated business so that you
24 can jack them up in rates, you can't do that if rate cap is
25 effective.

1 Then, of course, with respect to the specific pricing
2 of electricity provided to its own customers, as we've
3 discussed, those prices would be established on the basis of
4 prevailing market rates, so that your own costs don't
5 matter, in other words.

6 So you are in a situation in which all of those kinds
7 of protections provide the mechanisms by which from a
8 regulatory point of view, quite rationally, would be
9 blocking cross-subsidization.

10 Q. Let me just ask you: there was a consolidated
11 proceeding that took place a few weeks ago in which the
12 hearings were held for two days, and in the proceeding, one
13 of the parties, intervenors, I believe -- in fact, it may
14 have been a supporting utility -- submitted a document which
15 purported to show that the price of power sold at retail in
16 two pilot programs in New England, I think one in
17 Massachusetts and one in New Hampshire, were significantly
18 below the wholesale price for power in the same region, in
19 the power pool that was applicable at the time.

20 One of the questions is: why wouldn't the CTC income
21 recovery to a utility allow it to dump; in other words, to
22 sell blow cost for whatever competitive reason it might
23 have?

24 A. Well, now you're talking about what I refer in
25 my testimony to as arguments really about predation. You

1 called it dumping. I believe that such a strategy as a
2 business strategy would be wholly implausible. We know from
3 anti-trust economics that predation as a strategy has to
4 have, the lawyers use the phrase, a dangerous probability of
5 success. That turns out to be a phrase that we economists
6 use to describe whether predation is rational or not.

7 In a setting in which your competitors have already
8 bolted significant supply capability to the ground with
9 other utilities, non-utility generators, self-generators and
10 so forth, have already bolted capacity to the ground, that
11 kind of setting is exactly the setting in which predation
12 doesn't make any sense.

13 The reason for that is if you try to underprice them
14 -- we call it the Rustoleum solution -- that is they shut
15 down until you try to raise your price, and then they turn
16 the machines back on. So predation in an industry where you
17 can't force the cap to leave and then prevent it from coming
18 back simply doesn't make sense, and I think that this
19 analysis of predation in the electric power industry I think
20 is a correct application of anti-trust economics to the
21 situation at hand.

22 Q. One final question. You will admit, will you
23 not, that the independent producer when it sells power must
24 recover in its price its capital cost and its transactional
25 cost in addition to the cost of producing the unit of energy

1 that it sells? Isn't that true?

2 A. No. At any particular time what any competitor
3 will be able to recover is the incremental cost of providing
4 power. When markets are strong, you will tend to call in
5 higher marginal cost units. That will mean that those who
6 have lower marginal cost units will tend to make their money
7 on their capital and their investment and their overhead at
8 that time. If markets are soft, maybe nobody is making the
9 return on their capital. Competitive markets are driven to
10 price basically on marginal costs, and it's not that you
11 recover it in the price. You recover it from the market's
12 workings of supply and demand if you're lucky. That is if
13 the supply and demand operate to help you.

14 Q. Let me just ask you, because I am confused now,
15 not being an economist, about what you said. If I have a
16 \$100 million loan out there and I have to make loan payments
17 every month and I have to amortize that loan at the rate of
18 \$7 million or \$10 million a year, let's say, and I'm selling
19 power at the cost of producing it, regardless of what that
20 is, I'm not making my loan payments, am I?

21 A. No, that's inaccurate.

22 Q. Well, how am I making my loan payments if I'm
23 only talking about the variable cost of producing the unit
24 of power that I'm selling if that's my market price? In
25 other words, if I can produce the power at 2 cents and that

1 is my variable cost of production and it doesn't include my
2 debt service, it doesn't include the transactional cost of
3 acquiring the customer, it doesn't include my G&A, it
4 doesn't include any of that stuff, how am I paying off my
5 loan?

6 A. At the risk of sounding like a professor --

7 Q. I'm here to be a student.

8 A. Most people in this room are used to the
9 regulatory mind set where you think of the price as a
10 buildup of cost. People have to get reused to thinking
11 about this like a competitive market, because in a
12 competitive market here's what happens.

13 You say you have 2-cent power. If the market
14 clearing price is 4 cents, you make money. That's why you
15 invested, because you hoped you could beat the low-cost
16 supplier in a competitive market. If it turns out that 6
17 cents is the cost that you have to bear and the market price
18 is 4 cents, you lose money. But you don't make money by
19 building up your price as a function of your cost. You in a
20 competitive market in our language as an economist, you take
21 the price from the market and do the best you can with it.
22 In a strong market, you may make money. In a weak market,
23 you tend to lose money. But the market will dictate where
24 you sit, if you will, in the array from high cost to low
25 cost producers.

1 Q. That's a wonderful explanation and it helps me
2 ask the final question I have. Isn't it correct, sir, that
3 during the transition period, I can go broke because I am
4 dependent for my amortization of debt on where the market
5 price of energy goes vis-a-vis the cost of producing in my
6 plant, whereas PP&L through the CTC and its regulated
7 recovery of rates can't go broke because they don't have to
8 worry about that payment? Isn't that true?

9 A. I don't know if it's true. You say you. Let me
10 tell you this. If it were the case that an independent
11 power producer -- that's who I'm assuming you are.

12 Q. Yes.

13 A. -- were to go bankrupt, that would not upset the
14 competitive balance in and of itself. If the independent
15 power producer had lots of debt and went broke but had low
16 marginal cost, then upon restructuring either under same
17 ownership or separate ownership, the market would dictate
18 that that plant would continue to operate because it can
19 compete in the marketplace. So individual investors would
20 lose their money, but consumers wouldn't lose the benefit of
21 the low-cost power being produced by the independent power
22 producer.

23 Q. You didn't answer my question. Isn't it
24 correct, sir, that I as the independent power producer
25 during the transition period face the distinct prospect of

1 going into bankruptcy because I can't pay my debts depending
2 upon where the market price for energy goes, but PP&L can't
3 face that prospect for the transition?

4 A. No, I don't think even that's accurate. I
5 understand the thrust of your remark. I would say as part
6 of the transition that the Act is setting up, the collection
7 of stranded costs obviously makes PP&L less susceptible to
8 bankruptcy than it would, but it is not to say that if, for
9 example, market prices were to skyrocket, say fuel prices
10 were to go up, so you as an independent power producer were
11 seeing your major input -- maybe you're gas-fired -- seeing
12 your major input go up, the company subject to the rate cap,
13 presumably also having to buy power on the market from
14 people such as yourself or use the same kind of high-cost
15 fuels, might indeed find itself in deep financial trouble,
16 and I don't want to create the spectrum, but the logic of it
17 would be potentially bankrupt.

18 Q. Well, then it goes back to the PUC and asks for
19 the extraordinary relief of an increase in the CTC or some
20 other relief which the Act does provide. In other words,
21 there is right now a statutory remedy in that circumstance
22 which is unavailable to the independent producer. You must
23 admit that; true?

24 A. I don't know if the scenario that I just
25 described would be an extraordinary circumstance. We're

1 often in sort of never-never land. I know that the Act does
2 provide some mechanisms for relief. How those would be
3 interpreted in the situation you and I just hypothesized, I
4 don't know.

5 MR. CAPLAN: Thank you. I have no further questions.

6 JUDGE KASHI: Thank you. Mr. Rubin.

7 MR. RUBIN: Thank you, Your Honor.

8 CROSS-EXAMINATION

9 BY MR. RUBIN:

10 Q. Good afternoon, Professor Kalt. I represent the
11 International Brotherhood of Electrical Workers, Local 1600.

12 MR. RUBIN: Your Honor, I would like to have marked
13 for identification as IBEW Exhibit 1 --

14 JUDGE KASHI: Cross 1?

15 MR. RUBIN: Cross 1.

16 JUDGE KASHI: So marked for purposes of
17 identification.

18 MR. RUBIN: Thank you.

19 (Whereupon, the document was marked
20 as IBEW Cross-Examination Exhibit
21 No. 1 for identification.)

22 BY MR. RUBIN:

23 Q. Professor Kalt, do you have IBEW Cross Exhibit 1
24 in front of you?

25 A. Yes.

1 Q. Was this prepared by you or under your
2 supervision?

3 A. Yes.

4 Q. Could you take a moment to review those? I'm
5 just going to ask you if what is contained here is accurate
6 and reflective of your opinion today.

7 (Witness perusing document.)

8 A. I believe these statements are accurate.

9 MR. RUBIN: Thank you. That's all I have, Your
10 Honor. I would ask to move this exhibit into evidence.

11 JUDGE KASHI: That which has been marked as IBEW
12 Cross-Examination Exhibit No. 1 is received into the
13 evidentiary record without objection.

14 (No response.)

15 JUDGE KASHI: Without objection.

16 (Whereupon, the document marked as
17 IBEW Cross-Examination Exhibit No. 1
18 was received in evidence.)

19 JUDGE KASHI: Thank you very much.

20 MR. RUBIN: Thank you, Your Honor.

21 JUDGE KASHI: Redirect, counsel?

22 MR. KAPLAN: If we could have just one minute, Your
23 Honor -- I think the witness is suggesting that we take our
24 afternoon break at this point.

25 JUDGE KASHI: All right. We'll take our 15-minute

1 recess at this particular time and be back at 3:00.

2 (Recess.)

3 JUDGE KASHI: Going back on the record.

4 Redirect, Mr. Kaplan?

5 MR. KAPLAN: Yes, Your Honor.

6 **REDIRECT EXAMINATION**

7 BY MR. KAPLAN:

8 Q. Dr. Kalt, under cross-examination by counsel for
9 the Environmentalists, they offered Environmentalists Cross-
10 Examination Exhibit No. 1, which is your study entitled,
11 "Re-Establishing the Regulatory Market in the Electric
12 Utility Industry."

13 In that study, Dr. Kalt, did you conclude that
14 investors in Pennsylvania utilities in the mid-1970s
15 anticipated the end of the exclusive utility franchise and
16 the introduction of competition of retail?

17 A. We were focused more on the mid-1980s, but I did
18 not conclude that with respect to the 1970s or the 1980s.

19 Q. Under examination I believe from Mr. Kohler
20 earlier today, you discussed the price at which PP&L's
21 electric delivery group would sell power to last resort
22 customers, people who had failed to choose a supplier.

23 Can you clarify the cost, how the price of that power
24 would be determined?

25 A. It is my understanding that that power would be

1 priced with no profit markup as I say in my testimony, that
2 it would be the wholesale market price, acquisition cost, in
3 other words, of the power, and that the company would also
4 intend to recover any procurement costs, but not any general
5 overhead costs in that price of power.

6 Q. Is it your understanding that the company will
7 be in the business of marketing this power as a product to
8 retail customers?

9 A. My understanding is that the company's intention
10 is not to be aggressively marketing that to try to create a
11 business out of it. Independent of their intention, I can
12 tell you that the absence of profit opportunity, since there
13 is no profit markup on the power and the T&D revenues would
14 come anyway from whoever supplies the power, the company
15 does not have an incentive to build a business, if you will,
16 or aggressively try to market this power.

17 Q. Is there any reason to be concerned that
18 aggressive retail marketers will not be able to compete
19 effectively against this service?

20 A. No; except insofar as market prices are driven
21 to bump people up against the rate cap, then that would, as
22 I indicated in my testimony, create some incentive for
23 customers to want to buy at the rate cap if market prices
24 are much higher, but that is a complaint about the rate cap,
25 not about any aspect of the company's claim.

1 Q. And one last question, Dr. Kalt. Would you take
2 a look at Enron Cross-Examination Exhibit No. 2, which is
3 the excerpt from the Economic Report to the President? On
4 that same page where you were asked to read during the
5 examination by Mr. Kohler, page 163, will you read the last
6 full paragraph on that page beginning with "Such forced
7 structural separation"?

8 A. Sure. This is coming after the discussion about
9 divestiture as a possible solution. "Such forced structural
10 separation helps promote level-playing-field competition in
11 the unregulated markets, but it may sacrifice economies of
12 scope, efficiencies in joint ownership and operation of
13 related segments of an industry. How to prevent
14 discrimination without unduly sacrificing economies of scope
15 is a central challenge in assessing whether and under what
16 safeguards the RBOCs should be permitted to offer long
17 distance service while they still dominate local telephone
18 networks; and whether electric utilities should be allowed
19 to sell unregulated power in competition with rivals while
20 they still control the vital transmission grids."

21 MR. KAPLAN: Thank you, Dr. Kalt. Your Honor, with
22 that we have no further questions. We would just like to
23 reserve the opportunity to offer into evidence additional
24 sections of Dr. Kalt's report "Re-Establishing the
25 Regulatory Market in the Electric Utility Industry," which

1 is now Environmentalists Cross-Examination Exhibit No. 1.

2 JUDGE KASHI: Is there any follow-up on that, Mr.
3 Zalcman?

4 MR. ZALCMAN: No, Your Honor.

5 JUDGE KASHI: Mr. Kohler?

6 MR. KOHLER: No, Your Honor.

7 JUDGE KASHI: Thank you very much. That which has
8 been marked and identified as PP&L Statement No. 1 and
9 Exhibit JPK-1, Statement No. 1R and Exhibit JPK-2 are
10 received into the evidentiary record without objection.

11 (No response.)

12 JUDGE KASHI: Without objection.

13 (Whereupon, the documents marked as
14 PP&L Statements Nos. 1 and 1R and
15 PP&L Exhibits Nos. JPK-1 and JPK-2
16 were received in evidence.)

17 JUDGE KASHI: Thank you very much, sir. You are
18 excused.

19 (Witness excused.)

20 MR. KAPLAN: Your Honor, PP&L calls Robert M.
21 Geneczko.

22

23

24

25

1 Whereupon,

2

ROBERT M. GENEZKO

3 having been duly sworn, testified as follows:

4

DIRECT EXAMINATION

5

BY MR. KAPLAN:

6

Q. Mr. Genezko, do you have before you Statement

7

No. 13 of Pennsylvania Power and Light Company, which is the

8

direct testimony of Robert Genezko, consisting of 11 pages?

9

A. I do.

10

Q. And Exhibits RMG-1, 2 and 3 thereto?

11

A. I do.

12

Q. Do you have before you Statement No. 13-R, the

13

rebuttal testimony of Robert M. Genezko, a statement of 28

14

pages?

15

A. I do.

16

Q. And Exhibit RMG-4 thereto?

17

A. Yes, I have that as well.

18

MR. KAPLAN: Pursuant to our procedure, Your Honor, I

19

would simply ask the witness whether he has any corrections

20

to that exhibit.

21

THE WITNESS: Yes, I do. I have three typos. On

22

page 4, line 11, --

23

BY MR. KAPLAN:

24

Q. Of which exhibit?

25

A. I'm sorry; this is my rebuttal testimony.

1 Q. Thank you.

2 A. Statement 13-R, page 4, line 11. Insert the
3 word "it" after the word "if." It should now read, "...but
4 even by a stretch, if it were."

5 Again, rebuttal, page 16, line 11, about the middle
6 of the line it says, "fully located value." That should
7 read "fully allocated value."

8 And in Statement RMG-4, page 2, the first line under
9 the heading "Communications to Employees and Enforcement,"
10 it should read, "Number 1, the code or conduct" -- I'm
11 sorry; "the code of conduct" -- two typos in that line --
12 "will be communicated," instead of "commercial." So where
13 it says "commercial," that should say "communicated."

14 Q. Thank you, Mr. Geneczko.

15 MR. KAPLAN: With that, Your Honor, we would like to
16 offer into evidence Statement No. 13, Statement No. 13-R and
17 Exhibits RMG-1 through 4.

18 JUDGE KASHI: Thank you. Subject to any motions
19 and/or objections, that which has been previously marked
20 will be received into the evidentiary record.

21 (Whereupon, the documents were marked
22 as PP&L Statements Nos. 13 and 13-R
23 and PP&L Exhibits Nos. RMG-1 through
24 RMG-4 for identification, and were
25 received in evidence.)

1 MR. KAPLAN: Your Honor, we do have some very brief
2 oral rejoinder for Mr. Geneczko.

3 JUDGE KASHI: Go ahead.

4 BY MR. KAPLAN:

5 Q. Mr. Geneczko, do you have any comment on the
6 Environmentalists Witness Dirmeier's opposition to the use
7 of PP&L's name by PP&L's retail energy supply group as
8 stated on pages 28 to 34 of his surrebuttal testimony?

9 A. Yes, I do. That's Enron's witness, by the way.

10 Q. I'm sorry.

11 A. Yes, I do. Following up on Dr. Kalt's testimony
12 and basically confirming a point Mr. Dirmeier had made, PP&L
13 will make sure there is no confusion among customers by
14 establishing clear product branding. In other words, in
15 dealings with customers we will clearly and explicitly
16 distinguish delivery service and generation supply service
17 as separate operations.

18 Q. OCA Witness Alexander testifies on page 23 of
19 her surrebuttal testimony that customer load profile
20 information provided to PP&L's supply group should be made
21 available to all suppliers. Is this acceptable to PP&L?

22 A. There are actually two points made by Witness
23 Alexander, one has to do with the type of information, and
24 one has to do with the access already granted to that
25 information. Witness Alexander refers to load profiles,

1 demographics for customer groups and suggests that these
2 groups do not require specific customer sign-off for that
3 information to be released. To the extent that we make such
4 information available to any alternate supplier, including
5 PP&L's supplier, we will make it available to all under
6 comparable terms and circumstances.

7 In response to the second portion of that, I have
8 confirmed that the alternate supplier, that is PP&L's retail
9 electric supply group, does not have access to that
10 information.

11 Q. Thank you.

12 Several witnesses, such as Enron's Mr. Dirmeier, for
13 example, at pages 26 and 27 of his surrebuttal testimony,
14 and OCA's Witness Alexander, at page 24 of her surrebuttal
15 testimony, have commented on joint marketing by the delivery
16 group and alternative suppliers. Can you please clarify
17 PP&L's position for the record?

18 A. Yes. We intend to continue to joint market
19 where it is concerning things specifically concerning
20 economic development. It has been PP&L's long-standing
21 tradition to help attract new industries and businesses into
22 the area, and we will joint market not only with our own
23 retail energy supply group, but we will joint market with
24 anyone who would help bring additional industry into the
25 State of Pennsylvania.

1 Q. Just to clarify, what part of that joint product
2 will the electric delivery group be offering?

3 A. Basically wire service, transmission,
4 distribution, transportation. We will not engage in any
5 kilowatt-hour marketing, if you would like to term it
6 kilowatt-hour marketing.

7 MR. KAPLAN: Thank you, Your Honor. That is all the
8 rejoinder we have. Mr. Geneczko is available for cross-
9 examination.

10 JUDGE KASHI: Mr. Kohler?

11 MR. KOHLER: Thank you, Your Honor.

12 **CROSS-EXAMINATION**

13 BY MR. KOHLER:

14 Q. Good afternoon, Mr. Geneczko.

15 A. Good afternoon.

16 Q. I'll be relatively brief and hopefully try to
17 keep things moving.

18 Is it your position that there should be no
19 difference in the code of conduct which should be applicable
20 at the early stages of competition as to the code of conduct
21 that would be applicable in a mature competitive market?

22 A. Yes, it is.

23 Q. You may have just blew by me in your oral
24 rejoinder; you may have just said that. You may have
25 already answered this question, and I apologize. In

1 referring you to page 3 of your surrebuttal, lines 15 to
2 17 --

3 MR. KAPLAN: I believe it's rebuttal, just to make
4 the record clear.

5 MR. KOHLER: I apologize.

6 THE WITNESS: Yes. Go ahead. I'm there.

7 BY MR. KOHLER:

8 Q. I believe you say that PP&L has been operating
9 as though its proposed code of conduct was in effect as of
10 the date of the filing; is that correct?

11 A. That is correct. We have conducted training
12 sessions, have had information in our internal publications.
13 My own direct boss has warned us on no uncertain terms that
14 we will act as if this is in place right now.

15 Q. When you say in effect, does that mean that each
16 of these provisions is applicable, for example, to the
17 generation supply group now?

18 A. Yes.

19 Q. What do you mean by "in effect"?

20 A. "In effect" basically says that the code, as it
21 is attached to my testimony, the conditions of those codes
22 are expected to be followed by all PP&L employees.

23 Q. For example, and this is a point that you may
24 have said, for the generation supply group to get -- and I'm
25 referring to the first --

1 A. Load profiles.

2 Q. -- the first point of the code of conduct under
3 restricted access to information.

4 For individual customer consumption, the generation
5 supply group does not have access to that information; is
6 that correct?

7 A. That is correct.

8 Q. Let me ask you how the code applies in the two-
9 year period of phase-in to direct access. I believe the
10 way --

11 A. I'm sorry; I didn't hear that.

12 Q. In the two-year phase-in for direct access.

13 A. Okay.

14 Q. I believe the way your proposal works, the
15 generation supply group will continue to provide service to
16 customers who are not eligible to choose; is that right?

17 A. That is my understanding, yes.

18 Q. And, in fact, that generation supply group is
19 providing generation to all PP&L customers now; is that
20 right?

21 A. Right now, yes.

22 Q. Were you here for Professor Kalt's testimony
23 this morning and this afternoon?

24 A. Yes, I was, although sitting back there I
25 couldn't hear absolutely everything.

1 MR. FOGEL: Same thing over here.

2 (Laughter.)

3 BY MR. KOHLER:

4 Q. Did you hear him testify as to his
5 recommendation that a code include crisp edicts as opposed
6 to specific language?

7 A. Yes, I did, and I remember reading that in his
8 testimony.

9 Q. And you looked at page 35 of his testimony where
10 it lists the crisp edicts?

11 A. I'm sure I have, yes.

12 Q. Do you believe that all of those crisp edicts
13 are included in RMG-4?

14 A. I believe they are, yes.

15 Q. And so, if the code is subject to interpretation
16 at any point in time, we can refer back to those crisp
17 edicts and interpret the code; is that fair?

18 A. Yes, as well as the implementation of the actual
19 roll-out of the code. We intend to make it absolutely clear
20 to all employees.

21 Q. Just a point of clarification. I'm going to
22 briefly go through each of the provisions, maybe one
23 question for each.

24 On number 1 there where you're listing persons who
25 have access to confidential information, where it says "for

1 the purpose of customer billing, supply scheduling,
2 reconciliation, supplier payments and customer assistance,"
3 should that be "or customer assistance"?

4 A. I'm sorry; I'm not where you are.

5 Q. I'm sorry. Code of conduct provision number 1
6 under "Segregation and Other Restricted Access to
7 Information."

8 A. Yes.

9 Q. At the end of that first paragraph. My question
10 is, would an employee have to be involved in all of those
11 functions or is that "and" at the end there more
12 appropriately an "or"?

13 A. "Or" is more appropriate.

14 Q. Throughout the code you have reference to
15 suppliers. I take it that the reference to supplier means
16 all electric generation suppliers including the generation
17 supply group; is that correct?

18 A. That is correct.

19 Q. In the first provision of the code of conduct
20 where it indicates that individual customer consumption is
21 confidential information that requires the permission of the
22 customer in order to be released to any supplier, how or
23 would that rule apply to aggregated customer consumption
24 information?

25 A. That was basically what I had just gone through

1 in rejoinder. From a standpoint of aggregated customer
2 information, to the extent that we would release it, we
3 would release it under the same terms and circumstances to
4 all suppliers. As Witness Alexander points out, it's likely
5 that no one customer has to sign off to release that
6 information.

7 Q. I'm sorry I missed that. So you clarified that
8 that in fact is not confidential information under this
9 rule?

10 A. That's correct. We have not developed --

11 Q. And number 2 would not kick in; is that correct?

12 A. That's correct. Likewise, we have not made a
13 decision as to whether or not we will release that type of
14 information generally as of yet, but if we do --

15 Q. When you say generally, beyond -- to those other
16 than suppliers?

17 A. No. Specifically to suppliers. We have not
18 decided we will or will not, exactly.

19 Q. But if you do release it, you will release it at
20 the same time, in the same manner, to all suppliers, --

21 A. Exactly.

22 Q. -- including generation suppliers?

23 A. Yes, sir.

24 Q. Moving on to assignment of responsibilities. It
25 says "employees in the generation supply group directly

1 involved." What did you intend by using the term
2 "directly"?

3 A. "Directly involved," basically, you could take
4 it back to what I'll call four buckets of information that
5 we just decided, buckets being customer-specific
6 information, customer-aggregated information, supplier
7 information, and facility information. Any employees having
8 access to that type of information, and which having access
9 would confer an undue competitive advantage, that's what we
10 mean by that term.

11 Q. Those are the four buckets of --

12 A. Yes.

13 Q. -- employees that are directly involved in
14 marketing?

15 A. Yes. That's four types of information.
16 Employees having access to that type of information, yes.

17 Q. My problem is with the word "directly". If you
18 define the four groups that are involved in marketing
19 energy, why do you need the term "directly"? Are there
20 employees that are indirectly involved in marketing
21 information?

22 A. No. We could scratch the word "directly," if
23 you like.

24 Q. Thank you. That would be helpful.

25 A. Okay. Our point is that a janitor ought to be

1 able to go from one group to the other.

2 Q. Does the code provide any restriction on an
3 employee that perhaps was involved in one of those four
4 buckets that changed assignment so that potentially it was
5 aware that that employee had what has been defined as
6 confidential information change assignments completely out
7 of marketing activities -- would that type of employee be
8 subject to number 1 under "Assignment of Responsibilities"?

9 A. I'm not sure I'm following your question.

10 Q. Would it apply in any cases to employees who, in
11 the recent past, not at the time of transfer but in the
12 recent past, were in one of the four buckets?

13 A. May they be transferred? The answer is yes,
14 they may be transferred.

15 Let me clarify that. At the point they are
16 transferred, they no longer have access to that information.
17 At the point at which they left their old position, they no
18 longer have access to that information.

19 Q. So the fact that they only had access to that
20 type of information in the recent past would not preclude
21 the transfer; is that correct?

22 A. That's correct.

23 MR. KOHLER: Bear with me for one second.

24 (Pause.)

25

1 BY MR. KOHLER:

2 Q. In the phrase in number 1 under "Assignment of
3 Responsibilities" it says, "involved in marketing energy to
4 customers choosing competitive generation service" -- since
5 you defined the four buckets, I'll withdraw that question.

6 Let's move on to comparability on page 2.

7 A. Yes.

8 Q. I'm particularly interested in the provision
9 related to tying of products. I believe comparability
10 number 1 precludes -- will not condition any discount to a
11 customer, but it's application is restricted to the
12 generation supply group; is that correct?

13 A. Yes; that's correct.

14 Q. Would this particular provision prohibit the
15 tying of services, the tying of two services, both of which
16 were provided by the delivery group?

17 A. Would you restate the question, please?

18 Q. Let me give you a hypothetical question or else
19 the question is going to be confusing. What about the tying
20 of the discount to using the delivery group for a single
21 bill, is that precluded?

22 A. I'll ask the question. Could you clarify that
23 one more time? What about the tying what?

24 Q. Well, you're aware that the Act allows, by
25 anybody's interpretation, allows the delivery group to

1 provide a single bill?

2 A. That's correct.

3 Q. At a minimum, allows the delivery group to
4 provide a single bill, or allows two bills if that's what
5 the customer wants.

6 A. Correct.

7 Q. At a minimum.

8 A. Yes.

9 Q. Would this provision -- and that billing service
10 is provided by the delivery group?

11 A. Correct.

12 Q. Is that right?

13 A. That's correct.

14 Q. Would this provision prohibit tying of the kind
15 of a discount to the delivery group providing a single bill?
16 Am I being clear?

17 A. Let me try it back to you. Are you saying we
18 can discount billing services?

19 Q. No. Can you tie a discount to continuing to use
20 the utility for a single bill as opposed to the generation
21 supplier for two bills?

22 A. No, we cannot.

23 Q. Okay.

24 A. Thank you.

25 MR. KAPLAN: Mr. Kohler, that's without regard to

1 whether we can discount a tariffed rate.

2 MR. KOHLER: Fair enough.

3 BY MR. KOHLER:

4 Q. Can you discount a tariffed rate?

5 (No response.)

6 JUDGE KASHI: Did you seriously ask that question?

7 MR. KOHLER: No, Your Honor.

8 (Laughter.)

9 BY MR. KOHLER:

10 Q. Related to comparability standard number 3.

11 A. Yes.

12 Q. Just a point of clarification. What it says is

13 "The electric delivery group will process requests for
14 access by all generation suppliers in a non-discriminatory
15 manner." I assume that that also applies to, for example,
16 customers returning to the electric delivery group?

17 A. Yes, it does.

18 Q. Even though the language doesn't seem to imply
19 that; is that right?

20 A. That's right.

21 MR. KOHLER: Nothing further, Your Honor.

22 JUDGE KASHI: I'm sorry; that's all you have, Mr.
23 Kohler?

24 MR. STEWART: He's done, Your Honor.

25 JUDGE KASHI: Mr. Stewart.

1 MR. STEWART: I just have one or two questions, Your
2 Honor.

3 CROSS-EXAMINATION

4 BY MR. STEWART:

5 Q. Good afternoon, Mr. Geneczko. My name is Todd
6 Stewart and I represent the Mid-Atlantic Power Supply
7 Association.

8 A. Good afternoon.

9 Q. At page 8 of your direct testimony, I believe,
10 you state that one purpose of the proposed code of conduct
11 is -- and I think I have this as a quote -- "to ensure that
12 the electric delivery groups will provide delivery service
13 in a non-discriminatory manner"; is that correct?

14 A. That's correct. I'm not sure where you're
15 reading from, but the words sound right.

16 Q. Would you agree then that suppliers should have
17 access to transmission and distribution system and other
18 similar bottleneck facilities on comparable terms and
19 conditions?

20 A. Yes.

21 Q. Would you also agree that the fact that PP&L has
22 control over the transmission and distribution system has
23 the potential, and I use the word "potential," to lead to
24 abuse?

25 A. No, I would not agree because the tenet that we

1 have control over the transmission system is really not
2 proper any longer; the transmission system, in effect, has
3 been turned over to the PJM Interconnection for basically
4 day-to-day operation, determining and assigning access,
5 things of that manner.

6 Q. But then for the purposes of distribution, would
7 you agree with that statement?

8 A. No. I believe, again, we have an obligation to
9 transport, and with that obligation we will hook up or allow
10 access to, backed up by the code of conduct, to the
11 distribution system.

12 MR. STEWART: I have nothing further, Your Honor.

13 JUDGE KASHI: Thank you very much.

14 Mr. Fogel.

15 MR. FOGEL: Thank you, Your Honor.

16 **CROSS-EXAMINATION**

17 BY MR. FOGEL:

18 Q. Good afternoon, Mr. Geneczko.

19 A. Good afternoon.

20 Q. The structure that will be in place after this
21 proceeding comes to its fruition would involve the holding
22 company of PP&L Resources, under which there will be one
23 subsidiary, which would be Pennsylvania Power and Light,
24 which would be the regulated utility, with the other
25 operations of generation supply; correct?

1 A. No, that is not correct. What will happen is
2 PP&L, the utility, will have two functions, it will have --
3 well, actually, it will have three functions, it will have
4 the regulated portion, the wires portion, if we call it that
5 way, a services group and a competitive, we'll call it the
6 generation supply group. Along with that are the other
7 subsidiaries of PP&L Resources.

8 Q. However, those functional groupings would still
9 be under PP&L, which in its entirety would be a subsidiary
10 of PP&L Resources?

11 A. That's correct.

12 Q. And then the second subsidiary of PP&L Resources
13 would be a company called Power Marketing Development
14 Company?

15 A. That's correct.

16 Q. And the third one would be Spectrum Energy
17 Services Corp.?

18 A. That's correct.

19 Q. Now, would you agree, based on information
20 supplied in response to interrogatories, that Spectrum would
21 be engaged in the following activities: energy management,
22 energy efficiency, operation and maintenance services, rate
23 analysis and negotiation, energy supply evaluation and full
24 service energy management?

25 A. I believe that's how the interrogatory was

1 answered.

2 Q. Now, if Spectrum wanted access to PP&L's
3 customer information base, would that be allowed in the new
4 order?

5 A. Again, there's two types of customer
6 information. There is individual customers; if they were to
7 have the individual customers release that information or
8 sign a release for that information to be provided, yes. If
9 it had to do with customer aggregated information, whether
10 it be demographics or load profiles, economic conditions,
11 the answer would be we would consider it, however, if we
12 provided it to Spectrum, it would be provided to all other
13 entities, all other energy suppliers, for instance, at the
14 same time, in the same manner.

15 Q. Let's say Spectrum requested customer lists that
16 were held by the electric delivery group of PP&L, what would
17 be the process -- (a) would that information be provided,
18 and, if so, what process, if any, would you use to determine
19 whether that information would be provided?

20 A. The second one, I do not know the mechanics of
21 the process. In fact, I'm not even sure we have a process
22 set for that because -- well, I don't know that we have a
23 process set for that.

24 Your first question is, would it be provided, and the
25 answer is, again, only to the extent we provided it to all

1 other people interested in the supplier list -- I'm sorry;
2 all other entities interested in the customer list.

3 Q. So are you saying if there was another company
4 that was engaged in the provision of energy efficiency or
5 energy management services, you would make that list
6 available to that competitor of Spectrum?

7 A. Only to the extent -- in other words, I'll go
8 back to comparability. We will grant information -- if we
9 choose to let the information go, we will grant information
10 on comparable terms and circumstances.

11 Q. Now, if I could direct your attention to page 25
12 of your rebuttal testimony, beginning on lines 1 through 8
13 you indicate that the electric delivery group will continue
14 to promote competitive products such as electronic
15 thermostats, power watch devices and heat comfort controls.
16 Is that a correct reading of your testimony?

17 A. You just read the question; yes.

18 Q. Okay. Well, let me ask you this question more
19 directly. Will the electric delivery group actually
20 continue to promote these types of products?

21 A. I think the answer is as stands, "The electric
22 delivery group may market such products to customers within
23 the franchise territory as a means of providing customer-
24 oriented services closely associated with safe and reliable
25 energy utilization."

1 Q. Now, in the question, I guess as you drafted it,
2 you use the term "competitive products." Do you see that?

3 A. Yes, I do.

4 Q. Can you, in your own words, explain what you
5 mean by that term?

6 A. Competitive products is basically -- it says it
7 is available from other sources in the market.

8 Q. So that basically it would not be a regulated
9 product, it would be one which other competitors freely are
10 able to provide that product?

11 A. I'm not sure about power watch. I believe power
12 watch may actually be a tariffed product.

13 Q. When you say competitive products, you mean
14 there are other providers who provide these type of
15 products?

16 A. That's correct.

17 Q. Now, assume for the moment that such market
18 promotion activities take place, okay? In those promotion
19 activities, will the electric delivery group have access to
20 customer data in order to conduct those promotional
21 activities?

22 A. By definition, yes.

23 Q. In response to -- let me step back. Will that
24 same data be made available to other competitive providers
25 of, let's say, electronic thermostats, if they request that

1 data?

2 A. We do not have a policy on that at this point.
3 We view this proceeding here as looking at the activities of
4 the generation side of business, not necessarily what I
5 continue to call the wire side of the business. We really
6 have not contemplated that at this juncture.

7 Q. Now, if I could direct your attention to the
8 company's response to Enron's Interrogatory Set I, Question
9 2, which was dated May 19, 1997.

10 A. Dated May 19, 1997; yes.

11 Q. Right. On the second page, part of your answer
12 where you state, and I quote, "PP&L also proposes to sell to
13 end-use customers energy-related services including but not
14 limited to energy efficiency, energy auditing and energy
15 consulting services." Is that a correct reading of your
16 answer?

17 A. Excuse me; could you point me to that again?
18 I'm sorry.

19 Q. This will just go easier.

20 A. That's probably right.

21 Q. Right here (indicating).

22 (Document shown to witness.)

23 A. Yes. I'm there. Go ahead.

24 Q. Now, when PP&L conducts these activities, will
25 that be the electric delivery group that will be conducting

1 them?

2 A. In the context of this answer, this answer was
3 intended for the fact of the alternate supplier, PP&L's
4 alternate generation supplier, conducting these activities.

5 Q. So that would be -- I'm starting to get a little
6 lost here with all the different functional separations.
7 Even the customer may get a little confused, too.

8 A. The competitive side. We'll call it that.

9 Q. That would be the competitive side of PP&L?

10 A. Correct.

11 Q. Now, in conducting those activities, would the
12 competitive side have access to customer information and
13 data that's gathered by another functional group or any
14 other functional group of PP&L?

15 A. Again, only on comparable terms and conditions
16 and circumstances. In other words, if we made it available
17 to them, it would be made available to all comers at the
18 same time, the same place, et cetera.

19 Q. Now, in response to PPA's Interrogatory No. 9,
20 you had indicated that the electric delivery group will
21 continue to promote the use of energy efficient electro-
22 technologies to its customers to enhance the effective
23 utilization of PP&L's facilities and economic development
24 within PP&L's service territory.

25 A. Yes.

1 Q. Could you explain what you mean by energy
2 efficient electro-technologies?

3 A. Yes. PP&L has had a history of essentially
4 helping to make businesses more competitive by applying new
5 technology. For instance, I'll cite an example. From an
6 environmental standpoint, the use of lacquers and other
7 paints and adhesives has caused some environmental problems,
8 or has the potential that it could cause some environmental
9 problems, so from a customer standpoint, we have helped set
10 up education where that customer can go and watch it's
11 called powders being applied for pigment, and I can't give
12 an example to what, let's call it the casing of a pump as
13 opposed to spraying, using lacquers and oil-based paints.
14 We do not charge for that service. The point is to keep the
15 customer more competitive.

16 Q. Now, you've indicated in a couple of your
17 responses that in certain situations, if customer data is
18 provided, it will be provided comparably to all providers of
19 such products and services.

20 A. Correct.

21 Q. In ascertaining the value -- let me step back.
22 Would you agree that the customer-related information and
23 data has been acquired by the company through the exercise
24 of its monopoly function?

25 A. I would agree it has been gathered over history

1 while we were one company called Pennsylvania Power and
2 Light.

3 Q. Has the company made any effort to determine
4 what the fair market value of that customer list and
5 customer data is?

6 A. I am not aware of such studies.

7 Q. Now, assume for a moment that there was -- let's
8 say it turned out that per customer it comes out to \$10.00,
9 just to take a --

10 A. Our customers are worth more than \$10.00, but
11 that's okay.

12 Q. And assume, however, that the actual allocated
13 cost of service per lead came out to \$2.00. What would be
14 the charge to either Spectrum or to the competitive
15 operations for that customer data, would it be the fair
16 market value or your allocated cost?

17 A. Again, I am not aware of such policy, and it's
18 hypothetical; I won't provide an answer because I just don't
19 know what we would be thinking on that point.

20 Q. Would you, however, agree, as a conceptual
21 matter, that in order to maximize the return for ratepayers,
22 the company should endeavor to obtain the highest value for
23 any assets that it can if it disposes or sells those assets?

24 A. In principle, yes.

25 MR. FOGEL: I have nothing further. Thank you.

1 JUDGE KASHI: Thank you very much, Mr. Fogel.

2 Mr. Kleppinger?

3 MR. KLEPPINGER: We have no questions, Your Honor.

4 JUDGE KASHI: Mr. Caplan.

5 MR. CAPLAN: Yes. Thank you, Your Honor. I have
6 just a few questions.

7 **CROSS-EXAMINATION**

8 BY MR. CAPLAN:

9 Q. What is the mechanism for enforcing the code
10 other than internal discipline? Is there any proposal or
11 concept for dealing with violations which, for example, have
12 some kind of negative impact on the ability of a competitor,
13 a third party, to compete effectively with PP&L?

14 A. You're asking what we would pay a third party,
15 and --

16 Q. No, no. I'm interested in what the enforcement
17 mechanism is other than internal disciplinary proceedings
18 within the company. Is there any contemplation for having
19 some form of outside review of compliance?

20 A. There is a dispute resolution procedure, as
21 noted in the last point of the code, but other than that,
22 no.

23 Q. How does that work? Is that defined anywhere?

24 A. It is under development at this point.

25 Q. Would you admit that the independence of the

1 arbiters of this dispute resolution procedure would be of
2 significance to the efficacy of the procedure itself?

3 A. That seems reasonable.

4 Q. Would you also admit that whatever procedure is
5 implemented would have to be one that provided expeditious
6 resolution since we're dealing with a dynamic economic
7 marketplace?

8 A. Once again, that seems reasonable.

9 Q. Was it contemplated that this procedure would be
10 conducted by outsiders other than PP&L, or has that not yet
11 been addressed?

12 A. That has not yet been addressed, but that option
13 has been discussed.

14 Q. Is it your understanding that the definition of
15 that procedure would be included in the final submission to
16 the PUC in this proceeding, or would it be something that
17 would be provided later?

18 A. I can't answer that for sure, but I believe we
19 would like to have that done before the proceeding is
20 concluded.

21 Q. Is it going to be subject to review during these
22 hearings, to your knowledge, or would that have to be
23 addressed in some subsequent filing?

24 A. I do not know.

25 Q. You indicated that transfers of personnel from

1 the regulated arm to the competitive arm or vice-versa would
2 be published on PP&L's OASIS; is that correct?

3 A. That's correct.

4 Q. What is the intent of doing that, in other
5 words, for the public at large? What advantage, if any,
6 would that afford members of the public who would find this
7 on the Internet?

8 A. First of all, if I recall right, it's a FERC
9 requirement that we do so, but what it does is it's kind of
10 like Sunshine, it opens it up and suggests if you see one
11 person transferring back and forth, particularly at maybe
12 the same level versus a promotion, that would send up, I
13 believe, a red flag that says: they're doing it for the
14 purpose of what I called revolving door, the purpose of
15 transferring information, competitive information, as
16 opposed to for the betterment of the company or the
17 betterment of the individual.

18 Q. In your rebuttal testimony, I believe it was, or
19 it may have been in your direct, you talked about having the
20 corporate auditing division on some basis do internal audits
21 of, I assume, complaints with the code.

22 A. Yes.

23 Q. Are those audits going to be made available to
24 the public on the OASIS or in some other form, or are they
25 going to be exclusively internal to PP&L's own management?

1 A. That procedure is being developed by the
2 auditing department now, and I do not know what they intend
3 to do at this point.

4 Q. And as far as you are aware, there is no current
5 regulation that would require the PUC to conduct an audit in
6 compliance with such codes on any kind of periodic basis; am
7 I correct?

8 A. I am not aware of such a provision.

9 Q. Now, is there any plan with regard to minimizing
10 the temptation to breach the code, to minimize or eliminate
11 incentive compensation for those employees that are in fact
12 involved in the competitive sale of electricity in the open
13 market? Do you understand what I'm saying? You could
14 compensate these people by fixed salary, you could
15 compensate them by salary plus a commission, et cetera, and
16 you could get more and more performance-related measures of
17 compensation which, I think you would agree, would tend to
18 increase the temptation to cut corners in order to increase
19 one's --

20 A. The incentive compensation on the generation
21 supply side, what you're really saying is they have to find
22 a way to mole themselves back into the electric delivery
23 group to get that specific information. I don't see that as
24 easily happening, and I believe our code of conduct stands
25 in place.

1 MR. KAPLAN: I have no further questions, thank you.

2 JUDGE KASHI: Mr. Burgraff?

3 MR. BURGRAFF: We have a few questions, Your Honor.

4 Mr. Mullins is going to ask them.

5 JUDGE KASHI: Mr. Mullins?

6 MR. MULLINS: Thank you, Your Honor.

7 CROSS-EXAMINATION

8 BY MR. MULLINS:

9 Q. Good afternoon. My name is James A. Mullins.

10 I'm one of the attorneys litigating this case on behalf of
11 Pennsylvania OCA.

12 A. Good afternoon.

13 Q. Mr. Geneczko, I'd like to direct you to page 24
14 of your rebuttal testimony. There you discuss joint
15 marketing between the electric delivery group and the
16 generation supply group?

17 A. Yes.

18 Q. On line 3, you also state that comparable
19 opportunities will be available to alternate suppliers; is
20 that correct?

21 A. That's correct, and again, specifically in the
22 area of economic development.

23 Q. Now, what sort of documentation will there be as
24 far as any joint marketing activities undertaken by the
25 electric delivery group and the generation supply group?

1 A. We have not worked out any procedures such as
2 that.

3 Q. What sort of time frame are we looking at as far
4 as when you will have worked out that particular provision?

5 A. Would you restate your first question? Maybe I
6 didn't understand it.

7 Q. You state that the electric delivery group will
8 engage in joint marketing of supply products with the
9 generation supply group, and if they do, comparable
10 opportunities will be made available to alternate suppliers.

11 I want to know what sort of documentation will PP&L
12 undertake as far as apprising alternate suppliers and the
13 public in general as to what activities they have undertaken
14 with the generation supply group.

15 Q. First, the operative word is not "will," it's
16 "may". Again, we have not devised any such procedures, and
17 we have not contemplated a time frame for devising such
18 procedures.

19 Q. Who would be the sole determiner of what a
20 comparable opportunity is?

21 A. It would be the electric delivery unit.

22 Q. Would an alternate supplier be made aware of
23 previous joint marketing activities?

24 A. Oh, yes. For instance, we may bring that up on
25 the OASIS or some other common reporting forum. Let's put

1 this in perspective. If we're doing economic development --
2 let's kind of give an example; I think that might work best;
3 a couple of ways we've done economic development.

4 We have essentially provided funding for property
5 sites in the form of low interest loans or helped develop
6 backbone systems.

7 In the future world, that may or may not be the case,
8 but I would suspect more than likely, rather than the
9 delivery unit coming up with the sales lead, I could see
10 someone such as an Enron or an alternate generation supplier
11 saying, "I understand that such and such a company would
12 like to locate in Pennsylvania and his options are Illinois
13 or California. And we'd like you as the wires company, we
14 understand the site is within the PP&L service territory, we
15 would like you to join us and develop a package and bring it
16 to the customer to show him along with a local tax package
17 and anything else that we could develop to show the customer
18 the benefits of locating in Pennsylvania versus Illinois or
19 California." That's the type of activity we're talking
20 about here.

21 Q. Say in May of a future year, the electric
22 delivery group engages in a joint marketing activity with
23 the generation supply group. When would an alternate
24 supplier be apprised of that particular activity?

25 A. I don't know. I would suggest it would have to

1 be rather immediate.

2 Q. Continuing on page 24, you refer to the electric
3 delivery group and the generation supply group.

4 A. Yes.

5 Q. Do you have any idea what the official name of
6 the generation supply group will be?

7 A. I am aware that that is under discussion at this
8 stage of the game.

9 Q. Once again, what sort of time frame are we
10 looking at as far as that determination?

11 A. You have to talk to my management about that. I
12 honestly cannot answer that question. I do not know.

13 Q. What about the electric delivery group? What
14 will be the official name of that particular entity within
15 PP&L?

16 A. I do not know.

17 Q. What steps has PP&L undertaken or what steps
18 does PP&L plan on undertaking to insure that all customers
19 are aware that there is a regulated portion of the entity
20 and an unregulated portion of the entity?

21 A. I believe that probably could be addressed
22 better by Don Lennon who is a witness later on for customer
23 education. But having said that, I do not know of any
24 specific steps.

25 MR. MULLINS: Your Honor, if I may, I'd like to

1 provide the witness with a copy of the Massachusetts
2 Department of Public Utility Statute of Conduct regarding
3 electric distribution companies within that state.

4 JUDGE KASHI: To what end, sir?

5 MR. MULLINS: Pardon me?

6 JUDGE KASHI: To what end?

7 MR. MULLINS: This particular document sets forth
8 prohibitions promulgated by the DPU in Massachusetts as to
9 how an EDC should interact with its affiliate.

10 JUDGE KASHI: And what relation does it have to
11 Pennsylvania?

12 MR. MULLINS: I would like to ascertain this
13 witness's opinions as to some of these prohibitions set
14 forth in Massachusetts.

15 MR. KAPLAN: Your Honor, we have this Pennsylvania
16 statute, Pennsylvania law. It seems to me that
17 Massachusetts is not terribly relevant to this proceeding.

18 We don't know what the law is. We don't know what
19 negotiations were involved in achieving that code of
20 conduct.

21 JUDGE KASHI: If there are questions that you want to
22 formulate based upon that without referring to it -- I mean,
23 I just don't see any need to bring in something from
24 Massachusetts into this hearing.

25 MR. MULLINS: If you prefer, we can do it that way.

1 JUDGE KASHI: You can just ask him the questions, do
2 you think this should be in or that should be in,
3 hypothetically, fine. I quite frankly don't care what's
4 going on in Massachusetts.

5 MR. MULLINS: That's fine, Your Honor. We'll proceed
6 that way.

7 BY MR. MULLINS:

8 Q. Mr. Geneczko, is it appropriate for an EDC and
9 its generation affiliate to share employees?

10 A. No, it is not.

11 Q. How come?

12 A. Our code already addresses that, but sharing of
13 employees would suggest that you have an employee that has
14 an assignment on both sides of the firewall, both sides of
15 the fence. And that to me is a prescription for information
16 transferring back and forth across the firewall.

17 Q. So just to recap, will the electric delivery
18 group share employees with the generation supply group?

19 A. I will clarify that. The electric delivery
20 group, to the extent you have janitorial services, sure, we
21 would share employees. To the extent you have people
22 involved in, again, the four aspects of information:
23 customer information, that specific customer information
24 that might be generic, supplier information and
25 transmission/distribution information, we will not share

1 those employees.

2 Q. What about physical separation of the two
3 entities?

4 A. We will physically separate our entities.

5 Q. Do you have any idea how that is going to be
6 done?

7 A. There is a master plan being developed, and we
8 are starting to make moves and have made moves, but for
9 instance there is a group on the floor I am that will be off
10 the floor within a matter of, by September 1st, I believe,
11 as a matter of fact.

12 Q. Mr. Geneczko, in Exhibit RMG-4, your surrebuttal
13 testimony, page 3, you discuss the dispute resolution
14 process.

15 A. Yes.

16 Q. Once again, what sort of time frame are we
17 looking at as far as establishing a provision to deal with
18 that?

19 A. It is under development now, and I do not know
20 the time frame it will be concluded.

21 Q. One more question, Mr. Geneczko. On page 23 of
22 your surrebuttal, towards the middle of the page, you're
23 discussing the prohibition against alternate suppliers using
24 the electric delivery group's billing process to communicate
25 with customers or potential customers.

1 Q. Could you direct me to a specific line, please?

2 A. I believe it's line 13, 13 through 15.

3 A. Yes.

4 Q. Now, will that also apply to the generation
5 supply group?

6 A. Yes, it will.

7 MR. MULLINS: Thank you for your testimony.

8 Your Honor, I don't have anything further.

9 JUDGE KASHI: Thank you very much, Mr. Mullins.

10 Redirect, counsel?

11 MR. KOHLER: Just one minute. I just want to see if
12 we have anything.

13 JUDGE KASHI: Sure.

14 (Pause.)

15 REDIRECT EXAMINATION

16 BY MR. KOHLER:

17 Q. Mr. Geneczko, you were asked on cross-
18 examination about how the code of conduct will be enforced.
19 Do you have any understanding about the obligations of the
20 company with respect to the code of conduct?

21 A. Yes. Again, not being a lawyer, it is my
22 understanding that at the end of this proceeding, the code
23 will become an order and we will be bound under the
24 Pennsylvania utility code to act by the code.

25 MR. KOHLER: Thank you, Mr. Geneczko.

1 I have no further questions, Your Honor.

2 JUDGE KASHI: Thank you very much, sir.

3 You are excused, sir.

4 (Witness excused.)

5 JUDGE KASHI: That which has been marked and
6 identified as PP&L Statement No. 13 and 13-R, Exhibit
7 RMG-1 to 3 and Exhibit RMG-4 are received into the
8 evidentiary record, without objection?

9 (No response.)

10 JUDGE KASHI: Without objection.

11 (Whereupon, the documents marked as
12 PP&L Statements Nos. 13 and 13-R
13 and PP&L Exhibits RMG-1 through 4
14 were received in evidence.)

15 JUDGE KASHI: Mr. Kohler, do you wish to call your
16 first witness, sir?

17 MR. KOHLER: Yes, Your Honor. I call Dr. John Mayo.
18 Whereupon,

19 JOHN MAYO

20 having been duly sworn, testified as follows:

21 DIRECT EXAMINATION

22 BY MR. KOHLER:

23 Q. Good afternoon, Dr. Mayo.

24 A. Good afternoon.

25 Q. Have you submitted pre-filed testimony in this

1 proceeding?

2 A. Yes, I have.

3 Q. And would that direct testimony be Enron
4 Statement 1?

5 A. It is I believe Enron Statement No. 2.

6 Q. No. 2.

7 A. I didn't know I was going to be cross-examined
8 by you.

9 Q. And does that consist of 33 pages and one
10 exhibit?

11 A. Yes.

12 Q. And then you also submitted surrebuttal
13 testimony in this proceeding?

14 A. Yes, I did.

15 Q. And would that be Enron Statement 2.1?

16 A. Yes.

17 Q. And does that consist of 19 pages?

18 A. Yes.

19 Q. Do you have any changes to that pre-filed
20 testimony or corrections at this time?

21 A. I have one correction, and that is in the
22 rebuttal testimony on page 11, line 8. For the life of me,
23 I do not know how this happened, but what should have come
24 out with the words "rules based" came out "rykes based,"
25 R-Y-K-E-S. It should have been "rules based."

CROSS-EXAMINATION

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

BY MR. RUBIN:

Q. Good afternoon, Dr. Mayo.

A. Good afternoon.

Q. My name is Scott Rubin and I represent IBEW, Local 1600. I'd like to begin with your direct testimony, page 22.

On this page, you discuss the consumer benefits that you believe will flow from allowing retail competition in the electric industry.

You mentioned Cleveland, Ohio as a place where there is direct competition for retail electric customers. Are you familiar with the way that retail electric service is provided in Cleveland?

A. No, only to the extent that it was represented to be a city where there is competitive jurisdictions in the text written by Professor Quoka.

Q. So you don't have any firsthand knowledge of what is happening in Cleveland in terms of retail electric competition?

A. I have neither been to Cleveland nor have I studied it.

Q. Do you know from what you have read if customers in Cleveland have the right to choose where their electric generation will come from, who their generation supplier

1 will be?

2 A. I do not know that, no.

3 Q. And do you know if customers in Cleveland have
4 the ability to choose if an entity other than their electric
5 utility will provide them with billing services or metering
6 or meter reading or any other services?

7 A. No, I do not know that.

8 Q. On page 24 of your direct testimony, you suggest
9 that revenue cycle services should be opened up to
10 competition. By that, do you mean that a customer should be
11 able to choose who provides the customer with a bill for
12 service?

13 A. Yes.

14 Q. In a retail market, isn't it the provider of the
15 good or service who decides how a customer will be billed
16 for that service?

17 A. Well, the provider of the service can offer
18 those services to the customer. The customer then will pay
19 the bill. If the customer is not happy with the service,
20 then presumably he or she can switch providers.

21 Q. Right, but isn't it up to the provider of the
22 service to issue a bill for that service? And obviously, as
23 you said, if the customer is not happy, then the customer
24 can go somewhere else.

25 A. Well, what I guess we're discussing here is

1 whether the billing of the service can be provided apart
2 from underlying provision of the service, and I think
3 there's no economic reason why those services need be
4 bundled together.

5 If for instance there were a provider of billing
6 services that were superior at providing those services than
7 the underlying carrier of the service that might like to be
8 the billing agent, then it would seem to be in the
9 consumer's interest to have the availability or have the
10 right to choose an alternative billing agent.

11 Q. Dr. Mayo, just so we're clear, I'm not asking
12 you what could happen. I'm asking you, in the marketplace
13 today, if I'm selling a service, isn't it up to me to decide
14 how I'm going to bill my customers for that service?

15 A. Typically, that's correct.

16 Q. And isn't it also up to the seller of a good or
17 service to provide customer service, whether it's dealing
18 with complaints or problems or calculating the bill,
19 whatever it might be?

20 A. That may or may not be the case. As I said, the
21 question really is whether the services or activities --

22 Q. Dr. Mayo, I wanted you to answer the question
23 that I'm asking. Don't tell me what the question really is.
24 We'll just be here longer.

25 A. Okay, I'm sorry. I was trying to answer your

1 question. If you'll state the question, I'll try my best to
2 answer it.

3 Q. What I'm asking is, again, in the marketplace
4 today, if I'm selling a good or a service, isn't it up to
5 me, the seller, to decide how customer service will be
6 provided to my customer, and again, if the customer is not
7 happy, the customer can go someplace else?

8 A. As a typical matter, you describe the
9 marketplace. It's not clear in all marketplaces that that
10 is the case. It may or may not be the case that for the
11 services provided by a particular provider, that they
12 provide all services including billing service, including
13 all aspects of customer care, or whether those services
14 might be provided by someone other than the underlying
15 carrier.

16 It certainly can be the case for purposes -- and the
17 reason that I was responding the way I did -- the economic
18 question on the table on this proceeding is whether they
19 have to be economically bundled to benefit customers in the
20 state of Pennsylvania.

21 I think there the answer is, they don't from an
22 economic perspective need necessarily to be bundled.
23 Indeed, the bundling of those may eliminate a more efficient
24 provider of those end use customer interface functions.

25 Q. Dr. Mayo, I'm going to get back to what I've

1 been trying to ask you. In the marketplace today, is it up
2 to the seller or the buyer to decide how a customer will be
3 billed?

4 A. Certainly the seller has the opportunity to
5 offer whatever billing arrangements it wants to to consumers
6 and to put those on the table.

7 Q. Are you suggesting by your testimony that PP&L
8 should be required to let someone else bill for the services
9 that PP&L is providing to its customers?

10 A. I'm saying, what I am saying is that customer
11 interface functions -- and that may include customer billing
12 and a variety of customer care functions -- are not to my
13 knowledge naturally monopolistically provided by the
14 utility.

15 There is nothing from my study of this market or any
16 other market or any indication of the empirical evidence to
17 suggest that those are most efficiently supplied necessarily
18 by the incumbent utility. They may be. Therefore, I have
19 absolutely no problem at all with PP&L offering those
20 services.

21 What I do think ought to be available is the
22 opportunity for alternative suppliers to compete for the
23 right to supply those services to make consumers happier.

24 Q. Dr. Mayo, again, I appreciate the response you
25 gave, but you didn't answer my question, so I have to ask it

1 again.

2 Are you suggesting that PP&L should be required to
3 let someone else bill for services that PP&L is providing to
4 its customer?

5 MR. KOHLER: Your Honor, I think he has answered the
6 question. He said he is an economist and he is answering it
7 from an economic standpoint.

8 JUDGE KASHI: Well, how about if he just answers as a
9 layman, so I can understand what he's saying?

10 Can you answer that question?

11 THE WITNESS: Okay. Should PP&L be required to allow
12 alternate suppliers of retail level services --

13 JUDGE KASHI: No, that's not the question. Should
14 PP&L be required to let someone else bill for services that
15 PP&L provides?

16 THE WITNESS: The answer is, not exclusively, but the
17 opportunity to do so, yes.

18 BY MR. RUBIN:

19 Q. Dr. Mayo, are you familiar with any other
20 service in our economy where a seller of a good or service
21 is required to let someone else handle the billing, payment
22 or customer service?

23 A. Not as I sit here right this minute, no.

24 Q. Now, on page 26 of your direct testimony, you
25 state that PP&L should be required to provide revenue cycle

1 services on an unbundled basis.

2 In your opinion, should PP&L be required to provide
3 these services at all?

4 A. For the moment, yes, and for the long run,
5 perhaps not. And let me explain. In the short run, as I
6 understand it, PP&L is the only provider of those customer
7 interface functions.

8 Q. I'm sorry. Before you go on, could you define
9 what you mean by "short run" for us?

10 A. What I mean by the short run is for the period
11 in which PP&L provides the services subject to significant
12 monopoly power.

13 To the extent -- and once the market, if that market
14 becomes subject to effective competition so that there are
15 alternative suppliers, so that customers would not be
16 disadvantaged from the exit of one particular supplier,
17 whoever that supplier is, then the answer I think becomes
18 no, you shouldn't require or put a burden on any particular
19 competitive -- in an effectively competitive market.

20 Q. How will we know it when we see it? How do we
21 know that the market is developed enough so that PP&L can
22 decide we don't want to provide the services anymore?

23 A. If you're asking me the question, how do we know
24 when the market is subject to effective competition, then I
25 think the answer is that there's a relatively well defined

1 economic literature on how you determine whether a firm has
2 significant monopoly power or, in the alternative, is
3 subject to effective competition. That literature exists,
4 and I think there is a standard approach.

5 Q. That's really what I was asking you, and not
6 very well. The same kinds of things we use to decide
7 whether a telecommunications service is competitive or not,
8 whether a merger would result in significant market power,
9 that's what you use here for billing and metering and
10 customer service functions?

11 A. Standard market power analysis, yes.

12 Q. Under your proposal, does PP&L have the option
13 of refusing to provide revenue cycle services to any
14 particular customer? And just so we're clear, I'm not
15 talking about them getting out of the business completely,
16 but saying to a particular customer, "No, I will not be your
17 provider for these services."

18 A. Again, with the consumer --

19 MR. KOHLER: I'm sorry, I missed the first part of
20 the question. Are you asking under this particular Act --

21 MR. RUBIN: No. I'm asking under his proposal, what
22 he has testified to.

23 MR. KOHLER: You're asking, under his economic
24 theory, whether that would be appropriate?

25 MR. RUBIN: Well, as I understand the witness's

1 testimony, he has indicated that these services should be
2 competitive, and that at some point in time in the future,
3 if the market really takes off, then they might be so
4 competitive that perhaps PP&L could drop out of providing
5 these services.

6 MR. KOHLER: From an economic perspective.

7 MR. RUBIN: And what I'm asking is, under the
8 witness's testimony, does PP&L have the option of refusing
9 to provide revenue cycle services to a particular customer?

10 THE WITNESS: I think the answer would go back to the
11 answer I gave earlier. In the short run, defined the way we
12 did earlier, if PP&L were to refuse to provide those
13 services and they had significant monopoly power in the
14 provision of those services, it would drive up the price of
15 providing those services and harm consumers in Pennsylvania.

16 So I think the answer is that in the absence of
17 effective competition, that that sort of obligation would
18 remain.

19 BY MR. RUBIN:

20 Q. So, PP&L would have to provide the revenue cycle
21 services to every customer who wanted PP&L to provide them,
22 and would not have the option of saying no?

23 A. I think that's correct, though as I suggested,
24 consumers should also have the converse option of choosing
25 an alternative supplier should they choose.

1 Q. Still staying with your direct testimony, on
2 page 31, you refer to the presubscription process in
3 telecommunications.

4 Under that process, can long-distance companies
5 choose whether or not to provide service in a particular
6 exchange?

7 A. Yes, they can.

8 Q. And just so we're clear, one of your clients is
9 AT&T, isn't it?

10 A. I have testified, yes, in that capacity.

11 Q. So I just want to make it clear that you are
12 familiar with the long-distance market to some extent?

13 A. For a variety of reasons. It's an area I do a
14 lot of research in.

15 Q. So if, hypothetically, I live in an area that is
16 less desirable for some reason, there may be only one or two
17 long distance companies that participate in the
18 presubscription process. Is that possible?

19 A. Well, the presubscription process is generally
20 over now, but the answer is yes, that could have been the
21 case. But in reality, many more firms engaged in that
22 solicitation of consumer business than one or two.

23 Q. In every exchange?

24 A. In almost every exchange, even in very rural
25 areas, as it turns out. I'll give you an example of

1 Solomon's Island, Maryland, which is a relatively rural
2 area, that has about a hundred providers of long-distance
3 service. Hope, Arkansas has 12. Carthage, Tennessee has
4 34. Those are not randomly chosen.

5 Q. I'd like to invite you to Snyder County,
6 Pennsylvania someday to do the same analysis.

7 But in any case, if I live in a more desirable area,
8 would you expect that there are more long-distance companies
9 who were willing to participate in that process?

10 A. As a general matter, if you observe more of
11 them, it's because they find that area attractive to serve.

12 Q. And the suppliers get to choose where they will
13 compete for customers and where they won't compete for
14 customers?

15 A. Yes, they do.

16 Q. Are you proposing a similar process for electric
17 generation supply?

18 A. A similar process as what?

19 Q. As presubscription.

20 A. I think it does make some sense as we open the
21 market to competition to open the market as widely as
22 possible to competition and to consumer choice. To do that
23 may be or is a policy decision on the part of the
24 Commission.

25 A presubscription or a balloting process would

1 certainly involve some cost, but it would allow consumers to
2 make an affirmative choice of which electricity supply
3 provide they would like to have serve them, yes.

4 Q. Again, I appreciate that response. I'm not sure
5 I got a direct answer to my question. Are you specifically
6 proposing that process in Pennsylvania within PP&L's service
7 territory?

8 A. I am suggesting that the Commission consider
9 that policy, yes.

10 Q. And in telecommunications, I sort of understood
11 how that worked. There were areas that are called exchanges
12 where a supplier would either agree to participate in that
13 exchange or they wouldn't; is that right?

14 A. Yes.

15 Q. And what would be the comparable area to an
16 exchange for the provision of electric generation supply?

17 A. There's probably some amount of complication due
18 to the fact that the statute requires that competition be
19 implemented in thirds.

20 As I understand the law, at least chronologically,
21 one-third would occur in 1999, one-third in 2000, one-third
22 in 2001.

23 But presumably, for whatever geographic region is
24 chosen, whether it's one-third of the customers in the
25 eastern half and then the middle half and then the western

1 half the PP&L service territory, those customers would
2 receive the option of picking affirmatively the supplier of
3 choice for those suppliers who indicate a willingness and an
4 ability to serve them as retail providers of electricity in
5 Pennsylvania.

6 Q. I'm trying to look to this analogy of
7 presubscription.

8 A. Yes.

9 Q. And from what you just described, it sounds like
10 the supplier might have to be willing to serve all of PP&L's
11 service territory in order to participate.

12 Is that what you envision, or are there going to be
13 some kind of smaller geographic areas where a supplier could
14 say, "I'll serve this area but not this other area over
15 here"?

16 A. I think that's a good question. I think,
17 though, remember again that the goal of that is to bring
18 competitive benefits to consumers and to open the market as
19 widely as possible. So I would not favor imposing a burden
20 on new entrants of necessarily saying, if you're going to
21 serve these three customers, you must serve the remainder of
22 the customers in the PP&L service territory.

23 To do so and to require that of new entrants I think
24 would raise a barrier to entry.

25 JUDGE KASHI: Now, can you answer the question?

1 THE WITNESS: Your Honor, I thought I did.

2 JUDGE KASHI: I thought you went all the way around
3 it and you never got even close to it. I mean, you tell us
4 what you wouldn't do and all the rest of it.

5 He asked you, what is comparable to the exchange in
6 the telephone services that you would be talking about?
7 What is the area that you're going to have ballot? What is
8 the area that you're going to do presubscription?

9 THE WITNESS: Your Honor, I'm sorry. I perhaps --

10 JUDGE KASHI: You're telling me what you wouldn't do.

11 THE WITNESS: Perhaps I was not clear. What I said
12 was there are some complications invoked by the fact that
13 chronologically, the Act requires one-third, one-third,
14 one-third.

15 The answer is, I don't know precisely how you would
16 implement that process.

17 JUDGE KASHI: Let me see if I have it straight.
18 You're proposing presubscription and a ballot process. You
19 have no idea how that would work because if we start with
20 one-third, you don't know what you would do with that, but
21 you're still going to propose presubscription and balloting?

22 THE WITNESS: Let me suggest this, that what I am
23 suggesting and raise for the Commission's consideration is a
24 balloting process or an option to choose.

25 The reason I offer that as an option -- and I'll

1 grant you I did not lay out, line by line, specifically how
2 it was done. You're correct about that.

3 JUDGE KASHI: I don't want line by line. I want some
4 basic idea.

5 THE WITNESS: The basic idea is that the Commission
6 would offer consumers affirmatively a choice of which
7 supplier to pick from, that's all.

8 JUDGE KASHI: In the whole one-third we're going to
9 start with, we're going to offer everybody, everybody is
10 going to come in and we're going to put a ballot for
11 everybody who wants that?

12 THE WITNESS: I'm sorry.

13 JUDGE KASHI: You just got done saying you wouldn't
14 force an entrant to serve a whole one-third.

15 THE WITNESS: That's correct, I would not.

16 JUDGE KASHI: So then you're going to come down to
17 discrete pockets and levels of what?

18 THE WITNESS: As I said, I have not laid this out
19 line by line. Before you dismiss my suggestion, though,
20 however, let me suggest that the presubscription process did
21 reduce consumer rates in telecommunications and benefit
22 consumers.

23 I'm not suggesting that if done improperly it might
24 not be a bad idea.

25 JUDGE KASHI: But, sir, all I've heard from you is

1 some very nice words and theories and ideas without anything
2 to back it up, to substantiate it, to give me any kind of
3 factual basis to work it from.

4 THE WITNESS: Your Honor, the fact is that the
5 presubscription process reduced rates. That's a fact. And
6 I can't point toward that in the --

7 JUDGE KASHI: But we were talking about, in the
8 presubscription process, we had exchanges.

9 THE WITNESS: Yes, sir.

10 JUDGE KASHI: And we're trying to get you to, for
11 God's sake, please tell us what we're going to use in it,
12 and you say you can't, so I don't know how it can be valid
13 if you don't have anything -- you're taking it from the
14 telecommunications sense that had particular valid exchanges
15 to work from, and now just throwing it out as an idea
16 because it worked there, but we don't know how it would
17 work, I haven't done any line by line ideas. I definitely
18 wouldn't ask new entrants to take a big chunk like a third,
19 but let's ask everybody to ballot. I mean, that's what your
20 testimony is.

21 MR. KOHLER: Your Honor, that is his testimony, and I
22 think we have to remember that Dr. Mayo is testifying as an
23 economist and whether certain things in his opinion are
24 economically sound. I think if --

25 JUDGE KASHI: He's got to give me a basis, Mr.

1 Kohler, for something to be economically sound, not merely
2 the idea that it worked some other place.

3 MR. KOHLER: I think my point is that if Enron wanted
4 to put on a specific proposal as to how presubscription
5 would work in the electric market with or without the
6 economics, we would do that through another witness.

7 JUDGE KASHI: All right.

8 BY MR. RUBIN:

9 Q. Dr. Mayo, if we can look again for a minute at
10 your proposal that generation suppliers be given the option
11 of providing revenue cycle services, if your recommendations
12 in that regard are adopted, would suppliers, generation
13 suppliers be restricted or regulated in the price that they
14 can charge for revenue cycle services?

15 A. Only to the extent that there was a good public
16 policy reason, for instance the possession of significant
17 monopoly power. Otherwise, no.

18 Q. So as things stand today, with PP&L providing
19 these services for all of its customers, what would your
20 recommendation be for whether the rates should be regulated
21 for a generation supplier who wants to provide revenue cycle
22 services?

23 A. That they should not be regulated unless it is
24 shown that they had significant monopoly power, that there
25 were a good public policy reason to do so.

1 Q. So that might happen at some point off in the
2 future if one supplier had 80 percent of the market, but
3 that wouldn't happen immediately?

4 A. That would be my understanding.

5 Q. And would PP&L's price for revenue cycle
6 services be regulated, again under your proposal?

7 A. Only to the extent that it possessed significant
8 monopoly power in the supply of those services.

9 Q. And again, if we could look initially to January
10 1, 1999, what would your recommendation be?

11 A. I have not analyzed the issue of whether, if
12 properly unbundled, those revenue cycle services offered by
13 PP&L would be subject to significant monopoly power. I have
14 not done that factual investigation, so I can't really offer
15 a suggestion other than the economic guidepost of a turning
16 point on whether they do have significant monopoly power or
17 not.

18 Q. So as things stand today and based on the work
19 that you've done so far, you have no recommendation to this
20 Commission as to whether PP&L's rates for providing revenue
21 cycle services should continue to be regulated?

22 A. It would be dependent upon an empirical
23 investigation, a factual investigation of whether PP&L
24 retained significant monopoly power in the provision of
25 those services.

1 Q. And you have not done that investigation?

2 A. No, I have not.

3 Q. And you do not have a recommendation for how we
4 should start, when you get into this new era some 15 or 16
5 months from now?

6 A. I apologize. The question seemed open ended
7 about --

8 Q. I'm sorry. It was a lousy question. Let me try
9 it again. I just want to make it clear -- you said you
10 haven't done the investigation and I understand that.

11 The problem we're faced with is, in about 15 or 16
12 months, generation suppliers are going to be coming into the
13 market, PP&L is going to be providing these revenue cycle
14 services.

15 I'm asking you, should PP&L's rates for providing
16 those services on January 1, 1999 be regulated by this
17 Commission or should they not be regulated by this
18 Commission?

19 A. I think I gave you as much of a guidepost as I
20 can, and I have confidence that the Commission can and has
21 analyzed market power issues and has established a mechanism
22 for doing that.

23 MR. RUBIN: Thank you.

24 That's all I have for this witness, Your Honor.

25 JUDGE KASHI: Thank you very much, sir.

1 Mr. Mullins?

2 MR. MULLINS: No questions, Your Honor.

3 JUDGE KASHI: Mr. Kaplan?

4 MR. KAPLAN: Thank you, Your Honor.

5 If I may inquire, Your Honor, how much further you
6 intend to go?

7 JUDGE KASHI: Until we're finished.

8 MR. KAPLAN: With this witness?

9 JUDGE KASHI: And the next.

10 CROSS-EXAMINATION

11 BY MR. KAPLAN:

12 Q. Dr. Mayo, do you believe that the Commission
13 determination -- oh, I'm sorry. My name is Donald Kaplan.
14 I'll be examining you for Pennsylvania Power & Light.

15 A. Fine. Thank you.

16 MR. FOGEL: Mr. Kaplan, could you speak up? We just
17 can't hear you.

18 MR. KAPLAN: I'll try to be louder.

19 BY MR. KAPLAN:

20 Q. Dr. Mayo, do you believe that the Commission
21 determination of the issues in this case should be guided by
22 sound economic principles?

23 A. Yes.

24 Q. Would you agree that the Commission's decision
25 in this case should have a solid factual support as well?

1 A. As best as possible, yes.

2 Q. I'm going to show you four responses to
3 interrogatories, just to move this along. These are Enron's
4 responses to PP&L interrogatories Nos. 29, 7, 4 and 30, in
5 that order. And I'll inquire as to them once we get them
6 circulated.

7 (Pause.)

8 BY MR. KAPLAN:

9 Q. Just to move this along, have you had a chance
10 to examine those four interrogatory answers?

11 A. Yes.

12 Q. Do you agree with those answers as they are
13 reported in the interrogatory answers?

14 A. Yes.

15 MR. KAPLAN: Your Honor, we would like to move the
16 introduction of PP&L Cross-Examination Exhibits Nos. 1, 2, 3
17 & 4, Enron's responses to PP&L Interrogatory Nos. 29, 7, 4,
18 and 30 respectively.

19 MR. RUBIN: Could you repeat that, please?

20 JUDGE KASHI: Received without objection.

21 MR. RUBIN: Your Honor, could I ask which
22 interrogatory answer is which exhibit number?

23 JUDGE KASHI: Let's do it this way. Could somebody
24 hand the Judge a set of them?

25 MR. KAPLAN: Oh, our apologies, Your Honor.

1 JUDGE KASHI: Mr. Kaplan, do you want to just give us
2 1, 2, 3 and 4?

3 MR. KAPLAN: All right. PP&L Interrogatory No. 29,
4 Enron's response is Number 1. Enron response to PP&L
5 Interrogatory No. 7 is Number 2. Enron response to PP&L
6 Interrogatory No. 4 is Exhibit 3, and Enron response to PP&L
7 Interrogatory No. 30 is Number 4. And my apologies for the
8 confusion, Your Honor. We'll try to be more organized.

9 JUDGE KASHI: They have been received in.

10 (Whereupon, the documents were
11 marked as PP&L Cross-Examination
12 Exhibits Nos. 1, 2, 3 and 4 for
13 identification and received in
14 evidence.)

15 BY MR. KAPLAN:

16 Q. Are you aware, Dr. Mayo, that Enron is one of
17 the largest marketers of natural gas in the country?

18 A. Yes.

19 Q. To your knowledge, does Enron engage in monopoly
20 leveraging?

21 A. I have no knowledge of that.

22 Q. Enron, of course, owns two regulated interstate
23 natural gas pipelines; is that correct?

24 A. I'll accept that as correct, yes.

25 Q. You're not aware that they own two interstate

1 regulated industries?

2 A. I'm generally aware that they do own pipelines.

3 Q. Do you know the name of those pipelines?

4 A. No, I do not.

5 Q. Do the names Northern Natural Gas and
6 Transwestern Pipeline ring a bell?

7 A. No.

8 Q. Are you aware that Enron owns Portland General
9 Electric Company?

10 A. I have been made aware of that, yes.

11 Q. Is it your understanding that Portland General
12 Electric Company is regulated by the Oregon Public Utility
13 Commission?

14 A. That would be my understanding.

15 Q. And I'll show you a list.

16 MR. KAPLAN: And we do not intend to mark this as an
17 exhibit, Your Honor, as a record of the Commission. It's a
18 list of applications for --

19 JUDGE KASHI: Show it to counsel.

20 MR. KAPLAN: -- power to be alternate suppliers under
21 the Pennsylvania Customer Choice and Competition Act. This
22 is a document we obtained from the Commission.

23 BY MR. KAPLAN:

24 Q. Looking at this list, are you familiar with CNG
25 Energy Services Corporation or CNG Retail Services

1 Corporation?

2 A. Not other than the fact that it's listed here.

3 Q. Are you familiar with a company called

4 Consolidated Natural Gas?

5 A. No, not generally.

6 Q. Are you aware that Consolidated Natural Gas owns

7 Peoples Gas and Distribution Company in Pennsylvania?

8 A. I believe I have heard that, yes, but that's

9 all.

10 Q. Are you familiar with Dupont Power Marketing?

11 A. Only in a vague sense that it's mentioned here,

12 yes.

13 Q. Do you understand it's affiliated with a company

14 once known as Conoco, a large energy supplier?

15 A. Again, if you say that, I think that is correct.

16 Q. Are you familiar with NorAM Energy Management,

17 Inc.?

18 A. No.

19 Q. Do you have knowledge whether NorAM Energy

20 Management, Inc. is affiliated with Houston Industries which

21 owns Houston Light and Power, a large utility in Texas?

22 A. No.

23 Q. Have you heard of GPU Advanced Resources, Inc.?

24 A. Yes.

25 Q. Are you aware that GPU Advanced Resources is

1 affiliated with General Public Utilities, which owns
2 Metropolitan Edison and Penelec?

3 A. Yes, I am.

4 Q. Are you familiar with Xenergy, Inc.?

5 A. No.

6 Q. Are you familiar with Delmarva Power and Light
7 Company?

8 A. Yes, I am aware of Delmarva.

9 Q. Is it your understanding that Delmarva Power and
10 Light is a member of the PJM?

11 A. Yes.

12 Q. Are you familiar with Equitable Power Services
13 Company?

14 A. No, I don't think so.

15 Q. Are you familiar with Virginia Electric and
16 Power Company?

17 A. Yes.

18 Q. Are you familiar with Southern Energy Retail
19 Trading and Marketing, Inc.?

20 A. Generally, yes.

21 Q. Are you aware that they are affiliated with the
22 Southern Company, a holding company for several large
23 utilities in the south?

24 A. Yes.

25 Q. Are you familiar with Peco Energy Company?

1 A. Yes, I am.

2 Q. They are a utility in Pennsylvania; is that
3 correct?

4 A. Yes.

5 Q. Are you familiar with PanEnergy Trading and
6 Market Services, LLC?

7 A. Yes, I think so.

8 Q. And you understand they recently were acquired
9 by Duke Energy, a large utility in North Carolina?

10 A. That's correct.

11 Q. Are you familiar with PacificCorp?

12 A. Yes.

13 Q. And they are a large utility serving several
14 western states; is that correct?

15 A. That's my understanding, yes.

16 Q. Are you familiar with West Penn Power Company,
17 doing business as Allegheny Power?

18 A. No, I don't think so.

19 Q. Are you familiar with the Allegheny Power
20 System?

21 A. Only in the most general sense.

22 Q. Do you understand that they do business in
23 Pennsylvania?

24 A. Yes, that would have been my understanding.

25 Q. You have no reason to doubt that all these

1 companies have in fact applied for licenses to be suppliers
2 in Pennsylvania?

3 A. Yes. If you secured this list from the
4 Commission, I have no doubt that they have in fact filed
5 applications.

6 Q. Are you familiar with Order 497 of the Federal
7 Energy Regulatory Commission?

8 A. Only in the most general sense.

9 Q. What's your general sense of what Order 497
10 does?

11 A. That it exists and that it is part of the FERC
12 process of regulating the transmission and wholesale aspects
13 of the industry.

14 Q. Are you aware of whether 497 is applicable to
15 Enron's regulating interstate pipelines?

16 A. No.

17 MR. KOHLER: Your Honor, can we at least have an
18 offer of proof of where this is going? I don't see any
19 connection to his testimony at this point.

20 JUDGE KASHI: Mr. Kaplan?

21 MR. KAPLAN: I am done with this line.

22 MR. KOHLER: Excuse me?

23 MR. KAPLAN: I am done with this line of questioning.
24
25

1 BY MR. KAPLAN:

2 Q. Is it true, Dr. Mayo, that one of the first
3 steps in assessing competition is to define a relative
4 geographic market?

5 A. In a formal analysis of market power for
6 monopolization cases, yes.

7 Q. Is it true that the relevant geographic market
8 under retail competition will be determined in large part
9 based upon the availability of transmission and distribution
10 at a reasonable and non-discriminatory price?

11 A. I think that is part of the market definition
12 exercise that would be undertaken, is an examination of the
13 ability of alternative suppliers outside the region to
14 supply power within the region.

15 It could either be handled as part of a market
16 definition exercise or, alternatively, as an analysis of the
17 height of barriers to entry.

18 Q. Would you agree that once retail competition is
19 implemented, both transmission and distribution will be
20 available to all participants at rates regulated either by
21 the Federal Energy Regulatory Commission or by the
22 Pennsylvania Public Utility Commission?

23 A. That would be my understanding, that T&D
24 services are subject to regulation.

25 Q. Would you agree that those rates would apply not

1 only to alternate suppliers in PP&L's retail distribution
2 system but to PP&L's competitive generation suppliers as
3 well?

4 A. Yes.

5 Q. Now, is it true, Dr. Mayo, that you have no
6 specific knowledge of any transmission or distribution
7 constraints that would affect the delivery of power by
8 alternate suppliers into PP&L's retail distribution system?

9 A. It is true that I have not engaged in that
10 empirical analysis. I think Dr. Tabor as a witness for
11 Enron may have spoken to that issue.

12 Q. Do you know if he dealt with the PJM
13 transmission or PP&L's distribution system?

14 A. I think his testimony speaks to constraints
15 generally I think in the PJM system and PP&L, but I will let
16 his testimony speak for itself. I'm just pointing to you
17 where that empirical analysis exists, to the extent that it
18 does. It does not exist in my testimony.

19 Q. Do you know the difference between PP&L's
20 distribution system and PP&L's transmission system?

21 A. Yes.

22 Q. What is that difference?

23 A. Between distribution and transmission system?

24 Q. Yes.

25 A. The distribution system is generally conducted

1 at a lower voltage for residential consumers, for instance,
2 and transmission is for higher voltage power.

3 Q. Do you know where the dividing line between the
4 distribution and transmission system is?

5 A. I'm not an engineer, no, if that's what you're
6 asking. I do not have engineering knowledge of that. Those
7 terms are generally referred to in the way I've described
8 them in the literature. I know that.

9 Q. Have you read the testimony of Mr. Whitehead in
10 this proceeding?

11 A. No, I have not.

12 (Pause.)

13 Q. Do you have before, Dr. Mayo, a copy of Enron's
14 response to PP&L Interrogatory No. 17?

15 A. Yes, I do.

16 Q. Would you agree, if you were asked that question
17 here today, you would give the same answer?

18 A. Yes.

19 MR. KAPLAN: Your Honor, we would like to move for
20 admission as PP&L Cross-Examination No. 5 Enron's response
21 to PP&L's Interrogatory No. 17.

22 JUDGE KASHI: It is received into the evidentiary
23 record without objection?

24 (No response.)

25 JUDGE KASHI: Without objection.

1 (Whereupon, the document was marked
2 as PP&L Cross-Examination Exhibit
3 No. 5 for identification and
4 received in evidence.)

5 BY MR. KAPLAN:

6 Q. Would you please turn to page 14 of your direct
7 testimony, focusing on your answer beginning on line 11?
8 Are you there, sir?

9 A. Yes.

10 Q. Is it true that you have not engaged in a
11 comprehensive study of the treatment of costs by PP&L in its
12 proposed restructuring plan?

13 A. That is true, I have not engaged in a
14 comprehensive analysis. I would point you toward Mr.
15 Reisling's testimony for a more detailed examination. I
16 speak to the economic incentives for firms to misallocate
17 costs.

18 Q. But you have no evidence that PP&L has done
19 that; is that correct?

20 A. Well, I think I do speak on the page prior to
21 15, on page 14 to an example of the sort of cost shifting
22 that I believe is inappropriate.

23 It is not meant to be a comprehensive study as I just
24 mentioned a moment ago, but it is indicative of a problem.
25 The problem is that if you take costs that are at the retail

1 level and you put them in the distribution category for
2 purposes of establishing a price cap for distribution
3 services today, that that sort of cost shifting is I think
4 antithetical to both economic efficiency and competition.

5 Q. Do you have any idea what those costs you cited
6 reflect, what they are for?

7 A. They are for what is referred to as a sales
8 category, I believe, in Mr. Kleha's testimony.

9 Q. But you have no idea what they're about?

10 A. They are listed as sales, sales expenses. I'm
11 assuming sales expenses are incurred at the retail level as
12 opposed to the distribution level. I did not look at the
13 underlying account codes or company books to make that
14 analysis.

15 Q. You were assuming?

16 A. I'm assuming sales means sales expenses.
17
18
19
20
21
22
23
24
25

1 Q. Dr. Mayo, please turn to your rebuttal testimony.
2 Would you agree that as a matter of general principle that
3 if the Commission is satisfied that it has taken adequate
4 steps to neutralize the ability to exercise market power
5 through the control of the distribution system that there is
6 no need to take further steps in the generation market to
7 achieve workable competition?

8 A. I agree that you're a large portion of the way
9 there. I think you'd have to look at a specific examination
10 of the generation market to see if there are any potential
11 competitive problems that may arise at the generation stage.
12 If you've satisfied yourself at both levels, then certainly,
13 yes, the Commission would be covered in its public policy
14 approach.

15 Q. And those particular problems would be, for
16 example, barriers to entry at the generation level?

17 A. Yes, that would be a potential problem, yes.

18 Q. Would you agree that with respect to the service
19 territories of other Pennsylvania utilities that PP&L
20 possesses no significant competitive advantage?

21 A. I'm sorry, you'll have to repeat the question,
22 I'm not quite sure I understand.

23 Q. Would you agree that with respect to the service
24 territories of other Pennsylvania utilities that PP&L
25 possesses no significant competitive advantage?

1 A. In competing in those markets, you're saying?

2 Q. In competing in the service territories.

3 A. In those service territories? I would agree to
4 that.

5 Q. All right. Would you agree that, Dr. Mayo, with
6 respect to PP&L's service territory, other Pennsylvania
7 utilities such as PECO, GPU or Allegheny Power System,
8 possess no significant competitive advantage?

9 A. That would be my general understanding, yes.

10 Q. Would you agree that to the extent that you
11 believe PP&L has the incentive and ability to exercise
12 market power, that incentive and ability flows from its
13 control of the means of delivering power within its service
14 territory?

15 A. Yes.

16 Q. Would you agree that it is sound economic policy
17 to encourage monopolies to compete vigorously?

18 A. Well, I think the answer is to open those
19 monopoly services to competition to allow competition to be
20 vigorous. Yes, that was the essence of my testimony.

21 Q. Well, I want an answer to my specific question.
22 Will you agree that it is sound economic policy to encourage
23 monopolies to compete vigorously?

24 A. Certainly to compete on its efficiency merits,
25 yes.

1 Q. Dr. Mayo, would you agree that the goal of both
2 regulation and competition should be the same, lower prices
3 and better service for consumers?

4 A. Yes.

5 Q. Would you agree that the Commission should not
6 avow policies that have the effect of raising prices to
7 consumers or preventing suppliers from providing them with
8 better service or lower cost service?

9 A. Yes, that's the essence of my testimony. And
10 speaking to those impediments that may exist in the
11 restructuring plan, to eliminate those and reduce those
12 impediments and barriers.

13 Q. The Commission should reduce the eliminate
14 impediments to consumers receiving lower prices and better
15 service?

16 A. Yes, sir, that's what I was saying.

17 Q. Dr. Mayo, would you please turn to page 5 of your
18 surrebuttal testimony? At line 5. Will you focus on line
19 5, please.

20 Do you understand that PP&L is not proposing that all
21 alternate supplier services be arranged through PP&L?

22 A. I'm sorry; could you repeat the question again?

23 Q. Never mind, I'll withdraw the question and go on
24 to the next area.

25 Dr. Mayo, would you agree that if the code of conduct

1 adopted by PP&L were incorporated in the order that emerges
2 from this proceeding, and that order and this code of
3 conduct were enforceable at the PUC and under Pennsylvania
4 public utility law, that this would go a long way toward
5 meeting the competition enabling approach that you espouse?

6 A. I think there are elements of that, yes. I think
7 the issue is, does it go far enough, and does the
8 restructuring policy proposed by PP&L go far enough in
9 opening the electricity market as wide as possible to
10 accomplish the goals that we just spoke of, of lowering
11 prices to consumers. I think the answer to that is that I
12 think we may disagree on whether it goes far enough.

13 Q. But you would agree that one of your principal
14 concerns is that PP&L not be under an obligation enforceable
15 under law to live by its code of conduct?

16 A. Could you say that again, please?

17 Q. Would you agree that one of your principal
18 concerns expressed in your testimony is that PP&L's code of
19 conduct would not be enforceable under law?

20 A. My concern is that the code of conduct as
21 structured fails to identify or proscribe various anti-
22 competitive actions that are, by virtue of the structure of
23 this industry, quite likely to arise. That is my concern.

24 Q. Dr. Mayo, it is indeed quite late, and I want to
25 ask a question. Is it true or not true that you have a

1 concern that PP&L's code of conduct is not enforceable under
2 law?

3 A. I cannot offer a legal conclusion. I can speak
4 to the economic incentive on the part of PP&L to engage in
5 actions that will financially benefit it, but not help
6 consumers. That's my point.

7 Q. Was it your understanding in writing your
8 testimony that PP&L's code of conduct would be a legally
9 enforceable document?

10 A. Yes.

11 Q. Will you agree with the following definition?
12 Market power is the ability of a firm to raise and maintain
13 prices above competitive levels where price approaches
14 marginal cost without losing so many sales that the above
15 marginal cost price is unprofitable.

16 A. Yes.

17 Q. Would you agree with the following statement?
18 For a firm to possess market power it must base sufficiently
19 low intensity of actual competition from firms currently in
20 the market, and a correspondingly low intensity of potential
21 competition from firms not currently in the market, to
22 sustain super-competition pricing.

23 A. Yes, I think those were my words.

24 Q. Will you agree with the following statement? The
25 concept of market power implies the ability to control price

1 by exercising control over the total amount of output
2 available in the market.

3 A. Yes.

4 Q. Would you agree with the following statement?
5 Because government intervention into markets is not
6 costless, such intervention is only warranted where firms
7 possess a significant amount of market power where
8 competitive market forces are not adequate to keep the
9 amount of monopoly power in check.

10 A. Yes, I do agree with that. Again, I think I've
11 written that.

12 Q. Do you agree with the following statement? If a
13 firm does possess significant market power, it will have the
14 ability to extract monopoly profits or to engage in
15 predatory pricing.

16 A. Yes.

17 Q. Dr. Mayo, do you agree that the lure of future
18 profits attracts entrepreneurs, businessmen, to produce
19 goods and services, that such firms may indeed invest
20 substantial funds in a market before realizing positive
21 returns to their investment, or that total compensation for
22 that investment may actually take several years to recover?

23 A. Certainly as a general proposition that may be
24 true.

25 Q. Will you agree with the fact that in capital

1 intensive industries it may take numerous years, in some
2 cases twenty or thirty years, to fully recover capital,
3 including a reasonable return, a competitive return on
4 investment?

5 A. It's certainly possible that that's the case. It
6 may happen very quickly, it may happen over a long time.

7 Q. Dr. Mayo, isn't it true that you have testified
8 for various regulatory agencies on behalf of American
9 Telephone and Telegraph Company attempting to seek the
10 removal of asymmetrical regulation to AT&T?

11 A. Yes, I have. And the reason is that once --
12 along the lines of our earlier discussion, once significant
13 monopoly power is absent, then those asymmetric regulations
14 are unwarranted. Prior to the removal of that significant
15 monopoly power, regulatory safeguards to protect the
16 competitive process may indeed be necessary.

17 Q. And wouldn't you agree that one of the most
18 important factors you cite in that testimony is the
19 elasticity of supply; is that correct?

20 A. The elasticity of supply of fringe firms, yes.

21 Q. You say fringe firms?

22 A. Yes. I just was being precise. Referring to the
23 elasticity of supply of a set of competitors to the firm in
24 question as opposed to the supply elasticity of the entire
25 market.

1 Q. To the former supply elasticity of the
2 competitors to the former monopoly?

3 A. I'm sorry, I thought I had it straight the first
4 time.

5 Q. All right.

6 A. If you want to say it again, --

7 Q. Well, let's take --

8 A. -- and I'll agree or disagree.

9 Q. -- the scenario --

10 A. I don't think we were disagreeing, but --

11 Q. We probably were not, but let's make the record
12 perfectly clear.

13 The supply elasticity is of the firms other than the
14 former monopolies?

15 A. That's correct.

16 Q. Okay. Would you agree that where competing firms
17 have abundant capacity, these are firms other than the
18 former monopolies, their ability to capture customers and
19 expand output is heightened, and that the ability to expand
20 output is what will limit the ability to charge monopoly
21 prices?

22 A. Yes, and the only caveat I would add to that,
23 though, is that while that capacity may be in place, and it
24 may impose an important competitive check, the ability to
25 impose that competitive check also is contingent upon the

1 willingness of consumers to switch suppliers to the firm
2 with the existing capacity. So it really requires both of
3 those.

4 Q. And in fact, you have testified that the
5 willingness of customers in the telephone industry, once it
6 was opened up to competition, was phenomenal, in fact, to
7 switch to alternate suppliers?

8 A. It was really remarkable in the long distance
9 industry how willing they were to switch.

10 Q. Do you have any information about the amount of
11 excess generation capacity in the PJM interconnection area?

12 A. No.

13 Q. You have not studied that?

14 A. No, I have not.

15 Q. Now, Dr. Mayo, would you agree that predatory
16 pricing is a competitive concern only when price is below
17 marginal costs?

18 A. That's both the general economic proposition and
19 the legal composition, I think, yes.

20 Q. Do you agree that the introduction of competition
21 in the market for generation of electricity will likely lead
22 to lower prices rather than higher prices?

23 A. Based on history I would suggest yes. And the
24 question is how much lower. And that depends on how policy
25 is implemented here.

1 Q. Please turn to page 6 of your surrebuttal
2 testimony.

3 I'm sorry, it may be your direct testimony, Dr. Mayo.

4 A. Okay.

5 MR. KOHLER: Direct testimony?

6 MR. KAPLAN: Yes.

7 BY MR. KAPLAN:

8 Q. Yes, it is page 6. It's line 8.

9 A. Okay.

10 Q. Is it your understanding that historically in
11 Pennsylvania non-wire activities have been treated as part
12 of the distribution stage of the industry?

13 A. Yes, that's what I wrote here on line 10, that
14 they have historically been treated as part of the
15 distribution stage.

16 What I go on to suggest is that they need not
17 necessarily be provided as a monopoly function on a going-
18 forward basis.

19 Q. Would you agree, Dr. Mayo, that the Pennsylvania
20 Electricity Generation, Competition and Customer Choice Act
21 balances a number of goals as well as competition?

22 A. There are a variety of things mentioned in the
23 act. I don't have any particular unique insights into it.
24 I'd say generally, yes, is my --

25 Q. And among those goals are fairness to customers,

1 electric utilities, investors, and the employees of the
2 electric utilities, local communities and utility
3 generators?

4 A. Yes.

5 Q. Non-utility generators.

6 A. There's some broad language in the act itself to
7 that effect.

8 Q. And reliability is one of those concerns, as
9 well?

10 A. Yes, it is; I believe so.

11 Q. And low-income assistance is one of those
12 concerns?

13 A. I'm sorry?

14 Q. Low-income assistance?

15 A. Yes, it is, there's a section of the act that
16 deals with low-income assistance.

17 Q. Dr. Mayo, are you familiar with a book entitled
18 "Government and Business, the Economics of Antitrust and
19 Regulation," by David L. Kaserman and John W. Mayo?

20 A. Yes, I am.

21 Q. Your very proud of your work; right?

22 A. No, I'm just glad to see someone bought it.

23 Thank you.

24 (Laughter.)

25 A. You'd flatter me more if you'd actually read it.

1 (Laughter.)

2 MR. FOGEL: Who says he bought it?

3 (Laughter.)

4 BY MR. KAPLAN:

5 Q. But that is a copy of your book; is that correct?

6 A. Yes, it is.

7 Q. Okay. Could you read the first two sentences in
8 the penultimate paragraph on that page, beginning with
9 "following precedent"?

10 A. Which page?

11 Q. Page 449; I'm sorry.

12 A. 449. And what would you like me to read?

13 Q. The first two sentences in the paragraph
14 beginning "following precedent."

15 A. Okay.

16 Q. And you can delete the reference to the equation,
17 which no one else will ever see.

18 A. Following the precedent established in the Hope
19 case, regulatory bodies have a legal mandate to assure a
20 utility's rates are, quote, just and reasonable, and that
21 the prescribed rates enable the firm to, quote, maintain its
22 financial integrity, to attract capital, and to compensate
23 its investors for the risk assumed. In practice, regulatory
24 commissions have attempted to set rates that will generate
25 sufficient revenues in equation 13.1 -- which I'm told no

1 one is going to read -- to satisfy this legal standard.

2 Q. Thank you.

3 MR. KAPLAN: If Your Honor can give me about a minute
4 to sort of organize, I've tried to move through very quickly
5 in light of the hour, and I just want to see if I have all
6 business done.

7 JUDGE KASHI: Fair enough.

8 (Off-the-record pause.)

9 BY MR. KAPLAN:

10 Q. Dr. Mayo, are you familiar that alternate
11 suppliers in Pennsylvania must post a bond in order to
12 obtain a license?

13 A. I was not aware of that, but that would be
14 consistent with the way other markets have opened up.

15 Q. And would you have any reason to doubt if I said
16 that the bond ordered by the Commission is \$250,000?

17 A. No, I have no reason to disagree with you about
18 that.

19 Q. Would you agree that a bonding requirement of
20 \$5 million would have eliminated a large number of potential
21 competitors from the market?

22 A. I don't know that.

23 Q. But it certainly would have eliminated some?

24 A. I don't know that either. We know that a higher
25 price is likely to have a deterrent effect. Whether it

1 would eliminate zero, one, 100, I don't know.

2 Q. It would be a barrier --

3 MR. KOHLER: Your Honor, this is way outside the
4 scope.

5 MR. KAPLAN: We're talking about competition,
6 barriers to entry into the market, Your Honor.

7 JUDGE KASHI: Right. I'll overrule the objection.

8 BY MR. KAPLAN:

9 Q. Relative to a \$250,000 bond, a \$5 million bond
10 would be a higher barrier to entry?

11 A. To the extent that that \$5 million is non-
12 recoverable in the event of exit in the market, then it
13 would represent higher sunk cost, and therefore a higher
14 barrier to entry.

15 MR. KAPLAN: With that, Your Honor, we have no
16 further questions of this witness.

17 Thank you very much, Dr. Mayo.

18 THE WITNESS: Thank you.

19 JUDGE KASHI: My plan is we're going to take a ten-
20 minute recess, have redirect, and then we're going to come
21 back with the redirect. And my hope is to be able to finish
22 the last two witnesses today.

23 The scheduled time for them is an hour and a half.
24 So that should have us out of here before 7:00 Is that a
25 problem for anybody?

1 MR. KAPLAN: Yes, it is, Your Honor. And if I may
2 ask a point of company privilege here, we did get served
3 with, as I said, with six inches of rebuttal testimony, some
4 of which was not on time on Saturday. We've been
5 struggling, and we've also been answering all last week
6 interrogatory answers from participants. In fact, we were
7 still answering them today.

8 I can commit to Your Honor that if I proceed now, it
9 will take me longer than if I proceed in the morning. We
10 had time to organize Dr. Mayo, and I think we managed to do
11 Dr. Mayo in 40 minutes, or my cross examination was under 40
12 minutes long. I think we can be equally expeditious if we
13 can do the next two witnesses first thing in the morning.
14 And I think we will ultimately have a more productive
15 session. And we would ask that we finish with this witness
16 today.

17 JUDGE KASHI: I'm not going to push anybody today.
18 But let me say this. The scheduled time for the witnesses
19 tomorrow is over thirteen hours.

20 MR. KAPLAN: We realize that, Your Honor. I think in
21 light of today's experience and cooperation of counsel, I
22 think Your Honor's lead counsel proposal has actually
23 effectively made this hearing much more efficient, and I
24 hope we will move it along. Certainly PP&L will do
25 everything it can to move the process along.

1 JUDGE KASHI: Mr. Kohler, do you need some time for
2 redirect? Or are you prepared to go ahead now?

3 MR. KOHLER: I don't need a ten-minute break before
4 redirect, Your Honor. If I could have one minute.

5 JUDGE KASHI: All right.
6 Then everybody stand easy here.

7 (Off-the-record pause.)

8 JUDGE KASHI: Mr. Kohler, are you ready?

9 MR. KOHLER: Yes, I am, sir.

10 JUDGE KASHI: Redirect.

11 **REDIRECT EXAMINATION**

12 BY MR. KOHLER:

13 Q. Dr. Mayo, in responding to Mr. Rubin's questions
14 about under what circumstances an EDC should be required or
15 shouldn't be required to continue to provide revenue cycle
16 services, was your answer as an economist consistent with
17 your view of economic theory?

18 A. Yes.

19 Q. Was it intended to in any way interpret
20 Pennsylvania's law or any other law?

21 A. No.

22 Q. Would you agree that with or without market
23 power, if PP&L were required to offer certain services, that
24 that law would govern?

25 A. Yes.

FORM 2

1 Q. In your view, in bringing product to market, do
2 competitors typically design a product and services to meet
3 what customers want?

4 A. Yes, they do, to whatever degree of bundling or
5 unbundling the consumer desires.

6 Q. And if customers want some product or service
7 other than what is being offered, is it your view that it's
8 likely that some entity will develop that product to meet
9 the consumer need?

10 A. In a typical unregulated competitive market with
11 no barriers to entry, the answer is yes.

12 MR. KOHLER: No further redirect, Your Honor.

13 JUDGE KASHI: Thank you very much.

14 I take it there's no follow-up on that. Thank you
15 very much, Dr. Mayo.

16 That which has been marked and identified as Enron
17 Statement No. 2 and No. 2.1 are received into the
18 evidentiary record. Without objection?

19 (No audible response.)

20 JUDGE KASHI: Without objection.

21 (Whereupon, the documents marked as
22 Enron Statement Nos. 2 and 2.1 were
23 received in evidence.)

24 JUDGE KASHI: You're excused, sir.

25 THE WITNESS: Thank you.

(Witness excused.)

1
2 JUDGE KASHI: It looks like we're behind the eight
3 ball by two hours today. And tomorrow, for some reason, we
4 had scheduled thirteen and a half hours, four and a half
5 hours the following day. So that doesn't make a lot of
6 sense. That looks like, what, nineteen, twenty hours over
7 the next two days.

8 What I'm suggesting is, should we consider convening
9 at 9:00 a.m. as opposed to 10:00?

10 MR. KAPLAN: Your Honor, let me make the following
11 suggestion. First of all, if I can suggest for tomorrow a
12 compromise of 9:30 to begin.

13 We will also take a look at the schedule and perhaps
14 propose moving some of the company witnesses, and perhaps
15 maybe some of the other witnesses, and try to even out the
16 week.

17 I think we have a lumpy problem tomorrow. We know
18 PP&L's witnesses, of course, will be available to be carried
19 over. And we do have one problem on Wednesday with Dr. Kahn
20 needs to be on first in the morning. It's very difficult,
21 thanks to airline deregulation, to get here.

22 (Laughter.)

23 MR. KAPLAN: But our witnesses were prepared to flip
24 over and pick up after Dr. Kahn. And why don't we take a
25 look at the schedule beginning tomorrow morning at 9:30,

1 maybe we can propose, after we've had a chance to talk with
2 some of the counsel, a schedule that makes the week look a
3 little bit more well balanced.

4 JUDGE KASHI: All right.

5 Does 9:30 bother anyone?

6 MR. BURGRAFF: No, Your Honor.

7 JUDGE KASHI: I would like lead counsel to take a
8 look at this problem, too, and see what we can do about some
9 further coordination to bring down some of the time on this.
10 All right?

11 If there's nothing further, then we will recess until
12 9:30 tomorrow morning. Thank you very much.

13 (Whereupon, at 5:24 p.m., the hearing was adjourned,
14 to reconvene on Tuesday, August 19, 1997, in Harrisburg,
15 Pennsylvania.)

16 ***
17
18
19
20
21
22
23
24
25

C E R T I F I C A T E

I hereby certify, as the stenographic reporter,
that the foregoing proceedings were taken stenographically
by me, and thereafter reduced to typewriting by me, or under
my direction; and that this transcript is a true and accu-
rate record to the best of my ability.

COMMONWEALTH REPORTING COMPANY, INC.

By: John A. Kelly
John A. Kelly

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25

FORM 2